COMMONWEALTH OF PENNSYLVANIA
OFFICE OF THE GOVERNOR
HARRISBURG

THE GOVERNOR

April 12, 2000

The Honorable Trent Lott
Majority Leader
United States Senate
The Capitol, S-230
Washington, DC 20510

The Honorable J. Dennis Hastert
Speaker of the House
U.S. House of Representatives
The Capitol, H-232
Washington, DC 20515

Dear Senator Lott and Speaker Hastert:

I understand that Congress may soon consider proposals addressing the Internet Tax Moratorium set to expire next year. Technology has been a central focus of my administration since I took office 5 years ago. From education to public safety, our commitment to information technology is helping Pennsylvania to remain competitive in the global economy and preserve the high quality of life in the Commonwealth. Internet based commerce is changing the face of how we do business in Pennsylvania and providing rapid access to a whole new world of information.

To foster the electronic boom I support an extension of the current Moratorium on access, multiple, or discriminatory taxes. The Internet has been growing at a record pace and I believe the moratorium has facilitated that process by assuring that commerce over the Internet is not singled out and taxed in new and creative ways. That is why I proposed and the Legislature approved a repeal of Pennsylvania sales taxes on computer services as well as a tax prohibition on Internet access charges. More recently, in my 2001 budget, I have proposed a Sales Tax Holiday for Commonwealth residents who buy personal computers.

Pennsylvania is rather unique because we continue to manufacture goods. Thus, technological advances are often applied to many of those goods produced in Pennsylvania. Decisions on the taxation on Internet commerce therefore, are very complex and must balance the needs of both Internet and Main Street based businesses.

The report submitted by the ACEC Business Caucus to the Advisory Commission on Electronic Commerce acknowledged that "In addressing whether and how the Internet should be subject to taxation, a major priority should be reducing or removing access barriers to perhaps the most advanced and useful medium of communication and commerce yet devised". I concur.

I also agree with the Caucus position that the system taxation of remote sales should be simplicity, efficiency and fairness---and that "(o)ur system of federalism mandates that the burden to produce such a system falls on the states".

My concerns with the report include their preemption of the state role, albeit for allegedly a period of five years, during which time the Caucus recommends that Congress pass laws preempting state sovereignty. We, state and local elected officials, are best suited to reach a consensus on what changes need to be made to our sales and property taxes without creating a competitive disadvantage for any of our businesses. The magnitude of the undertaking is only equaled by its importance. States must work with local governments and its stakeholders---consumers, telecommunication and other remote businesses as well as our Main Street business to address these challenges.

As Congress considers legislation on Internet taxation, I hope that a guiding principle will be fair competition between Main Street businesses and Internet businesses. An extension of the Moratorium will provide us more time to asses the situation and ensure that we do no harm to either side. I strongly urge that when considering the impact of electronic commerce on our economy, any changes to the state tax structure should be done gradually and with consultation of all stakeholders.

Sincerely,

Tom Ridge

Tom Ridge

EDWARD T. SCHAFER
GOVERNOR

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April 7, 2000

The Honorable J. Dennis Hastert
Speaker of the House
2263 Rayburn House Office Building
Washington, DC 20515-1314

Dear Speaker Hastert:

I am concerned about the current dialogue on taxation of e-commerce and the recent report of the Advisory Commission on Electronic Commerce.

I do not know of a single Republican governor who wants to raise taxes. At the same time, I agree with Governor Leavitt and others who oppose any of the commission's findings that would allow Congress to infringe on a state's sovereignty or mandate tax exemptions for certain goods.

Yet, I am equally concerned about the need for a simplified and equitable tax structure. It is complex, I know: We should avoid doing anything to stifle the growth of the Internet and the new economy, and yet I refuse to put my Main Street businesses at a competitive disadvantage.

States and Congress will doubtlessly need to work together to address these issues, which is why the Commission was established. It is clear to me that these issues have not been resolved, and Congress should not consider a piecemeal approach at the expense of states' autonomy.

I look forward to working with you as we make our way through this complicated and important issue.

Sincerely,

Edward T. Schafer

Edward T. Schafer
Governor

13:27:07

cc: Senate Majority Leader Trent Lott

OFFICE OF THE GOVERNOR
STATE CAPITOL
SANTA FE, NEW MEXICO 87503

GARY E. JOHNSON
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April 12, 2000

The Honorable Trent Lott
Majority Leader
United States Senate
The Capitol, Room S-230
Washington, D.C. 20510

The Honorable Thomas A. Daschle
Minority Leader
United States Senate
The Capitol, Room S-221
Washington, D.C. 20510

The Honorable J. Dennis Hastert
Speaker
U.S. House of Representatives
The Capitol, Room H-232
Washington, D.C. 20515

The Honorable Richard A. Gephardt
Minority Leader
U.S. House of Representatives
The Capitol, Room H-204
Washington, D.C. 20515

Dear Senator Lott, Senator Daschle, Speaker Hastert and Representative Gephardt:

I are writing to urge support for a fair and equitable system to ensure that all Main Street retail stores and Internet commerce can compete on a level playing field and to ensure that all Americans can join us in supporting the Internet as part of our new economy, and to urge you to reject the Advisory Commission on Electronic Commerce (ACEC) report. Instead of proposing a means addressing the requirements laid out in the law to recommend a new state and local sales tax system to ensure a level playing field and to protect the sovereignty of states, the report proposes unprecedented interference into the rights and responsibilities of the citizens of New Mexico and their ability to determine how they want to finance vital public services and infrastructure.

The new economy offers incredible opportunities. It imposes a great responsibility on all of us to enhance electronic commerce, but not at the expense of our small, Main Street businesses. In a world like this, if remote sales over the Internet are taxed differently than intra state sales, we will have a system based upon a tangle of legal maneuvering that will create separations between local merchant and their Internet counterparts, and a playing field that will be viewed as inherently unfair. Such unfairness, if left to fester, will bring contempt and non-compliance. It is hard to argue with the need for an enormous simplification of state and local sales taxes that can pave the way toward a level playing field that does not discriminate between methods of access. Congress needs to ensure we in New Mexico can move toward a level playing field. It needs to make sure the federal government does not act in a way that permanently discriminates against our small businesses and retailers.

The most important reason I oppose this proposal is that it would substantially interfere with state sovereignty. The U.S. Constitution was very clear in both ensuring state sovereignty and creating a critical balance between federal and state authority. For well over 200 years the federal government has respected state sovereignty and has been extremely careful not to interfere with the states' ability to independently raise revenues. This proposal would dramatically undercut this precedent.

It is hard to think of any more fundamental responsibility of governments and elected officials in our nation than that of determining which taxes and fees are utilized to pay for the services that our citizens want and need. It is my responsibility, working with our state legislature, to determine what taxes to cut in New Mexico—not anyone else's. Our state relies primarily on sales, property, and income taxes—all areas proposed for mandated federal cuts by the report. Such a proposal would intrude very deeply into the rights and responsibilities of our state and local governments.

Sincerely,

Gary E Johnson

Gary E. Johnson
Governor

Cc: The Honorable Pete Domenici
U.S. Senator

The Honorable Jeff Bingaman
U.S. Senator

OFFICE OF THE GOVERNOR

DON SIEGELMAN
GOVERNOR

STATE OF ALABAMA

STATE CAPITOL
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April 11, 2000

The Honorable Trent Lott
Majority Leader
United States Senate
The Capitol, S-230
Washington, D.C. 20510

The Honorable J. Denis Hastert
Speaker of the House
U.S. House of Representatives
The Capitol, H-232
Washington, D.C. 20515,

Dear Senator Lott and Speaker Hastert,

I am writing to express my grave concerns regarding the Advisory Commission on Electronic Commerce (ACEC) proposal that was included in the Internet Tax Freedom Act (ITFA). I believe the proposal represents an attempt by the federal government to take control of fiscal policy away from the states, and I strongly urge you to reject the report.

As Governor, I have pursued responsible, conservative fiscal policies. In some instances, targeted tax cuts are an important part of this State's overall financial plan. However, these are decisions that must rest with the State, and not with Congress. As you may know, any such measure would potentially infringe on this State's ability to support public schools. Therefore, I am unequivocally opposed to any attempt by the Federal government to interfere with the states' rights to collect sales taxes.

In addition, while I appreciate the policy challenges posed by the new global economy, I have concerns with Congress establishing a series of tax breaks for a few special interests. This is particularly true when doing so would undermine a more-than 200-year tradition old of respecting states' sovereignty. Again, I ask you not to advance any effort to take control from the states and send it to Washington.

Sincerely,

Don Siegelman
Governor

Frank Keating
Governor

April 10, 2000

The Honorable Dennis Hastert
Speaker of the House
U. S. House of Representatives
Washington, DC 20515

Dear Speaker Hastert,

As you prepare to consider legislation concerning taxation of sales made on the Internet, I ask that you consider these important factors:

First, I believe it is important to extend the existing moratorium on taxation of Internet transactions to allow more debate and discussion of this vital issue. We are dealing with new technologies and new forms of commerce which are still being developed and refined. The taxation moratorium has helped stimulate that early growth, and premature action by the federal government could represent a stifling influence.

Second, Congress should not pre-empt the states on this issue. Each state has its own unique tax structure. It would be a mistake to impose a "one size fits all" standard on 50 separate states and the District of Columbia. We currently do not have a national sales tax; sales taxes have traditionally been the province of state and local governments, and each has chosen its own path in this regard. To suddenly impose a new national standard would contradict our party's traditional adherence to the principle of federalism.

Third, no matter what form legislation ultimately takes, it must have as a central goal the creation and preservation of a level playing field. It would simply be unfair to establish a system where one state or one region or one industry has a special advantage.

Fourth, as you will recall from our visits during my chairmanship of the Republican Governors' Association last year, GOP governors (and some Democrats) have been most active in reducing state tax burdens and in reforming and restructuring state tax systems. In Oklahoma, for example, we have won the first reduction in personal income tax rates in 50 years and capped property taxes. State-level tax reform is a work in progress; we are planning further income tax reductions and cuts in the cost of vehicle license tags, and I know other governors are doing the same. In many cases, state and local sales taxes remain a central component of the respective budgets of those jurisdictions. It is essential that the states retain the freedom to set tax rates and policies concerning those revenue sources that fund state and local government.

STATE CAPITOL BUILDING • OKLAHOMA CITY, OKLAHOMA 73105 • (405) 521-2342 • FAX (405) 521-3353

I appreciate the leadership you have shown on this issue and ask that your future actions and deliberations be fully informed by the needs of the states and the requirement of fairness to all.

Sincerely,

Frank Keating

fak/mb

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.
- The Project anticipates each participating state with a clothing exemption will adopt a uniform regulation to accompany the definitions. The regulation will provide lists under each definition above.
- The Project anticipates that a Legislature will not exempt an item of clothing within one of these definitions and tax the others.

PARTICIPATING/OBSERVER STATES

At its March 2000 meeting, the rules adopted by the Streamlined Sales Tax Project anticipated two levels of activity in the Project as dictated by the executive and legislative branches in each interested state. "Participating" states represent those states in which the Governor has signed an Executive Order or the legislature has passed legislation authorizing state personnel to participate in the discussions of the Project. Participating states are also voting representatives in the Project. "Observer" states represent those states that have expressed an interest in the Project's mission but have not received the executive or legislative authorization to become a Participating state. Observer states participate in all Project meetings but do not have voting status within the Project.

As of February 26, 2001, the following list represents Participating and Observer states in the Project.

Participating States (32)

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

Observer States (7)

California
Colorado
Connecticut
Georgia
Idaho
New York
Pennsylvania

ORGANIZATIONS AND COMPANIES THAT HAVE TESTIFIED BEFORE THE PROJECT, ATTENDED PROJECT MEETINGS OR VOLUNTEERED THEIR EXPERTISE TO THE PROJECT'S WORK GROUPS

Azko Nobel, Inc.
Albertsons
Alcoa
American Automobile Leasing Assn.
American Bar Association
American Electronics Association
American Express Company
American Management Systems
Apria Healthcare, Inc.
Arthur Andersen LLP
AT&T
ATRACS Corporation
Bureau of National Affairs
Boerio and Company, CPAs
Burr Wolff
Carnegie Mellon University
CCH Incorporated
Chevron U.S.A., Inc.
Citigroup
Clifton Gunderson LLC
Committee on State Taxation
Consumer Healthcare Products Association (CHPA)
Dean Foods
Dollar General Stores
Dryden Matrix Technologies
DuCharme, McMillen & Associates
EDS Corporation
Electronic Commerce Association
Equipment Leasing Association
Ernst & Young
Esalestax.com
Federated Department Stores, Inc.
First Data Corporation
Food Marketing Institute
General Electric Company
Grocery Manufacturers of America
Group 1 Software
Halliburton Company
Hewlett-Packard Company
Illinois Tool Works, Inc.
Independent Systems & Programming
Internet Tax Fairness Coalition
Internet Tax Group
Interstate Solutions, LLC
J.C. Penney Company, Inc.
Jones Day Reavis & Pogue
KPMG LLP
Kraft Foods
Lowe's
Mastercard International, Inc.
McDonald's
Michael, Best & Friedrich, LLP
Micro General/Fidelity Natl. Financial
Microsoft
Midwest Hardware Association
National Association of Realtors
National Confectioners Association
National Retail Federation
National Soft Drink Association
Nationtax Online, Inc.
Natl. Automatic Merchandising Assn.
NPRC, Inc.
Pitney Bowes
Qwest
Sara Lee Corporation
Sears Roebuck & Company
Sherwin-Williams
Sprint
State Tax Notes
Stephens Law Firm
TaxNet Systems, Inc.
Taxware International
Texas Taxpayers & Research Assn.
The Chocolate Manufacturers Association
Toys "R" Us, Inc.
Tribune Company
University of Georgia Law School
USAA
Verizon Services Group
Vertex, Inc.
Wal-Mart Stores, Inc.
Wheels, Inc.
Williams Communications
Williams Companies
Zucker, Scoutt & Rasenberger, LLP

Selected Quotes
Streamlined Sales Tax

"Forrester believes that the Streamlined Sales Tax Project is the only viable effort with the ability to preserve state sales taxes."

"The Streamlined Sales Tax Project has momentum, wide buy-in, and timing on its side."

2000 Forrester Research, Inc.
November 2000

"The National Retail Federation believes that the Streamlined Sales Tax Project draft proposal...has taken the first big step to laying the ground work for a major overhaul of the current sales and use tax system..."

Maureen Riehl, Esq.
National Retail Federation

(This is the) "last best chance for states to determine the future equity and relevance of sales and use taxes in the new economy."

Wayland Waggoner
Albertson's, Inc.

"You have demonstrated to the nay sayers that more than half the states can work together to accomplish simplification of their tax system..."
Joe Brooks, National League of Cities

"This project has gone further and made a more sincere effort than all previous groups that grappled with the issue."

"With regard to the exemption administration proposal, we believe that this is a shining example of the state participants' ability to question the current system and find an easier, less cumbersome, more rational solution."

"Truly innovative..."
Diann Smith, General Counsel, Committee on State Taxation (COST)

"Significant progress in many areas of this enormous undertaking..."
Robert Jenner, Toys "R" Us, Inc.

"Tremendous strides have been made toward a more workable system, even toward many of those simplification goals set forth by the Advisory Commission on Electronic Commerce."
David Bullington, Wal-Mart Stores, Inc.

By Jeremy Sharrard

With John C. McCarthy

Michael J. Tavilla

NOVEMBER 2000

Making Net Sales Tax Pay

eCommerce growth exposes deficiencies in sales tax laws. State reforms, Web-based collection technologies, and the changing complexion of online retail will ultimately force retailers to collect taxes on all remote sales.

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FORRESTER®

2

THE LANDSCAPE

The Net Brings Tax Debate To The Fore

State governments had given up on going after sales taxes on catalog purchases. But looming revenue losses from eCommerce combined with eroding tax bases have spurred them into action. States are now working together to simplify their sales tax systems in hopes of collecting taxes on all remote sales.

ONLINE TRADE'S GROWTH HAS CAPTURED TAX ATTENTION

Sales tax laws that date back to the 1930s are ill-equipped to preside over the borderless world of eCommerce (see Figure 1). Their shortcomings will become even more starkly apparent as online trade explodes -- with US business-to-consumer (B2C) and business-to-business (B2B) eCommerce growing to $207 billion and $2.7 trillion, respectively, by 2004 (see the September 2000 Forrester Report "Online Retail's Ripple Effect" and see the February 2000 Forrester Report "eMarketplaces Boost B2B Trade").

Net sales exacerbate two issues that have long plagued public tax administrators and tax counsels at retail companies: 1) uncertainty about how to tax commerce in which the buyer and seller are in different states, and 2) administering and complying with an increasingly complex and varied web of sales tax laws. But the debate over how to collect taxes on Web transactions has moved to center stage because:

- **Eroding tax bases bring a sense of urgency to the debate.** The economy has tilted toward services -- which are largely untaxed -- and only 40% of consumption is presently subject to sales taxes, according to one estimate. To compensate, states have steadily raised rates. When sales taxes were first introduced during the Great Depression, rates were below 1%; now they are estimated to average 6% nationally. Even in good economic times, states fear their surpluses will evaporate unless new revenue sources are found.

- **Physical-presence requirements limit tax collection.** The Supreme Court has ruled that a firm -- online or offline -- must have nexus, physical presence, within a state or it can't be required to collect sales taxes from customers in that state. Consumers are supposed to pay taxes on anything they purchase from a catalog over the Internet, but no one does. States have done little to collect these "use taxes" or educate constituents about them.

Figure 1 The Evolution Of Sales Tax

1932	**The Depression forces states to find new revenue sources** Mississippi is the first state to introduce a sales tax to help increase lagging revenues and broaden its tax base
1967	**Sales tax nexus emerges** The US Supreme Court rules that some minimum contact is needed for a state to tax an out-of-state business
1992	**Supreme Court upholds nexus requirement** Under North Dakota law, Quill Corp. was required to collect taxes from state residents, even though Quill had no physical presence there. The Court overturned the law – ruling that Quill was not obligated to remit use taxes because it lacked nexus in North Dakota. The opinion also recommended that Congress act to remedy the lack of clarity surrounding tax collection on remote sales
1998	**Internet Tax Freedom Act bars new net taxes** Congress passes the Internet Tax Freedom Act (ITFA), establishing a three-year moratorium barring states from enacting new Internet-only taxes
2000	**Use tax confusion pervades** All states that collect sales tax also collect a use tax, though few taxpayers know about it. Use tax is supposed to be paid by a purchaser when he buys from an out-of-state business, like a catalog or Dot Com retailer, but typically it is not paid. States are seeking to recoup this lost revenue

Source: Forrester Research, Inc.

- **eCommerce tax myths predominate.** Many believe -- incorrectly -- that the Internet Tax Freedom Act (ITFA) passed by Congress in 1998 made the Internet tax free. It did *not*. Consumers are charged taxes on Internet purchases from companies that have nexus in their state, and they are supposed to pay use taxes on the rest of their online purchases. ITFA legislation merely prevents states from adopting new Internet-specific taxes.

The Net Has Emerged As A Catalyst For Long-Languishing Tax Reform Efforts

The states have been confronted with a buzz about eCommerce and predictions that Net sales will soon dwarf catalog sales. In this environment, previously unpalatable proposals to reform the US sales tax system have been resuscitated:

- **The Streamlined Sales Tax Project (SSTP) owns the most mindshare.** States are working to create model legislation intended to simplify their current buffet of more than 7,500 tax codes (see Figure 2). Tax administrators from 27 participating and 12 observing states comprise the group and have high hopes for simplification efforts (see Figure 3).

4

Figure 2 The Streamlined Sales Tax Project's Agenda

Streamlined Sales Tax Project (SSTP)	Challenge	Goal
• Established in March 2000 • Comprises tax administrators from 39 states	There are more than 7,500 tax jurisdictions in the US. The Supreme Court has ruled that it is an undue burden for remote sellers to collect taxes, maintain records, and remit taxes to multiple jurisdictions	States want to gain the ability to collect use taxes from remote sellers

Critical issues to be addressed

- Audits
- Exemption administration
- Privacy policy
- Rounding rules
- Tax rates
- Technology models
- Uniform definitions
- Uniform rules for bad debts

Strategy

1) To craft model legislation to be adopted by each state that would modernize sales tax systems by simplifying state tax codes and tax administration processes uniformly across the US

2) The group hopes to reduce the collection burden placed on remote sellers enough so as to convince Congress to mandate that remote sellers collect and remit use taxes to states

Source: Forrester Research, Inc.

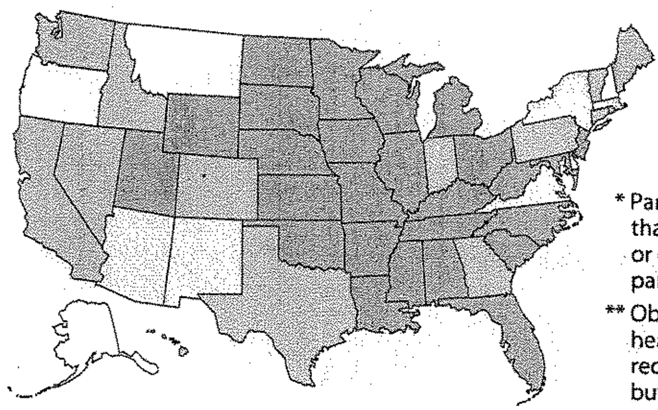
- **Renegade state initiatives dot the landscape.** Individual states have already begun working on their own to expand collection of taxes from remote sellers. Earlier this year, the California legislature proposed expanding the definition of physical presence in the state for the purpose of tax collection (though Gov. Gray Davis subsequently vetoed it).

- **Many have stepped up use tax collection efforts.** A number of states have made short-term efforts to recoup lost sales tax revenue. Some, such as Maine and North Carolina, include a line on their income tax return forms prompting taxpayers to report taxable out-of-state purchases. North Carolina and Connecticut have also entered into agreements with other states to share audit information and go after negligent purchasers.

- **The ITFA extension clouds the issue.** In 2001, Congress will consider whether to extend the current moratorium mandated by ITFA on new Internet-specific taxes. Sen. John McCain (R-AZ) has favored permanently enacting the moratorium on new Internet taxes. Meanwhile, Sen. Byron Dorgan (D-ND) has thrown his energy behind legislation that would sanction states' abilities to collect use taxes if enough of them simplify their tax codes.

Figure 3 The Streamlined Sales Tax Project's Membership

3-1 **Who supports the SSTP and who doesn't**



Participating states* (27)
Observing states** (12)
Not involved (6)
No sales/use tax (5)

* Participating states are those that have issued an executive order or enacted legislation allowing participation

** Observing states may attend hearings and have their input recorded just as participating states, but they exercise no voting power

3-2 **What states think will happen**

SSTP optimists

The time is right for reform
"There is much more cooperation in the Streamlined Sales Tax Project Project than in any prior attempt at reform. States know that this is a necessary and real opportunity for simplification and for ensuring revenues for the future."

A sensible and realistic approach
"I think ultimately it will succeed. The proposals are generally good and have realistic aims. It will result in a much simpler tax system. The commitment is to a simpler system, easier registration, easier filing and payment -- simpler rules in general."

Great concerns about revenue losses
"They'll have to be successful if the sales tax and associated revenue is to be preserved. There will be too big a loss in revenue and too much of a shift in business to the Dot Com world to ignore. We will succeed only together, cooperatively."

Everybody wins with simplification
"These simplifications are good for retailers, good for manufacturers. Narrowing down definitions may present some minor problems, but I can't see anyone as against simplification."

SSTP pessimists

Just too many taxing authorities
"We'll never get every one of those states to standardize, never mind the numerous local tax authorities. We'll never get the uniformity necessary to make it work."

Concerns over loss of state authority
"SSTP successful? No, no way. State legislators like to use their base as a 'gimme' tool. An overarching plan like the SSTP takes away legislative authority and a plum that legislators like to use to reward specific industries. As long as you have 50 legislatures, it can't go anywhere."

Common definitions are *the* major hurdle
"I think it will be very, very difficult. Common and uniform definitions will be extremely difficult to reach. How do you define what's a snack food, what's candy? Seemingly arbitrary tax laws are everywhere. It will be a very difficult process to agree on these definitions."

Political ego and inertia will thwart efforts
"The SSTP, as designed, will not be successful. There may be very small gains. No one is a proponent of the antiquated mess we are now dealing with, but there is a huge tendency to pay political lip service, doing little to affect real change."

Based on interviews with 27 state and local tax administrators

Source: Forrester Research, Inc.

ANALYSIS

Remote Sellers Will Ultimately Collect Taxes

After decades of wrangling, the one-two punch of watered-down simplification and improved tax collection technology will be enough to compel Congress to mandate that remote sellers remit use taxes -- but not before 2005.

A LACK OF VIABILITY WILL DERAIL MOST SOLUTIONS

States' sales tax laws reflect 70 years of logrolling by parochial interests. The labyrinth of issues under discussion, tangled legal precedents, and the political combustibility of any tax changes will limit the impact of most proposed reforms.

- **Federal proposals will go nowhere.** Federal legislators are loath to open the sovereignty can of worms that comes with any new law regarding sales tax collection on remote sales. They would risk angering taxpayers and the states, while receiving no federal revenue in return. For now, federal legislation will only serve as a club to spur state action.
- **Renegade states won't be able to go it alone.** Efforts by states like California to expand collection will merely scare away businesses and mire states in legal challenges from angry retailers. With more than 7,500 individual tax jurisdictions in the US, reform must combine a critical mass of them, or businesses will just relocate to jurisdictions that fit their needs. Forrester believes that any significant effort to reform sales tax must include at least 20 states.
- **Supreme Court action will be little more than a wild card.** Some believe that a state audit of an e-tailer not collecting taxes will make its way to the Supreme Court and generate a ruling on nexus and eCommerce that will resolve the debate. But judicial resolution won't come before years of appeals make their way up through the courts. Even if the Supreme Court acts, the judicial branch has shown its strong preference that Congress legislate any redefinition of nexus.

Streamlined Sales Tax Effort Controls The Debate

Despite the Streamlined Sales Tax Project's limited visibility and even more limited resources, Forrester believes that the SSTP is the only viable effort with the ability to preserve state sales taxes. The group has assumed the central place in the debate by:

- **Targeting long-problematic administration and tax code complexity.** Differences among individual states' and tax jurisdictions' product definitions have grown more complex as states have carved out exemptions to attract business. And sellers are burdened by administrative tasks like authenticating and storing tax-exemption certificates. In response, the SSTP is creating common definitions for goods and looking at automating and transferring the burden of proof for exemptions to buyers.
- **Bringing a broad coalition of players to the table.** State tax administrators lead the project, but since its beginning, the group has sought assistance from the business community (see Figure 4). The project has held public hearings to elicit comments, and it will rely on the lobbying muscle of sympathetic retail chains when it submits model legislation to state legislatures early next year.
- **Bundling policy reform with new technology solutions.** The SSTP is attacking the definitional and administrative problems that predate the Internet and fusing its proposals for resolution with recommendations for employing new Net-based tax collection software. A pilot project wherein vendors will remit use taxes to four states using new tax collection technology starts this month.

STATES WILL CLEAR HURDLES TO REACH SALES TAX RESOLUTION

The Streamlined Sales Tax Project has momentum, wide buy-in, and timing on its side. Working with states, the group will help to compel Congress to require Internet retailers to collect use taxes on purchases -- but not before 2005. Prior to gaining the ability to collect taxes, state efforts will face a series of hurdles through four phases (see Figure 5).

1) **Educating (2000-2001).** Tax reform groups will scramble to draft legislation while informing legislatures about the necessity of reform.

2) **Legislating (2002-2004).** State legislatures will pass politically palatable laws that lighten businesses' administrative responsibilities.

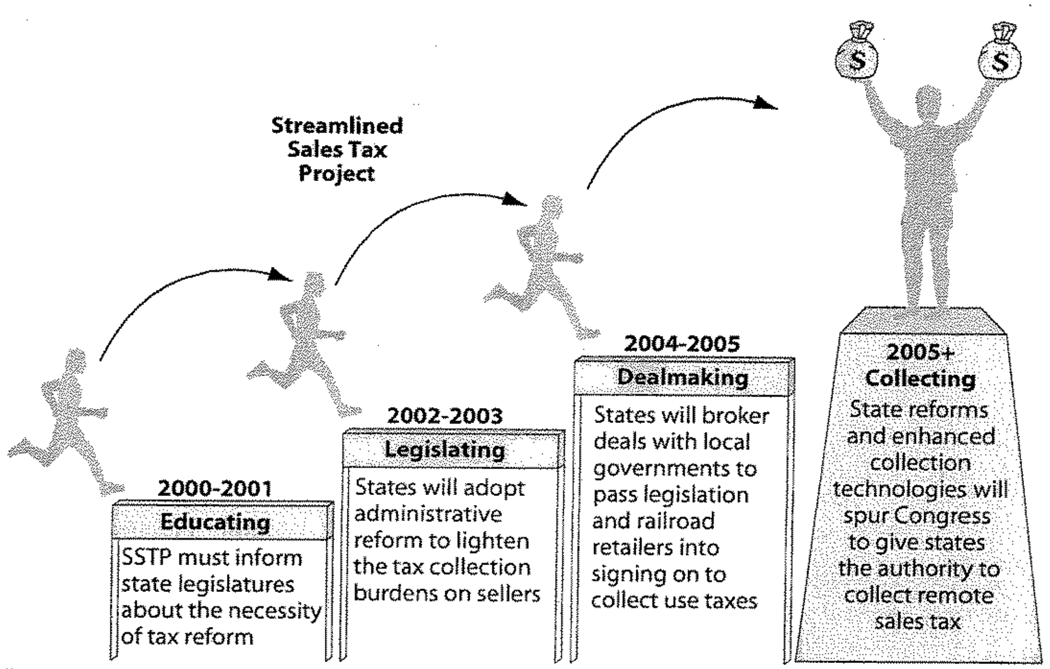
3) **Dealmaking (2003-2005).** After initially kowtowing to retailers, states will work to coerce remote sellers to voluntarily collect use taxes.

4) **Collecting (2005+).** The combination of light simplification and advanced technology will compel Congress to mandate remote sales tax collection.

Figure 4 SSTP Decision-makers Have A Range Of Motivations

Who's in	**What they say**	**What they mean**
State governments	Our burdensome and overly complex sales tax system is ripe for reform	The Net presents a great opportunity to get revenue from remote sales and usurp local taxing authority
Traditional retailers	We would like for the tax system to be streamlined to reduce the burden for everyone	We're tired of these Dot Coms getting away without paying these taxes. If we have to pay, they should, too
Technology vendors	With the cooperation of the states, the technology exists to craft a national tax system	We want to help the states simplify the tax code but not to the point where our services are not needed
Who's out	**What they say**	**What they mean**
Local governments	We are amenable to tax reform to level the playing field for our Main Street retailers	We are in a tough spot -- we rely on the revenue and know reform is needed but are reluctant to lose local authority
e-tailors	Nothing -- maybe if we're quiet this issue will just go away	We don't want to lose the competitive advantage that lax tax collection allows
B2B Sector	What SSTP?	No really, there's a project currently underway to simplify tax codes? No one told us about it

Figure 5 SSTP Will Overcome Hurdles On The Way To Reform



Source: Forrester Research, Inc.

Phase One: Educating (2000-2001)

Dissemination and education efforts will consume streamlined sales tax advocates for the immediate future. Few state legislators even know that a project is underway to allow states to begin collecting use taxes from remote sellers. Streamliners had hoped to pass legislation in at least four states next year, but Forrester believes they've underestimated the work needed to educate legislatures about the need for streamlining. For the next year, tax reformers will work to assure state and federal representatives that proposed legislation does not impose new taxes on eCommerce. At the same time, they'll closely monitor the progress of the technology pilot.

- **SSTP will pass the baton to the NCSL.** The National Conference of State Legislatures (NCSL) plans first to tweak and then to endorse the coming model legislation. When legislatures convene next year, the National Governors' Association (NGA) will join the NCSL in proselytizing sales tax simplification legislation to states as a means of reducing government bureaucracy.

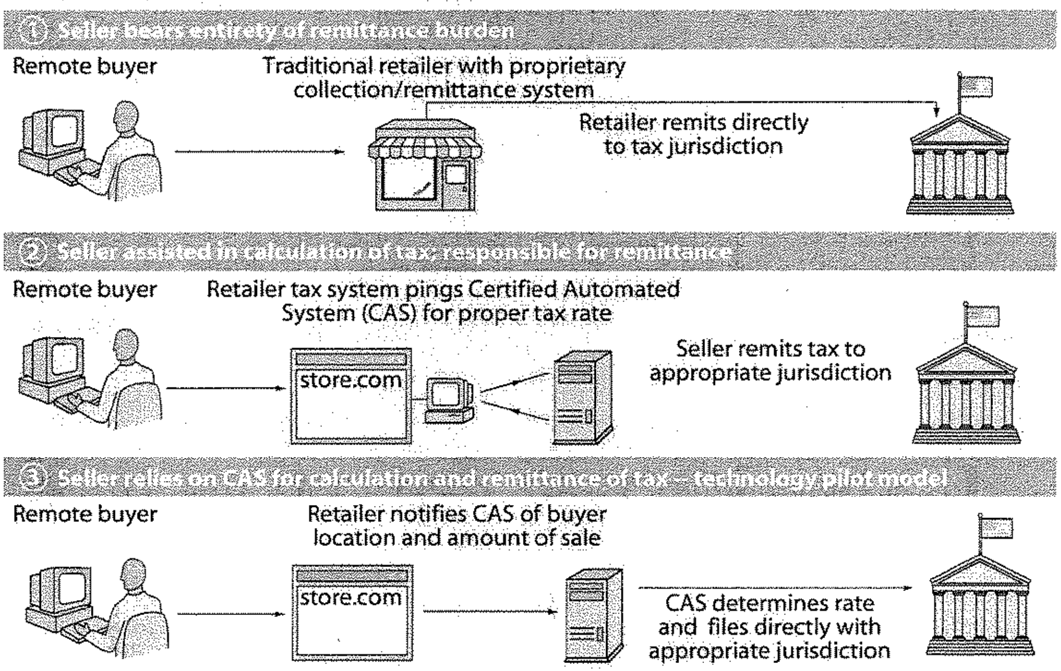
- **Tax technology will take a test-drive.** Working with Kansas, Michigan, North Carolina, and Wisconsin, volunteer retailers will test the ability of technology to make collecting taxes easier. Tax software vendors TAXWARE, Vertex Software, and esalestax.com will get their shot to prove that technology can solve much of the tax collection problem (see the February 7, 2000 Forrester Brief "Internet Sales Taxes Don't Need A Tea Party"). The pilot will test the certified automated service method of automating use tax collection and remittance (see Figure 6). States hope to announce their results in 2001.

- **Congress will extend ITFA with minimal additions.** States will closely watch the progress of a rider to the ITFA moratorium extension proposed by Sen. Dorgan that would grant states the ability to collect use taxes once 20 states simplify their systems uniformly. Though the ITFA moratorium will likely be extended, Dorgan's automatic trigger will likely be defeated -- because Congress would prefer to postpone discussions about expanding states' ability to collect taxes. But deliberations over the rider's fate will presage how Congress will respond to the expansion of states' tax collection responsibilities.

Phase Two: Legislating (2002-2004)

In the second phase of sales tax deliberations, streamliners' efforts will focus on building legislative momentum. Having educated legislatures about the issues at stake, the SSTP will focus on actually getting something passed. By the end of this phase, advocates will finally begin to convince skeptics that the debate can be resolved -- pointing to their political victories and successful returns from the technology pilots.

Figure 6 Tax Collection Technology Models



Source: Forrester Research, Inc.

- **States will trumpet pilot results to dispel collection burden concerns.** In the wake of the 2001 holiday season, states will announce favorable results from the pilot tax collection effort -- highlighting the ease of the system for retailers. Streamlining advocates will craft politically viable legislation that highlights states' ability to reduce burdens by standardizing administrative hassles like tax remittance frequency.

- **Five states will take the lead in passing new regulations.** Though advocates had hoped legislation would be passed earlier, they'll sign on their first five states in 2002. The first to approve will be North Carolina, Michigan, and Florida (see Figure 7). Legislatures will bundle reforms to Web-enable exemption processing and seller registration with popular eGovernment initiatives.

- **States will use momentum to bring locals aboard.** In return for a share of new revenues, locals in holdout states like Pennsylvania will soften their hard-line stances and allow their tax bases to match the states' -- one of the prerequisites for streamlined legislation. However, streamlining efforts in the three states that have tax home rule will stall -- Denver's already projected that it would lose 27% of its revenue if it cuts the number of items it taxes to sync with the state of Colorado.

Figure 7 States Will Adopt Tax Simplification Legislation At Different Times

Proving ground states (2001-2002)	Cautious optimists (2002-2004)	SSTP swing states (2004+)	Holdouts
States that are participating in the technology pilot project and depend heavily on sales tax revenue will be the first to adopt SSTP legislation	States with uniform bases will wait until the first wave of state adoption proves successful before passing legislation	States that rely less on sales tax revenue and have more complex tax codes will take longer to adopt streamlined legislation	States with no sales tax or great local control over tax bases and rates may never take the necessary steps to streamline their tax systems
• Florida • Kansas • Michigan • Mississippi • North Carolina • Wisconsin	• Connecticut • Kentucky • Maryland • Nevada • New Jersey • Rhode Island • South Dakota • Tennessee • Washington • West Virginia	• Alabama • Arizona • Arkansas • California • Georgia • Hawaii • Idaho • Illinois • Indiana • Iowa • Louisiana • Maine • Massachusetts • Minnesota • Missouri • Nebraska • New Mexico • North Dakota • Ohio • Oklahoma • Pennsylvania • South Carolina • Texas • Utah • Vermont • Wyoming	• Alaska • Colorado • Delaware • Montana • New Hampshire • New York • Oregon • Virginia

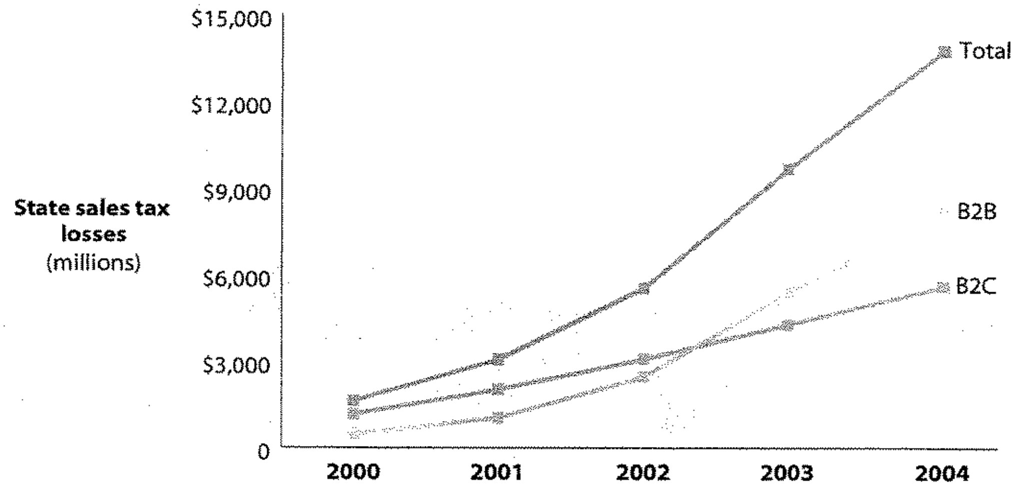
Source: Forrester Research, Inc.

- **Lessening of liability will drive voluntary retailer sign-ups.** Sellers with both online operations and a wide physical presence like JCPenney will be the first to sign on to remit taxes. They'll reduce audit liability and shift the burden of proof for tax exemption to buyers in return for collecting taxes they would have had to collect anyway. It makes sense; Forrester's research shows that consumers don't care that much about paying sales tax online anyway -- shipping charges are a far greater concern (see the February 24, 2000 Forrester Brief "States Lose Half A Billion In Taxes To Web Retail").

Phase Three: Dealmaking (2003-2005)

In this phase, streamlined system advocates will bargain in many states -- forsaking contentious definition legislation to get more acceptable administrative streamlining approved. States will also play hardball with retailers to force them to voluntarily remit sales and use taxes. By 2003, a renewed sense of urgency will pervade the Net sales tax debate. By this time, there will likely be a slowdown in the economy. Online retail will reach $155 billion -- almost four times its total in 2000. Combined with increased business utilization of eMarketplaces, states' potential revenue loss will be $14 billion if no measures are taken to expand their collection of use taxes (see Figure 8).

12 **Figure 8** eCommerce Sales Tax Loss Will Grow to $13 Billion By 2004



	2000	2001	2002	2003	2004
Business-to-consumer (B2C)	$1,169	$2,022	$3,079	$4,274	$5,580
Business-to-business (B2B)	$468	$1,042	$2,465	$5,389	$8,156
Total (millions)	**$1,637**	**$3,064**	**$5,544**	**$9,663**	**$13,736**

Source: Forrester Research, Inc.

- **A second round of proposals will allow states to opt out of definitions.** While states will pass administrative simplification legislation, many will hesitate to redefine their state's tax definitions out of fear that they'll lose the ability to attract and retain businesses in their states. Reformers will begin to give states more legislative flexibility to decide if they want to revise definitions. They'll present legislation with mandatory administrative elements and an optional, à la carte set of definitions from which states can choose in areas like food and clothing.

- **Threatened lawsuits will force participation of nexus-dodging retailers.** Early on, brick and mortars like Barnes & Noble and Wal-Mart ran an end-around against existing nexus laws by spinning off Dot Com businesses as separate entities. But now that they've realized that a brick-and-mortar presence is an asset, they're accepting in-store returns and offering cross-promotions. States that have passed streamlined legislation will use the threat of legal action to coerce retailers like Walmart.com to begin to use the SSTP system to remit taxes.

- **States will audit B2B eMarketplaces.** Though states have focused their attention on the retail sector, by 2003 they'll realize that the larger opportunity is lost revenue from businesses failing to remit use taxes. States will run use tax education campaigns aimed at businesses and audit office-supply eMarketplaces like PurchasingCenter.com to nab small and medium-sized businesses that haven't paid use taxes on nonproduction materials they've bought online.

- **Efforts to bring Dot Coms on board will sputter.** Current policies limit the credits states can offer retailers in return for collecting taxes. Because states are leery about giving special treatment to remote sellers, they won't be able to grant significant incentives to Net retailers to collect use taxes. Pure-play Dot Coms will hold out on voluntarily collecting while struggling to differentiate themselves in an environment requiring profit-oriented business models.

Phase Four: Collecting (2005+)

By 2005, the tax issue will begin to lose its political combustibility. Most surviving Dot Com retailers will necessarily expand their presence to meet customers' needs with warehouses, strategically placed stores, and local delivery partnerships (see the April 2000 Forrester Report "The Demise Of Dot Com Retailers"). As a result, Dot Coms will be collecting taxes they had previously avoided -- tax reform or not. States will use a few highly publicized audits of businesses negligent in remitting use taxes to scare the rest into complying with reporting. Legislative action, brought by the new Congress in January 2005, will be packaged as an eGovernment initiative -- rewarding with revenue those states that simplify businesses' remote sales tax burdens.

- **States will upgrade their internal systems.** As retailers retool collection systems and plug in to tax collection technology solutions, states will focus efforts on their own tax collection back ends. To reduce retailers' burdens, they'll encourage online reporting and eliminate monthly forms in favor of automated transfers. Retailers will be able to file at their convenience -- ranging from daily to annually.

- **Businesses will focus lobbying efforts on burden reduction.** Realizing that Congressional action is inevitable, businesses will lobby Congress to mandate that states must simplify to the point of one tax rate per state in order to collect remote taxes. Lobbyists will advocate the creation of a sales tax structure like that of the International Fuel Tax Association (IFTA). Within IFTA, truckers submit fuel tax returns to their home states, relying on them to remit to any other owed states.

- **Congressional action will occur as an eGovernment play.** After more than two-thirds of states have done the dirty work of streamlining their systems, the issue will have cooled off enough for Congress to step in. Congress will craft a bill as an eGovernment incentive package for states -- thus ducking anti-tax proponents. In return for upgrading their collection systems and simplifying requirements placed on vendors, states will receive taxes from remote sales.

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ACTION

Traditional retailers should change their tune.

While traditional retailers have helped to forward the efforts of the SSTP, their goal has been more to burden online retailers with onerous tax collection responsibilities than achieving simplification. By coming to the table with this narrow motivation, brick-and-mortar chains risk missing an unprecedented chance to work with governments to reduce tax collection burdens for all sellers. Retailers should invite Dot Coms to the table and both should work with states to create a truly simpler system for collecting taxes. Simpler tax structures mean increased profitability for all retailers.

Dot Coms should pull their heads out of the sand.

Online retailers have been conspicuously absent from sales tax reform deliberations. That tactic may have worked at first, but now that states are organizing to expand collection, Dot Coms should work with -- rather than ignore -- tax reformers. If they remain on the sidelines while traditional retailers help shape tax policies, Dot Coms will find themselves crippled once they are legally required to collect taxes.

Accounting firms should buy tax collecting technology vendors.

Large systems integrators and accounting firms like EDS and Ernst & Young should snap up tax collection technology vendors like esalestax.com or TAXWARE before their price tags go up. Getting involved in tax collection automation will make up for the revenues their tax practices will miss out on once states ease compliance burdens on retailers -- reducing sellers' need for accountants.

Democrats should make the tax issue their own.

Democrats have neither embraced nor distanced themselves from the Internet tax debate. Republicans are divided on the issue -- caught between states' rights and anti-tax leanings. Democrats should endorse the streamlining efforts and push Congress to pass enabling legislation. Though they'll initially face resistance from anti-tax and pro-technology critics, they'll win out if they cast their proposals as eGovernment reform. Plus, they'll garner valuable political capital from appreciative governors -- and fluster Republicans by highlighting an issue that divides them.

WHAT IT MEANS

The implications of simplified taxes and remote seller collection of use taxes are significant:

SSTP will provide a model for future state deliberations.

The ageographical nature of the Internet will spark further showdowns between fragmented state-level policies and the need for uniform standards. States will turn to the SSTP model as they scramble for control over issues like state franchise laws, insurance, and financial privacy policies. By collaborating closely in crafting new policies, states retain their sovereignty while eliminating the newly glaring inconsistencies in individual states' policies.

Streamlined project will pave the way for a VAT discussion.

Even as legislators sort out sales tax in the US, they'll be preparing to take their discussions international. Global eCommerce will continue to grow -- forcing countries to discuss how to administer taxes on eCommerce purchases that travel across borders. Most of the rest of the world uses a value-added tax (VAT), which at present would be political impossible in the US. But after legislators spend five years overhauling tax systems, the VAT might be easier to imagine as a way of easing US-international trade discrepancies.

States will use Net cash registers to ease retailers' pain.

Once states start collecting taxes from remote sellers, they'll turn their focus to small and medium-sized retailers within their borders. States will offer these sellers assistance to buy and implement Web cash registers from NCR and IBM. Offering registers that automate tax remittance will help states get their hands on taxes more quickly and easily, and it will free retailers from their current audit risks.

The tax system will create a real-time economic indicator.

When remote sellers are collecting taxes on all purchases and traditional retailers are using Net cash registers to ring up sales, the result will be a wellspring of retail data. With immediate information about buyers' spending habits, clothing makers will be able to see which styles are selling where and adjust distribution accordingly. More significant, governments will be able to release daily retail indexes charting consumer attitudes and the economy's health.

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Improved collection will force states to cut rates.

As states have historically exempted more purchases from taxes, they have responded by raising tax rates. Taxing remote sales will -- at least temporarily -- reverse this trend, allowing states to expand some of their shrinking base. It won't be long before consumers rally for their tax rates to be cut. States will respond in kind -- once they're gaining new revenue and spending less pursuing tax dodgers, they'll be able to reduce sales tax rates without having to downsize police departments.

Retailers will race to recast themselves as service providers.

Product sellers are increasingly turning toward bundled services to differentiate their offerings. Most states don't tax services. The trend toward bundled services will accelerate as sellers continue to look for loopholes to avoid charging taxes to consumers. On-demand deliverers like Peapod.com will classify their business as a grocery-replenishing service. States will have to make another effort to streamline definitions -- this time, between goods and services -- or risk missing out on a new generation of tax revenue.

eMarketplaces will plug in use tax services as a value-add.

As states expand efforts to collect use taxes from businesses, smart eMarketplaces will plug in tax collection providers like TAXWARE to offer buyers the service of automatically collecting and remitting use taxes on goods. Business buyers will welcome the service, anxious to avoid audits on their buying. Governments will sanction the process and offer incentives to eMarketplaces that take the initiative in assuming this responsibility.

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Star Wars Meets the Sales and Use Tax: An Interim Objective Review of the Streamlined Sales Tax Project

© by Susan K. Haffield, Arthur Andersen LLP, Minneapolis, Minnesota and Arthur R. Rosen, McDermott, Will & Emery, New York, New York

The Star Wars defense project was - and to some degree remains - an attempt to utilize cutting-edge technology to address issues raised by the advent of other cutting-edge technology as well as by older, traditional threats. In a similar way, the state and local tax community is looking to cutting-edge data processing/telecommunications technology to address sales and use tax issues raised by the new world of e-commerce as well as those raised by older traditional remote and over-the-counter merchants.

THE PROBLEMS

Tax practitioners are well aware of the most significant compliance-related problems, which can generally be placed into three categories: taxability, sourcing, and administration. "Taxability" refers to determining whether the sale of a specific item is subject to tax. This can be a function of the nature of the item, the identities of the seller and the buyer, and/or the manner in which the item will be used. "Sourcing" refers to determining for which jurisdiction, if any, tax is to be collected. "Administration" refers to responsibility for updating tax rates, preparing/filing returns, making tax payments, and dealing with audit responsibilities.

Taxability issues have been a major concern to remote as well as over-the-counter merchants. Arcane, complex statutes and regulations that classify taxable and exempt items and transactions require merchants to perform difficult analyses and reach debatable conclusions. The current prevalent "good faith" standard puts merchants in jeopardy when they must reach a conclusion regarding whether a specific purchase or a purchaser=s purported intent is entitled to the benefit of an exemption (or exclusion). These problems are, of course, multiplied for each jurisdiction for which a merchant is to collect tax.

Determining where a sale is to be sourced is generally not a problem for over-the-counter transactions. For remote sellers, however, identifying the correct jurisdiction and knowing and implementing its unique tax requirements is often a virtually impossible task.

Similarly, the administration problems arise most often for remote sellers. Such businesses must contend with a multitude of rate updates, distinct return forms, filing dates, payment dates, etc. Moreover, dealing with numerous separate audits causes substantial burdens on remote merchants.

HISTORY

Serious consideration of utilizing modern technology, coupled with substantial and substantive law changes, to address these issues began with the NTA Communications and Electronic Commerce Project. In that process, state and local government representatives suggested that tax compliance software, in coordination with systems maintained by financial intermediaries (e.g., credit card businesses), could solve many of these problems. The work of the Project, however, ended before this approach could be fully explored.

In connection with the deliberations of the Advisory Commission on Electronic Commerce (established by the Internet Tax Freedom Act), state and local government representatives proposed establishing a "trusted third party" arrangement that would be developed by states working with data processing firms. The arrangement would have merchants being required to input only minimal amounts of data for each transaction. Such information would be processed by a third party, pursuant to simplified and uniform sales and use tax laws. That third party would also be involved in the customer's payment transaction, so that the appropriate sales or use tax would be remitted directly to the correct jurisdiction. The merchant would be largely removed from the tax payment process and associated liabilities.

THE STREAMLINED SALES TAX PROJECT

In response to these issues, the states formed the Streamlined Sales Tax Project ("SSTP" or "Project") in March of 2000. Over 40 states are now participating as either formal members or active observers of the Project. The stated goal of the Project is to "design and implement a simplified sales tax collection system that can be used by traditional brick and mortar vendors and vendors involved in e commerce." Such design and implementation is expected to take several years and is to be accomplished through at least two phases. Phase I is nearing completion; Phase II will, presumably, commence in 2001.

Phase I commenced shortly after the Project's inception by establishing four work groups to address specific issues as follows: Tax Base, Uniformity and Exemption Administration; Tax Rates, Registration, Returns, and Remittances; Technology, Audit, Privacy and Paying for the System; and Sourcing and Other Simplifications. The work groups have made numerous recommendations for simplific tion. Model legislation incorporating these recommendations is expected to be drafted by the end of December 2000, in anticipation (or hope) that they will be considered in state legislative sessions during 2001 Phase II is expected to continue through 2001 to address additional elements of the system. This work would include additional uniform definitions and the development of a uniform return for all states.

TAX BASE, UNIFORMITY, AND EXEMPTION ADMINISTRATION

The Tax Base, Uniformity and Exemption Administration work group has primarily focused on the creation of uniform definitions of certain terms. The initial efforts have concentrated on "sale price," "tangible personal property," "retail sales," "delivery charges," "food," and "clothing". Under the simplified system, legislatures would still choose whether to tax or exempt items, but would use these common definitions. The Project acknowledges, however, that the adoption of uniform definitions will, in fact, result in the expansion of the tax base in some states and the contraction of the tax base in others. For example, delivery charges would be included in the term "sale price" in all states adopting the simplified system even though such charges are currently excludable in several states.

In addition to the uniform definitions, this work group has recommended relief of the "good faith" requirement for sellers who accept exemption certificates. Sellers would have complete immunity from any liability for uncollected tax (absent, one would assume, fraud) if they accept an exemption certificate (which might be in electronic form) from a purchaser. States would seek any tax due from the purchaser that was responsible for providing an incorrect or invalid exemption certificate.

TAX RATES, REGISTRATION, RETURNS, AND REMITTANCES

The recommendations of the work group for Tax Rates, Registration, Returns, and Remittances attempt to address some of the administrative burdens associated with compliance. The "single rate per state" concept was abandoned early in the discussions as far too difficult - from a political and governmental financing perspective - to implement. However, the recommendations would simplify rate changes and shift the burden to the states to ensure accuracy. Taxing jurisdictions would be required to provide 60 days notice prior to a rate or boundary change, and the effective date would have to fall on the first day of a calendar quarter. States would also be required to develop and provide databases for use by retailers that would identify a single tax rate for each "zip plus four" area within the state. Merchants who rely on such information would no longer be concerned about - nor fear audit assessments due to - tax jurisdictions whose boundaries are not coterminous with zip code areas.

Perhaps one of the most controversial policy recommendations thus far is to require localities to conform to the state's tax base. Representatives of local government have urged the members of the SSTP to strongly consider the use of technology to solve the complexities rather than require the cities to conform to the state.

Other recommendations of this work group include simplified procedures for registration, single returns per state, state administered distribution of local taxes, electronic payments, and due dates no earlier than the 20th of the month following the sale. States would also be prohibited from placing caps on selling prices subject to tax.

SOURCING AND OTHER SIMPLIFICATIONS

The Sourcing and Other Simplifications work group has developed recommendations for sourcing sales to taxing jurisdictions, rounding, and bad debts. In general, the proposed sourcing recommendation would require sellers to source sales on a destination basis. The recommendation contains a hierarchy of alternative sourcing rules when there is insufficient information available to source the sale purely on such a basis. In addition, for certain sales, a "Substitute Address" rule or a "Multiple Points of Use" rule may apply. Exceptions to these general rules have been recommended for advertising services and telecommunications.

Under the fundamental destination-based rule, the seller would source the sale to the seller's business location for over-the-counter sales and to the customer's "ship to" location for items delivered to the customer. If these did not apply, the next level in the hierarchy would be the purchaser's address as maintained by the seller in the ordinary course of business. If none of these applied, the seller would be directed to use the location provided by the purchaser during the consummation of the sale, which could include the address of the purchaser's payment instrument (such as a credit card).

The "Substitute Address Rule" would apply when the seller could not apply the destination-based rules noted above. This rule primarily relates to the sale of intangible items such as services and digital products. The Substitute Address Rule contains two alternative

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New Jersey One-Day Tax Seminar
Hilton Woodbridge
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Los Angeles Airport Marriott
Los Angeles, California
May 1, 2001

Pennsylvania One-Day Tax Seminar
Hilton Valley Forge
King of Prussia, Pennsylvania
May 31, 2001

Ohio One-Day Tax Seminar
Adam's Mark Hotel
Columbus, Ohio
July 11, 2001

Iowa One-Day Tax Seminar
Radisson Quad City Plaza
Davenport, Iowa
July 26, 2001

Michigan One-Day Tax Seminar
Dearborn Inn
Dearborn, Michigan
October 25, 2001

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Star Wars Meets the Sales and Use Tax: *(continued)*

approaches including the use of either: 1) an origin-based approach, which is the address from which the intangible was first shipped or the service was primarily provided (disregarding, for these purposes, a location that merely provided the digital transfer of the product sold), or 2) the commercial domicile of the seller.

The Multiple Points of Use Rule applies to transactions involving the sale of an intangible or service that will be used concurrently in more than one jurisdiction. In this case, a purchaser may provide the seller with a "Multiple Points of Use ("MPU") Exemption Form and relieve the seller from any obligation to collect the tax. The purchaser will be required/allowed to apportion the tax based on "any reasonable, but consistent and uniform" method.

Another feature is the uniform rounding proposal which would include the required use of a 5/4 rule: rounding up for anything .5 and over, and rounding down for anything .4 and lower, a three decimal places rule, allowance of rounding on returns, and rounding on either an invoice amount or an item amount.

The uniform bad debt provision would tie the allowance of the bad debt deduction to the internal revenue code provisions (i.e., when a bad debt is written off for federal tax purposes, it will be allowed for sales tax purposes). The deduction would be from the sales figures, so the tax rate in effect at the time of the deduction, rather than the time of the sale, would determine the amount of the tax benefit. Taxpayers would have one year from the month that the bad debt is recognized for federal tax purposes to take the deduction on the sales tax return. Under the recommendation, tax would be due on recovered bad debts, and no third party assignments (such as to credit card companies) would be allowed.

TECHNOLOGY, AUDIT, PRIVACY AND PAYING FOR THE SYSTEM ("TECHNOLOGY")

The Technology work group has focused on integrating technology into the sales tax collection process to make the seller's sales tax collection burden as light as possible. The group has been exploring three technology-related sales tax collection and remittance models. These include: use of a third party Certified Service Provider ("CSP"), use of a Certified Automated System ("CAS"), and certification of a retailer's Proprietary System ("CPS"). All three models require the use of software that must meet certification standards established by the states.

The CSP model could be described as a complete outsourcing of the sales tax collection function. Using this model, a retailer would select form a list of state-certified CSPs. A CSP would be responsible for determining the amount of tax due on the retailer's transactions, paying the tax to the states, and filing the tax returns using a state-certified system. The CSP would assume the liability for accurate and timely payment of the tax and submitting the returns. While determining the taxability of a retailer=s products would most likely be a joint effort between the CSP and the retailer, the states would hold the CSP responsible for inaccurate decisions. Failure by the retailer to provide accurate information to the CSP would be an issue between the CSP and the retailer. Neither the CSP nor the retailer would be liable for errors in the system that the state failed to discover in the certification process. However, upon discovery of an error, the CSP would have an agreed-upon amount of time to correct the problem. States would be responsible for compensating the CSPs. Retailers would be responsible for remitting use tax on purcha es. Under this model, a joi audit performed on behalf of states participating in t Streamlined System would performed, but the retail would be liable only for unc lected sales tax if it had engag in fraud. Retailers would rema liable for use tax on purchas for their own use.

A pilot program began October 2000 to test certain el ments of the CSP model. T SSTP has contracted with va ous software/data-processi vendors to operate as CSPs the pilot program.The four stat participating in the pilot pr gram include Kansas, Michiga North Carolina and Wisconsi CSP contracts for the pilot pr gram were awarded esalestax.com, Inc.; Pitne Bowes, Inc. (Vertex, Inc., su contractor); Taxware Inte national, Inc. (Hewlett-Packar Company, subcontractor); an Taxware International, In (Pitney Bowes, Inc., subcontra tor).

As noted above, the other tw models under consideratio though not part of the pilot pro gram, include the CAS and th CPS. The CAS model woul allow a retailer to select a soft ware system that had been certi fied by the state to perform onl the sales tax calculation func tion. States would certify partic ular systems that would be host ed on a server and available t multiple users, or would resid on the seller's system. After th amount of tax were determined this information would be pro vided to the retailer, and th retailer would be responsible fo filing the returns. The CAS would be subject to periodic sys tem checks, and the retaile would be held harmless fo transactions that were processe through the CAS. However, the retailer would be subject to audi for tax remittance, return filing, and use tax calculations. Compensation for use of this model has not yet been determined.

The CPS model would accommodate large, nationwide retailers who have developed their own proprietary systems for calculating sales tax. The states would review the system and offer certification if the system were to meet certain performance standards. The retailer would have to meet activity thresholds for multistate sales (that are yet to be determined). In addition, the retailer would be required to agree to process all of its sales using the system and meet an accuracy standard set by the states. The system would be subject to periodic system checks. Under this model, the retailer would remain responsible for all sales tax functions and be subject to audit. The retailer would be compensated in some manner for using the system to remit the sales tax.

SIMPLIFIED COMPLEXITY

The SSTP has clearly gained momentum and made significant progress on complicated issues in its short period of existence. It appears that the draft legislation of Phase I recommendations will be completed by December, 2000. Whether these efforts will result in actual simplification will remain unclear until after the states hold the legislative sessions for 2001.

Most noteworthy - perhaps even monumental - are the Project's recommendations regarding allowing reliance on zip codes, requiring statewide tax base uniformity, adopting absolute immunity for accepting exemption certificates, and the setting of a sourcing rule for sales of digitized products. While each of these may draw criticism from various groups, these recommendations represent a truly courageous start at long-needed radical reform. As noted above, individuals and groups have been talking about doing something like this for years, but real movement has not occurred until now.

Of course, any time an effort of this magnitude is undertaken, unresolved questions, concerns, and underlying implementation will make it somewhat complicated to achieve. The Phase I proposals are not absent of business as well as legislative concerns. Therefore, substantial effort will be required on the part of legislators, states businesses, the CSPs, and the software vendors to implement simplification.

Businesses and local governments have participated in the SSTP process by making comments and recommendations regarding the Phase I proposals. The SSTP has been very open and flexible in its attempt to address the business community's concerns. Extensive work was done, for example, with the National Retail Federation regarding the uniform definitions. Questions regarding the proposed definitions, however, do remain. For example, there has been some discussion regarding whether digitized products and items such as electricity would fall within the definition of "tangible personal property." In addition, the proposed hierarchy in the sourcing rules may produce unexpected results without further clarification of terms. For example, the recommendations call for the use of an address that may be contained within a seller=s records for reasons other than making the sale at issue or, for that matter, for a non-sale reasons. Upon audit, states could nevertheless treat this as an address "maintained" by the seller. Consider a retailer that purchases some supplies from a manufacturer. Months later, the retailer makes a sale to that same manufacturing. Since the retailer has the first address on file, the rule could be interpreted as requiring the retailer to tax the manufacturing company based on the location on file. This result could be mitigated if the concept of "maintained" were substantially narrowed.

Local governments were also represented at the public hearings through the United States Conference of Mayors and the National Association of Counties. The local governments have urged the SSTP to maintain some of the more complex aspects of the current system such as local rates and local tax bases. The Phase I proposal maintains the local rates but simplifies compliance with new 'rate change procedures' but recommends that localities follow the state base. While it is clear that technology will play a key role in the implementation of many of the SSTP's recommendations, technology should not be viewed as a means to keep the more complex aspects of the current sales tax system.

Sales tax software systems have, of course, existed for many years to assist the traditional, multistate retailer with the tax collection requirements of the vast number of state and local sales and use tax jurisdictions. But the mere existence of such software should not entice the SSTP to waver from the stated goal of simplifying the current system. The existing software systems were designed, out of necessity, to handle as many of the complexities as possible. But businesses that have implemented such software systems can attest to the burden of the current sales tax collection process that remains despite the capabilities of the technology. The more variables that the software is required to handle (e.g. varying rates, tax bases, product types, customer types, locations), the more complicated and costly it is to implement and ensure accuracy. The on-going maintenance also requires significant attention as the variables change or new types of transactions are added. Implementation, operation, and maintenance require human and financial resources. Technology

Just one MORE

David Machlan
Mark A. Maloney
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Cindy L. Mires
Kenneth J. Monahan, CMI
Stephanie Moncebaez
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Kenneth White
Christina M. Wood

IPT members who have obtained "Just One More" member since the Annual Conference.

Star Wars Meets the Sales and Use Tax: *(continued)*

alone cannot materially lighten the burden - true simplification in the underlying legal requirements is needed.

Overconfidence in technology (for example, on the part of local governments) as a means to keep the system complex should be avoided. Legislatures should pay close attention to any discussion regarding technology, particularly if technology is used to support exceptions and carve out suggestions from simplification. In fact, the legislatures will have a vested interest in keeping it simple if states remain responsible for paying for the system. Using existing technology as a starting point to design and implement simplification seems far more in line with the SSTP's goals than relying on technology to keep the complexities in the current system.

At times during the project, the NCSL task force meetings have also reflected some disconnect between the politicians and the SSTP work groups. While the politicians understand the need for change, it is questionable whether they have the political will to effect the changes in their respective states. Legislators will no doubt consider (1) whether the proposed simplification will ultimately result in a net benefit to the state and (2) which specific interest groups or constituencies will be winners (lower tax burden) and which will be losers (greater tax burden). Using a cost/benefit approach, simplification would cost the states in that the states will be required to pay for the system and some may lose tax base if the uniform definition eliminates an item that is currently taxed. On the benefit side, states might gain the ability to tax remote commerce (see "Nexus" discussion below). However, since there is no guarantee that passing the legislation will result in Congress allowing the taxation of remote sellers, the legislators may need to take seemingly extraordinary positions to implement simplification.

Assuming the current recommendations are passed by the legislatures, states will then need to work on a significant number of details. In addition to continuing simplification efforts, states will need to develop a certification process and identify resources that can certify the system(s). The people with the skills needed to perform such certifications are in high demand, and this could present difficulties in obtaining these resources. In addition, the process will likely require a certification on a company by company basis, since each company will have unique products that will require a taxability classification. Such certification will be an enormous task. States will also be required to provide training for auditors to accommodate the multistate audit responsibilities that will be imposed by the new system.

Perhaps one of the most complicated implementation roles will be that of the CSPs. While the CSPs participating in the pilot program have extensive experience in certain aspects of the system, this type of arrangement has not been attempted. Implementing sales tax software with one company is currently a labor-intensive process and includes such tasks as configuring and formatting the host system data to properly communicate with the tax software, assigning taxability codes to products and customers, training of people in areas such as order entry and billing (to the extent such business processes are affected by the tax calculation), and numerous other tasks. While interfaces currently exist between the tax software vendors and the major financial and/or ERP systems, smaller companies may not be using such financial systems. This could require the CSP to develop new interfaces with lesser used packages. Multiplying these tasks by the number of retailers that could participate in the CSP model results in an enormous resource requirement.

While businesses stand to benefit from a number of the simplification recommendations, they will also experience implementation issues. Under the current recommendation, the CSP is liable for inaccurately classifying taxable items a "exempt." CSPs will undoubtedly need to control their risk and will likely require significant involvement of the retaile in making tax determinations Such involvement would likel occur, not only initially, but an time a new product or custome is added by the retailer. In addi tion, CSPs are likely to negotiat some level of liability with th retailer. In addition, if not a states adopt the simplification, dual system would be require by any businesses that currentl have multistate filing obliga tions. For example, a busine could be using a CSP model f the states which adopt the use the CSP and its existing syste for states which have not adop ed the simplification. Operatir dual systems could be compl cated and would require bus nesses to maintain the syste and resources despite the simp fication efforts. Even if all stat did adopt the simplificatio businesses would be required review the uniform definitio and change the current tax trea ment to comply with the ne uniform definition.

In sum, the SSTP recomme dations appear to portend gre advances in easing the burde the current sales and use tax sy tems place on governments a businesses alike. As the proce proceeds, however, it is essent that the focus remain on simp fication and that the hopes (i. fantasies) of technologi panaceas do not distract the p ticipants from that focus.

NEXUS

It would be incomplete to d cuss sales and use tax simplifi

Star Wars Meets the Sales and Use Tax: *(continued)*

tions/mechanization without at least alluding to the government representatives motives in developing and promoting these proposals. Some of those representatives are, quite honorably, merely seeking to do what is right, i.e., reducing unnecessary burdens that truly benefit no one. Other representatives see simplification/mechanization as a tool to override Quill's physical presence standard (under which a state may require remote sellers to collect that state's use tax only when the remote seller has a non de minimis physical presence in the state). Some of those representatives believe that the U.S. Supreme Court, when addressing the next National Bellas Hess/Quill case (if the Court decides to take it) will see the newly implemented simplification and therefore remove the physical presence standard; based on the Quill court's reliance on stare decisis and its invitation to Congress to act in this area, such a Court decision seems extremely unlikely. Others of those representatives believe that Congress, if shown extreme simplification by the states will legislate an override of the Quill physical presence test. It seems that this could be a realistic possibility, but if - and only if - there is extreme simplification and perfect, 100% uniformity. If there are any deviations from absolute uniformity, the portion of the business community that wishes to maintain the Quill physical presence test will likely be invincible in its quest for Congressional codification of that test or, at least, in preventing any Congressional override of the test.

2001 COURSE 1 COMMITTEE MEETING

The 2001 Course I Committee met in Kansas City, Missouri on December 6th to finalize details of the school program. The school will be held February 25 - March 2, 2001 at Indiana/Purdue University in Indianapolis. Registration materials were sent to the membership in November, and early registration is encouraged since the school is typically over-subscribed.

The following faculty were present at the meeting: Robert B. Atkinson, CMI, CPA (School Chair) — AmeriTax Services Inc.; Julia S. Bragg, CMI, CPA — International Paper Company; Anita M. DeGumbia, CMI, Chandler, Arizona ; Rolston A. Dyer, CMI (School Vice Chair) — The Coca-Cola Company; Carolyn L. Elerson, CMI — FedEx Express; Brenda S. Kelley — Fontaine & Kelley, LLP; Mary Pat Kloster, CMI — American Tax Associates, Inc.; Lynn D. Krebs, Ph.D. — Institute for Professionals in Taxation; Barbara A. Sweasy, CPA — Teligent, Inc.

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WHO MAY APPLY FOR CMI-SALES TAX CANDIDACY?

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The Business Journal
SERVING GREATER MILWAUKEE

Editorial

Comment

No Internet tax means more taxes elsewhere

On Internet Taxes Tom Somodi

Any business person who believes you can have something for nothing has probably not been in business very long. Yet this is what proponents of a "no Internet sales tax" policy would like you to believe.

The idea of no sales tax on Internet commerce sounds great. Just don't ask the question of how state and local governments will fill the void created from lost revenues. It's an amount projected to be as much as $15 billion in the year 2003, according to a December 13, 1999 article in The Industry Standard.

Of course, most American business people know such a shortfall is unlikely to be offset by a reduction in government spending. Instead, history tells us the shortfall will be compensated for through a different set of taxes. Given the political climate and robust economy, the most likely shift will be to business income and property taxes.

So what is the net result? A reduction in the consumer based sales tax for an increase in business-based taxes.

While a "no Internet sales tax" policy will definitely create a reallocation of resources, it unfortunately will probably yield no real overall net dollar benefit. Of course, this immediately leads to the next question. Is there an overall benefit through the reallocation of resources that will occur?

It seems most people agree that the current "no Internet sales tax" policy favors heavily funded national and offshore Internet business enterprises that distribute nationally via a handful of strategically placed distribution centers. In other words, the current reallocation of resources creates a disadvantage for business operations with a local presence. It is estimated that consumers spend 80 percent of their money locally. It is not surprising that a January 2000 USA Today/CNN/Gallup Poll showed 65 percent of the respondents indicated that people should be required to pay the same sales tax for purchases made over the Internet as they would if they had bought items in person at a local store.

That's right. Even the average American consumer recognizes there is no long-term advantage to a "no Internet sales tax" policy. Instead of penalizing local businesses and merchants with an arbitrary government influenced policy, Internet commerce and ultimately business and consumers will be better served through a standardize method of sales tax on Internet commerce.

Let's be real. These taxes will be collected one way or another. We should seize this opportunity to create a simplification and standardization in the sales tax systems among the various taxing authorities. Internet commerce is the wave of the future because it has inherent cost saving advantages, is convenient and expands the opportunities of choice to the consumer. A policy of no Internet sales tax provides a competitive advantage to a few businesses that can capitalize off of a specific organizational structure while hurting many businesses and merchants providing service at a local level.

The old adage still holds true. There is no such thing as a free lunch, and you cannot get something for nothing through a "no Internet sales tax" policy.

Tom Somodi is President of ICanShopOnline.com, an Internet mall that features local businesses in southeastern Wisconsin. The company is based in New Berlin.

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'The cultural dreams and aspirations of the entire Madison community cannot be contained in one building.'
Anne Katz, guest column

OPINIO

Monday, May 15, 2000

WISCONSIN STATE JOURNAL

OUR OPINION

Devise fair e-commerce tax plan

A tax system that benefits e-commerce while penalizing traditional stores is unfair and potentially troublesome for state and local governments.

Without holding so much as a single public hearing, the House of Representatives have overwhelmingly approved a five-year extension of the e-commerce tax moratorium. Senate Republicans, unlike their eager-to-please colleagues in the House, need to do what they can to shorten and scale back this massive moratorium.

The House vote came after a federal commission failed to come up with a plan for fairly taxing Internet commerce. Apparently, there are no easy answers to the question: How should sales taxes be applied to purchases over the Internet, if at all?

The economy needs an answer. Many members of Congress understandably want to send the message that Uncle Sam does not want to interfere with the growth in e-commerce. But the moratorium passed by the House tilts public policy unfairly in favor of Internet e-tailers and against bricks-and-mortar stores. Why should a dot-com company be exempt from charging a sales tax that a store selling the identical items is required to charge?

Moreover, permitting dot-coms to escape the sales taxes that regular stores charge is likely to drive more sales to the Internet, depriving state and local governments of revenue. To compensate, those same governments are likely to raise property taxes or income taxes or both. It's not a happy prospect for taxpayers.

The 19-member federal Advisory Commission on Electronic Commerce failed back in March to muster a two-thirds majority required to forward a recommendation to Congress on Internet tax policy. The best the commission could do was to vote to send to Capitol Hill a report containing a proposal supported by the commission's business members. That proposal advocated a permanent ban on Internet access taxes and a five-year moratorium on any new Internet taxes, beyond the current moratorium, which expires in October 2001.

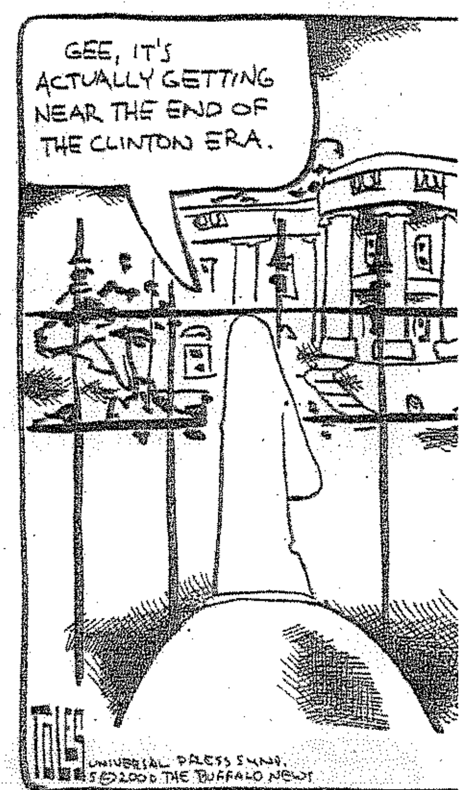
Officials who had counted on the commission to recommend a plan for a fair sales tax system that would penalize neither bricks-and-mortar stores nor e-tailers were justifiably miffed. "What we really don't like is when government steps in and says, 'We like your business better than other businesses,' " said Dallas Mayor Ron Kirk.

The job of developing a fair tax plan is complicated. A 1993 Supreme Court ruling bars state and local governments from imposing sales taxes on Internet sales, as well as catalog company sales, unless the business doing the selling has facilities in the state doing the taxing.

The alternative, however — a two-tier tax system that penalizes traditional stores and risks budget disasters for state and local governments — is simply not acceptable. The Advisory Commission on Electronic Commerce failed. So has the House, which approved the five-year moratorium in an election-year rush.

It is up to the Senate to slow this measure down. The current moratorium runs for another 17 months; let's use that time to devise a system that's fair for all.

Much ado about 'virtual' e-mail tax



No campaign for the Maste

"Rriiinnng! Rriiinn — "

"Whassup?!"

"Good morning. Kevin Niblick please."

"I'm Kevin."

"This is the White House, Mr. Niblick. Please hold for a call from the president."

RICK HOROWITZ

"Yeah, right. The president's got nothing better to do with his — "

"Hey, Kevin, it's Bill Clinton! How's it going, young man?"

"Justin, is that you? I'm gonna get you in gym, you gnat, doing me like this!"

"No, really — it's Bill Clinton! You *are* the Kevin Niblick who's running for sophomore-class president at Chutney-

EDITORIAL: Fair play online

Government should take a hard look at damage done by the free culture on the Internet.

WISCONSIN'S REVENUE DEPARTMENT issued a startling report this week, suggesting that millions of dollars in sales taxes were not collected for purchases made online or through catalogs.

Sales taxes are supposed to be collected on items purchased elsewhere but used in Wisconsin. According to the state report, as much as $109 million in uncollected sales tax revenue may have been lost. More than $300 million in goods are estimated to have been bought via the Internet, which should have amounted to somewhere in the range of $14 million in sales taxes.

The problem will only get worse, the state officials say. They estimate Internet purchases could reach $4.3 billion to $5.8 billion by 2004.

SALES TAXES comprise almost a third of state government's revenue, so this trend obviously could have serious implications.

It could result in less money for schools, towns and cities. And a serious pinch in overall revenue could bring layoffs and reduced services from state government.

But that's not the only problem or, for that matter, the most serious problem.

There's a basic fairness question involved which could adversely impact Main Streets all over Wisconsin _ and elsewhere. That question revolves around local communities' retail climate.

CONSIDER: IF A consumer wants to buy a new music CD, and takes his business to Shopko or Wal-Mart, he'll pay the price of the goods and the store will add on the sales tax.

But if the consumer buys that same CD from an Internet music site, the sales tax goes uncollected.

That's not just a problem for the state budget, it's a serious disadvantage for local businesses. As more and more dollars flow to the Internet, the problem will only get worse.

Mind you, we are not trashing the Internet. It is a marvelous network of sophisticated technology, which is bringing all sorts of new opportunities to convey information and do business. In fact, the ***Daily News*** is a pioneering player on the World Wide Web. The ***BDN Connection***, the newspaper's electronic edition, was the first such site in Wisconsin and has been active for more than five years.

Even so, we strongly believe a vibrant retailing community is a key component of a full-service city. Beloit has made strides in that area in recent years, and is actively pursuing strategies to enhance retailing opportunities. It's not an easy task, persuading investors to put major money into new retail ventures. And the work isn't made any easier by situations which place neighborhood stores at a competitive disadvantage.

OBVIOUSLY, NO ONE likes to pay taxes of any sort. Consumers certainly may be forgiven for seeking out ways to buy goods and services without the add-on collections.

But fair is fair. One means of selling should not be given preference over another. If that CD will cost the consumer sales tax at Shopko, it ought to cost sales tax if purchased over the Internet.

This issue should not be viewed strictly as a challenge for state treasuries. It's a significant problem for the stores you love to shop, too.

And that's not fair.

Beloit Daily News - Friday, Ju...

Today's debate: MAIL-ORDER TAXES

Dodging taxes by mail unfair to taxpayers, states

11/19/97

OUR VIEW **As mail-order and Internet sales grow, pressure is on to collect sales taxes. That's only fair.**

No consumer likes a freebie taken away.

So when reports leaked a couple weeks ago of a possible deal between big states and major mail-order companies to apply sales taxes to catalog purchases, the firms got an earful.

Customers blistered L.L. Bean, Lands' End and others over their 800 lines. They warned that any tax would affect buying decisions. And the firms immediately denied any deal was even close.

Too bad.

Mail-order customers may not know it, but they owe the taxes anyway. Two Supreme Court decisions have exempted out-of-state mail-order houses from having to collect sales taxes, but not purchasers from the responsibility to pay them.

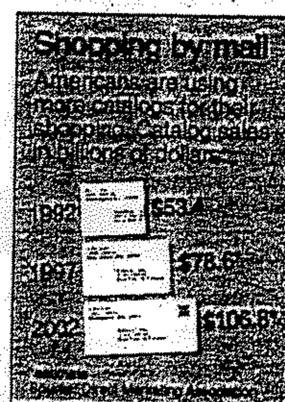
Virginia, Maine and Wisconsin even provide lines on income tax forms demanding that consumers pay up. If state tax audits discover they haven't, they face penalties. Mail-order houses' refusal to collect the tax turns their customers into scofflaws.

And that's the least of the problems.

A decade ago, taxes on out-of-state sales would have produced a minuscule $6 per household in revenue. But mail order sales are growing rapidly — up nearly 50% to $78 billion in just five years. And now another form of tax-exempt commerce — Internet sales — is coming on line with the potential for $200 billion in annual sales.

Those sales likely will come by drawing business away from Main Street retailers and in-state mail-order firms, such as J.C. Penney, that now collect sales taxes.

As these firms lose business, states — which rely on sales taxes for a third of all revenues — will either have to cut back on services or raise other taxes on property owners and businesses. So, too, will local governments.



By Quin Tian, USA TODAY

States already are considering imposing new taxes on Internet traffic or applying their sales taxes to all transactions there. In response, some in Congress want to ban state taxes on Internet commerce for up to five years.

The negotiations between mail-order firms and the states pointed to a way out of that taxing dilemma.

States offered to simplify their array of 46 state and 6,700 local sales taxes so mail-order firms could collect them easily, using recently developed software. In return, states would drop efforts to audit the firms' books in search of lost revenue.

A similar voluntary approach might work with Internet commerce. States would get their money. Mail-order and Internet firms could better serve their customers. And taxpayers would avoid losing services or being hit by other charges.

The lesson is simple: Nothing is free. The one thing government can do with taxes is ensure they treat everyone fairly.

Poll: 70% back Internet sales tax

September 27, 2000

BY LUCIO GUERRERO STAFF REPORTER

Seventy percent of Illinoisans support taxing Internet purchases, according to a poll released Tuesday by a retail group.

The International Council of Shopping Centers found that 69 percent of those polled agreed that Internet businesses should be required to collect sales taxes on online purchases.

That was after the pollsters explained the issue. Before being told about the money and services that municipalities say they're losing because Internet companies remain untaxed, the approval rate was just 46 percent.

That, say leaders of the push to tax e-sales, shows that once people are aware of the issue they'll support a new Internet tax.

"When people hear the arguments they say, `This makes sense,' " said state Sen. Steve Rauschenberger (R-Elgin), who has been a proponent of the Internet tax. "It seems that the public is understanding the issue a lot better than some members of Congress."

Congress is debating whether to extend a current moratorium that allows most e-retailers to exist tax-free, while brick-and-mortar stores are required to charge customers sales tax.

Local leaders are concerned that more and more shoppers will turn to the lower prices on the Internet and stop shopping at local stores. If that happens, local officials say, shops would close and cities would have to reduce services such as police, fire, and sewer and road repairs.

A University of Tennessee report found that by 2003, state and local governments could lose more than $20 billion a year in revenue because of e-tailers.

"This is a way to have an even playing field," said Palatine Mayor Rita Mullins, who is the president of the Northwest Municipal Conference.

Simplifying the Sales Tax is a Matter of Fairness

–Kathleen Falk, Dane County Executive

Wisconsin counties have a vested interest in fair and uniform application of sales tax laws.

It is, therefore, encouraging that Wisconsin is in the vanguard of a nationwide effort to simplify the often bewildering and contradictory welter of sales tax laws. The goal is to bring the sales tax into the 21st Century by making it easier for retailers to administer and consumers to understand while leveling the playing field for all.

That is especially important in this age of multi-state businesses where goods cross state lines at the click of a computer mouse. Determining the correct amount of sales tax – or even what is taxable – in which jurisdiction is a daunting task for retailers and confusing to customers.

Wisconsin Revenue Secretary, Cate Zeuske, says that if there is one guiding principle for good tax policy, it is that the tax should be easy to understand, simple to administer, and fair to everyone.

Impact on Counties

The sales tax is important to Wisconsin's quality of life. Of the $10.9 billion collected in taxes last year, about $3.5 billion came from the sales tax, second only to the personal income tax. The sales tax is also an important source of local revenue in 54 of our 72 counties, reducing reliance on the property tax by $200 million a year.

Dane County's budget illustrates the importance of the sales tax to those 54 counties. Dane County would have to raise property taxes by over 40 percent or make almost $36 million in cuts, mostly in law enforcement or human services, if the county lost the sales tax.

> GOOD TAX POLICY ... SHOULD BE EASY TO UNDERSTAND, SIMPLE TO ADMINISTER, AND FAIR TO EVERYONE.
>
> *–Cate Zeuske, Secretary Department of Revenue*

The Wisconsin Counties Association also states that substantial changes are necessary if the sales tax is to continue as an integral part of the state and local revenue system.

Wisconsin leads a multi-state effort

Under the umbrella of such national organizations as the National Governors' Association, the National Conference of State Legislatures, the Multi-State Tax Commission, and the Federation of Tax Administrators, 29 participating states (another 12 are observing states) have banded together to form the Streamlined Sales Tax Project. Diane Hardt, administrator of the Wisconsin Department of Revenue's Income, Sales and Excise Division, co-chairs the national project.

Forrester Research Inc., a firm that analyzes the future of technology change and its impact on businesses, consumers and society, says that the Streamlined Sales Tax Project is at the center of sales tax reform efforts that will reduce the tax collection burden for all sellers.

The Streamlined Sales Tax Project will,

- develop common definitions of taxable items;
- harness computer technology to automatically identify taxable products;
- apply the tax rate; and
- remit the proper amount to the taxing jurisdiction.

Model legislation proposed

On December 22, 2000, the Streamlined Sales Tax Project approved a Model Act and Interstate Agreement for the consideration of the states' legislatures. The model legislation and agreements provide for improved sales and use tax administration systems for all sellers and for all types of commerce through the following features in the system:

- State level administration of sales and use tax collections
- Uniformity in state and local tax bases
- Central, electronic registration for all member states who enact the legislation
- Simplification of state and local tax rates
- Uniform sourcing rules for all transactions
- Uniform definitions within tax bases
- Simplified administration of exemptions
- Simplified tax returns
- Uniform rules for deductions for bad debts
- Simplification of tax remittances
- Protection of consumer privacy

Easier on all retailers

The work of the Streamlined Sales Tax Project will make it easier for all retailers – whether on-line, catalog, or bricks and mortar – to handle their sales taxes. Retailers would file a single, uniform return for all tax jurisdictions in a state and they would do so on-line. Multi-state businesses would have a uniform, electronic, "one-stop" registration system.

There would be limits on the frequency with which local tax rates can be changed and a requirement that the state provide a notice of local rate and boundary changes. But states would retain the right to determine what is taxable and at what rate they will be taxed.

Computer software is being developed to seamlessly assess the correct tax on the right item for the proper jurisdiction, based on the nine-digit zip code. That will streamline tax accounting for all retailers.

The model legislation and agreement provide for uniform definitions of clothing and related items and of food and food ingredients. They also provide for uniform definitions of delivery charges, purchase price, retail sale and sales price. State legislatures will determine what is taxable and exempt in each state but they will use the uniform definitions to achieve the simplification.

The Forrester Group reports that: "As retailers retool collection systems and plug into tax collection technology, states will focus efforts on their own tax collection back ends. To reduce retailers' burdens, they'll encourage on-line reporting and eliminate monthly forms in favor of automated transfers."

No wonder the International Mass Retail Association says the Streamlined Sales Tax Project "is the most significant effort at (tax) simplification that has been undertaken in some time."

If you would like more info on the Streamlined Sales Tax Project, visit them on the web at /www.streamlined-salestax.org/.

By James L. McQuivey

With Gillian DeMoulin

FEBRUARY 24, 2000

States Lose Half A Billion In Taxes To Web Retail

Although consumers seem nonchalant about online taxes, they leave a trail of unpaid state and local taxes in their Web-shopping wake. In 1999, more than half a billion in sales taxes went uncollected. States won't suffer this outrage for long.

WEB BUYERS DON'T MIND SALES TAXES MUCH

Consumers love online shopping -- they say it's easy, convenient, and can even save money. But one small potential benefit of buying online is sales tax savings -- only online stores that have a physical presence in a consumer's state are required to charge sales tax online. We recently surveyed 8,900 online purchasers to find out just how much they care about avoiding sales taxes online. In spite of the bad taste taxes leave in the mouth of the average American, online sales taxes don't get them too excited (see Figure 1).

- **Taxes barely stand in the way of purchases today.** Only 22% of online buyers regularly shop around to avoid paying sales taxes online. Even fewer -- just 13% -- have ever abandoned a shopping cart after deciding the sales taxes were too high.
- **Shoppers figure online sales tax is no worse than everyday sales tax.** When asked, 38% of Web buyers say that since they already pay sales taxes on everything they buy in the offline world, Net sales taxes don't bother them. Another 27% are undecided -- only 35% expect to beat the sales tax online.
- **Shipping is a bigger downer than taxes.** To compare their feelings about taxes to other eCommerce inhibitors, we asked about shipping costs. A cool two-thirds agreed that shipping costs are more important to them than sales taxes.

STATES FEEL THE IMPACT OF SALES TAX AVOIDANCE

The fact that consumers are only slightly annoyed with sales taxes stems from the fact that most of them aren't paying it online. In fact, of the nearly $13 billion in taxable

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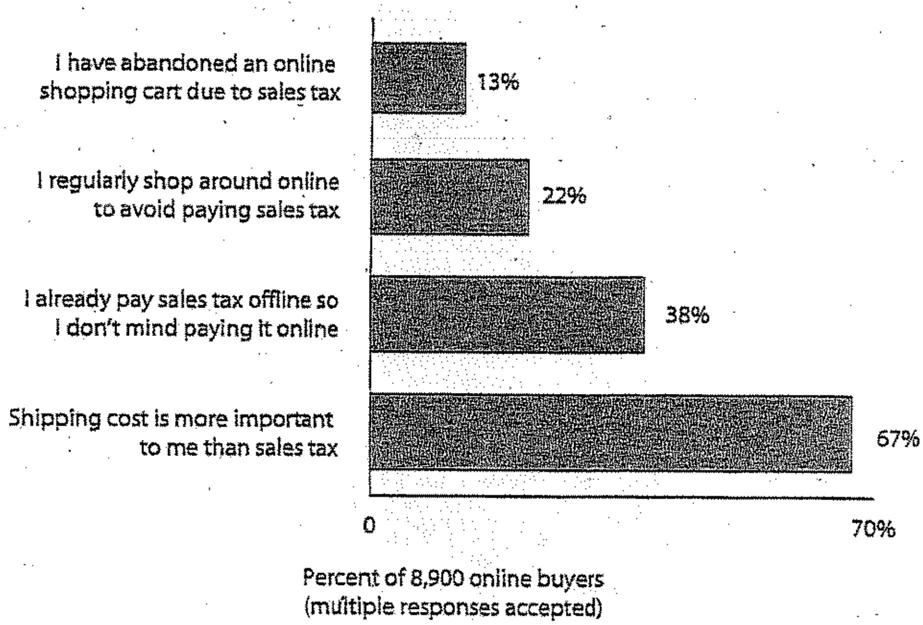
Figure 1 Consumers Express Few Concerns With Online Sales Taxes



Source: Forrester Research, Inc.

retail goods sold online in 1999, only 20% was taxed by states. So although $140 million in revenues came in, an additional $525 million in lost taxes was left on the table. Because online spending and tax rates vary dramatically from state to state, Forrester calculated 1999 sales taxes earned and lost for each state (see Figure 2).

- **Wired states collect the most money but still feel the pain.** States like California, Massachusetts, New Jersey, and Washington that have large numbers of eCommerce startups and retailers earn the most sales tax per online buyer. However, the fact that these states also have more active Web buyers than the norm means those buyers will eventually spend money across state lines.

- **Large states without eCommerce players lose more than their fair share.** States that have large, educated populations bent on shopping on the Web but have few online retailers with a physical presence in their states lose the big bucks. In this group are Florida, Illinois, Michigan, and Pennsylvania, which each lost from $18 million to $33 million last year to untaxed online purchases.

Figure 2 1999 State-By-State Sales Taxes Earned And Lost

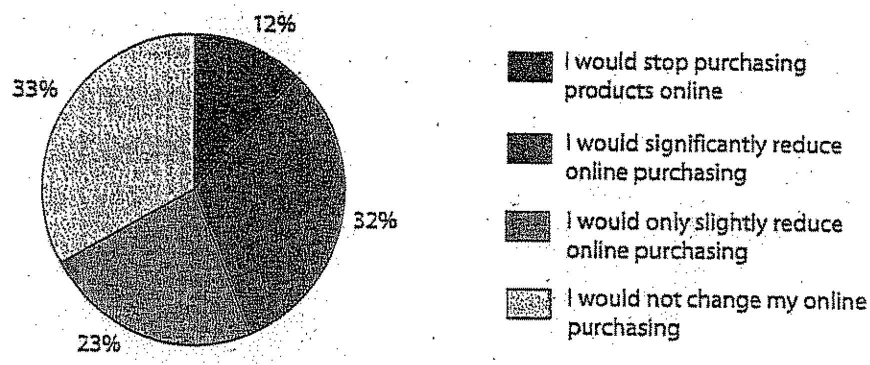
State	Total Web spending[1] (in thousands)	Percent taxed	State tax rate[2]	Collected taxes (in thousands)	Uncollected taxes (in thousands)
Alabama	$148,114	16%	4.00%	$975	$4,949
Alaska	$38,857	N/A	N/A		
Arizona	$242,328	14%	5.00%	$1,711	$10,405
Arkansas	$50,731	4%	4.63%	$101	$2,245
California	$1,832,181	33%	6.00%	$36,082	$73,848
Colorado	$235,168	14%	3.00%	$978	$6,077
Connecticut	$215,540	20%	6.00%	$2,603	$10,330
Delaware	$35,539	N/A	N/A		
D.C.	$45,121	15%	5.75%	$390	$2,206
Florida	$643,126	21%	6.00%	$8,271	$30,317
Georgia	$414,518	16%	4.00%	$2,583	$13,998
Hawaii	$58,034	15%	4.00%	$350	$1,971
Idaho	$52,770	11%	5.00%	$290	$2,348
Illinois	$635,119	18%	6.25%	$7,133	$32,562
Indiana	$204,232	16%	5.00%	$1,668	$8,544
Iowa	$76,751	16%	5.00%	$605	$3,232
Kansas	$114,160	8%	4.90%	$447	$5,147
Kentucky	$102,357	23%	6.00%	$1,400	$4,742
Louisiana	$129,694	15%	4.00%	$768	$4,420
Maine	$39,790	23%	5.50%	$503	$1,685
Maryland	$282,412	19%	5.00%	$2,634	$11,486
Massachusetts	$393,922	26%	5.00%	$5,124	$14,572
Michigan	$409,634	23%	6.00%	$5,729	$18,849
Minnesota	$195,891	15%	6.50%	$1,853	$10,880
Mississippi	$81,626	14%	7.00%	$800	$4,914
Missouri	$195,138	17%	4.23%	$1,420	$6,825
Montana	$29,352	N/A	N/A		
Nebraska	$59,015	11%	4.50%	$298	$2,358
Nevada	$97,758	13%	4.25%	$541	$3,614
New Hampshire	$77,001	N/A	N/A		
New Jersey	$525,860	22%	6.00%	$6,916	$24,635
New Mexico	$88,185	8%	5.00%	$333	$4,077
New York	$922,236	28%	4.00%	$10,323	$26,567
North Carolina	$339,130	26%	4.00%	$3,516	$10,049
North Dakota	$13,944	9%	5.00%	$65	$633
Ohio	$461,955	17%	5.00%	$3,941	$19,157
Oklahoma	$127,978	11%	4.50%	$631	$5,127
Oregon	$150,732	N/A	N/A		
Pennsylvania	$480,356	19%	6.00%	$5,585	$23,237
Rhode Island	$42,566	11%	7.00%	$338	$2,642
South Carolina	$142,560	10%	5.00%	$698	$6,435
South Dakota	$21,745	13%	4.00%	$111	$759
Tennessee	$203,815	15%	6.00%	$1,791	$10,437
Texas	$1,002,656	17%	6.25%	$10,816	$51,850
Utah	$90,396	10%	4.75%	$422	$3,872
Vermont	$54,644	7%	5.00%	$187	$2,545
Virginia	$480,507	19%	3.50%	$3,147	$13,671
Washington	$319,218	19%	6.50%	$3,967	$16,782
West Virginia	$36,340	9%	6.00%	$186	$1,994
Wisconsin	$172,323	20%	5.00%	$1,710	$6,906
Wyoming	$22,259	13%	4.00%	$117	$774
TOTAL	**$12,835,281**	**20%[3]**	**N/A**	**$140,052**	**$524,671**

[1] Web spending excludes travel booking, which is subject to separate travel and tourism taxes
[2] Tax rates current as of February 1, 2000 (http://www.salestaxinstitute.com), [3] Weighted average

Source: Forrester Research, Inc.

Figure 3 Consumers Don't Approve Of Special Internet Taxes

If the government passed a universal sales tax on internet purchases . . .



Source: Forrester Research, Inc.

- **A handful of no-tax zones could care less.** Five states -- Alaska, Delaware, Montana, New Hampshire, and Oregon -- have no state taxes and therefore feel no pain from the effects of Web buying.

STATES WILL WANT RADICAL CHANGE, BUT CONSUMERS WON'T

With one look at these lost revenues, states will call on the Electronic Commerce Advisory Commission to tighten the holes through which this money has slipped. In a moment of weakness, federally minded politicians may recommend a national Internet sales tax. We urge restraint: Although consumers have little opposition to current sales tax laws, 44% say that a special Internet tax would completely stop or significantly reduce their online buying (see Figure 3). We don't have to lecture anyone on what this would do to our economy's unprecedented expansion. Instead, Forrester recommends that governments advocate applying current sales taxes to all Internet and catalog sales (see the February 7, 2000 Forrester Brief "Internet Sales Taxes Don't Need A Tea Party").

NATIONAL CONFERENCE
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The Forum for America's Ideas

**EXECUTIVE COMMITTEE TASK FORCE ON
STATE AND LOCAL TAXATION OF TELECOMMUNICATIONS
AND ELECTRONIC COMMERCE**

CONTENTS

NCSL Task Force on State and Local Taxation
of Telecommunications and Electronic Commerce

Saturday, January 27, 2001

Decisions to be decided by Task Force:

1) GOVERNANCE
   a) How many states constitute or trigger an agreement as a legal document?
   b) Should there be a time trigger as well?
   c) Do states that only pass the "Act" have the same or an equal vote as those states who have enacted the "Act and Agreement?'
   d) How long do states that only passed the "Act" have before they must pass the Agreement as well or be dropped as a participant state?

March, April May -

2) Do we proceed
   a) Act only
   b) Act and Agreement / w states deciding to pass Act only or Act and Agreement?

3) Proceed with Streamlined Sales Tax Project's AGREEMENT or NCSL make amendments to Agreement?

304/308 - motion

1 * 4) Proposed Uniform Base? LEAVE AS IS - FIX or OMIT?

→ AFTER 5 years - all tax law -

2 5) Proposed Uniform Definitions? LEAVE AS IS - AMEND or $\boxed{\text{OMIT?}}$

X 6) Uniform Bad Debt Provisions? LEAVE AS IS - FIX or $\boxed{\text{OMIT}}$?

- Finan - Principle

Big Debate

7) Uniform Sourcing Rules? LEAVE AS IS - FIX or $\boxed{\text{OMIT?}}$ * Tennessee

Which jurisdiction should get the revenue

8) Vendor Monetary Allowance? LEAVE AS IS - FIX or OMIT?

Worth study -

9) Other Governance Provisions? LEAVE AS IS - FIX or OMIT?

10) Should the Task Force ask the Executive Committee to authorize NCSL's participation with the other government groups and the private sector to determine the actual costs to vendors to collect a state's sales and use tax?

Delete 308.5 Rounding - Manzano -

NCSL

EXECUTIVE COMMITTEE TASK FORCE ON STATE AND LOCAL TAXATION OF TELECOMMUNICATIONS AND ELECTRONIC COMMERCE

January 26-27, 2001

Westin Savannah Harbor Resort
Savannah, Georgia

AGENDA

Representative Matthew Kisber, Tennessee
Senator Steven Rauschenberger, Illinois
Task Force Co-Chairs

Friday, January 26

12:00pm - 1:00pm **Working Lunch**
Grand Ballroom B

Review/Briefing on Recommendations from the Streamlined Sales Tax Project as adopted on December 22, 2000 and amended on January 24, 2001.

1:00pm - 3:00pm Overview of options for the Task Force to consider in making recommendations to the NCSL Executive Committee

3:00pm - 5:00pm Task Force discussion of the options.

6:00pm - 7:30pm Executive Committee Opening Reception
Harbor B

6:30pm Dinner for the Task Force at **The Olde Pink House**
23 Abercorn Street, Savannah
(Members should meet in the Hotel Lobby by 6:15 PM)

The dinner will provide the Task Force members an opportunity to discuss further the recommendations the Task Force will make to the Executive Committee the following afternoon.

<u>Saturday, January 27</u>

8:00am - 11:00am Working Breakfast

Trade Center - *via a walkway from the Westin*

Formulation of official Task Force recommendation to the Executive Committee, including any potential amendments to the proposals of the Streamlined Sales Tax Project.

11:00am - 12:00pm Discussion on state strategy to move the process forward.
-Future Task Force Meetings

12:00 noon Task Force Meeting Adjourns

12:00pm - 1:00pm Lunch

Grand Ballroom A

3:00pm - 5:00pm Executive Committee Business Meeting

Grand Ballroom E-F

6:30pm - 10:00pm

Grand Ballroom C Monsanto Dinner for Members of the Executive Committee and the Task Force on State and Local Taxation of Telecommunications & Electronic Commerce