Internet Tax Simplification: Is It Really That Simple?

Submitted By: The Direct Marketing Association

Under the Supreme Court's Quill decision out-of-state sellers with no physical presence in a state or "nexus," are not required to collect sales tax when selling into a state. However, under Quill, Congress with its Interstate Commerce Clause authority could grant the states the right to force out-of-state companies (without nexus in a state) to collect sales tax if Congress viewed such tax collection as not being burdensome to Interstate Commerce.

The Streamlined Sales and Use Tax Agreement, which is currently being considered for adoption by a number of states, represents an attempt (however meager) to simplify and modernize sales and use tax collection. Although voluntary, the acknowledged goal of the participating states has been to ultimately make the Agreement mandatory.

Accordingly, it is the goal of most state revenue commissioners to have as many states as possible ratify the voluntary Streamlined Sales and Use Tax Agreement, and then make the argument to Congress that the Agreement relieves interstate sellers of burdensome sales tax collection responsibilities. Thus, Congress will be asked to repeal Quill protection for interstate sellers and in its place force interstate sellers to comply with a now mandatory Agreement. Although the states have touted the Agreement as representing tax simplification, if the Agreement is coupled with Congressional repeal of the Supreme Court's 1992 Quill decision (the acknowledged goal of the participating states), its result will be just the opposite. As noted below, the agreement fails to meet the basic elements of simplification: a limited number of rates, uniform definitions, and easy compliance:

*__The Agreement makes no reduction in the 7,600 state and local sales tax rates__. In fact, it allows the states to increase the number of rates.
*__The Agreement fails in terms of "uniformity" of definitions of products__. Specifically, the Agreement only requires that a state adopt definitions which are "in substantially the same language." Thus, states have a grey area to interpret nuanced definitions opening a "Pandora's Box" of non-uniform definitions of products.
*__The Agreement's provisions concerning digital products are unworkable and unfairly expose interstate sellers to liability__. Specifically, the Agreement obligates purchasers of digital goods and services to allocate the use of such digital products across multiple jurisdictions AND holds the seller liable if the purchasers misrepresent their intent to use the product in multiple jurisdictions.
*__The system relies on a multitude of computer programs, databases, etc., which do not exist__. The states must prove that their system can work and is, in fact, "user friendly" before it can be mandated to all sellers.
*__There is no guarantee of compensation for collecting sales tax.__ There is absolutely no assurance that there will be adequate compensation for collecting sales tax.
*__Many states are using the Agreement as an excuse to increase taxes__. For example, by adopting the uniform definition of "clothing," Minnesota could no longer tax fur coats, so the state instituted a new "excise" tax on retailers that sell fur coats.
*__The Agreement's governance provisions result in the states policing themselves__. Compliance is turned over to a non-elected and self-regulating Governing Board, which is empowered to determine each state's compliance with the Agreement. In effect, "the foxes will be guarding the hen house."
*__Audit exposure will be substantial.__ Where a seller may be subject to audit by only one state or a few states under the Quill standard, it will now be subject to audit in dozens of states.

THE BOTTOM LINE – If Congress were to make mandatory the Streamlined Sales and Use Tax Agreement as justification for eliminating the Quill standard, Interstate Commerce would be severely burdened.

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