

Streamlined Sales Tax Project

A Report to the Legislature on the Streamlined Sales Tax Project

Board of Governance

Honorable John Chiang, Chairman, Board of Equalization
Honorable Steve Westly, State Controller and Chairman, Franchise Tax Board
Honorable Roy Ashburn, California State Senate
Honorable Debra Bowen, California State Senate
Honorable Rudy Bermudez, California State Assembly
Honorable Mark Wyland, California State Assembly
Ms. Anne Sheehan, Department of Finance

June 29, 2005

Report to the Legislature on the Streamlined Sales Tax Project (SSTP) as of **June 30, 2005**.

BOARD OF EQUALIZATION (BOE) STAFF PARTICIPATION

- BOE staff attended SSTP, Conforming States Committee and Implementing State meetings in:
 - Phoenix, Arizona – January 2005
 - Atlanta, Georgia – March 2005
 - Washington DC – April 2005
 - San Antonio, Texas – June 2005
- BOE staff reported to the Board of Equalization Members during the March 22, 2005, meeting on the status of California's involvement in the SSTP. Staff provided a brief history of the SSTP, the status of the Streamlined Sales and Use Tax Agreement (SSUTA), California's evolved participation in the SSTP, and an overview of issues relating to California, local taxing jurisdictions and businesses. Staff responded to questions from Board Members regarding staffing and workload issues.
- BOE staff met with staff representing the Senate and Assembly Revenue and Taxation Committees in April 2005, and provided an overview of the SSTP and California's involvement in the project. Staff from both committees conveyed an interest in the SSTP and efforts to analyze the SSUTA.
- BOE staff also met with representatives from the Legislative Analysis Office, the Department of Finance and the California Research Bureau in April 2005, to discuss the status of the SSTP and California's involvement in the project. The following issues were identified as concerns for California.
 - Destination sourcing
 - Administration of the Agreement
 - Uniform tax bases – the elimination of partial exemptions
 - Fee structure
 - Monetary Allowances
 - Voting authority – one vote per state
 - Database requirements

ACCESS TO SSTP INFORMATION

- California SSTP Internet Website

Information on California's involvement in the SSTP can be found at www.boe.ca.gov/sstp. This website can be accessed directly or through links found on the California State and BOE websites. This site allows users to view historical documents, review and comment on draft analyses of the SSUTA, access links to other related websites, and contact staff familiar with the project.

California's website now has a link available to the California State Library, California Research Bureau report, *The Streamlined Sales and Use Tax Agreement: A California Perspective*.

STATUS OF THE SSUTA

The Implementing States group met on April 16, 2005, to consider motions to amend the SSUTA. Sixteen original motions were submitted as required by Article IX, Section 901 of the SSUTA, allowing sixty days notice prior to consideration of the motions. Five substitute motions were proposed within the sixty-day period. Substitute motions can be proposed within the sixty-day period if they are germane to an original motion.

The Board of Governance (BOG) reviewed the 16 original and 5 substitute motions during their April 13, 2005, meeting. Authorization was given to the BOG representative to vote on behalf of California on 16 of the motions and abstain from the vote on the remaining 5 motions.

During the Implementing States meeting, 8 additional substitute motions were introduced and found to be germane to one or more of the original motions. Ultimately, 10 motions were voted on during the Implementing States meeting. California's representative was only authorized to vote on motions that were reviewed by the BOG and that met California's public notice requirements. Accordingly, California's representative participated in 3 votes on motions to amend the SSUTA.

The following is a summary of each motion to amend the SSUTA.

- Associate Membership

The SSUTA was amended to establish a two-tier membership into the Governing Board by creating an Associate Membership. An Associate Member will include any state not found in compliance with the SSUTA either because of a delayed effective date or by vote of all petitioning states. The first category of associate members will include any state that is found to have enacted all necessary conforming provisions, but with delayed effective dates. Provided the statutes or rules take effect on or before January 1, 2008, the state automatically will become a full member state upon the effective date of the provisions. The second category consists of any state that is found to have achieved substantial compliance with the SSUTA taken as a whole, but not necessarily with each provision as required and there is a reasonable expectation that the state will achieve compliance by January 1, 2008.

Associate Member states will be counted for the purposes of the thresholds that bring the SSUTA into effect. The Implementing States group will retain the authority to amend the SSUTA and issue interpretations of it until the 10 states/20% thresholds are met without the need to count associate members. Once that point is reached, the Governing Board, consisting of full members and associate members, will take over this responsibility. However, Associate Members will not be allowed to vote on amendments or interpretations to the SSUTA. Associate Members will have until January 1, 2008, to come into compliance with the SSUTA. There will be no Associate Members status after January 1, 2008.

Sellers volunteering to participate in the SSUTA may, but cannot be required, to collect sales and use tax on sales into the state until the Associate Member has been found in compliance with the SSUTA. A seller may volunteer to collect in one or more Associate Member State, but cannot be required to collect in each Associate Member State. Associate Member states will have limited access to information relating to sellers registered through the centralized registration system.

Associate Member States will be required to pay monetary allowances for sellers that volunteer to collect sales and use taxes in their state and will also be required to pay the \$20,000 initial assessment and annual dues while an Associate Member State.

California did not participate in this vote due to the late submission of a substitute motion.

- Business Advisory Council

The SSUTA was amended to reflect changes previously approved by the SSTP in the characterization of the Business Advisory Council (formerly the Business and Taxpayer Advisory Council) that recognize the autonomy of the Council and its nature as a forum for business interests. The Business Advisory Council will not be held to the same open meeting and operational rules as the Governing Board. Additionally, there will likely be more than one recognized Business Advisory Council.

California did not participate in this vote as directed by the BOG.

- Product Buy-downs – Sales Price

The SSUTA was amended to clarify the definition of “sales price” when that term includes consideration received by a seller from third parties (e.g., buy-downs or manufacturers’ coupons). Furthermore, it was provided that states may exclude from “sales price” either employee discounts that are reimbursed by a third party on sales of motor vehicles, or manufacture rebates on motor vehicles, or both. A series of examples were provided that states and businesses will use for guidance in the definition’s application. Member states will have until January 1, 2008 to conform to these provisions.

California did not participate in this vote due to the late submission of a substitute motion.

- Bundled Transactions

The SSUTA was amended to add the definition of “bundled transactions,” delete a section from the definition of “sales price” relating to the application of tax to bundled transactions, and to add rules relating to the application of tax to bundled transactions. The rules specify, among other things, that states are not restricted in their tax treatment of bundled transactions or in their ability to treat some bundled transactions differently from others.

However, a state must allow a provider of “telecommunication services” to establish from its books and records the portion of the total price of a bundled transaction that is attributable to products that are nontaxable (or subject to tax at a lower rate). Member states will have until January 1, 2008 to conform to these provisions.

California did not participate in this vote due to the late submission of a substitute motion.

- Exemption Administration

The SSUTA was amended to provide that relief from liability does not apply to a seller that accepts a completed exemption certificate for (1) an entity-based exemption that is not available in the state in which the seller is located and its unavailability is clearly indicated by the state (e.g., graying out exemption reason types on the uniform form and posting it on a state's web site as an indicator), or (2) an MPU exemption for tangible personal property other than software.

Another amendment expanded the good faith standard beyond sellers who obtain an exemption certificate at the time of purchase. A state must relieve a seller of liability if the seller obtains a fully completed exemption certificate, or captures the relevant data elements within 90 days after the date of sale. Furthermore, a seller may, within 120 days of a state's request for substantiation, prove that a transaction was not taxable by other means or obtain a fully completed exemption certificate from the purchaser taken in good faith. A state must also relieve a seller of the tax otherwise applicable if the seller obtains a blanket exemption certificate from a purchaser with which the seller has a recurring business relationship.

California did not participate in this vote due to the late submission of a substitute motion.

- Drop Shipments

The SSUTA was amended to provide that in the case of drop shipment sales, a member state must allow the third-party supplier (i.e. the drop shipper) to claim a resale exemption, regardless of whether the seller is registered to collect and remit sales and use tax in the state where the sale is sourced. Member states will have until January 1, 2008 to adopt this new language.

California voted "no" on this motion.

- Monetary Allowance

The Implementing States did not pass a motion that would have amended the SSUTA to provide a monetary allowance to sellers rather than to certified service providers (CSPs), and at a rate to be set by each member state, rather than by the Governing Board. Several states indicated that they would not support leaving the amount of the monetary allowance to each state. However, it was agreed that it would be incumbent on the Governing Board to make sure that any contract with a CSP would not require states to pay CSPs an allowance on sales where no revenue was received by the state.

California voted "yes" on this motion.

A group was appointed to study compensation issues and report back to the Implementing States group.

- Software and Multiple Points of Use (MPU)

The SSUTA was amended to require states to permit business purchasers of software delivered electronically, by load-and-leave, or in tangible form to give the seller an exemption certificate

claiming MPU. Use of the MPU exemption shifts to the purchaser the obligation to apportion and pay tax directly to each jurisdiction where concurrent use occurs. Previously, the SSUTA only required states to allow an MPU exemption for software delivered electronically.

Furthermore, when a seller knows that a product will be concurrently available for use in more than one jurisdiction, but the purchaser does not provide an exemption certificate claiming MPU, the seller may work with the purchaser to produce the correct apportionment using any reasonable method supported by their business records as they exist at the time the transaction is reported for tax purposes. If the purchaser certifies the accuracy of the apportionment and the seller accepts the certification, the seller is relieved of any further collection obligation, absent bad faith.

California did not participate in this vote due to the late submission of a substitute motion.

- Telecommunication Definitions

The SSUTA was amended to add a number of telecommunication related definitions. In addition, the definition of “sales price” was amended to allow states to exclude a separately stated charge for the installation, connection, change, or initiation of telecommunication services. The telecommunication sourcing provisions were also amended to account for a new definition of “prepaid wireless calling services.”

California did not participate in this vote due to the late submission of a substitute motion.

- Open Meeting Rules

The SSUTA was amended to allow closed Governing Board meetings to consider pending litigation when the Governing Board is a party to the litigation. The SSUTA already allows closed meetings when a member state is a party to the litigation.

California voted “yes” on this motion.

The SSUTA will become binding and take effect when at least 10 states comprising at least 20 percent of the total population, as determined by the 2000 Federal census, of all states imposing a state sales tax have been found to be in substantial compliance with the requirements of the SSUTA as a full Member or as an Associate Member. The SSUTA will take effect on the first day of the calendar quarter at least 60 days after the tenth state is found to be in compliance. Twenty-one states have passed legislation in an attempt to conform to the SSUTA.

To date, 18 states have petitioned for membership in the SSUTA and submitted a certificate of compliance to document compliance with the provisions of the SSUTA and cite applicable statutes, rules, regulations, or other authorities evidencing such compliance.

COMPARATIVE ANALYSIS OF SSUTA

The comparative analysis currently underway by BOE staff involves a detailed review of each section and definition of the SSUTA and a comparison to California’s Constitution, statutes, regulations, Policy and Procedure Manuals, and other information relating to the administration of sales and use tax. The SSUTA

is comprised of 82 sections and 39 definitions. The analysis will strive to identify the impact of conforming to the SSUTA in the following areas:

- Changes necessary to California's Constitution, statutes, regulations, Policy and Procedure Manuals;
- Tax revenues, including revenue shifts for local jurisdictions;
- Administrative and operational costs for the state and local governments;
- Compliance and cost issues for businesses; and
- The responsibility of the Governor, California Legislature, BOE, and courts.

The analyses for the following sections of the SSUTA are complete.

- 309 - Application of General Sourcing Rules and Exclusions from the Rules
- 310 - General Sourcing Rules
- 311 - General Sourcing Definitions

Sections 309 and 310 require further study to determine the impact conforming to these sections would have on the state, local governments and businesses. Accordingly, the analyses of these sections have been forwarded to the BOE's Research and Statistical Section for further action.

SSUTA Section 302, State and Local Tax Bases, will be the next section available for review followed by Section 313, Direct Mail Sourcing, Section 326, Direct Pay Permit, the definition for "direct mail" and Section 308, State and Local Tax Rates.

SSTP MEETING SCHEDULE

A Petitioning States meeting is scheduled for June 30 and July 1, 2005, in Chicago, IL.

This meeting is being held for the purpose of reviewing the compliance of the Petitioning States with the terms of the SSUTA. The following states will participate in this meeting and will vote on each state's compliance with the SSUTA. Petitioning States cannot vote on their own compliance.

Arkansas
Indiana
Iowa
Kansas
Kentucky
Michigan
Minnesota
Nebraska
Nevada
New Jersey
North Carolina
North Dakota
Ohio
Oklahoma
South Dakota

Tennessee
Utah
West Virginia
Wisconsin
Wyoming

SUMMARY

BOE staff will continue to attend and monitor SSTP meetings and observe the activities of other participating states. Work on the comparative analysis of the SSUTA will move forward with an estimated completion date in early 2007.

BOE staff will continue to work with local government and business representatives regarding the analysis of the SSUTA and any new emerging issues.