

DEPARTMENT OF TAXATION

2004 Fiscal Impact Statement

1. **Patron** Emmett W. Hanger, Jr.

2. **Bill Number** SB 514

House of Origin:

 Introduced

 Substitute

 Engrossed

3. **Committee** House Finance

4. **Title** Retail Sales and Use Tax: Streamlined
Sales and Use Tax

Second House:

 X **In Committee**

 Substitute

 Enrolled

5. Summary/Purpose:

This bill would conform the Virginia Retail Sales and Use Tax Act to the provisions of the National Streamlined Sales and Use Tax Agreement.

This bill would be effective July 1, 2006.

6. **Fiscal Impact Estimates are:** Unknown. (See Line 8.)

7. **Budget amendment necessary:** No.

8. Fiscal implications:

This bill would require changes to the Department's systems; however, the degree of change and the costs cannot be determined at this time. Over the next 12 months as the issues continue to evolve at the national level and as the Department embarks on extensive discussions with the Virginia business community on how best to implement the legislation, the Department will develop cost estimates.

Until such time as Congress requires out-of-state vendors to register and collect sales and use taxes, any additional revenue would come from vendors who voluntarily register and file. It is impossible to determine the amount of revenue that will be received from voluntary registrants. In order for Virginia to benefit from filers who voluntarily come forward under the terms of the agreement adopted by the SSTP, or to benefit for any future Congressional action, Virginia must conform its sales and use tax laws to the terms of the agreement. These conforming changes would result in additional General Fund, Transportation Trust Fund and Local revenue. While the amount is unknown, it potentially significant and would first affect Fiscal Year 2007 revenues.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Streamlined Sales Tax Background

In the United States Supreme Court decision in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), the court determined that the Commerce Clause barred a state from requiring an out-of-state mail-order company to collect use tax on goods sold to customers located within the state because the company had no outlets, sales representatives, or significant property in the state. In *Quill*, the court determined that only Congress has the authority to require out-of-state vendors, without a physical presence in a state, to register and collect that state's tax. In reaction to this decision and in an attempt to create a level playing field whereby out-of-state vendors and in-state vendors are both operating under the same tax rules, 40 states and the District of Columbia have come together through the Streamlined Sales Tax Project (SSTP) and have endorsed the concepts embodied in the national Streamlined Sales and Use Tax Agreement.

The SSTP originated as a cooperative effort between the National Conference of State Legislators, the Federation of Tax Administrators, and the National Governor's Association, with significant involvement from the private sector. The objective of the project is to make it easier for multistate retailers to collect state sales tax in both in-state and out-of-state transactions.

The agreement seeks to improve the sales and use tax administration systems used by the states through:

- State level administration of sales and use tax collections.
- Uniformity in the state and local tax bases.
- Uniformity of major tax base definitions.
- Central, electronic registration system for all member states.
- Simplification of state and local tax rates.
- Uniform sourcing rules for all taxable transactions.
- Simplified administration of exemptions.
- Simplified tax returns.
- Simplification of tax remittances.
- Protection of consumer privacy.

In order for a state to benefit from filers who voluntarily come forward under the terms of the agreement adopted by the SSTP, or to benefit for any future Congressional action, a state must conform its sales and use tax laws to the terms of the Agreement adopted by the SSTP on November 12, 2002.

Virginia's consistency with the agreement

In many ways, Virginia's sales tax law is more consistent with the SSTP objectives than some states. Virginia's sales tax law already meets three of the important requirements under the SSTP agreement:

- State level administration of sales and use tax.

Virginia's sales tax is centrally administered by the Department of Taxation. All registrations, payments, rules and regulations, and audits are done by the Department.

- Uniformity in state and local tax bases.

The base upon which the tax is applied (or not applied) is uniform. In Virginia, unlike some other states, the same items are either taxable or exempt for purposes of both the state and the local sales tax. The only exception under current law is fuel for domestic consumption. Home heating fuels are exempt from the state sales tax; however, the local exemption is permissive.

- Simplification of state and local tax rates.

Unlike most other states, Virginia's 1% local tax rate is applied by all localities statewide.

Changes necessary for Virginia to conform to SSTP agreement

Virginia's ability to continue to set sales tax policy will be preserved, even if Virginia conforms its sales tax laws to the terms of the agreement. The agreement requires that states must adopt uniform definitions and procedures. However, states will independently determine the taxability of transactions and items based on uniform definitions. However, conformity to the agreement, will require some changes to Virginia's law.

- Revised definitions for items such as food for home consumption and nonprescription drugs.

The definition adopted under the agreement does not use the same definition for "food for home consumption" that is used under Virginia law. The change in definitions will result in minor changes in the types of food or food products taxed at a lower rate. The same is true for the change in the definition from nonprescription drugs to over-the-counter drugs that would qualify for the Virginia exemption.

- Repeal of partial exemption for maintenance contracts and commercial modular buildings.

Since 1996, Virginia has taxed maintenance contracts that provide both for services and tangible personal property at 50% of the value of the contract. Similarly, since 2000, Virginia has taxed certain modular buildings at 60% of their value. These partial exemptions appear to conflict with the SSTP agreement requirements and are being repealed.

- Exclusion from some administrative requirements unique to Virginia sales tax dealers for volunteer registrants.

In order not to subject voluntary registrants who come forward under the terms of the agreement, certain administrative requirements related to registration, filing, penalties and dealer discount are being revised.

- Revision of local meals tax definition of food to be consistent with revised sales tax definition of food.

To clarify that the same food and food items will be subject to the local meals tax as will be subject to the retail sales tax, the definition of food is being amended for purposes of the local meals tax.

Sourcing

The one area where Virginia is not conforming to the agreement is related to the sourcing for purposes of the local sales tax. This is being done to preserve the status quo for Virginia dealers and limit the shifting of local sales tax revenue. Under the terms of the agreement, all sales, both interstate and intrastate, would be sourced to the locality where the goods are destined. This would require Virginia to source the 1 penny local sales tax to the locality of use or delivery, instead of the locality of the sale. Making this conforming change would impose significant burdens on in-state dealers and shift revenue between localities. Several states that have changed their local sourcing rules have encountered significant problems and resistance from in-state dealers in trying to implement a change in local sourcing. Ohio and Kansas, which adopted the "destination" sourcing rules, have both delayed implementation of this change due to concerns from local vendors. Texas and Washington have adopted the other requirements of the SSTP agreement, without the sourcing rules.

This bill would follow the approach taken by Texas and Washington and adopt the agreement terms without the sourcing change. Because this bill has an effective date of July 1, 2006, Virginia would have time to determine whether the issue can be renegotiated among the states.

cc : Secretary of Finance

Date: 2/24/2004 mch