

HOUSE BILL REPORT

HB 1722

As Reported by House Committee On:

Finance

Title: An act relating to the taxability of persons with limited connections to Washington.

Brief Description: Limiting the taxability of certain internet transactions.

Sponsors: Representatives Gombosky and Cairnes.

Brief History:

Committee Activity:

Finance: 2/13/03, 2/28/03 [DPS].

Brief Summary of Substitute Bill

- Exempts remote sellers from business and occupation taxes and sales and use tax collection requirements for transactions via internet servers owned by unaffiliated businesses.

HOUSE COMMITTEE ON FINANCE

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 9 members: Representatives Gombosky, Chair; McIntire, Vice Chair; Cairnes, Ranking Minority Member; Orcutt, Assistant Ranking Minority Member; Ahern, Conway, Morris, Roach and Santos.

Staff: Bob Longman (786-7139).

Background:

A person doing business in this state is required to pay business and occupation tax (B&O) and must collect retail sales tax or use tax from the customer for retail sales. Questions have arisen about the meaning of "doing business in this state" in the context of electronic commerce, particularly in regard to out-of-state retailers who conduct business via internet computer hardware ("servers") located in this state. Out-of-state retailers who do business via internet or mail order are often referred to as "remote sellers." As a general rule, remote sellers do not have to pay B&O tax or collect sales tax unless they have a physical presence in this state. This physical presence requirement

is met if the business has agents, employees, offices, warehouses, or other property in this state. A remote seller who owns internet servers in this state meets the physical presence requirement. If a remote seller does business through a third-party internet service provider with equipment in this state, the remote seller could be viewed as having an agent in this state, which would satisfy the physical presence requirement.

The Federal Internet Tax Freedom Act (ITFA) prohibits state and local governments from imposing multiple or discriminatory taxes on electronic commerce. Under the ITFA, a remote seller cannot be required to collect sales tax merely because it conducts business through an online service provider that has equipment located in this state. The ITFA was enacted in 1998 and was originally set to expire in 2001. In 2001 Congress extended the ITFA until November 1, 2003.

The revenue departments of states that impose sales taxes have been working on a project known as the streamlined sales and use tax agreement (Agreement). The Agreement is designed to simplify taxation for all retailers, and increase the collection of taxes by remote sellers by providing uniform sales tax definitions, exemptions, and other rules to be adopted by the participating states. The Agreement will become effective when at least 10 states, comprising at least 20 percent of the total population of states with a sales tax, amend their tax laws to comply with the model tax laws set forth in the Agreement.

Summary of Substitute Bill:

A remote seller making sales in Washington is not liable for B&O tax or required to collect sales or use tax if the remote seller's activities are conducted electronically via a website on computer equipment owned by a business that is not affiliated with the remote seller in this state, and are limited to: (1) Storage, dissemination, or display of advertising; (2) taking of orders; or (3) processing of payments. Businesses are affiliated for this purpose when one business or group of businesses has an ownership of 5 percent or more in another business or group.

These provisions expire when: (1) The United States Congress grants individual states the authority to impose sales and use tax collection duties on remote sellers; or (2) It is determined in a final court decision that a state can impose sales and use tax collection duties on remote sellers.

Substitute Bill Compared to Original Bill:

The substitute clarifies that the exemption applies only if the internet server is neither owned nor operated by the seller or an affiliated person.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Substitute Bill: The bill takes effect 90 days after adjournment of session in which bill is passed.

Testimony For: Seattle-based Amazon.com is the world's largest on-line retailer, employing more than 2,000 employees in Washington. It has expanded its business beyond traditional retailing and now provides transaction processing for third-party sellers. Many of these out-of-state companies would not do business with Amazon if they were subjected to Washington taxes. As long as the federal Internet Tax Freedom Act is in effect, remote third-party sellers are not subject to Washington taxes. If the federal law expires in November 2003, these business opportunities could dry up. This bill preserves the B&O tax that Amazon pays on its income from these business activities.

Testimony Against: None.

Testified: Paul Misener, Amazon.com; and Will Rice, Department of Revenue.