

Sales and Use Tax: To Collect or Not to Collect Streamlined Sales Tax Project

by Gerard F. Wehle, Jr. and James H. Sutton, Jr., Arthur Andersen LLP, Tampa, Florida

Generally, a company that sells tangible personal property to a Florida customer must collect Florida sales tax from the customer and remit the tax to the State. If the vendor does not collect the sales tax at the time of the sale, it may be liable for the tax. Alternatively, Florida may pursue the purchaser to collect the tax in the form of a use tax. However, since the United States Supreme Court's holding in *Quill Corp. v. North Dakota*,¹ it has been very clear that even though an out-of-state vendor may purposefully avail itself of Florida's economic market through the sale of goods to Florida customers, Florida may not require the seller to collect sales tax on sales to Florida customers unless the retailer has a "physical presence" in the State. Now that many companies are making sales of tangible personal property through the Internet, a.k.a. "e-tailers," many out-of-state vendors have been able to claim "no physical presence" in the State, thereby avoiding any sales tax collection responsibilities.

This leaves states with the option of collecting the complementary use tax from the in-state purchasers of tangible personal property. While states can easily monitor and collect use tax from businesses, the states have generally determined that the cost of enforcing and collecting use tax on all individual consumer transactions would be more expensive than the potential revenue. In other words, if you buy one of those new \$2,000.00 digital cameras over the Internet for only \$900.00 and the company does not require you to pay Florida sales tax, then you may feel fairly confident and secure that you not only will get one of the best priced deals in the country, but also that the Florida Department of Revenue is not going to come banging on your door to collect the use tax that you are legally obligated to pay.

Lower prices, lower taxes, and less sales tax compliance burdens – this is a good thing, right? Not necessarily. The "brick and mortar" companies

with some type of physical presence in many states are screaming foul because they have not only been left with the competitive disadvantage of having to charge their customers a sales tax (thereby increasing the economic cost to the purchaser), but these companies also have the added cost of complying with the various states' sales tax collection responsibilities. The compliance burdens can be more costly to a company than the direct competitive effect of the tax itself. With 45 states and the District of Columbia charging sales tax on the sale of tangible personal property, the cost of compliance can be enormous for companies with a significant multistate presence. Add this to the cost of complying with the approximate 4,700 cities, 1,600 counties, and 1,000 other taxing jurisdictions that impose a sales tax, and it's easy to understand why the states force companies to collect and remit the tax on behalf of the states.

It is also easy to see that this is a bad situation from the states' perspective, especially states like Florida that depend on sales and use taxes as its primary source of revenue. Since the Supreme Court's holding in *Quill*, states may not impose sales tax collection responsibilities on out-of-state companies unless the company has a "physical presence" in the state. Therefore, the states have been basically powerless to impose collection responsibilities on these "e-tailers" and other out-of-state companies without any physical presence in the state. Furthermore, Congress has stepped in with the Internet Tax Freedom Act ("ITFA") to ban states from imposing any new taxes on Internet access or any discriminatory taxes on Internet services until at least November 1, 2003. Between *Quill* and the ITFA, states and the "brick and mortar" companies have little means to change their situation.

It is possible that Congress could let the ITFA expire in 2003 and Congress could overturn *Quill* via its Commerce Clause powers, thereby allowing states to force out-of-state

companies with no physical presence in the state to collect sales tax on sales to customers in the state. However, given Congress's determination to let the realm of e-commerce grow freely and the enormous sales tax compliance burdens that small e-tailers may face if *Quill* is overturned, it is not likely that Congress will statutorily overturn *Quill* – at least not the way the web of complexities lay throughout the over 7,000 sales tax jurisdictions in this country.

Sensing a stalemate, the states have reacted by trying to simplify the overall sales tax arena in an effort to convince Congress to statutorily overturn *Quill*. With *Quill* out of the way, states would likely be able to assert economic nexus jurisdiction over out-of-state retailers and e-tailers without a physical presence in the state for sales tax.

In March 2000, the effort by state governments with input from local governments and the private sector focused into one group called the Streamlined Sales Tax Project ("SSTP"). The SSTP's stated goals are to simplify and modernize sales and use tax collection and administration through:

- * a system of uniform definitions,
- * simplified exemption administration,
- * rate simplification,
- * uniform sourcing rules,
- * uniform audit procedures, and
- * utilizing emerging technologies to substantially reduce the burdens of tax collection.

While the concept of the SSTP seems simple, bringing to fruition the goals of the SSTP is proving to be very challenging. Sales and use taxes are creations of state law and local ordinances. Therefore, a simplification of the whole country's sales tax system (without help from the U.S. Congress) must be effectuated through the legislatures of the 47 states with sales and use taxes and, potentially, the local governments of the 7,000-plus other jurisdictions that

continued...

impose a sales and use tax. If this does not make the challenge seem overwhelming enough, then also consider the political pressures imposed on state and local governments by the lobbying efforts of companies that could be negatively affected by the overturn of *Quill* – namely the e-tailers and mail order sales companies.

Other nationwide efforts at simplifying certain taxing systems have had mixed results. The Multistate Tax Commission has been instrumental in several successful simplification efforts, such as the uniform resale certificate. Other efforts, such as the National Tax Association's Telecommunication and Electronic Commerce Project, have been dramatically less successful.

To make matters even more challenging, there are currently two versions of the enacting legislation subject to consideration. First, the SSTP's version ("SSTP Act") and second, the more watered down, yet more politically palatable version produced by the National Conference of State Legislatures ("NCSL Act"). Additionally, it is also possible for a state to pick and choose which parts of the new legislation it wants to enact, thereby creating a variety of versions.

The SSTP is attempting this overwhelming task via three steps:

1. A state must enact model legislation allowing the state to participate in multistate discussions and enter into a multistate compact;
2. A state must amend its statutes to conform to any agreed upon compacts; and
3. The state is granted a position on the SSTP governing body.

As of February 26, 2002, the legislation required for Step 1 above has been introduced in at least 37 states, and has been enacted in 22 states, including Florida (which enacted the NCSL Act on June 13, 2001). While some states have refused to participate in the SSTP, most notably California and New York, other states, such as Minnesota, North Carolina, and Wyoming have not only passed the SSTP Act, but have also completed Step 2 above by amending their sales and use tax statutes to conform to the SSTP agreement. A regularly updated list of the progress of legislation in the various states can be found at www.geocities.com/streamlined2000/.

To accomplish its goals, the SSTP anticipates awarding contracts to companies to develop national sales and use tax compliance software. The software would incorporate all the sales and use tax rules and rates for the various taxing jurisdictions (presumably only for states that have completed at least Step 2 above). The software could be used either by vendors to complete their own sales and use tax returns or by third party

companies that would provide compliance services to the vendors.

The prospect of efficient and economically feasible sales and use tax software appears to be very beneficial to companies that make sales of tangible personal property around the country. In fact, the simplification of any taxing system has obvious benefits for commerce and free trade in this or any other country. However, there are also potential detriments to vendors as well as to the localities.

Local Jurisdiction Concern: From the local taxing jurisdiction's perspective, the SSTP means that the localities may no longer have autonomous control over their taxing system because the locality's tax base may have to conform to the state tax base.

Vendor Concerns: It is possible that the "uniform definitions" of the SSTP could actually increase the tax base by increasing the goods that are subject to sales tax. Increasing the tax base would mean that companies would be required to collect taxes on more types of goods. Another concern faced by all vendors is the added cost of implementing and learning to use the new software. Furthermore, in a period when states are facing revenue shortfalls, legislatures may see an opportunity to raise additional revenue via either higher tax rates or the removal of certain exemptions. Most importantly, as previously mentioned, certain types of companies are very concerned that states may use the SSTP to springboard the political process of overturning *Quill* at the federal level. This could dramatically increase the number of companies that are required to collect and remit sales and use taxes in more than one state.

In fact, one could speculate that the Internet Tax Freedom Act's moratorium on new taxes is merely a Congressional holding pattern waiting for the SSTP to successfully simplify the process. Until then, it looks like e-tailers and mail order companies are free to ride the competitive advantage wave of *Quill*. Thereafter, it is anyone's guess as to whether Congress or the Supreme Court will step in and change everything.

Endnotes:

¹ *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

www.FLABAR.org

Instant access to...

Links to a wide range of useful information, including:

- Florida statutes
- State and Federal court opinions
- Legal Research Links

..... and much, much more!