

SENATE BILL REPORT

SB 6544

As Reported By Senate Committee On:
Ways & Means, February 23, 2004

Title: An act relating to conforming Washington's tax structure to portions of the streamlined sales and use tax agreement not implemented by chapter 168, Laws of 2003.

Brief Description: Conforming Washington's tax structure to portions of the streamlined sales and use tax agreement not implemented by chapter 168, Laws of 2003.

Sponsors: Senators Winsley, Brown and Regala; by request of Department of Revenue.

Brief History:

Committee Activity: Ways & Means: 2/3/04, 2/23/04 [DPS, DNP].

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: That Substitute Senate Bill No. 6544 be substituted therefor, and the substitute bill do pass.

Signed by Senators Zarelli, Chair; Hewitt, Vice Chair; Parlette, Vice Chair; Carlson, Doumit, Fairley, Hale, Honeyford, Johnson, Pflug, Prentice, Rasmussen, Roach and Sheahan.

Minority Report: Do not pass.

Signed by Senator Regala.

Staff: Catherine Suter (786-7442)

Background: In the 2002 session, the Legislature adopted the Simplified Sales and Use Tax Administration Act, which authorized the Department of Revenue to be a voting member in the Streamlined Sales Tax Project (SSTP), a multi-state effort to simplify state sales and use tax structures and make them more uniform. Many other states have also authorized such participation, and representatives have met to develop an agreement to govern the implementation of the SSTP. This agreement, called the Streamlined Sales and Use Tax Agreement (SSTA), was adopted by 34 states and Washington D.C. in November 2002.

During the 2003 legislative session, the Legislature enacted legislation at the request of the Department of Revenue to implement the uniform definitions and administrative provisions of the SSTA. However, the legislation did not implement seven additional provisions that are necessary for the state to conform fully to the SSTA. The provisions concern:

- On-line registration of remote sellers;
- Monetary allowance for sellers using certified service providers or tax compliance software. (Certified service providers are third parties that are authorized to collect and remit sales and use taxes to states that participate under the SSTA);
- Conditional amnesty for previously unregistered sellers;

- Requirements governing the location to which tax is attributed during a transaction (i.e., "Sourcing");
- Confidentiality and privacy protections for sellers using certified service providers;
- The development of a taxability matrix to facilitate the administration of tax for sellers; and
- An amendment to the original SSTA agreement concerning how tax is applied to delivery charges when a delivery includes both taxable and nontaxable items.

Under the sales and use tax in Washington State, local sales and use taxes are sourced according to the following rules:

- Sales tax from the sale of goods is sourced to the retail outlet at or from which delivery is made.
- Sales tax from the sale of a service, with or without a sale of goods, is sourced to the place where the service is primarily performed.
- Sales tax from the lease or rental of goods is sourced to the place of first use. In the case of short-term rentals, this is the place of business of the lessor. In the case of rentals or leases involving periodic payments, this is the primary place of use by the renter or lessee for each payment period.

Summary of Substitute Bill: Provisions are included that would allow the state to conform fully to the Streamlined Sales and Use Tax Agreement.

Sellers are authorized to designate an agent to register the seller with the state, if not already registered. Sellers who agree to collect and remit sales and use taxes under the SSTA may register through an on-line system authorized under the SSTA.

The Department of Revenue is required to adopt rules providing for monetary allowances for sellers who use certified service providers, tax compliance software, or another means of collecting and remitting tax that is authorized under the SSTA. In addition, the department may adopt rules to provide vendor compensation for sellers who collect and remit sales and use taxes to the state, but this authority is contingent upon action by Congress or the courts that would allow states to require remote sellers to collect sales or use taxes.

The department is prohibited from making assessments for past uncollected sales and use taxes against an unregistered seller who, within 12 months of the effective date of the state's participation in the SSTA, registers under the agreement and then collects and remits sales and use taxes to the state for a period of at least 36 months. This amnesty does not apply if the seller has already received an audit notice from the department, if the seller has in fact collected sales and use taxes but not remitted them to the state, or if the seller is liable for sales and use taxes in the seller's capacity as a buyer.

The SSTA general sourcing rules are adopted to be effective six months after federal action allows Washington to require remote sellers to collect sales tax on sales to Washington residents. The rules provide:

1. If a good or service is received by the purchaser at the business location of the seller, the sales tax is sourced to that business location.
2. If the good is not received by the purchaser at the business location of the seller, the sales tax is sourced to the location where receipt occurs, if known by the seller.

3. If neither of the first two rules apply, the sales tax is sourced to the address indicated for the purchaser in records normally maintained by the seller, if the use of this address by the seller does not constitute bad faith.
4. If none of the first three rules apply, the sales tax is sourced to the address for the purchaser obtained during the consummation of the sale, including the address of the purchaser's payment instrument, if the use of this address by the seller does not constitute bad faith.
5. If none of the first four rules apply, the sales tax is sourced to the address from which delivery is made.

The general sourcing rules do not apply to purchases of motor vehicles, aircraft, watercraft, modular homes, manufactured homes, and mobile homes. In such purchases, the tax is sourced to the location from which delivery was made.

For the lease or rental of tangible personal property, tax is sourced depending on whether the lease or rental requires periodic payments. If periodic payments are required, tax on the first payment is sourced like sales of tangible personal property, but tax on subsequent payments are sourced to the primary property location of the lessee. If payments are not periodic, then tax is sourced like sales of tangible personal property.

Special sourcing provisions apply to sales of digital goods, electronically delivered software, direct mail, and services, where the property or service sold is delivered to multiple jurisdictions concurrently. In these circumstances, the purchaser is obligated either to provide a form to the seller relieving the seller of the requirement to collect and remit tax or to provide sufficient information to the seller to allow the seller to determine the proper amount of tax to collect. If the seller is relieved of the requirement, the purchaser must remit tax directly.

An 80 percent sourcing mitigation program is established for when this bill's new sourcing rules go into effect. The Department of Revenue will collect point-of-sale and point-of-delivery information from select retailers to determine appropriate redistributions among local governments. A \$500 business and occupation tax credit is established for selected retailers who supply the information and a \$500 penalty is assessed if a selected retailer does not.

Protections are provided with respect to confidentiality and privacy for businesses that use certified service providers under the SSTA. Certified service providers are required to perform tax calculations, remittance, and reporting functions and may not retain the personally identifiable information of consumers, with very limited exceptions. The department will provide public notification to consumers of its practices relating to the collection, use, and retention of personally identifiable information. Personally identifiable information will not be retained any longer than required to ensure the validity of exemptions. This provision may be enforced by petitioning the Superior Court of Thurston County for injunctive relief.

The department is required to complete a taxability matrix and will provide notice of changes in the taxability of products or services listed in the matrix. Sellers and certified service providers are relieved from liability to the state and to local jurisdictions for having charged or collected the incorrect amount of sales or use tax if the error resulted from reliance on erroneous information provided by the department in the matrix.

The taxability of delivery charges is changed to allow sellers to apportion their delivery charges between taxable and nontaxable property within a shipment and apply tax to only that portion that represents delivery charges for taxable property.

Substitute Bill Compared to Original Bill: Amnesty provisions are effective four months after the rest of the bill is effective. A sourcing mitigation program is provided, contingent on federal action.

Appropriation: None.

Fiscal Note: Available; requested on substitute on February 25, 2004.

Effective Date: The amnesty provisions of the bill are effective four months after the effective date of the bill. The provisions concerning vendor compensation, sourcing, and sourcing mitigation are effective when Congress or the court determines that the state may impose sales and use tax collection and remittance duties upon remote sellers.

Testimony For: We need to move forward with the SSTA and collection of sales tax on remote sales. Mitigation should be limited and temporary. Winners tend to be poorer jurisdictions, not able under the Growth Management Act to build the types of development affected by the sourcing provisions. This bill would get some retail sales revenue into communities that have lost it over the years. Counties cannot raise property taxes any more, and these sourcing rules are a valid way to bring money back. Citizens are forced to go outside their communities and subsidize urban areas.

This bill tries to entice remote sellers: a dozen started remitting sales tax when last year's bill passed. The policy change was made last year for the business and occupation tax to be sourced by point-of-delivery. If we wait for federal action, we will be requiring business to keep two sets of books. Washington has been told by an SSTP advisor that without the sourcing provision in effect, Washington is not in conformance with the Agreement and therefore could not be part of the governing board. Sellers must be treated the same, and collect tax the same way. Because remote sellers usually have only delivery addresses, that is all that can be used for tax purposes.

Technology and a busy society have shifted us to remote shopping. By 2008, 10 percent of retail sales in the U.S. will be remote, representing \$1.3 billion in revenues, but our tax structure is not keeping up with this. This bill, all provisions, needs to pass now for the state's business climate, to relieve the burden on all businesses by keeping the system modern. Brick-and-click retailers have different systems of taxation, and this is too much. Many spin off the "click" part to avoid sales tax collection, but would prefer to remain as one retailer for customer service purposes. If the retail industry is not healthy, no warehouses will be necessary. Businesses cannot shoulder the burden of double bookkeeping when the business and occupation tax sourcing changes; that would put small ones out of business. Often customers do all their research in a store, purchase at the store, and then return the item when they have found it tax-free on the internet. This destroys local businesses.

Testimony Against: This bill [its sourcing provisions] severely, adversely impacts 91 cities, representing two-thirds of the state's population. Cities would have poorer bond ratings, debt repayment, and budgets. Significant changes like this require more time to work through, and there is no reason to act before Congress or the Supreme Court does so. SSTA is a good

effort and must be implemented without harming local governments. Mitigation must be permanent and must be full. Cities have made large investments in infrastructure, particularly for distribution, in order to diversify their economies, but this would ignore those investments. There will be fundamental changes in land use policies as a result [of the sourcing provisions]. Interstate revenues should pay for mitigation: concurrency. This bill pits cities against cities. Voluntary collections are a big "if" and \$3 million for the state does not balance the locals' losses.

Testified: PRO: Maureen Morris, Washington State Association of Counties; Merrill Ott, Stevens County; Scott Simmons, Ferry County; Julie Sexton, Department of Revenue; Jan Gee, Washington Retail Association; Tom Dooley, Association of Washington Business; Madeleine Colb and Perry Sal, Olympia business owners. CON (as currently drafted): Doug Levy; Jim White, Mayor of Kent; Mark Foutsch, Mayor of Olympia; Carol Moser, Mayor of Richland; Pete Lewis, Mayor of Auburn; John Wise, Mayor of Enumclaw; Mike McKinnon, City of Lynnwood; Hank Thomas, Issaquah Councilmember; Ted Hikel, Lynnwood Councilmember; Jim Justin, Association of Washington Cities; Bill Nal, City of Fife.