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Submission of the National Retail Federation

to the

Senate Committee on Finance

Hearing on Tax Reform: What It Means for State and Local Tax and Fiscal Policy

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As the world's largest retail trade association and the voice of retail worldwide, NRF represents retailers of all types and sizes, including chain restaurants and industry partners, from the United States and more than 45 countries abroad. Retailers operate more than 3.6 million U.S. establishments that support one in four U.S. jobs – 42 million working Americans. Contributing $2.5 trillion to annual GDP, retail is a daily barometer for the nation's economy. NRF's Retail Means Jobs campaign emphasizes the economic importance of retail and encourages policymakers to support a Jobs, Innovation and Consumer Value Agenda aimed at boosting economic growth and job creation. www.nrf.com

Summary of Comments

Members of the National Retail Federation believe that Congress must resolve the Constitutional questions posed by the *Quill* decision in a fashion which promotes a level playing field among retail competitors. As retailing evolves and Internet sales become a more prominent portion of total retail sales, it is critical that Congress address the sales tax collection discrimination that exists between brick-and-mortar and remote retailers.

Brick-and-mortar retailers compete vigorously with each other and with remote retailers for market share. Different retailers have different strategies for going to market, but one feature is beyond a retailer's control: only some competitors collect sales taxes. This disadvantage is not created by the marketplace, but rather it is imposed by the current state of the law following the *Quill* decision, stifling retailers across the country.

In addition to the pricing disadvantage caused by sales tax being included in the cost of the purchase from the brick-and-mortar store, local stores also bear a significant compliance burden for collecting the tax. Compliance costs for small retailers are extremely high, placing them at more of a competitive disadvantage.[1] The national average annual state and local retail compliance cost in 2003 was 3 percent of sales tax collected for all retailers: 13.47 percent for small retailers, 5.20 percent for medium retailers, and 2.17 percent for large retailers.[2]

Brick-and-mortar retailers are major contributors to the health of local communities and should not be placed at a disadvantage compared to remote sellers that have no local presence. Brick-and-mortar sellers employ people in the community, pay state and local income taxes, as well as property taxes. They sponsor local causes like the Little League, soccer, and Booster Clubs.

Simplification is a key component for reform of the sales tax collection system for both brick-and-mortar sellers and remote sellers who voluntarily collect sales tax. Many members of the NRF voluntarily collect sales tax on remote sales into states where they do not have a physical presence. In many instances, the retailers that voluntarily collect sales tax do so only from states that have adopted the Streamlined Sales and Use Tax Agreement ("SSUTA") because of the Agreement's simplified collection requirements.

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[1] PricewaterhouseCoopers LLP, *Retail Sales Tax Compliance Costs: A National Estimate Volume One: Main Report*, April 2006. That study defined "small retailers" as having less than $1 million in annual retail sales.
[2] *Id*. That study defined "medium retailers" has having over $1 million and up to $10 million in annual retail sales, and "large retailers" as having over $10 million in annual retail sales.

Granting states the authority to collect sales tax from remote sellers will add significant resources to state budgets to support essential local services including teachers, police officers, firefighters and ambulance crews. Remote sales include e-commerce, mail order sales, telephone orders, and deliveries made across state lines. By 2012, total e-commerce sales are estimated to reach $4 trillion dollars.[3] Annual national state and local sales tax losses on e-commerce alone are conservatively expected to grow to $11.4 billion by 2012 for a six-year total loss of $52 billion.[4]

NRF is encouraged by this Committee's interest in this issue as well as the several legislative proposals that have been introduced this Congress to address sales tax fairness, especially the Marketplace Fairness Act, S. 1832, introduced by Senator Enzi, Senator Durbin, Senator Alexander, and Senator Johnson. NRF supports Congress granting states remote collection authority with simplifications that ensure retailers are not unduly burdened by collecting and remitting sales taxes. Congress needs to pass S. 1832 this year.

Background

Consumption taxes are imposed on the sale or use of goods and some services that are subject to tax. It is a tax on the consumer and is imposed where the consumption takes place. So all sales in a given state are subject to the sales tax, regardless of whether the sale occurs in a store in the state or in the home of a resident of the state through their computer or telephone. If Congress permits the state to only *collect* the sales tax on sales that occur in stores in that state and not sales that occur over the computer in that state, than Congress would be discouraging *intra-state* commerce because retailers that sell goods within the state are at a competitive disadvantage vis-à-vis remote sellers.

In 1992, the U.S. Supreme Court ruled in *Quill v. North Dakota* that "remote sellers" — a category that includes mail-order, telephone and Internet merchants — cannot be required to collect sales tax from customers in states where the merchant does not have a physical presence or "nexus." The court reasoned that the sales tax system was too complex for a merchant to know what sales tax to charge an out-of-state customer — 45 states and 7,600 local jurisdictions collect sales tax, each with its own rates, lists of taxable items and definitions of taxable items. But the justices suggested that sales tax collection could be required if the system were simplified and Congress authorized the collection authority because remote sellers are "purposely availing" themselves to a jurisdiction's authority by engaging in commerce.

In late 1999, in response to the Supreme Court ruling, states and the business community, including NRF, began the Streamlined Sales Tax Project, with an aim toward significant simplification of state sales tax systems. Since then, a baseline multi-state agreement, the SSUTA, which includes common definitions, uniform processes and procedures, and significantly simplified administrative features has been passed by 24 states (21 full member states and 3 associate member states), establishing the necessary groundwork for action by Congress. The 21 full member states with voting rights include: Arkansas, Iowa, Indiana, Georgia, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North

[3] Donald Bruce, William F. Fox, and LeAnn Luna, *State and Local Government Sales Tax Revenue Losses from Electronic Commerce*, University of Tennessee, April 2009, available at http://cber.utk.edu/ecomm/ecom0409.pdf.
[4] *Id*.

Carolina, North Dakota, Oklahoma, Rhode Island, South Dakota, Vermont, Washington, West Virginia, Wisconsin and Wyoming. Three associate member states with negotiating authority but delayed voting rights are Ohio, Tennessee and Utah. Delegates from the 24 states administer the SSUTA through the Streamlined Sales Tax Governing Board.

As electronic commerce continues to grow, so will the losses to state and local revenues.[5] In fiscal year 2012, it is conservatively estimated that state and local governments stand to lose at least $23.2 billion in uncollected sales and use taxes from remote transactions, with over $11.4 billion uncollected from e-commerce transactions.[6] General sales taxes make up roughly one third of state tax revenue.[7]

The Effect of Simplification on Retailers

Through adoption of the SSUTA, 24 states have already implemented significant simplification of their sales tax laws. This simplification has incentivized collection of sales tax by many remote sellers that currently are not required to collect sales taxes. For example, a large regional retailer with a significant national business through their Internet channel has even made the decision to collect sales tax on remote sales but only in states that have adopted the SSUTA.

Many remote sellers recognize that collecting sales taxes may be a more efficient approach to dealing with the realities of their constantly evolving business model. Nonetheless, their good faith effort to collect sales tax would be undermined by collection authority that did not include significant simplification steps.

While NRF believes that a modest small seller exemption for remote sales is appropriate, raising the level too high will only exacerbate the potential for inequity between a small remote retailer that does not have to collect any taxes and a local small retail competitor who must collect sales taxes on the first dollar of sales. Congress should resist the temptation to envision that a small seller exemption is the easy answer to meaningful small business regulatory relief.

Current Sales Tax Fairness Legislation before Congress

The two leading bills introduced this Congress to address the issue of sales tax fairness are the Marketplace Fairness Act and the Marketplace Equity Act.

(1) Marketplace Fairness Act of 2011, S.1832, sponsored by Senators Enzi, Durbin, Alexander and Tim Johnson provides a path for states to collect sales tax that incorporates a combination of either nine simplification steps or adoption of the SSUTA. The Marketplace Fairness Act exempts remote sellers with less than $500,000 in remote U.S. sales, requires a single audit by states and localities within a state, requires a single state tax rate based on the destination of the sale, states must establish certification procedures for software and service providers (to calculate

[5] *Id*.
[6] *Id*.
[7] Lucy Dadayan and Robert B. Ward, *State Revenue Report*, The Nelson A. Rockefeller Institute of Government, Oct. 2011, No. 85, available at http://www.rockinst.org/pdf/government_finance/state_revenue_report/2011-10-26-SRR_85.pdf.

rates), and gives remote sellers liability protection for relying on incorrect information supplied by service providers.

(2) Marketplace Equity Act of 2011, H.R. 3179, sponsored by Representatives Womack and Speier allows states to collect sales taxes from remote sellers if they meet three minimum simplification requirements. These three simplification requirements may be met in an interstate agreement, presumably including the SSUTA. Sellers with less than $1 million in remote U.S. sales or $100,000 in remote sales into a particular state are exempted. The three simplification steps are: (1) a single revenue authority within a state for submission of a return; (2) a single tax base set by the state; and (3) the state must choose a single tax rate from three choices: a blended rate of state and locality rates, the maximum state rate, or the destination rate.

Each bill grants states the authority to require remote sellers to collect sales tax on transactions into their respective state if simplification steps are adopted. The varying simplification requirements include tax base, tax rate, and collection software requirements. We generally prefer the "hybrid" structure of the Marketplace Fairness Act, which will allow states to choose between a state-based solution like the SSUTA or a set of federally mandated minimum simplification steps before gaining collection authority on remote sales.

Conclusion

The National Retail Federation has long supported sales tax fairness legislation, and we are encouraged by the momentum that is building toward a solution. We look forward to working with the Committee on legislation to ensure effective and fair sales tax collection while relieving burdens placed on a growing sector of the economy.