Testimony of

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On the Issue of

Exploring Alternative Solutions on the Internet Sales Tax Issue

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Chairman Goodlatte, Ranking Member Conyers and Members of the Committee, I am Joe Crosby, a principal with MultiState Associates. I have devoted most of my professional life to state tax policy questions, and in particular, to state taxation of interstate commerce.

I appreciate the opportunity to testify today. I advise many businesses and trade associations on state tax policy issues, and my firm works closely on sales tax collection issues with several large retailers and their associations. However, I do not appear here on behalf of any client. The views I will express reflect my independent professional judgment.

Advisory Commission on Electronic Commerce

Fifteen years ago, I testified before the federal Advisory Commission on Electronic Commerce. In reviewing that testimony in preparation for today, I was struck by the fact that, in many ways, little has changed in the intervening period with regard to the issue before you, which is how best to facilitate collection of sales taxes on remote sales.

My comments from 1999 still ring true:

> Simplification of the sales and use tax system is the only solution. Simplification is the only solution that removes an objectionable burden from vendors without shifting a burden to other parties. Simplification is the only solution that can lead to a level playing field, which I define as an equitable, consistent, easily administered, and technologically-neutral sales and use tax system.

If, as I contend, my assertion was correct then and remains correct now, why has simplification failed to take root in all sales tax states? Why have many of the sales tax states declined to adopt the Streamlined Sales and Use Tax Agreement?

Streamlined Sales and Use Tax Agreement

Today, the benefits of the Streamlined Agreement today accrue primarily to sellers. The sales tax simplifications within the Streamlined Agreement benefit sellers by reducing the administrative costs and uncertainty associated with sales tax collection. The mere fact that 24 states now have identical administrative provisions and definitions also drives reduced costs for sellers. The only direct benefit for states that are party to the Streamlined Agreement is a modest revenue stream from approximately 2,000 sellers who have volunteered to collect sales taxes in all Streamlined states. The real potential

benefit to states, gaining from Congress the authority to require remote sellers to collect legally owed sales taxes, has yet to be realized.

Viewed from that perspective, it is surprising that 24 states have simplified and made uniform their sales tax systems despite receiving little direct benefit. For the states that have not adopted the Streamlined Agreement, the pain of simplification today is greater than the potential future benefit of federal authorization of remote sales tax collection.

There are two main stumbling blocks to the remaining states adopting the Streamlined Agreement. The first, and most obvious, is that there is no guarantee that adopting the Streamlined Agreement will lead to collection of legally due sale taxes by remote sellers. As I testified fifteen years ago, "States may be unwilling to embark on such a radical change to any major component of their revenue systems without a clear idea of the exact level of change [that the Congress will demand]." Unless and until the Congress sets forth a clear path by which states can obtain the authority to require remote sales tax collection, there is no incentive for the remaining states to simplify their sales tax systems.

The other stumbling block is that the Streamlined Agreement requires states to make changes to their sales tax systems that apply both to remote and intrastate activity. As noted in the hearing summary, "many states…are hesitant to surrender autonomy over their internal taxing policy."

The initial decision for the Streamlined Agreement to apply both to remote and intrastate activity was well considered. From many perspectives, it remains the correct decision. The goal of the Streamlined Agreement was not merely to obtain authority to require remote sellers to collect tax, but also to make the sales tax system less burdensome and more efficient for all sellers. That was and is a laudable goal, but it has proved thus far too ambitious for many states in the absence of a Congressional guarantee that the effort will be rewarded.

An Alternative Framework: Simplification for Remote Sellers and Remote Sales

An alternative framework would be to fashion an interstate agreement that applied only to remote sellers and remote sales. Such an agreement would allow states to retain full autonomy over intrastate sales while providing sufficient simplification and uniformity to minimize the sales tax collection burden on remote sellers.

Such an alternative framework must be defined by Congress. After fifteen years of difficult substantive and political discussions among state and local governments, the existing Streamlined Agreement states would have no inclination to make further changes to their

sales tax systems without certainty that those changes would automatically provide authority to require remote sales tax collection. And the states that never adopted the Streamlined Agreement because of skepticism that Congress would ever grant such authority will undoubtedly take continued Congressional inaction as proof of their position.

Like the existing Streamlined Agreement, the alternative framework would require numerous, specific elements, but those elements would be directed at remote sellers and remote sales only. The necessary elements fall into three buckets.

The first bucket includes substantive simplifications to minimize the burden of tax administration. Examples of these simplifications include a single point of registration for sales tax collection in all states, a single uniform sales tax return, and a single point of remittance for sales taxes for all states.

Theoretically, this bucket could also include simplifications to sales tax bases, rates and sourcing regimes for remote sales but not for intrastate transactions. Addressing bases, rates and sourcing, however, would create challenges for taxpayers (purchasers) and nexus (in-state) sellers. A taxpayer could be placed in the position of having a tax liability in a state different than the tax collected by the remote seller because of base, rate or sourcing differences between the federal standards and state law. Similarly, sellers would carefully need to determine, for each state, whether they are “remote” or “nexus” sellers and follow the appropriate federal or state rules. Such a determination is not easily made, and the status of a seller as “remote” or “nexus” in a state is subject to change based on the activity of a single employee (where such activity is unlikely to be known by those in the company required to comply with sales tax laws).

The second bucket addresses software and related services to facilitate the collection of tax under a simplified system. Remote sellers would have the option to choose from different software and service providers whose programs work in all sales tax states, and that software and related services would be provided free of charge to the remote seller. The software would be required to be capable of calculating sales and use taxes due on each sale at the time the sale is completed, filing sales and use tax returns and being updated to reflect tax rate changes or tax base changes. It may also be advisable to include provisions to address the costs remote sellers will face to integrate such software into their existing systems.

The final bucket deals with sales tax audits and enforcement. The alternative framework should include a “consolidated audit agreement” among the states that provides that one state shall have the authority to audit a remote seller on behalf of all states. The remote seller should have the option to challenge the findings of such an audit in the state of its

choosing. The alternative framework should also exempt smaller sellers that use certified software from being subject to audit at all.

The appropriate level at which to set the small seller audit exemption is a purely a question for the Congress, but recent research from the Small Business Administration (SBA) is helpful in this regard. According to the SBA study, there are more than 5 million online sellers. The vast majority of those sellers are very small; if the threshold for audit exemption was set at $5 million in annual sales, then, according to the SBA, only 750 online sellers would be subject to audit. In other words, a $5 million threshold would exempt 99.99% of all online sellers from audit. A threshold of $1 million would exempt 99.96% of all online sellers; $500,000 would exempt 99.93% of online sellers; and a threshold as low as $150,000 would still exempt 99.76% of all online sellers.

Last year, the Committee on the Judiciary released a set of seven principles by which it would evaluate proposals to facilitate the collection of sales taxes on remote sales. I have attached at the end of my testimony an evaluation showing how this alternative framework adheres to the principles along with a discussion of various options to implement the principles in a legislative proposal. This alternative framework should be designed to dovetail with the existing Streamlined Agreement wherever possible. Although the alternative framework is limited to remote sales, it would act as a floor, not a ceiling, for state simplification efforts. In other words, it would not prevent a state from extending the benefits and protections for remote sales and remote sellers to intrastate sales and nexus sellers, if the state so chooses to do so.

One caveat to this alternative framework, which I alluded to previously, is that it would create, de facto, two different sets of sales tax rules with which most sellers would be required to comply. The vast majority of sellers, both online and offline, are nexus sellers in some states and remote sellers in others. According to the aforementioned SBA report, large internet sellers—the top 750—currently collect sales tax in an average of 18 states. A federal law that differentiates between nexus and remote commerce will require sellers to comply with two different sets of sales tax rules depending upon their status as a nexus seller or remote seller. If the alternative framework is limited to administrative simplifications and protections for remote sellers, compliance with two sets of rules will be less difficult for such “dual status” sellers than if the alternative framework implicates the imposition of tax and taxability determinations (product definitions, sourcing, tax rates, etc.).

A second caveat to the alternative framework is that it creates an incentive for states to narrow the pool of remote sellers to the greatest extent possible. In other words, if the simplifications and protections are only afforded to sellers defined in federal law as “remote sellers,” states will have an intrinsic interest in stretching the concept of nexus as

much as possible and to assert that sellers are “nexus” and not “remote.” This is not a trivial issue: distinguishing between nexus and remote sellers essentially guarantees, over time, that the simplifications and protections provided by federal legislation will be enjoyed by an ever diminishing set of sellers.

Other Options

Four other options are being presented to you today. Interestingly, three of them are not the least bit novel. Origin sourcing, reporting by remote sellers to facilitate use tax collection and the International Fuels Tax Agreement model were all discussed and debated during the proceedings of the Advisory Commission on Electronic Commerce. In fact, all three concepts had been considered and rejected as incomplete solutions by state tax policy experts, economists and legal scholars even before that Commission began its work. The final concept—banning interstate commerce—is indeed new and speaks for itself.

Origin Sourcing

Origin sourcing is peddled as the simplest of all solutions: retailers must know and comply with only one set of sales tax rules. It avoids requiring a retailer to comply with a “foreign” state’s tax laws. It is also alleged to promote tax competition.

It is true that origin sourcing is simple, but it is better characterized as simplistic. In return for simplifying tax collection for sellers and ensuring that they are required to comply only with tax laws in states in which they have a physical presence, origin sourcing requires your constituents to pay taxes to other states, states in which they may never set foot and have no vote. The only way a taxpayer can avoid paying taxes to another state under origin sourcing is to never purchase goods from an out of state seller. Origin sourcing is the ultimate manifestation of taxation without representation.

The flaws of origin sourcing do not stop there. It also acts as a de facto tax on exports and a complete tax exemption on imports. To be clear, origin sourcing would exempt all foreign sales into the United States from sales tax and would impose sales tax on many exports from the United States to foreign countries. This is but one of the many reasons that no modern economy employs origin sourcing for cross border sales (or consumption) taxes.

Finally, the assertion that origin sourcing promotes tax competition is misguided at best. States like Florida and Texas attract residents for many reasons, one of which is the lack of a personal income tax. That is tax competition: people move to those states to benefit

from what they perceive to be a superior tax system. Residents of those states are well aware that the government they demand requires a certain level of resources, and, consequently, sales taxes in those states are above the national average. Suggesting that tax competition is furthered when a Florida or Texas resident places an order from an online company whose "origin" is in a state without sales tax is farcical. That is not tax competition; it is tax arbitrage and should not be encouraged by the federal government.

For these reasons, Professor Charles McLure, a senior fellow with the Hoover Institution and former official in the Treasury Department under President Reagan, testified against origin sourcing for state sales taxes in a hearing before the Senate Committee on the Budget 14 years ago. He also presented at that time an "Appeal for Fair and Equal Taxation of Electronic Commerce," which opposed origin sourcing and was signed by more than 170 tax economists and professors of law.

Reporting and Use Tax Collection

A second concept is to require remote sellers to report sales to the purchaser's home state. The state would then use this information to enforce its use tax. This approach has been attempted by states before, both cooperatively and by mandate. In the late 1990s, groups of states in both the Northwest and Northeast entered into agreements with each other and with businesses to share information that would facilitate use tax collection. The results of these efforts were not encouraging. More recently, Colorado and a few other states have attempted to mandate different types of notification and reporting.

Congress has authority to make some type of reporting mandatory. At best, however, mandatory reporting and use tax collection is a poor alternative to collecting the appropriate tax at the time a transaction is completed. Taxpayers would be required annually, or perhaps more frequently, to compile all of the notifications they receive from all remote sellers they patronize and complete a use tax return reporting—and paying—unpaid taxes. In aggregate, taxpayers would be required to file hundreds of millions of additional tax returns annually, and states would be required to process and audit those returns. Some consumers may endeavor to avoid making purchases from remote sellers in an effort to avoid the filing burden and need to make payment in a lump sum rather than on each transaction.

The larger concern with this approach relates to those audits. A remote seller would not simply be able to report to states the total amount of purchases made by a taxpayer in a year, or even the amount of each transaction made in a year. That information would be useless from a tax compliance perspective, because not all sales are taxable. Indeed, a remote seller would be required to report line item detail of each and every item a taxpayer purchased. One need not be a privacy expert to appreciate the implications of

such reporting. Consumers are unlikely to be comfortable with tax administrators having detailed information about their purchases of books, movies, medical devices, prescription drugs, entertainment products, etc. In fact, a federal district court, in a case involving North Carolina, held that such detailed reporting violates the First Amendment of the United States Constitution and the federal Video Privacy Protection Act.

The Congress has authority under the Commerce Clause to mandate some type of reporting. However, the First Amendment may bar the Congress from requiring the type of reporting sufficient for tax administrators to determine whether an item that has been purchased from a remote seller is taxable. Without that information, there can be no enforcement of the use tax, placing us back in exactly the position we are today.

Some have suggested these privacy concerns can be avoided by creating a federal database, or imposing an unfunded mandate on states by compelling them to fund reporting regimes run by third parties without providing the states with the authority to require collection at the time of sale. These are desperate efforts to overcome the fundamental flaws with such a regime. Clearly, the concept of reporting alone is no solution to the problem at all.

International Fuels Tax Agreement

Finally, I turn to the International Fuels Tax Agreement (IFTA) as a model for remote sales tax collection.

The IFTA was initiated in 1983 by Arizona, Iowa and Washington as an effort to ease fuel tax compliance for states and interstate commercial motor vehicles. In 1984, the Congress supported a National Governors Association (NGA) working group that incorporated IFTA and a regional fuels tax agreement between northeastern states. By 1990, 16 states had adopted the model created through the NGA process. IFTA became mandatory through the 1991 enactment of the Intermodal Surface Transportation Efficiency Act (ISTEA). ISTEA prohibited states from enforcing fuel taxes on interstate carriers after 1996 unless the state complied with IFTA.

IFTA operates on a “base jurisdiction” model. The base jurisdiction is the state where the qualified motor vehicle (QMV) is registered. Under the model, QMVs continue to pay fuel taxes at the time of purchase. QMVs also track miles traveled in each jurisdiction. QMVs file a quarterly return with the base jurisdiction indicating taxes paid in each jurisdiction and miles traveled in each jurisdiction. The base jurisdiction collects additional taxes due from, or pays refunds owed to (in aggregate) the QMV. The base jurisdiction, operating through a clearinghouse maintained by the International Fuel Tax Association, Inc., distributes revenue owed to/from the various states in which the QMV operated during the

preceding quarter. Finally, the base jurisdiction has responsibility for auditing QMVs on behalf of all IFTA jurisdictions.

The Streamlined Agreement was initiated by the NGA and the National Conference of State Legislatures (NCSL). Given those organizations' roles in developing and implementing IFTA, there has been discussion since the beginning of the Streamlined Agreement regarding the IFTA model and its applicability to sales taxes. In many ways, the Streamlined Agreement mirrors IFTA (uniform definitions, Streamlined Sales Tax Governing Board, Inc. to administer the agreement, a single system to register sellers in all jurisdictions, certified software providers for sales tax compliance, etc.).

Despite these similarities, there are fundamental political and substantive considerations that work against the base jurisdiction concept for remote sales tax collection.

The first political consideration is that the IFTA was broadly supported by the affected industry. In the sales tax arena, there are deep differences within the remote seller community. IFTA is also targeted at taxpayers; QMVs had nexus and an obligation to pay, and taxes were being collected. The only question was administrative simplification for taxpayers and states. Finally, fuel taxes, although an important source of revenue, are dwarfed by sales tax revenues. Fuel taxes are a dedicated revenue source more akin to a user fee, while sales taxes are general fund revenue sources in nearly every state (and locality) in which they are levied. States (and localities) will be very reluctant to relinquish control over a significant portion of their first or second largest general revenue source to their sister states.

From a substantive perspective, as is the case with QMVs, remote sellers currently must register to collect sales tax in their "base jurisdiction." Unlike QMVs, sellers with operations in multiple states cannot choose a single jurisdiction as a base jurisdiction; they must register to collect in each state in which they have a store or operation. Thus, for sellers who have a location in more than one state and sell remotely into other states, there is an initial question regarding which jurisdiction is the base jurisdiction. Perhaps it could be the jurisdiction where orders for remote sales are received, accepted and/or shipped, but for larger remote sellers those activities are likely geographically distributed as well.

Along the same lines, a seller will be a nexus seller in some states and a remote seller in others. How is the base state auditor easily to distinguish between nexus sales, on which tax should have been collected and remitted to the destination state, and remote sales, on which taxes should have been collected and remitted to the base state for further distribution to the destination states? The status of a seller in each state (as nexus or remote) will also change over time, perhaps frequently. That would require the seller to

register and terminate registration in nexus states and shift tax collection to/from the base jurisdiction.

Assuming these hurdles are crossed, the next one up is sheer number of taxable goods and services and the lack of uniformity among the states with regard to defining those goods and services. With IFTA, there is essentially only one product being sold: diesel fuel. There is one rate per state (there are no local rates or base differences). There are also no exempt goods or services or exempt purchasers (QMVs are by definition not exempt from fuels taxes). Thus, there are no real questions on audit regarding whether the good or service being sold was subject to tax, or whether the purchaser buying the good or service was subject to tax. In other words, the IFTA audit function is essentially an audit of the QMV's records of miles traveled and taxes paid.

Furthermore, all states participating in IFTA levy fuel taxes. If a base jurisdiction model were applied to sales tax, states without a sales tax, and thus no competency to audit sales tax, would be required to audit sales tax. Even states with sales taxes would be hard pressed to fairly audit based on the laws of other states. Finally, it could be argued that imposing a base state model, particularly on a state that does not have a sales tax, is an unfunded federal mandate.

Some of these hurdles may be able to be overcome, especially in the context of seller use of certified service providers (CSPs). With a CSP model, the audit could be limited to the CSP rather than the seller. However, absent a mandate that sellers use a CSP, or seek certification of their own compliance systems, a base jurisdiction model would require states to audit based on laws they are unfamiliar with, which could be a detriment to sellers.

The IFTA model is valuable and has informed the Streamlined Agreement as well as the alternative framework I have presented here. However, the IFTA cannot simply be bolted on as a solution to the problem of remote sales tax collection.

Conclusion

I began my testimony noting that, in many ways, little has changed with regard to this debate in the past fifteen years. In other ways, however, the differences between then and now are stark.

- **State Legislatures:** Fifteen years ago, sales tax simplification was only an idea. Now, 24 states have implemented significant simplifications and harmonized definitions, administrative provisions and other critical features of sales taxes while

maintaining sovereignty over fundamental aspects of their tax systems. This is a better track record than the IFTA had before it was mandated by Congress.

- **State Governors:** Governors across the country strongly support Congressional action to authorize remote sales tax collection. Governors who have spoken or acted in favor of a level playing field for all sellers include Paul LePage (ME), Mike Pence (IN), Chris Christie (NJ), Rick Snyder (MI), Robert Bentley (AL), Gary Herbert (UT), Butch Otter (ID), Nathan Deal (GA), Bill Haslam (TN) and Dennis Daugaard (SD).

- **Technology:** Software to calculate sales taxes due, remit taxes collected and file tax returns has advanced dramatically. For several years now, remote sellers who have volunteered to collect under the simplified system in the Streamlined states have had access to several software and service providers, free of charge, to handle sales tax administration.

- **Ecommerce:** According to the Census Bureau, ecommerce is ten times larger as a percentage of retail sales than it was fifteen years ago, rising from 0.7% of total retail sales in Q4 1999 to 7.0% of total retail sales in Q4 2013. Ecommerce has grown at double digit rates for 17 consecutive quarters and for all but six quarters since records were first kept.

- **State Tax Reform and Tax Reductions:** The two worst state fiscal recessions since the end of World War II have occurred in the past fifteen years. In response to revenue volatility, expected reductions in future federal revenue sharing and changes in the economy, elected state leaders are proposing bold reforms to make their economies, and our country, more competitive. In the past year alone, more than 10 states have debated extensive reforms that would decrease taxes on returns to investments in people, property and capital and instead relied more heavily on consumption taxes. These proposals all are projected to increase employment, raise wages and attract investment. Erosion of the sales tax base from uncollected taxes on remote sales seriously undermines these efforts. Already, eleven states have adopted or are considering proposals dedicating new revenues from remote sales tax collection to cuts in other taxes.

Some have asked why there is urgency to address this issue. There is urgency because retailers who have invested in your communities are at a severe disadvantage to those who have not because of government policies. The urgency is about government picking winners and losers in the marketplace which results in actual job losses in your districts. There is urgency because state and local governments do not have the luxury of borrowing to balance budgets or of time to kick problems down the road.

This is not about retailers with outdated business models not wanting to compete. This is about businesses that have made investments in your communities and their inability to compete on a level playing field in terms of tax policy with their online only counterparts who have not made a similar investment. It is not about state and local governments asking for new revenue. It is about elected state and local leaders who have made tough decisions to reform their sales tax systems but are hamstrung in their efforts by Congressional inaction. It is not about protecting consumers who, knowingly or not, evade tax laws. It is about easing the tax compliance burden on your constituents who make an honest effort to fulfill their duty as citizens and pay taxes they legally owe.

Mr. Chairman, I again thank you for the opportunity to speak before this Committee today. I welcome any questions that you or the Committee members may wish to pose.

Appendix: Comparison of Alternative Framework to Committee on Judiciary Principles on Internet Sales Tax

Tax Relief

Principle: Using the Internet should not create new or discriminatory taxes not faced in the offline world. Nor should any fresh precedent be created for other areas of interstate taxation by States.

Discussion: The Internet Tax Freedom Act, which expires in 2014 and which prohibits new or discriminatory taxes on online commerce, addresses the first sentence of this principle.

Under the Commerce Clause, as interpreted by the U.S. Supreme Court, sellers that do not have substantial nexus with a State—Remote Sellers—are not required to collect sales tax due on transactions with customers in the State. Any federal legislation seeking to rectify the disparity between Remote Sellers and those who are required to collect—Nexus Sellers—must, by definition, grant authority to the States to compel Remote Sellers to collect tax. To satisfy this principle, that grant of authority must be narrowly construed so that it applies only to the collection of State and local sales and use taxes and not to other taxes.

Implementation Options:

1. Provide that the Act shall not be construed as authorizing a State to subject a Remote Seller or any other person to franchise, income, occupation, or any other type of taxes other than sales and use taxes, affecting the application of such taxes, or enlarging or reducing State authority to impose such taxes.
2. Provide that the Act shall not be construed to create taxable nexus or alter the standards for determining taxable nexus between a person and a State or local jurisdiction.
3. Provide that nothing in the Act shall be construed as encouraging a State to impose sales and use taxes on any products or services not subject to taxation prior to the date of the enactment of the Act.
4. Provide that the sole recourse for States to require Remote Sellers to collect sales tax is to meet the requirements of the Act (“field preemption”).

Tech Neutrality

Principle: Brick & Mortar, Exclusively Online, and Brick & Click businesses should all be on equal footing. The sales tax compliance burden on online Internet sellers should not be less, but neither should it be greater than that on similarly situated offline businesses.

Discussion: As a result of the U.S. Supreme Court's interpretation of the Commerce Clause, Remote Sellers have two distinct advantages over Nexus Sellers. First, Remote Sellers cannot be legally required to collect tax, and thus Remote Sellers do not bear the administrative burden of sales tax collection that Nexus Sellers bear. Second, because few taxpayers actually pay use tax where sales tax is not collected, Remote Sellers also enjoy, in most of the country, a non-trivial price advantage over Nexus Sellers. It is worth noting that only non-U.S. businesses can be a Remote Seller in every State (U.S. businesses have substantial nexus with at least one State even if that State does not impose a sales tax) and that only some businesses are Nexus Sellers everywhere. Most businesses are Remote Sellers in some States and Nexus Sellers in others.

Implementation Options: The alternative framework would authorize States to require all sellers to collect sales tax on Remote Sales. To address the burden the may place on Remote Sellers, the Act would require States to simplify the administration of sales tax as a precondition for being granted the authority to require Remote Sellers to collect tax. There are nearly as many opinions as to what constitutes "true simplification" as there are people involved in the debate. The following list focuses on the simplifications that are most meaningful to Remote Sellers. It is worth noting that simplifying collection for all sellers has value in and of itself and benefits the economy overall.

1. Authorize States to require all sellers to collect and remit sales and use taxes, but only as long as the State implements legislation that includes certain Minimum Simplification Requirements.
2. Allow sellers to challenge a State's assertion that it has met the Minimum Simplification Requirements and incorporate provisions to terminate a State's authorization if it no longer satisfies the Minimum Simplification Requirements.
3. Require States to publish notice of intent to exercise authority under the Act, with a sufficient minimum period (e.g., 180 days) following the enactment of this Act and the publishing of such notice.
4. Require States to adopt, via legislation, the "Minimum Simplification Requirement" that:
    a. specifies the tax or taxes to which the authority granted by the Act applies and specifies any products or services otherwise subject to the tax or taxes identified by the State to which the authority of this Act shall not apply;

b. provides for a single, central registration system for all States;
c. identifies a single entity within the State responsible for all State and local taxing jurisdiction, sales and use tax administration and return processing;
d. provides for a single, uniform sales and use tax return for use in all States, including and all local taxing jurisdictions within the States, and provides that a Remote Seller is not required to file sales and use tax returns any more frequently than non-Remote Sellers;
e. provides for a single point of remittance (which could be a single State) for Remote Sellers for all States in which the Remote Seller makes Remote Sales;
f. provides that a Remote Seller is not subject to any requirements that the State does not impose on non-Remote Sellers;
g. provides a uniform sales and use tax base among the State and local taxing jurisdictions within the State;
h. provides for the sourcing of Remote Sales consistent with the Act;
i. defines a "Taxability Matrix" as a publication indicating what sales of tangible or intangible products or services are subject to or exempt from the sales and use tax;
j. provides a Taxability Matrix, and provides that sellers shall have no liability to the State for an error was the result of any reasonable interpretation by the seller of the State's Taxability Matrix;
k. provides for the publication of a rate and boundary database by each State, and provides that any person relying on such database shall have no liability to the State or local taxing jurisdictions within the State for the incorrect collection, remittance, or noncollection of sales and use taxes, including any penalties or interest; and,
l. provides at least 90 days notice of a rate or base change by the State or any local taxing jurisdictions within the State and provides that sellers shall have no liability to the State or local taxing jurisdictions within the State for the incorrect collection, remittance, or noncollection of sales and use taxes if sufficient notice of a rate or base change was not provided.

5. Require States to provide certified software free of charge to Remote Sellers that calculates taxes and files returns in all States authorized under the Act, provides all sellers using certified software with protection from liability, and provides transitional assistance to Remote Sellers to offset implementation costs associated with such software.

No Regulation without Representation

Principle: Those who would bear State taxation, regulation and compliance burdens should have direct recourse to protest unfair, unwise or discriminatory rates and enforcement.

Discussion: Under current law, taxpayers—consumers—have direct recourse to protest unfair, unwise or discriminatory sales tax rates and enforcement through their State legislatures and courts. That right remains unaffected by any proposed Congressional response to this issue.

A Congressional grant of authority to the States permitting them to require Remote Sellers to collect tax heightens the Remote Seller's exposure to potential audits or other enforcement actions by States in which the Remote Seller has no physical presence.

To minimize this potential burden, the Remote Seller should benefit from: 1) a single audit for all jurisdictions in which the Remote Seller makes Remote Sales; 2) the right to protest any assessment arising from such an audit in the jurisdiction of the Remote Seller's choosing; and 3) a small seller exemption for Remote Sellers using a certified software provider.

Together, these provisions would minimize the audit burden on a Remote Seller and ensure that the Remote Seller has recourse to its State courts in the event of a disputed audit finding.

Additionally, it may be appropriate to exempt certain remote sellers, as discussed below, from audits and other enforcement actions.

Implementation Options:

1. Provide for a "Consolidated Audit Agreement" among the States that provides that one State shall have the authority to audit a Remote Seller on behalf of all States under the authority granted by the Act. States which choose not to enter the agreement are prohibited from auditing the Remote Seller.
2. Provide that the result of any audit conducted under the Consolidated Audit Agreement is binding on the State and local taxing jurisdictions within that State, unless such results are challenged by the Remote Seller.
3. Provide that assessments based upon an audit conducted pursuant to a Consolidated Audit Agreement shall be reviewable by a court of competent jurisdiction in any State which is a party to the Consolidated Audit Agreement upon the consolidated appeal by the Remote Seller.

4. Exempt Remote Sellers which use certified software and which fall below a certain sales threshold from audit. According to a Small Business Administration (SBA) study, there are more than 5 million online sellers. The vast majority of those sellers are very small; if the threshold for audit exemption was set at $5 million in annual sales, then, according to the SBA, only 750 online sellers would be subject to audit.

Simplicity

Principle: Governments should not stifle businesses by shifting onerous compliance requirements onto them; laws should be so simple and compliance so inexpensive and reliable as to render a small business exemption unnecessary.

Discussion: As discussed under "Tech Neutrality" (above), reducing compliance burdens will benefit Remote Sellers large and small. In addition to providing equal footing for all sellers, reducing the administrative burden imposed by State and local sales taxes reduces deadweight loss in the economy and frees up those resources for productive investments.

Implementation Options: see implementation options under Tech Neutrality.

Tax Competition

Principle: Governments should be encouraged to compete with one another to keep tax rates low and American businesses should not be disadvantaged vis-a-vis their foreign competitors.

Discussion: The current State and local sales and use tax system encourages competition between the States for residents. Individuals are free to choose between governments that impose no or low sales taxes or higher sales taxes (perhaps in lieu of other taxes, such as income taxes).

On a more granular level, State and local governments compete by exempting whole segments of commerce (e.g., excluding services from the sales tax base) or specific areas to encourage investment (e.g., exempting manufacturing machinery and equipment from sales tax).

Finally, all States incorporate destination based sourcing for Interstate Sales, which ensures that exports are free from sales tax and imports (either from another State or

another country) are on equal footing, from a sales tax perspective, with domestically produced goods or provided services.

Implementation Options: The alternative framework is open to, but does not require, a uniform tax base among all the States and a single tax rate per State. Those elements tend to diminish tax competition between State—and local—governments. The following options to promote tax competition are limited by the simplification concepts enumerated previously; in other words, States' flexibility in this area should not trump the need for a reduced compliance burden.

1. Allow States to define their own tax bases (i.e., to determine whether a product or service should be taxable or exempt).
2. Allow States to set their own tax rates
3. Avoid sourcing regimes or other provisions which would effectively exempt from tax foreign commerce (e.g., a pure origin sourcing regime would impose tax on exports but make imports tax exempt).

States' Rights

Principle: States should be sovereign within their physical boundaries. In addition, the federal government should not mandate that States impose any sales tax compliance burdens.

Discussion: Tax Competition and States' Rights are related, and the implementation options under Tax Competition fit equally well here. The principle of States Rights' brings into consideration two additional issues: 1) the treatment of intrastate sales; and, 2) an overarching concern that the Act not tread on State and local governments beyond that which is required to solve the current problem.

Implementation Options:

1. Provide that the Act does not affect intrastate sales.
2. Provide that the Act does not impose any new taxes or regulatory requirements and does not require States to impose any new taxes or regulatory requirements.

Privacy Rights

Principle: Sensitive customer data must be protected.

Discussion: Federal and State laws currently provide for the protection of sensitive taxpayer (i.e., customer) data. Those laws generally extend not only to federal and State employees who have access to sensitive taxpayer data, but also to third party contractors and others, such as sellers and employers, who may be compelled by governments to participate in the tax collection structure.

Implementation Options: Presuming that existing federal and State laws protecting sensitive taxpayer data are sufficient, the Act could simply refer to those laws. Alternatively, the Act could set a standard for the protection of sensitive taxpayer data that States must meet in order to exercise the authority granted in the Act (similar to the grant of authority being conditioned on adoption of the Minimum Simplification Requirements).