10/6/03

SST

Issues

- Agricultural Equipment (Kerkman)
- Industry Involvement (Hahn)
  + businesses helped develop definitions
- Taxpayer Resistance ? (Nass)
  + most people feel they are already overtaxed
- Services (Nass)
  + may be battle over services
  + Diane - bill doesn't address services
- Cigars (Wirch)
  + Diane - federal legislation would require vendors out-of-state to collect taxes to level playing field for in-state business (small grocery in this instance)

10/6/03

SB 267/AB 547

Diane Hardt - DOR

- project underway since mid-90's
  + efforts to get sellers to collect tax voluntarily fell apart
- SST began in March of 2000
  + 34 states involved initially
  + now 41 states, including CA & NY
  + 20 states have enacted this year

certified service provider will determine amount of tax owed and collect $ for state

SST Issues 10/6/03

- federal law - what is benefit of passing now (Morris)
  + RB - some companies ready right now to collect under SST
  + Diane - feds won't act if they don't see significant # of states willing to participate
- new products (Wood)
  + if there is any question, SST board will clarify
- targeting particular industries for tax exemptions (J. Wood)
  + ML - again bill will provide clarity; legislature will need to evaluate category definition when making decisions
- internet sales (Berceau)
  + TB - won't ~~[illegible]~~ level playing field when add in shipping and handling - many cost more to buy via internet

Issues 10/6/03

- page 22/JC Penney case (W. Wood)
  + will be addressed by Vicki Gibbons/printers
- software (W. Wood)
  + Diane - 3 software models being developed
    - → software available in 2004 (?), pre-certified by states
    - → potential reimbursement of software costs by states
- services (W. Wood)
  + Diane - only telco industry being ~~[illegible]~~ addressed in SST

  will definitions created in future be a problem?
  + ex. if decided that wanted to tax legal services, need to abide by uniform definition if one is created
  + 75% vote required by states to amend agreement
- sales tax holiday (Morris)
  + Mickey - SST does not preclude ability of ~~[illegible]~~ legislature to offer creative forms of ~~tax~~ relief

SST Issues 10/6/03

- def. of clothing (W. Wood)
  + WI does not define because we tax all clothing
  + DOR can provide list of all definitions created but not utilized by WI

↓

Dave Warren, Dave's Ace Hardware

+ retailers already change what is taxable and not taxable on a regular basis, so SST will not create undue burden on businesses

Bob Lochner, hardware store

+ Fairness issue in retail community

SST Issues 10/6/03

- uniform definition of food (Bereaw)
  + ~~[illegible]~~ questions definition of candy
- process (Morris) - nutritionists involved?
  + Diane - state, local govt's, industry reps were involved & in creating bright line definitions

Scty. Morgan

SST included in Doyle's GROW WI plan

Jauch a national leader on this issue through involvement w/ NCSL

- pre-written software
  + modifications to software seen as personal property and taxable;
  → estimated fiscal impact of less than $25,000

SST Issues

10/6/03

Lands End/Sears

nexus is all 45 states w/ sales and use tax

favor simplification so know how products should be taxed in each taxing jurisdiction

want to level playing field with other mail order companies

does more the 30% of business over internet

Ward Brodt

want to stop "border ~~[illegible]~~ hawking" whereby other out-of-state companies tell people they won't have to pay sales tax on items purchased

software companies have ability to provide necessary programs

* question on taxation of shipping & handling does bill address?

SST issues

10/6/03

- compliance issues (Hahn)
  + Bob Lochner - currently burden of liability on retailers
  →

SST 10/6/03

WMC/Alliant

Areas of concern

— Custom software

+ tax increase for some businesses

+ currently modifications not taxable but under bill initial purchase would be taxable even if can't be used w/o modifications

+ more complicated administratively

→ at time of purchase, need to determine which part is pre-written

→ same problem at time of installation

SST Issues 10/6/03

Kohl's

soon will have 550 stores in 36 states

implementation should not create a problem

sell significant amount of merchandise over internet (Kohls.com)

+ already collect sales tax in all 50 states

internet sales about convenience more than cost

– postage & handling addressed in bill? (Jeskewitz)

SST issues 10/6/03

DOR

Multiple Points of Use
Exemption Certificate
+ elective

Definition of Pre-written
software came from
business community
(modeled after New York)

DOR will work w/
~~taxes~~ businesses on administrative
concerns

S & H currently taxed.
will continue but re-named "delivery"

European Union also has
SST project

SST issues 10/6/03

Art Hackett - Alliant

— Multi-sourcing issue
+ reasonable apportionment
method difficult to
determine

~~[illegible]~~

will pay additional taxes
on software, will create
administrative "nightmare"

Niall Power, Michael Tobin (Banta)

printing is 3rd largest
manufacturing industry in U.S.
print catalogues for companies
that sell remotely

THE LAWMAKER'S GUIDE

to the

Streamlined Sales Tax Project

2003, The Year of Decision

PUBLISHED BY:
The Deloitte & Touche
Center for Multistate Taxation

UNIVERSITY of WISCONSIN
UWMILWAUKEE

The Lawmaker's Guide to the Streamlined Sales Tax Project

2003, The Year of Decision

The Deloitte & Touche
Center for Multistate Taxation

University of Wisconsin – Milwaukee

This Lawmaker's Guide was written by Diane L. Hardt, Douglas L. Lindholm and Stephen P.B. Kranz, and was published by the Deloitte & Touche Center for Multistate Taxation at the University of Wisconsin-Milwaukee. The Center was established in 1996 to serve as a focal point for research and education regarding state and local tax issues. The Center's mission is to promote research aimed at making state and local tax systems more responsive to modern business realities, assist taxpayers in developing practical strategies for complying with state and local taxes, and enhance university and professional education in state and local taxation. Funding for the printing of this publication was provided by Wallace Computer Services, Inc. and R.R. Donnelley and Sons Company. Inquiries regarding this Lawmaker's Guide should be directed to John C. Healy, Managing Director, Deloitte & Touche Center for Multistate Taxation. Mr. Healy can be contacted at jhealy@uwm.edu, (414) 229-2262, or School of Business Administration, University of Wisconsin-Milwaukee, 3202 N. Maryland Ave., Milwaukee, WI, 53211.

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Prior to her appointment as administrator, Ms. Hardt held positions as an auditor, audit supervisor, Director of the Tax Processing Bureau and Director of the Audit Bureau. Ms. Hardt earned her bachelor's and Executive MBA degrees from UW-Madison in May 2001. She is also a CPA.

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The authors would like to acknowledge and applaud the hard work and dedication of the many talented individuals from the public and private sectors who have worked so diligently on the Streamlined Sales Tax Project for almost three years.

The Lawmaker's Guide to the Streamlined Sales tax project 2003

Executive Summary

The Streamlined Sales Tax Project is an effort created by state governments, with input from local governments and the private sector, to simplify and modernize sales and use tax collection and administration. The Project's proposals include tax law simplifications, more efficient administrative procedures, and emerging technologies to substantially reduce the burden of tax collection. The Project's proposals are focused on improving sales and use tax administration systems for both Main Street and remote sellers for all types of commerce.

Thirty-nine states and the District of Columbia are involved in the Project. Thirty-six states and the District of Columbia are voting participants in the Project because their legislators have enacted enabling legislation or their governors have issued executive orders or similar authorizations. Three states are non-voting participants in the work of the Project because they do not have the formal commitment of the state executive or legislative branches, but are still participating. Forty-five states and the District of Columbia impose a sales and use tax.

The Project was organized in March 2000. The Project is conducting its work through a steering committee with co-chairs, four work groups, and a number of sub-groups. Project participants are generally state revenue department administrators but there are also representatives of state legislatures and local governments. Businesses — including national retailers, trade associations, manufacturers, direct marketers, telecommunications companies, leasing companies, technology companies, printers, accounting firms, and others — have actively participated in the Project by offering expertise and input, reviewing proposals, suggesting language, and testifying at public hearings.

The goal of the Streamlined Sales Tax Project is to provide states with a Streamlined Sales Tax System that includes the following key features:

- **Uniform definitions within tax laws.** Legislatures still choose what is taxable or exempt in their state. However, participating states will agree to use the common definitions for key items in the tax base and will not deviate from these definitions. As states move from their current definitions to the Project's definitions, a certain amount of impact on state revenues is inevitable. However, it is the intent of the Project to provide states with the ability to closely mirror their existing tax bases through common definitions.

- **Rate simplification.** States will be allowed one state rate and a second state rate in limited circumstances (food and drugs). Each local jurisdiction will be allowed one local rate. A state or local government may not choose to tax telecommunications services, for example, at one rate and all other items of tangible personal property or taxable services at another rate. State and local governments will accept responsibility for notice of rate and boundary changes at restricted times.

- **State level tax administration of all state and local sales and use taxes.** Businesses will no longer file tax returns with each local government within which it conducts business in a state. Each state will provide a central point of administration for all state and local sales and use taxes and the distribution of the local taxes to the local governments. A state and its local governments will use common tax bases.

- **Uniform sourcing rules.** The states will have uniform and simple rules for how they will source transactions to state and local governments. The uniform rules will be destination/ delivery based and uniform for tangible personal property, digital property, and services.

- **Simplified exemption administration for use- and ent based exemptions.** Sellers are relieved of the "good fait requirements that exist in current law and will not be lia uncollected tax. Purchasers will be responsible for payin tax, interest and penalties for claiming incorrect exempti States will have a uniform exemption certificate in pape electronic form.

- **Uniform audit procedures.** Sellers who participate in o the certified Streamlined Sales Tax System technology r will either not be audited or will have limited scope audi depending on the technology model used. The states ma conduct joint audits of large multi-state businesses.

- **State funding of the system.** To reduce the financial bu on sellers, states will assume responsibility for funding s of the technology models. The states are also participati a joint business-government study of the costs of collect on sellers.

The Project proposes that states change their sales and use tax l conform with the simplifications as proposed by the Project. Th simplifications would apply to all sellers. Sellers who do not ha physical presence or "nexus" are not required to collect sales an taxes unless Congress chooses to require collection from all sell all types of commerce. Sellers without a physical presence can volunteer to collect under the proposed simplifications. Registr by sellers to voluntarily collect sales and use taxes will not infer the business must pay business activity taxes, such as the corpo franchise or income tax.

The Streamlined Sales Tax System will provide sellers the oppo to use one of three technology models. A seller may use Model where a Certified Service Provider, compensated by the states, v perform all of the seller's sales tax functions. A seller may use Mo a Certified Automated System, to perform only the tax calculati function. A larger seller with nationwide sales that has develope own proprietary sales tax software may use Model 3 and have its own system certified by the states collectively. However, some sellers may choose to continue to use their current systems and still enjoy the benefits of the Project's simplifications.

The Streamlined Sales Tax Project envisions two components to the legislation necessary to accomplish the Project's goals. First, states would adopt enabling legislation referred to as the Uniform Sales and Use Tax Administration Act ("Act"). The Act allows the state to enter into an agreement with one or more states to simplify and modernize sales and use tax administration in order to reduce the burden of tax compliance for all sellers and all types of commerce. The Act does not require any amendments to a state's sales and use tax law.

Secondly, states would amend or modify their sales and use tax laws to achieve the simplifications and uniformity required by the participating states working together. The Project refers to this legislation as the Streamlined Sales and Use Tax Agreement ("Agreement"). Some states will require only minor changes to current law to implement the requirements of the Agreement. Other states with more complicated sales tax laws may require significant changes to current law to be in accord with the Agreement.

A certificate of compliance will document each state's compliance with the provisions of the Agreement and cite applicable statutes, rules or regulations, or other authorities supporting such compliance. Public notice and comment will be provided before a state becomes part of the interstate Agreement. A state is in compliance with the Agreement if the effect of the state's laws, rules or regulations, and policies is substantially compliant with each of the requirements of the Agreement. If a state is found to be out of compliance with the Agreement, it will not be accepted into the interstate Agreement or will be sanctioned or expelled by the other participating states. In a voluntary system, sellers who are voluntarily collecting sales taxes for participating states may decide to no longer collect for the expelled state. Also, that state may not have a vote on changes in the Agreement.

A governing board will be comprised of representatives of each member state of the Agreement. Each member state is entitled t vote on the governing board. The governing board is responsible interpretations of the Agreement, amendments to the Agreement issue resolution. A State and Local Government Advisory Coun a Business and Taxpayer Advisory Council from the private sect advise the governing board.

On November 12, 2002, thirty states and the District of Columb approved the interstate Agreement provisions. States will move forward in 2003 and enact the conforming legislation. The Agre will become effective when at least ten states with twenty percer the total population of all states imposing a state sales tax have enacted the conforming legislation and are found to be in compl with the requirements of the Agreement.

It's anticipated that states that enact the conforming legislation a found to be in compliance with the Agreement will continue as t governing states of the interstate Agreement of the future.

For a discussion of the events and debate that led to the creation Streamlined Sales Tax Project, see "Historical Perspective on the SSTP: (The Great Sales Tax Collection Debate)."

THE LAWMAKER'S GUIDE TO THE STREAMLINED SALES TAX PROJECT 2003

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THE LAWMAKER'S GUIDE TO THE STREAMLINED SALES TAX PROJECT 2003

By Diane L. Hardt, Douglas L. Lindholm, and Stephen P.B. Kranz

INTRODUCTION

The Streamlined Sales Tax Project (SSTP) is an effort created by state governments, with input from local governments and the private sector, to simplify and modernize sales and use tax collection and administration. The SSTP's proposals include tax law simplifications, more efficient administrative procedures, and emerging technologies to substantially reduce the burden of tax collection. The SSTP's proposals are focused on improving sales and use tax administration systems for both Main Street and remote sellers and for all types of commerce.

Who is participating in the SSTP? The 36 states that are voting participants in the SSTP are shown in Table 1. The legislatures of these states enacted enabling legislation or their state executives issued executive or similar orders authorizing their participation. The District of Columbia is also a voting participant in the SSTP. Three other states are non-voting participants in the SSTP. They do not have

Table 1 – Participating States

Alabama	Michigan	Rhode Island
Arizona	Minnesota	South Carolina
Arkansas	Mississippi	South Dakota
Florida	Missouri	Tennessee
Illinois	Nebraska	Texas
Indiana	Nevada	Utah
Iowa	New Jersey	Vermont
Kansas	North Carolina	Virginia
Kentucky	North Dakota	Washington
Louisiana	Ohio	West Virginia
Maine	Oklahoma	Wisconsin
Maryland	Pennsylvania	Wyoming

nal commitment of their legislatures or their chief executives participating so as to be aware of the SSTP's work.

TP was organized in March 2000, after several earlier attempts lify sales tax administration. (The SSTP's long history is ed below, in Historical Perspective on the Project.) The SSTP tially sponsored by four organizations: the National Governors' ation, the National Conference of State Legislatures, the ion of Tax Administrators, and the Multistate Tax Commission. four groups identified the features of the SSTP's Streamlined ax System, which are listed in Table 2.

SSTP ORGANIZATION

TP has conducted its work through a steering committee led hairs Diane L. Hardt of the Wisconsin Department of Revenue arles D. Collins, Jr. of the North Carolina Department of ie. Other steering committee members come from states of it sizes including Kentucky, Missouri, New Jersey, lvania, South Dakota, Texas, and Utah. The SSTP assigned the s of the Streamlined Sales Tax System to four work groups: Base and Exemption Administration; (2) Tax Rates, ation, Returns, and Remittances; (3) Technology, Audit, , and Paying for the System; and (4) Sourcing and Other fications. The work groups and sub-groups have worked since 2000 to develop their work products.

sses and their associations — including national retailers, nent stores, trade associations, manufacturers, technology nies, telecommunications companies, airlines, leasing companies, s, direct marketers, electronic commerce businesses, and ting firms — have actively participated in the SSTP, which has d on simplifications for multistate sellers because of the exities these sellers face in complying with multiple state and ales tax laws and jurisdictions. The SSTP has maintained, er, that any solutions must also work for small brick-and-mortar which represent the majority of the sales tax collectors and n any state.

Table 2 Uniformity Features
1. Uniform Sourcing Rule
2. Standardized Geographic Coding System for Local Rates
3. Local Rate Simplification
4. Uniform Required Notice and Limited Frequency of Rate Changes
5. Uniform Product Codes for Exemptions by Product Category
6. Uniform Definitions
7. No or Minimal Sales Tax Returns or Reporting Requirements for Participating Sellers
8. Central One-Stop Registration System
9. Simplified Exemption Administration for Use and Entity Exemptions
10. Uniform Treatment of Bad Debts
11. Systems Checks of Sellers and Minimal Exposure to Audits
12. Uniform Audit Procedures
13. State and Local Taxes Remitted at State Level Only, with State Responsible for Distributing Funds to Local Governments
14. Voluntary Registration Not a Factor in Determining Nexus for Income or Other Taxes; Terms and Conditions for Past Liability Relief
15. Uniform Rounding Rules
16. Privacy Protections
17. Joint Certification of Software
18. State Compensation for System

THE STREAMLINED SALES TAX IMPLEMENTING STATES CONVENE

All SSTP states that adopted authorizing legislation (See Appendix) convened an initial meeting of the Streamlined Sales Tax Implementing States (SSTIS) in Salt Lake City, Utah on November 28-29, 2001. The group elected State Representative Matthew H. Kisber from Tennessee and Utah Tax Commissioner Bruce Johnson to act as co-chair. The purpose of the SSTIS was to vote on the simplification proposals of the SSTP and adopt a final version of the interstate Agreement for adoption by state legislatures.

A HISTORICAL VOTE

On November 12, 2002 in Chicago, the SSTIS adopted a final Agreement by a vote of 31 'yea", three states absent, and one abstention. The vote was considered a significant milestone in state tax administration for all of those involved in SSTP and SSTIS. The Agreement provisions must now be turned into legislation by participating states for adoption during 2003 state legislative sessions.

THE SSTP WILL CONTINUE

The SSTP will continue to meet periodically to work on unresolved issues and implement the provisions of the Agreement. States that enact the provisions of the Agreement in 2003 will be the governing states of the Streamlined Sales Tax System.

Background and explanations to each of the SSTP proposals are provided in the following sections to this guide.

STATE TAX ADMINISTRATION

Most states administer their state and local sales and use taxes. The home-rule states are the exception. Alabama, Arizona, Colorado, and Louisiana either constitutionally or statutorily allows their local jurisdictions to legislate their own tax bases, develop their own tax

Local governments from the home-rule states have helped deve state level tax administration provisions of the Agreement. The position is that each state and the local jurisdictions within that need to work out the optimal collection and audit procedures fc jurisdictions in the state; however, businesses should still have one point of administration for all state and local sales and use Local governments will not have separate forms, payments, or administrative functions such as audits. The business communit supportive of this solution.

SINGLE STATE AND LOCAL TAX BASE

Most states have a single tax base for the state and all of the loc jurisdictions within that state, except where prohibited by feder (For example, federal law prohibits local taxation of direct-to-h satellite services.) Any particular item or service is taxable or e at both the state and local level.

Under current law there are two exceptions to the single tax bas

- "Home-rule" states either constitutionally or statutorily their local jurisdictions to determine what is taxable witl that jurisdiction. Alabama, Arizona, Colorado, and Louis have separate tax bases for local jurisdictions.
- A few states statutorily provide for a local tax base that from the state tax base. For example, food may be exem from the state sales tax but subject to a local tax; resider electricity may be taxed at the local level but not by the

Multistate sellers have advised the SSTP that the single most di issue in sales tax administration is dealing with multiple tax bas within states. In fact, these sellers have indicated they devote m resources to administering sales taxes in the handful of home-ru states than in all of the other states combined.

The SSTP has taken the position that all participating states must toward a single state and local tax base and achieve that uniform December 31, 2005. The SSTP has made an exception for sales aircraft, watercraft, modular homes, manufactured homes, and mobile homes. The SSTP made this exception because of concerns about the various kinds of tax levies on these items and because of concerns about shifting revenues between state and local governments.

The business community has taken the position that participating states with separate state and local tax bases should be forced to harmonize those bases. Further, because of the administrative difficulty of dealing with separate state and local tax bases, businesses are recommending elimination of the SSTP's phase-in period.

UNIFORM DEFINITIONS WITHIN TAX BASES

Uniform definitions represent one of the most fundamental components of the Streamlined Sales Tax System. The SSTP envisions a glossary of uniform definitions from which a state would define its tax base. The glossary would include those items or services that could be taxed by a state. Legislatures would determine what is taxable or exempt but agree to use the uniform definitions. Because businesses now operate in a borderless and even global economy, uniform definitions would simplify multistate compliance by allowing definitive taxability determinations. In fact, tax software could be coded based on a matrix of states, defined property and services, and taxability determinations by the state.

As states move from their current definitions to the SSTP's definitions, a certain amount of impact on state revenues is inevitable. It is the intent of the SSTP, however, to provide states with the ability to mirror their existing tax bases closely through uniform definitions. State legislatures should not view participation in the SSTP as a means of raising, or lowering, state tax revenues.

There certainly have been questions raised as to why states need uniform definitions. Some have suggested that technological advances should enable states to have various definitions. Some state legislators have indicated they do not want to get boxed in by uniform definitions. Some businesses supported the concept of uniform definitions until

Businesses that collect and remit sales taxes for the states will r accept technology as a substitute for uniform definitions, and w good reason. They are familiar with current software packages : their limitations. They know how many employees are required make accurate sales tax law determinations, even with all of the software packages and research tools currently available. And tl know that incorrect sales tax determinations in their multistate businesses often result in audits, additional taxes due, and in so cases, class action lawsuits.

The SSTP has worked with the business community to identify tax terms and definitions most in need of uniformity and has m them a first priority. Ultimately, the SSTP would expect to defir products and services that create burdens on multistate business The SSTP does not expect to define use-based exemptions (e.g. manufacturing exemptions).

A participating state is expected to adopt all items specifically mentioned in a definition. A participating state may not vary fro definition except as provided in the agreement between the partic states. For example, the SSTP has defined food and food ingred and various subcategories of food, including candy, dietary supp ments, soft drinks, and prepared food. A participating state may (to tax all food and food ingredients, which include candy, dietar supplements, soft drinks, and prepared food. On the other hand, participating state may choose to exempt food and food ingredie defined by the SSTP but tax one or more of the subcategories as defined by the SSTP. A participating state may not, however, ch to tax a subcategory such as candy and exempt a particular kind candy that falls within the subcategory. See Exhibit 1 for the defi of "food and food ingredients" and the optional sub-categories.

The SSTP has also defined four mutually exclusive categories o clothing: (1) clothing, (2) clothing accessories, (3) sport or recrea equipment, and (4) protective equipment. A participating state m or exempt any or all of these four categories but may not vary fr the definitions of these categories. Therefore, a participating stat not choose to exempt one item within the category of protective

The SSTP has also defined purchase price, retail sale, sales price, delivery charges, and direct mail. Other definitions completed include those for tangible personal property, computer software, prewritten computer software, prosthetic devices, durable medical equipment, mobility enhancing equipment, prescription, over-the-counter drugs, grooming and hygiene products, and lease or rental.

TAX RATE SIMPLIFICATIONS

Some would say that a truly streamlined sales tax system would provide for one rate per state with no variances for local jurisdictions. Thus, sellers would have to contend only with one rate per state for the District of Columbia and each of the 45 states that impose a sales tax. States could distribute the sales tax collections to their local jurisdictions in any manner they chose.

This simple tax rate structure was abandoned early in the SSTP. Local governments are increasingly reliant on local sales taxes and may have issued bonds that are backed by the local tax revenue stream. Local government input to the SSTP suggested that a single tax rate structure would not be accepted politically. The business community, while preferring one rate per state, recognizes that technology is available to deal with multiple rates if there are restrictions on the frequency of rate changes, databases to help with rates, and a single tax base per state.

The SSTP's rate simplifications include the following:

- States may have only one state tax rate on items of personal property and services after December 31, 2005.
- States are encouraged to provide advance notice of rate changes and limit the effective date of rate changes to the first day of a calendar quarter.
- States with local jurisdictions that levy sales and use taxes must not have more than one sales tax rate or more than one use tax rate per local taxing jurisdiction. If the jurisdiction

- States and local jurisdictions may not have caps or thres on the application of sales and use tax rates or exceptio that are based on the value of a transaction or item after December 31, 2005.
- Local tax rate changes will be effective only on the first of a calendar quarter after a minimum of sixty days' not to sellers.
- Local tax rate changes applicable to catalog purchases v effective on the first day of a calendar quarter after a mi of 120 days' notice to sellers.
- States with local jurisdictions will provide a database th describes rates for all of the jurisdictions levying taxes i state. The databases will also include rate and boundary changes for all taxing jurisdictions.
- States will assign tax rates and jurisdictions to each nine zip code. States will work together to develop an addres system for assigning rates and jurisdictions.
- Tax rate limitations and limitations on caps and threshol not apply to sales and use taxes levied on the transfer of vehicles, aircraft, watercraft, modular homes, manufactu homes, and mobile homes.
- States and local jurisdictions will relieve sellers and cert service providers (CSPs) from liability for having charg collected the incorrect amount of sales or use taxes if th sellers or CSPs relied on erroneous data provided by a s tax rates, boundaries, or taxing jurisdiction assignments.

The most controversial SSTP proposal was that states could onl one state rate to be applied to all taxable property or services. A r of states have multiple state rates. In fact, the SSTIS provided fo exception to one state rate in the case of food and food ingredie and drugs, as defined by state law pursuant to the Agreement. T SSTP has recommended that states consider alternatives such as income tax credits and refunds to taxpayers to get to one state ra

UNIFORM SOURCING RULES

Sourcing refers to determining for which state and local jurisdiction, if any, tax is to be collected. The SSTP has proposed that sellers be required to source sales of property, services, and digital goods on a destination basis.

Under a destination-based rule, the seller would source the sale to the seller's business location for over-the-counter transactions and to the customer's shipping address for other transactions. If the "shipped to" address is not known to the seller, the next level in the sourcing hierarchy is the purchaser's address as maintained by the seller in the normal course of business. When none of these locations is known, the sale is sourced to the location indicated by an address for the purchaser obtained during the consummation of the sale, including the address of the purchaser's payment instrument if no other address is available. When the destination rules do not apply, the sale is sourced to the origin of the sale.

The destination rules may not adequately address a situation in which a product can be accessed or used by several persons in different locations at once, such as software accessed by remote employees, or a database accessed by various offices of a multistate company. The SSTP has proposed a multiple points of use (MPU) procedure in these cases. When a digital good, computer software delivered electronically, or a service is concurrently available for use in more than one jurisdiction, the purchaser may deliver to the seller a MPU exemption form. The seller will then be relieved of any obligation to collect the tax and the purchaser will be required to pay the tax by using a reasonable and consistent method of apportionment that is supported by the purchaser's business records.

Lawmakers of states with local taxes should be aware that the SSTP is recommending a destination approach for both state and local taxes. A majority of the states use destination for sourcing intrastate sales. Thus, although the destination approach will mean a change in some states that use origin sourcing, the destination approach was the least disruptive choice in a simplified and uniform system. In addition, the implementation of a different sourcing rule for intrastate sales and

interstate sales raises significant constitutionality issues. Since t[illegible] tax is a tax on consumption, destination was the policy prefere[illegible]

The SSTP has worked closely with telecommunications compa[illegible] and printers to address their unique sourcing issues. Special ru[illegible] been developed for various telecommunications services and d[illegible] mail. For mobile telecommunications services, the SSTP has f[illegible] the federal Mobile Telecommunications Sourcing Act. As of Ja[illegible] 2003, the Project is working with the florist industry to addres[illegible] unique situations.

SIMPLIFIED EXEMPTION ADMINISTRATION

There are three types of exemptions in sales tax law: (1) produ[illegible] exemptions, (2) entity-based exemptions, and (3) user-based exemptions. Product exemptions are easy to administer when t[illegible] states have uniform definitions. For example, many states do n[illegible] prescription drugs and sellers just do not collect tax on the pro[illegible] that fit the uniform definition for the exemption for prescription[illegible]

The exemptions for entities and users are more difficult to adm[illegible] Sales tax law carries a presumption that sales of all tangible pe[illegible] property are taxable unless specifically exempted by law. Entiti[illegible] users who qualify for an exemption because of who or what the[illegible] or how they use a product need to prove they qualify for the exemption. The entities and users use exemption certificates fo[illegible] purpose. For example, a school must provide an exemption cert[illegible] to a seller to purchase school supplies or books without tax; a f[illegible] or manufacturer must provide an exemption certificate to a sell[illegible] purchase machinery used in farming or manufacturing without [illegible]

The SSTP has identified numerous ways to improve sales tax administration related to exemptions. The business participants [illegible] been most helpful in developing the new procedures and propo[illegible] law. All participants agree that the SSTP has achieved radical simplification in exemption processing requirements while imp[illegible]

There are two components to the simplifications:

- Uniform exemption certificates (electronic where possible); and
- Relief for sellers from any tax if a purchaser improperly claims an exemption, as long as the seller obtains the required identifying information of the purchaser and the reason for claiming the exemption at the time of purchase.

Under current laws in many states, sellers can be held responsible for nonpayment of tax when a purchaser incorrectly claims an exemption. Sellers have been the enforcers of sales tax law even though it is often difficult to determine whether an exemption is being properly claimed. In recent years, several states have repealed these good-faith requirements on sellers without major compliance problems. Purchasers are held responsible for nonpayment of tax when it is due.

Lawmakers should be aware that states may need to amend their laws regarding exemption certificates so that the states collect the uniform identifying information of the purchaser and the reason for claiming the exemption. Purchasers will not be required to sign an exemption certificate unless a paper certificate is used. To ensure compliance, states should use a system in which a purchaser exempt from payment of tax is issued an identifying number that must be presented to the seller at the time of purchase. Sellers will then provide information on exempt purchases to the tax departments on a regular basis. The tax departments obtain a new means of verifying exemptions claimed.

The SSTP is currently developing one uniform exemption certificate. This uniform check-the-box certificate will replace the multiple exemption certificates used by many states.

CAPS AND THRESHOLDS

Several states or their local governments have dollar caps or rate caps in their sales and use tax laws. Dollar caps are limits on the amount of tax charged on a purchase. Rate caps are limits on the rate that can be applied when determining the tax amount.

Examples of dollar and rate caps follow:

- Florida provides for a local sales and use tax on the fir[illegible] $5,000 of the purchase price of a single item.
- South Carolina provides a sales and use tax dollar cap [illegible] on the purchase of an automobile.
- Texas has a rate cap of 8.25 percent on state and local t[illegible] levies.

Thresholds are an exclusion from tax or the application of a di[illegible] tax rate to purchases above or below a set level. For example, N[illegible] exempts all clothing priced below $110; Tennessee taxes airpla[illegible] 6 percent on a purchase price up to $100,000 and 3 percent on [illegible] purchase price exceeding $100,000.

The SSTP has proposed the phaseout of caps and thresholds o[illegible] and local sales and use taxes after December 31, 2005. These proposals were developed with the business community in min[illegible] Sellers have informed the SSTP that caps and thresholds are di[illegible] to administer.

The SSTP has proposed that the restrictions on caps and thresh[illegible] not apply to sales or use taxes levied on the transfer of motor v[illegible] aircraft, watercraft, modular homes, manufactured homes, and [illegible] homes or to instances where the burden of administration has b[illegible] shifted from the seller.

SALES TAX HOLIDAYS

Sales tax holidays are temporary sales tax exemptions on certai[illegible] for a specific period of time. The tax holiday typically falls dur[illegible] traditional back-to-school shopping period. Most states with sal[illegible] holidays place a ceiling on the price of eligible merchandise an[illegible] exempt purchases from state and local sales and use taxes. Curr[illegible] jurisdictions with sales tax holidays include Texas, Florida, Conn[illegible] South Carolina, Pennsylvania, Iowa, Maryland, North Carolina, [illegible] the District of Columbia. Florida, Maryland, and Pennsylvania [illegible] new legislation each year.

The two primary policy considerations set forth by proponents of sales tax holidays are tax relief and increased economic activity. Sales tax holidays are particularly important to states that border states with no sales taxes, lower sales tax rates, permanent exemptions on particular rates, or competing holidays.

From a sales tax administration perspective, sales tax holidays create numerous difficulties for both sellers and revenue departments. These administrative difficulties are especially pronounced for multistate sellers. Catalog and Internet sellers have difficulty determining when a sale actually takes place. Most, if not all, states use transfer of title or possession to set the time of sale. For catalog or Internet sales, this occurs when an item is shipped. In many cases, neither the customer nor the seller knows the shipping date at the time of the order.

An additional level of complexity exists when the seller must determine the consumer's ultimate use of an item. For example, some states provide a sales tax holiday on "computers for home use." Catalog and Internet sellers do not have the face-to-face contact to ask questions about use.

There are many other complex issues regarding sales tax holidays that must be resolved, including questions about layaway purchases, exempt and taxable items that are packaged together, coupons and discounts, rainchecks, exchanges, shipping and handling charges, service charges, restocking fees, and back orders.

The SSTP's position is that sales tax holidays should not be allowed in the Streamlined Sales Tax System. Brick-and-mortar sellers are divided on this proposal. Mail-order and Internet sellers support the prohibition of sales tax holidays. The SSTIS approved sales tax holidays with restrictions after December 31, 2003. These restrictions require that: items to be exempted must be uniformly defined in the Agreement; the customer's use of the item cannot determine taxability; the holiday is uniformly applied to state and local sales and use taxes; there is notice of the holiday provided at least sixty days prior to the beginning of a calendar quarter in which the holiday occurs; there can be no exemption for a portion of the price of an item; and uniform administrative procedures are to be developed.

CENTRALIZED REGISTRATION AND AMNES

The SSTP has proposed one online registration system that wi sellers to register in all of the participating states. By registeri this system, the seller would agree to collect and remit sales a taxes for all taxable sales into the participating states. The SS to make it easy for sellers to collect taxes voluntarily.

Registration with the central registration system and the collec sales and use taxes in the participating states will not be used factor in determining whether the seller has nexus with a state business activity tax, such as the income or franchise tax.

The SSTP is promoting an amnesty for uncollected or unpaid s use taxes to a seller that registers to pay and/or to collect and applicable sales and use taxes on sales made to purchasers in The amnesty is applicable to sellers that register within 12 mo the effective date of a state's participation in the Streamlined S System. The amnesty is not applicable to sellers that were regi in a state in the 12-month period preceding the commencemen state's participation in the system. The amnesty is also not ava sellers under audit or to sellers that owe sales and use taxes in capacity as a buyer. States may allow amnesty in terms and co more favorable to the seller than what is provided in the agree between the participating states.

UNIFORM RULES FOR RECOVERY OF BAD

The SSTP has developed uniform rules for a deduction for the debts of a seller. To the extent a state provides a bad debt dedu any other party (e.g., third-party assignments), the same unifo procedures will apply.

The bad debt deduction will be tied to the requirements of the Revenue Code (Code). Sellers will be allowed to claim a dedu the return for the period during which the bad debt is written uncollectible rather than being required to file refund claims f the sale was reported. The statute of limitations for claiming t debt deduction will be the state's otherwise applicable statute limitations for refund claims; however, the statute of limitations will be measured from the due date of the return on which the bad debt can first be claimed.

TECHNOLOGY MODELS AND CERTIFICATION

The SSTP has proposed the integration of new technologies and simplified tax laws to improve the tax collection process. Three technology models are envisioned under the Streamlined Sales Tax System. A seller can choose one of these three technology models or can continue to use a traditional tax collection system. If a seller chooses one of the technology models as certified by the states, however, the seller will benefit from reduced liability and audit scope.

Model 1 is a Certified Service Provider (CSP). Under this model, a seller selects a CSP as an agent to perform all of the seller's sales tax functions at no cost to the seller. The CSP then determines the amount of tax due, pays the tax to the states, and files returns with the states. The states will compensate the CSPs through a transaction fee, a percentage of revenues collected, or some combination of these. The states anticipate that several entities will be able to meet the requirements to be a CSP.

The CSP in this model is liable for the tax due unless there are errors by the states or fraud by the seller. The CSP is subject to audit and periodic system checks by the states. Any audit will be a joint audit performed on behalf of all of the states participating in the Streamlined Sales Tax System.

Model 2 is a certified automated system (CAS). A seller selects a CAS to calculate the amount of tax due on a transaction. Sellers benefit from the use of a CAS because they use standardized software that is certified by the states as accurate. The CAS in this model is subject to periodic system checks. The seller is subject to audit on its tax remittance and return filing functions.

Model 3 is a proprietary system that is certified by the states as a CAS. This model accommodates large sellers with nationwide sales that have developed their own sophisticated proprietary automated sales

tax systems. A seller with a proprietary system must agree to se
conditions to obtain certification of its system. The seller must a
to process all its sales using the system, to meet an accuracy sta
set by the states, to agree to a methodology for determining whe
the system is meeting the established performance and accuracy
standards, and to allow the states to examine its system periodic

The decision to use a CSP or CAS is entirely up to the seller. Se
that do not find the use of a CSP or CAS relevant or beneficial
continue to calculate, pay, and report sales tax under their curre
procedures. These sellers will nevertheless benefit from the sim
cations and uniformity achieved by the Streamlined Sales Tax S

UNIFORM AUDIT STANDARDS AND PROCEDU

The SSTP has proposed uniform audit standards and procedures
CSPs and sellers. The combination of certified software, unifor
definitions, and common audit procedures should substantially r
the tax administration burdens on sellers in making correct dete
nations of the taxability of property and services.

The uniform audit standards and procedures are as follows:

- Audits will be conducted by all participating states using statistical sampling techniques in accordance with gener accepted audit standards.
- States may conduct joint audits of CSPs and sellers, alth Model 3 sellers with more complex tax systems and requirements may choose to be audited by individual sta
- When joint audits are conducted and errors identified, a information will be provided to each participating state. state will then determine if an assessment or refund will required. All states will issue the assessments or refunds 90 days of the completion of the audit. States will conti follow their own statutes of limitations.
- Each participating state will provide a matrix of all defi (uniform definitions and definitions specific to each sta tangible personal property and services and the taxabilit

each item. Each state will be responsible for updating its matrix. CSPs and sellers will be held harmless from errors made by the state in its matrix.

- States will provide resources to answer questions of sellers and CSPs on a timely basis.

Audit procedures will vary depending on the technology model used by a seller and the business of the seller. Audits will determine (1) the accuracy of the data used to determine sourcing of a transaction, (2) the mapping of property or services sold, (3) the identity of purchasers if exemptions were claimed, (4) the reasons for the exemptions claimed, (5) the accuracy of tax calculations, and (6) the accuracy of reporting. Sellers will remain subject to use tax compliance audits on their purchases.

DIRECT PAY PERMITS

Direct pay is an authority granted by a tax jurisdiction that generally allows the holder of a direct pay permit to purchase otherwise taxable goods and services without payment of tax to the supplier at the time of purchase. Suppliers are to be furnished with a written notification of the purchaser's direct pay authority. The permit holder timely reviews its purchases, makes a determination of taxability, and then reports and pays the applicable tax due directly to the tax jurisdiction. The permit holder's tax determinations and adequacy of payment are subject to audit by the tax jurisdiction.

The direct pay permit is helpful to many purchasers in the determination of their use tax obligation. Thirty-three of the 45 states with sales and use taxes provide for the direct payment of tax. Several states impose the obligation to collect taxes strictly on the seller. For these states, it may be difficult to implement a direct pay program.

The SSTP has proposed that participating states be required to provide direct pay permits to purchasers but that each state be allowed to set its own limits and requirements (types of businesses eligible, criteria, eligible transactions). The SSTP will also develop a single uniform direct pay permit application and certificate.

SELLER COMPENSATION FOR COST OF COLLECTION

The Vendor Allowance — Forty-five states and the District of Columbia impose sales and use taxes on purchases of tangible
In addition, 4,696 cities, 1,602 counties, and 1,113 other tax jurisdictions impose sales taxes. For a variety of reasons, state
local governments that impose sales taxes require an outside thi
party (i.e., sellers) to collect them at the point of sale from cons
Sellers must then remit these taxes to state and local governme

In an effort to offset a portion of the economic burden sellers i
a result of this collection responsibility, many states allow selle
keep a small portion of the tax collected (an "allowance"). Twe
seven states currently provide some type of compensation to se
Eighteen states do not compensate sellers directly for any assoc
compliance costs. Sellers may also be able to offset the cost of
collection in some states through interest earned on taxes that h
been collected but not yet remitted (the "float") or through othe
financial mechanisms. In other states, however, sellers are requ
remit estimated taxes before collecting them; this results in a re
float (i.e., the state earns interest on the seller's money).

The Joint Collection Cost Study — Several studies have been commissioned to ascertain exactly how much money sellers ex
collect sales taxes. These studies, however, have been widely cr
as biased because they were conducted either on behalf of state
behalf of sellers. Recognizing the continued importance of this
and learning from the failure of past efforts, leadership from th
and the National Retail Federation, along with other representa
both state and local government and the private sector, have co
together to create the Joint Collection Cost Study.

Although the simplifications proposed by the Project will, when
mented, significantly reduce the current collection burden, this
important because sellers will continue to incur certain costs as
of the collection responsibility imposed on them. This study wil
policymakers by providing answers to three critical questions:

1. How much does collecting the sales and use tax under the current system cost sellers?
2. How will the simplifications recommended by the Project reduce these costs?
3. What residual costs of collection remain in the simplified system?

The answers to these questions will help legislators determine the value of the Project for both the state and the business community and determine at what level the seller allowance would have to be set to compensate sellers fairly for their costs.

A steering committee has been created to oversee the development of the Joint Collect Cost Study. Steering committee members include,

- **Public Sector:** Federation of Tax Administrators, Government Finance Officers Association, Multistate Tax Commission, National Conference of State Legislatures, and Streamlined Sales Tax Project; and
- **Private Sector:** Council on State Taxation, Direct Marketing Association, Federated Department Stores, J.C. Penney, National Retail Federation, Radio Shack, and Wal-Mart Stores.

Other members of the public and private sectors are welcome to participate in the study's proceedings.

A Detailed Description - The Joint Collection Cost Study will determine the costs under the current sales and use tax system and the effect on those costs — including costs shifted from sellers to state governments — of changes to the system proposed by the Project. The study will also seek to identify the factors that generate the costs under various relevant conditions, including various types of sellers, different state and local sales tax regimes, different technological circumstances, and different states of implementation of a collection process. The target deadline for delivery of the study has been moved

The study is intended to be a definitive one that will be widely recognized as objective and reliable, meeting the highest standa research practicable and avoiding any issues of conflict of inter will exclude any tax other than generally applicable sales and u taxes collected on sales to unaffiliated parties. It will not includ borne by sellers of complying with use taxes on their own purcl or by states and localities in administering such taxes.

It is anticipated that the study will enable a comparison of the c of collecting and administering sales and use taxes across a vari factors. It will include an identification and analysis of factors i operations of a seller and in the structure and administration of sales and use tax that affect the costs of collecting, remitting, ar administering sales and use taxes. The study will identify and a factors contributing to the cost of collecting, remitting and administering sales and use taxes in sufficient detail to allow th impact of changes in various features of the tax administration (e.g., those proposed by the Project) to be estimated.

The study should develop a model that will, when provided wit measure the cost of collecting and administering sales and use t The model must be capable of modification so that it measures only the current costs but also, when the recommendations of tl Project are implemented, the costs borne under the changed sys

The study will also gather the data to be used with the model, p the model with data, and present a final report with conclusion: the cost of collection under the current system. The study will p appropriately detailed descriptions of the methodology used to the data and build the model, as well as instructions and other i concerning methodology. The modified model can be used with available data or with additional data to measure the costs of col under the Streamlined Sales Tax System and compare them wit costs under the current system.

The study should examine all incremental and identifiable cost collecting and administering sales and use taxes from unaffiliat parties through the audit administration process. The study will compliance and administrative costs related to use taxes on a company's own consumption. In agreement with the steering committee, the study will separately identify and measure post-transactional costs which may be the subject of reasonable disagreement among policy-makers. Examples of such costs include, but are not limited to, costs of defending class actions when a seller overcollects, interest and penalties on "human errors" when the seller has a reasonable error rate and costs of appeals and litigation. Existing seller compensation and benefits provided by states and localities to sellers and the time value to sellers of the use of sales tax collections will be measured.

TAXPAYER CONFIDENTIALITY AND PRIVACY

The SSTP has proposed a privacy policy to protect confidentiality rights of all participants in the Streamlined Sales Tax System and the privacy interests of consumers who deal with sellers that use CSPs.

The CSP will normally perform its tax calculation, remittance, and reporting functions without retaining consumers' personally identifiable information. Personally identifiable information will be collected, used, and retained only with respect to exempt purchasers to ensure the validity of exemptions from taxation that are claimed by reason of a consumer's status or the intended use of goods or services purchased. In addition, CSPs must provide consumers, including exempt purchasers, with clear and conspicuous public notice of their information practices, including what information they collect, how they collect it, how they use it, how long they retain it, and whether they will disclose it to the participating states. Such notice will be satisfied by a written policy statement accessible by the public on the official Web site of the CSP.

CSPs must provide technical, physical, and administrative safeguards to protect personally identifiable information from unauthorized access and disclosure. When personally identifiable information regarding an individual is retained by or on behalf of a participating state, the state will protect that information under its strict confidentiality laws and regulations. In addition, the state will provide reasonable access by such individual to his or her information in the state's possession and

ONE ROUNDING RULE

One would think the states could agree to one rounding rule to si sales tax administration, but agreement on this rule has proven t challenge. Why is one rounding rule appropriate? Businesses an technology companies that operate cash register systems or deve and maintain software need to know the rounding rules. If a mu business with proprietary software can rely on one rounding rul all states, its technology maintenance costs go down.

There are multiple components to a rounding rule: (1) the rounc algorithm (rounding up at one-half cent or some other point), (2 bracket systems provided in the law of a handful of states, (3) th number of decimal places used in computing tax due, and (4) ta individual items or the aggregate when multiple taxable items a purchased at one time.

The SSTP worked with businesses and technology companies tc understand the problems in rounding. Businesses are concerned states cannot agree on something as easy as rounding, the states never agree on uniform definitions and other components neces a streamlined system. The businesses are also concerned about t costs of technology and the difficulty in keeping up with multip state laws.

The SSTP has proposed the following rounding rules: (1) elimi bracket systems, (2) carry all tax computations to three decimal (3) allow sellers to elect one consistent method of computing ta individual taxable items or the aggregate invoice of taxable item (4) provide one rounding algorithm. The fairest rounding algori for consumers is to round up to the nearest cent for anything on cent or more and round down for anything below one-half cent.

Two or three states have indicated that this proposal, and specif the rounding algorithm, will have a substantial negative revenue impact. The SSTP has proposed allowing states until December 2005, to move to one rounding algorithm. This is the same deac given to states for eliminating caps and thresholds, achieving o

UNIFORM TAX RETURN

The SSTP proposes that a seller would file a single return per reporting period with each state. The return would include the detail for the taxing jurisdictions within that state and would be due no sooner than the 20th day of the month following the month in which a transaction occurred. Sellers using one of the SSTP's proposed technology models would file a simple tax return with limited data fields. All participating states would provide for electronic filing of returns by January 1, 2003.

Sellers that register to collect taxes voluntarily for participating states would be allowed to file returns on an annual basis, with one exception. A participating state could require sellers that register to collect taxes voluntarily to file on a monthly basis if the seller collects $1,000 or more of combined state and local taxes for that state in the previous month.

The SSTP will develop a uniform state sales and use tax return for all states. Local jurisdiction information will be provided on attached schedules and tailored to a state's needs.

GOVERNANCE IN THE INTERSTATE AGREEMENT

The governance structure of the Agreement establishes rules for member states' interactions with each other and with the public. The governance provisions define operating parameters which, if implemented correctly, will effectively manage the joint state effort to administer the anticipated uniform multistate sales tax structure. The multistate nature of the Agreement requires a delicate balance between the true uniformity needed for effective simplification on the one hand and state sovereignty and federalism concerns on the other. The governance provisions included in the Agreement attempt to provide a workable balance. The general rules included in the governance model are discussed below.

Becoming a Member State — The SSTIS Agreement (as approved November 12, 2002) allows a state to become a party to the Agreement

membership and certification of compliance to the Governing E
Once ten states (comprising 20% of the population) have compl
these steps, and each has gained the approval of three-fourths o
other initial states, the Agreement becomes effective (but not be
July 1, 2003). Additional states petitioning for membership will
approved upon a three-fourths majority vote of member states,
acknowledging the petitioning state's compliance with the Agre
Each member state is allowed to appoint up to four representati
(from the executive or legislative branches of government) to th
Agreement's governing board. Regardless of the number of
representatives appointed, however, each state is entitled to only
single vote on the governing board.

Withdrawal or Expulsion — States may withdraw from the
Agreement at any time but are required to give a minimum of s
days' notice and may only withdraw on the first day of a calend
quarter. States that withdraw remain liable for any financial or
contractual obligations incurred during membership. States may
expelled from the Agreement for failure to comply with each of
requirements for membership. Expulsion of a member state req
three-fourths vote of the governing board.

Compliance — A member state may be admitted and remain a
member only if its state laws, rules, regulations and policies are
substantial compliance with each of the requirements in the
Agreement. The chief executive of each state's tax agency must
the state's compliance with the Agreement on an annual basis. F
of a state to comply with any one of the Agreement's provisions
state level administration of all taxes) would mean that a state is
compliance and subject to sanction, including possible expulsio
membership. The Agreement does contemplate that legislative c
conventions differ from state to state, and that these differences
not result in a state's noncompliance. The governing board has t
authority to review issues of compliance and to impose penaltie
commensurate to the particular noncompliance.

Public Input — The Agreement provides for public input into t and taxpayer advisory council from the private sector to advise the governing board on issues of admission of states into membership, noncompliance, interpretation, and amendments to the Agreement. Representatives of state and local governments comprise a second advisory council that advises and assists the business and taxpayer advisory council in making recommendations to the governing board.

Beyond the role of the advisory councils, the governing board is required to provide public notice and an opportunity for public comment prior to action on proposed sanctions, admission of states into membership, interpretation, and amendments to the Agreement.

Interpretation — Any person or member state may bring issues of interpretation of the Agreement before the governing board for resolution. The governing board decides issues of interpretation by three-fourths majority vote. Such decisions are considered part of the Agreement and have the same effect as provisions in the Agreement itself. It is anticipated that some interpretation decisions will require legislative action in the member states.

Definition Requests — Any person or member state may submit a request for the development of additional definitions or for interpretation on how an individual product or service fits within an existing definition. Such requests will be referred to the state and local government advisory council for its recommendation. The governing board will then take action on the recommendation.

Amendment — Any member state may request amendments to the Agreement. A minimum of sixty days notice of the request must be given to the presiding officer of each house of each member state. Amendments then require a three-fourths majority vote of the governing board. It is anticipated that any approved amendment will include an effective date allowing state legislatures adequate opportunity to conform state law to the amendment.

Issue Resolution — The governing board is authorized to promulgate rules creating an issue resolution process. Its rules will determine how

membership, compliance, sanctions, amendments, interpretation other matters in the discretion of the governing board. The rules define who can invoke the process, how it will work, the allocat costs for participation, possible involvement of a neutral third pa non-binding arbitration, and such further details as the governin board determines necessary.

State Sovereignty — The Agreement itself does not modify, inva or amend any provision of the law of a member state. Member s therefore retain complete sovereignty over their own law. In ord member states to remain uniform, however, the Agreement requ that member states remain in compliance or face possible expuls from membership. State legislatures, therefore, will occasionally called upon to conform their state law to the provisions of the A ment or risk expulsion from membership. While this mechanism to guarantee perfect uniformity among the member states, it ope to preserve state sovereignty, giving state legislatures the opport to withdraw from the Agreement instead of modifying state law.

HISTORICAL PERSPECTIVE ON THE SSTP: (THE GREAT SALES TAX COLLECTION DEBA

Background - Nearly every state that imposes a sales or similar transaction tax on the sale of tangible personal property and/or services imposes an identical compensating or use tax on the transaction if the sales tax does not apply. Because sales taxes ar generally imposed on a destination basis, the use tax, as its nam implies, is imposed on a transaction if the ultimate storage, use, consumption of a product or service is in a taxing jurisdiction different from the jurisdiction of the sale. Sales and use taxes ar meant to be complementary and are typically not imposed on th same transaction (at least by the same jurisdiction.) To collect su taxes, states impose a legal collection duty on sellers of goods o services that requires them to collect and remit sales and use tax the jurisdiction of sale or ultimate use. As remote sales (i.e., mai order and catalog sales) grew in popularity in the late 1950s and 1960s, the issue of when a state could constitutionally impose su

National Bellas Hess v. Department of Revenue — In 1967, in *National Bellas Hess v. Department of Revenue*, the U.S. Supreme Court found that a state could not impose the duty of use tax collection and payment on a seller whose only connection with customers in the state was through a common carrier or the U. S. mail. National Bellas Hess, a mail-order house located in Kansas City, Missouri, was licensed to do business in Missouri and Delaware (its state of incorporation) and conducted its mail-order business by means of catalogs and occasional advertising flyers mailed to past and potential customers nationwide, including those in Illinois. Although the company maintained neither outlets nor sales representatives in Illinois, the Illinois Department of Revenue sought to impose a collection duty based on its statutory definition of retailer, which included any retailer engaging in soliciting orders within the state from users by means of catalogs or other advertising. *National Bellas Hess* argued that the liabilities imposed on the company violated the Due Process clause of the 14th Amendment and created an unconstitutional burden on the free flow of interstate commerce.

In its majority opinion, the Court, noting that the tests for determining violations of the Due Process clause and the Commerce clause were similar, held that the imposition of a collection duty on National Bellas Hess was unconstitutional, largely because of the burden imposed by the complexity of state sales tax systems. The Court found that the many variations in rates of tax, in allowable exemptions, and in administrative and recordkeeping requirements could entangle the company's interstate business "in a virtual welter of complicated obligations." The Court noted the sharp distinction in its prior cases between mail-order sellers with retail outlets, personnel, and property in a state and those doing no more than communicating with customers in a state by mail or common carrier. The strongly worded dissent, however, noted that such large-scale, systematic, continuous solicitation and exploitation of the Illinois consumer market was sufficient nexus to require National Bellas Hess to collect from Illinois customers and to remit the use tax.

In the 25 years following the Court's decision in *National Bellas Hess*, the mail-order and catalog industry grew exponentially. Because of the

consumers, the amount of uncollected use taxes grew as well. In late 1980s, however, partly due to new Supreme Court Due Proc and Commerce clause jurisprudence, and partly due to the adver computer software developed to assist in the administration and c tion of use taxes on remote sales, state legislatures began enactir statutory language that closely mirrored the language in the *Nati Bellas Hess* dissent. Based on such statutes, and convinced that *National Bellas Hess* was anachronistic, departments of revenue number of states began issuing assessments against mail-order a catalog sellers engaged solely in the exploitation of a local mark a regular, continuous, and systematic basis. In 1992, in *Quill Co North Dakota*, the issue reached the Supreme Court for a second

Quill Corp. v. North Dakota — Quill Corporation (Quill) was a of-state mail-order house with neither outlets nor sales represent in North Dakota. It had offices and warehouses in Illinois, Calif and Georgia, and its only contact with North Dakota was throug delivery of products via U.S. mail or common carrier from out-o locations. North Dakota sought to force Quill to collect use taxe Quill's sales into the state. The North Dakota Supreme Court ha upheld the state's use tax assessment against Quill, based on a fi that the tremendous social, economic, commercial, and legal inn tions since *National Bellas Hess* had rendered its holding obsole

In *Quill*, the U.S. Supreme Court for the first time differentiated between the tests for determining whether a tax was constitution under the Due Process clause or the Commerce clause. The Due Process clause, the Court noted, is concerned with fundamental fa of governmental activity and is premised on whether a taxpayer notice or fair warning that a tax may be imposed. The Commerc clause, on the other hand, is concerned with whether a given tax unduly interferes with the free flow of interstate commerce. Bas this distinction, the Court tiptoed through its prior precedents to that the appropriate nexus standard under the Due Process claus "minimum contacts" while the standard for passing Commerce muster was "substantial nexus." Further, the Court noted that a r order house such as Quill may indeed have the minimum contac required for nexus under the Due Process clause, yet lack the

Based on the distinction drawn in *National Bellas Hess* between mail-order sellers with outlets, personnel, or property in a state and those with contacts limited to delivery via U.S. mail or common carrier, the Court found that *National Bellas Hess* had established a physical presence requirement for imposing sales and use taxes under the Commerce clause. The Court noted that such a bright-line rule was justified because it firmly established the boundaries of legitimate state authority in the area and reduced litigation over sales and use taxes. Further, the Court found that the *National Bellas Hess* rule had engendered substantial reliance and had become part of the basic framework of a sizable industry. Accordingly, the Court reaffirmed that the bright-line test established in *National Bellas Hess* was still good law.

Perhaps the most significant aspect of the decision for purposes of this article is the fact that the Court noted that the underlying issue, collection of use taxes on remote sales, not only is an issue that Congress has the power to resolve but also is an issue that Congress may be better qualified to resolve. By separating the Due Process clause determination (where Congress has no power to act) from the Commerce clause standard, the Court effectively cleared the way for Congress to decide whether, when, and to what extent the states may burden interstate mail-order concerns with a duty to collect use taxes.

In the several years following *Quill*, numerous pieces of legislation seeking to overturn the decision and compel use tax collection were introduced in Congress, with little success. A significant effort to negotiate an agreement for mail-order sellers during this time was made by representatives of several states and the Direct Marketing Association. Although a tentative voluntary compromise was reached at the negotiating table, it failed through lack of sufficient participation by remote sellers. By the mid- to late 1990s, a new variable — electronic commerce via the Internet — had entered the debate and raised the ante, particularly for the states. Although the tax issues remained the same, the growth of the Internet and its ability to facilitate remote transactions took the debate (and the amount of forgone revenue) out of the distinct and quantifiable catalog and mail-order industry and into uncharted territory, both politically and economically.

The NTA Communications and Electronic Commerce Tax Project — In late 1996, the National Tax Association (NTA), ir conjunction with the Federation of Tax Administrators, the Mul Tax Commission, and the National Conference of State Legisla convened a meeting in Boston designed to bring together represe of business, state and local governments, professional organizat and academia to discuss the impact of changes in telecommuni law and technology and the development of the Internet on fede state, and local tax systems. That meeting spawned the NTA Communications and Electronic Commerce Tax Project (the N Project), which quickly focused its debate on whether and how and local taxes, particularly sales and use taxes, should be appli electronic commerce.

The goal of the NTA Project was to develop a broadly available report that identified and explored the issues involved in applyi state and local taxes and fees to electronic commerce and that r recommendations to state and local tax officials regarding the application of such taxes. The NTA Project met nine times for t two and one-half years and ultimately produced a final report n one hundred pages long. Although the final report contained se recommendations that garnered varying degrees of consensus a participants, there were numerous issues on which participants not reach agreement, including how and whether to expand the collect use taxes to remote sellers, an adequate definition of telecommunications, and how to avoid spillover to other taxes (business activity taxes) if the *Quill* sales and use tax nexus stan was changed. At the outset of the NTA Project, participants agr a caveat underlying all work of the NTA Project: Nothing is ag until everything is agreed to. Consequently, the final report's recommendations must be viewed through the prism of this cav that is, ultimately as part of a non-agreement. Despite the lack agreement, the NTA Project served a valuable purpose. It force participants to examine opposing viewpoints and explore comp issues at a previously unexplored depth. The knowledge and te foundations gained thereby have been extremely helpful in the the Streamlined Sales Tax Project

The Internet Tax Freedom Act — As public acceptance and use of the Internet grew in the mid- to late 1990s, multiple state and local taxation of Internet access (e.g., America Online's monthly charge) was one of the early justifications given for the enactment of the Internet Tax Freedom Act (ITFA). Several groups argued that, since the underlying telephone service was already taxed via state and local telecommunications taxes, Internet access delivered via telephone should be granted an exemption from sales tax. Further, because many consumers accessed the Internet from points throughout the country using a single Internet access account, it was difficult to determine which state or local government was entitled to tax the monthly access charge. Finally, state and local taxing authorities had strained the application of preexisting sales tax statutes to apply them to Internet access. Beginning October 1, 1998, and expiring October 31, 2001, the ITFA placed a three-year moratorium on multiple taxes, discriminatory taxes, and taxes on Internet access. Existing access taxes were grandfathered. In November 2001, President George W. Bush signed a two-year extension of the ITFA moratorium, through November 1, 2003.

Passage of the moratorium had little effect on existing state revenues. Under the legislation, a multiple tax is a tax imposed on electronic commerce that is also subject to tax in another jurisdiction without a credit mechanism. (Nearly all states grant such a credit, however, if the question of liability is resolved.) In addition, a discriminatory tax under the ITFA is a tax imposed on electronic commerce that is not imposed on other forms of commerce — a scheme that was present in very few state statutes at the time, if any. The ITFA's definition of discriminatory tax also includes a limitation on the ability of state and local taxing authorities to consider the maintenance of a Web site as the sole factor in determining a remote seller's tax collection obligation — also a rarity among state nexus statutes.

Although the ITFA preempted mainly the states that sought to impose new taxes on Internet access, many in the media and the general public misconstrued the legislation as a blanket prohibition on all taxes imposed on sales over the Internet. Use taxes, imposed on a purchaser

sale, are still due from customers on most retail transactions ove Internet, even if states are not in a position to enforce such taxes Thus, the ITFA was more about limiting new taxes on Internet a than it was about keeping the Internet tax free.

The Advisory Commission on Electronic Commerce — The I added a significant factor to the sales tax collection debate — th creation of the Advisory Commission on Electronic Commerce (ACEC). To garner the support of state and local government le the ITFA called for a commission to conduct an eighteen-month of the impact of electronic commerce on all forms of taxation ar called specifically for an examination of the issues surrounding state and local taxation of transactions over the Internet. The AC was composed of nineteen members, eight representing state an governments, eight representing business and consumer groups, the remaining three representing the offices of the U.S. Trade R sentative, the U.S. Secretary of Commerce, and the U.S. Secreta the Treasury. To ensure a balanced inquiry, a two-thirds superma was required to reach agreement on any finding or recommenda

On April 3, 2000, eighteen days before its expiration, the ACEC delivered its final report to Congress. After numerous conferenc and four in-person meetings held in Williamsburg, New York Ci Francisco, and Dallas, the ACEC was able to gain sufficient con to offer recommendations in only three areas: the digital divide, implications of the Internet, and international trade and tariffs. T remainder of the majority report failed to achieve the two-thirds necessary for findings and recommendations contemplated by the

Nevertheless, the report included a list of majority policy propo including the following: 1) Extend the ITFA moratorium on mu and discriminatory taxes for five years, coupled with a five-year bition on sales taxation of digital goods and their tangible counte 2) enact a permanent moratorium on Internet access taxes; 3) re mend the states simplify their sales and use and telecommunica tax systems; 4) create bright-line nexus standards for sales and collection and business activity taxes; and 5) eliminate the three

Because the suggestions included in the report did not receive the two-thirds majority called for in the statute, the report's release was not without controversy. The ACEC's majority, instead of allowing a single minority report, limited each individual commissioner (including those in the majority) to a separate personal statement of one thousand words. The three federal representatives filed a consolidated personal statement that was scornful of the ACEC process. The federal representatives noted that the ACEC did not represent the full range of stakeholders, since no Main Street retailers had a seat on the ACEC and charged the chairman and other commissioners with changing the rules to allow submission of the majority report in contravention of the clear language of the statute. In sum, the three federal commissioners found the process fundamentally flawed.

On the Road to the Agreement — The origins of the Streamlined Sales Tax Project can be traced to September 1999, during proceedings of the ACEC, when Utah Governor Michael Leavitt (R), an appointed commissioner and then-Chair of the National Governors Association, noted that, "The existing system is a mess… [and] it needs to be radically simplified." He suggested putting the states' tax experts across the country to work towards the development of a radically simplified system. In response, state governments organized the Streamlined Sales Tax project, staffed primarily by sales tax experts at state departments of revenue. The project was also endorsed and adopted by the National Conference of State Legislatures' Executive Committee Task Force on State and Local Taxation of Telecommunications and Electronic Commerce. The NCSL Task Force, co-chaired by State Representative Matthew H. Kisber from Tennessee and State Senator Steven J. Rauschenberger from Illinois, initially developed model state legislation that authorized state revenue departments to work together on the Project. It has since maintained an oversight role to the Project.

All states that had adopted authorizing legislation became the Streamlined Sales Tax Implementing States (SSTIS). The purpose of the SSTIS was to vote on the many difficult issues left unresolved by the consensus-gathering process of the Project, and to adopt a final version of the Agreement for adoption by state legislatures. Under

procedural rules set up by the SSTIS, votes to modify or amend Streamlined Sales Tax Project Agreement required a simple maj for approval, but final adoption of the Agreement would require affirmative vote of three-fifths of the implementing states, with state entitled to one vote.

WHAT'S NEXT

On November 12, 2002 in Chicago, the SSTIS adopted a final "Agreement" by a vote of 31 'yea', three states absent, and one abstention. The Agreement must now be turned into legislation l participating states for adoption during 2003 state legislative ses Although an Agreement has been adopted, several outstanding i: remain. The Streamlined Sales Tax Project will continue to meet periodically to work on unresolved issues, which will be present the SSTIS for a vote as modifications to the Agreement. States t enact the provisions of the Agreement in 2003 will be the gover states of the Streamlined Sales Tax System.

Appendix

Implementing States (enacted legislation to develop interstate agreement):

Alabama	New Jersey
Arizona	North Carolina
Arkansas	North Dakota
District of Columbia	Ohio
Florida	Oklahoma
Illinois	Rhode Island
Indiana	South Carolina
Iowa	South Dakota
Kansas	Tennessee
Kentucky	Texas
Louisiana	Utah
Maine	Vermont
Maryland	Virginia
Michigan	Washington
Minnesota	West Virginia
Missouri	Wisconsin
Nebraska	Wyoming
Nevada	

xhibit 1

treamlined Sales Tax Project Definitions for Food

Food and Food Ingredients:
Substances whether in liquid, concentrated, solid, frozen, dried or dehydrated form, that are sold for ingestion or chewing by humans and are consumed for their taste or nutritional value. This definition excludes alcoholic beverages and tobacco.

Options:

[1] Soft Drinks

[2] Dietary Supplements

[3] Candy

'Soft drinks" means non-alcoholic beverages that contain natural or artificial sweeteners. Soft drinks do not include beverages that contain:

- milk or milk products;
- soy, rice or similar milk substitutes; or
- greater than fifty percent of vegetable or fruit juice by volume.

'Dietary supplement" means any product, other than tobacco, intended to supplement the diet that:

A. Contains one or more of the following dietary ingredients:
   - a vitamin;
   - a mineral
   - an herb or other botanical;
   - an amino acid;
   - a dietary substance for use by humans to supplement the diet by increasing the total dietary intake; or
   - a concentrate, metabolite, constituent, extract, or combination of any ingredient described in above; and
B. Is intended for ingestion in tablet, capsule, powder, softgel, gelcap, or liquid form, or if not intended for ingestion in such a form, is not represented as conventional food and is not represented for use as a sole item of a meal or of the diet; and
C. Is required to be labeled as a dietary supplement, identifiable by the "Supplemental Facts" box found on the label and as required pursuant to 21 C.F.R § 101.36.

'Candy" means a preparation of sugar, honey, or other natural or artificial sweeteners in combination with chocolate, fruits, nuts or other ingredients or flavorings in the form of bars, drops, or pieces. Candy shall not include any preparation containing flour and shall require no refrigeration.

'Prepared food" means:

1. Food sold in a heated state or heated by the seller;
2. Two or more food ingredients mixed or combined by the seller for sale as a single item; or
3. Food sold with eating utensils provided by the seller, including plates, knives, forks, spoons, glasses, cups, napkins, or straws. A plate does not include a container or packaging used to transport the food.

States may exclude any of the following from items 1 and 2 above:

a. Food sold by a seller whose proper primary NAICS classification is manufacturing in sector 31, except subsector 3118 [bakeries].
b. Food sold in an unheated state by weight or volume as a single item.
c. Bakery items, including bread, rolls, buns, biscuits, bagels, croissants, pastries, donuts, danish, cakes, tortes, pies, tarts, muffins, bars, cookies, tortillas.

'repared food" in 2 above does not include food that is only cut, repackaged, or pasteurized by the seller and eggs, fish, meat, poultry, and foods ntaining these raw animal foods requiring cooking by the consumer as recommended by the Food and Drug Administration in chapter 3, part 401.11 'its Food Code so as to prevent food borne illnesses.

xhibit 2

Streamlined Sales Tax Project Definitions for Clothing

Clothing:
All human wearing apparel suitable for general use.

Sport or Recreational Equipment:
worn in conjunction with an athletic or recreational activity and not suitable for general use (e.g., life preservers, ski boots, baseball gloves, etc.)

Clothing Accessories or Equipment:
incidental items worn on the person or in conjunction with clothing (e.g., watches, handbags, etc.)

Protective Equipment:
Protection of the wearer against injury or disease but not suitable for general use (e.g., protective gloves, hard hats etc.)

The Project anticipates that Legislatures could create an exemption for a particular definition above, a set of definitions, or all.

Streamlined Sales Tax Project 2003