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SFA



BILL ANALYSIS

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Senate Bill 433 (as introduced 5-1-01)
Sponsor: Senator Joanne G. Emmons
Committee: Finance

Date Completed: 5-1-01

CONTENT

The bill would create the "Streamlined Sales and Use Tax Administration Act" to do the following:

- **Allow the State to enter into a multistate streamlined sales and use tax agreement.**
- **Create a board of governance to represent this State with other states in matters related to the agreement.**
- **Provide for the registration of sellers, who would have to select a method for the collection and remittance of sales and use taxes.**
- **Allow sellers to contract with certified service providers for the collection and remittance of taxes.**
- **Provide for the use of an automated system that would calculate each jurisdiction's tax on a transaction.**
- **Limit the liability of a seller for taxes on transactions made before the seller's registration.**
- **Provide for consumer privacy.**

Agreement Requirements and Components

The bill would require the Department of Treasury, with the approval of the board of governance, to enter into the streamlined sales and use tax agreement with one or more states, "...to simplify and modernize sales and use tax administration in order to substantially reduce the burden of tax compliance for all sellers and for all types of commerce". The Department could not enter into the agreement unless it required each signatory state (a state that had entered into the agreement) to abide by the following requirements.

The agreement would have to do the following:

- Set restrictions to achieve more uniform state rates through limiting the number of state rates; eliminating caps on the amount of state tax due on a transaction; and eliminating thresholds on the application of state tax.
- Establish uniform standards for the sourcing of transactions to taxing jurisdictions; the administration of exempt sales; the allowances a seller could take for bad debts; and sales and use tax returns and remittances.
- Require signatory states to develop and adopt uniform definitions of sales and use tax terms. The definitions would have to enable a signatory state to preserve its ability to make policy choices that were substantially consistent with the uniform definitions.
- Provide a central electronic registration system that allowed a seller to register to collect and remit sales and use taxes for all signatory states.
- Provide that registration with the central registration system and the collection of sales and use taxes in the signatory states would not be used as a factor in determining whether the seller had nexus with a state for any tax.
- Outline any monetary allowances to be provided by the signatory states to sellers or certified service providers (described below).
- Require each signatory state to certify compliance with the terms of the agreement before joining, and to maintain compliance under the laws of the member state with all provisions of the agreement while a member.
- Require each signatory state to adopt a uniform policy for certified service providers that protected the privacy of consumers and maintained the confidentiality of tax information.

- Provide for the appointment of an advisory council of private sector representatives and an advisory council of nonmember state representatives to consult with the signatory states in the administration of the agreement.

Further, the agreement would have to provide for reduction of the burdens of complying with local sales and use taxes through the following:

- Restricting and eliminating variances between each signatory state's tax base and the local tax bases within that state.
- Requiring signatory states to administer any sales and use taxes levied by local jurisdictions within those states so that sellers collecting and remitting the taxes would not have to register or file returns with, remit funds to, or be subject to independent audits from local taxing jurisdictions.
- Restricting the frequency of changes in local sales and use tax rates, and setting effective dates for the application of local jurisdictional boundary changes to local sales and use taxes.
- Providing notice of changes in local sales and use tax rates, and of changes in the boundaries of local taxing jurisdictions.

Board of Governance/Department of Treasury

The bill would create a board of governance to represent this State in all multistate discussions regarding the streamlined sales and use tax agreement. The board could vote on behalf of the State and represent the State's position in all matters related to the agreement during multistate discussions before or after adoption of the agreement. The board or the board's designee would be authorized to represent the State before the other states that were signatories.

The board would consist of one member appointed by the Senate Majority Leader, one member appointed by the Speaker of the House of Representatives, the State Treasurer or his or her designee, and one member appointed by the Governor.

The Department could act jointly with other signatory states to establish standards for certification of a "certified service provider" and "certified automated system" and to

establish performance standards for multistate sellers. (A "certified service provider" would be an agent certified jointly by signatories to perform all of a seller's sales and use tax functions, other than the seller's obligation to remit tax on its own purchases. A "certified automated system" would be computer software certified jointly by the signatories to calculate the tax imposed by each jurisdiction on a transaction, determine the amount of tax to remit to the appropriate state, and maintain a record of the transaction.)

The Department also could take other actions reasonably required to implement the bill, including promulgation of rules, and the joint procurement of goods and services with other signatories in furtherance of the agreement.

Seller Registration/Collection Models

A person could participate under the bill only by registering in the central registration system provided for by the agreement. The Department would have to participate in an online registration system with other signatory states that allowed sellers to register online. (A "person" would be an individual, trust, estate, fiduciary, partnership, limited liability company, limited liability partnership, corporation, or any other legal entity. A "seller" would be any person who sold, leased, or rented tangible personal property or services to another person.)

A seller registered under the agreement in Michigan would be considered registered in each of the signatory states; however, a seller could choose to register directly with other signatory states if more information were required in those states. A seller could cancel its registration under the agreement at any time, according to the agreement. A seller that canceled its registration, however, would remain liable for remitting taxes collected to the appropriate states. By registering, a seller would agree to collect and remit sales and use taxes according to the agreement for taxable sales in all signatory states, including states that adopted the agreement after the seller registered.

The bill specifies that registration of a person under the agreement and collection of sales and use taxes by that person in signatory states would not provide nexus with any signatory state, and could not be used as a

factor in determining nexus with a signatory state for any tax purpose.

A registered seller would have to agree to one of the following models for purposes of collecting and remitting sales and use taxes under the agreement:

- Model 1. A seller that had contracted with a certified service provider to act as its agent to perform all of the seller's sales and use tax collection functions, other than the seller's obligation to remit sales or use tax on its own purchases.
- Model 2. A seller that had selected a certified automated system to perform part of the seller's sales and use tax collection functions, but retained responsibility for remitting the tax.
- Model 3. A seller that had sales in at least five signatory states, had total annual sales of \$500 million or more, had a proprietary system that calculated the amount of tax due in each taxing jurisdiction, and had entered into a performance agreement with the signatory states establishing a tax performance standard for the seller. (In model 3, a seller would include an affiliated group of sellers using the same proprietary system.)

In computing the amount of tax remitted to this State, a certified service provider under model 1 and a seller under model 2 could deduct a base rate that applied to taxable transactions processed through the certified automated system of the provider under model 1 or of the seller under model 2, in accordance with the terms of the contract entered into by the signatory states. A seller that took this deduction could not take a deduction under Section 4 of the General Sales Tax Act (which provides for a collection allowance, that is, allows a seller to deduct and keep a percentage of sales taxes collected from purchasers). A seller under model 3 could take only the deduction allowed under Section 4.

In addition to the deduction allowed under the bill, for up to 24 months following a voluntary seller's registration, the voluntary seller also could deduct a percentage of tax generated in Michigan by the voluntary seller in accordance with the terms of the contract entered into by the signatories. (As used in this provision, "voluntary seller" would mean a seller that

was not required to register to collect tax for this State.)

Liability Limitations

The bill provides that a person who registered as a seller would not be liable for any uncollected or nonremitted sales or use tax on transactions with purchasers in Michigan before the date of registration, if the seller were not licensed under the General Sales Tax Act or the Use Tax Act in the 12-month period preceding the date the State entered into the agreement. The seller also would not be responsible for any penalty or interest that could be due on those transactions. These provisions would not apply to the following:

- Any tax liability of the registered seller for transactions that were subject to sales or use tax in Michigan in which the registered seller was the purchaser.
- Any sales or use taxes already paid or remitted to the State.
- Any transactions for which the seller received notice of the commencement of an audit that was not finally resolved, including related administrative or judicial processes.

The liability limitations would apply to a seller absent the seller's fraud or intentional misrepresentation of a material fact if the seller continued to be registered and continued collection and remittance of applicable sales and use taxes in Michigan for at least 36 months. The statute of limitations applicable to assessing a tax liability would be tolled during that time.

Certified Service Provider

The bill specifies that a certified service provider would be the agent of a seller, with which the provider had contracted for the collection and remittance of sales and use taxes. As the seller's agent, the provider would be liable for sales and use tax due each signatory state on all sales transactions it processed for the seller, except as provided in the bill. A seller that contracted with a provider would not be liable to this State for sales or use tax due on transactions processed by the provider, unless the seller made a material misrepresentation of the type of items it sold, or committed fraud. In the absence of probable cause to believe that the

seller had committed fraud or made a material misrepresentation, the seller would not be subject to audit on the transactions processed by the provider. A seller would be subject to audit for transactions not processed by the provider. The signatory states acting jointly could perform a system check of the seller and review the seller's procedures to determine if the provider's system was functioning properly, and the extent to which the seller's transactions were being processed by the provider.

A person that provided a certified automated system would be responsible for the proper functioning of that system, and would be liable to this State for underpayments of tax attributable to errors in the functioning of the system. A seller that used a system would remain responsible and liable to the State for reporting and remitting tax.

A seller that had a proprietary system for determining the amount of tax due on transactions and had signed an agreement establishing a performance standard for that system would be liable for the failure of the system to meet the performance standard.

Consumer Privacy

A certified service provider would be prohibited from retaining a consumer's "personally identifiable information", that is, information that identified a specific person. A provider's system would have to be designed and tested to assure the privacy of consumers by protecting their anonymity, and to assure that personally identifiable information could be used only when necessary for administration of the model 1 process, and only if the provider had given clear and conspicuous notice of its use.

A provider would have to give clear and conspicuous notice of its information practices to consumers, including what information it collected, how it collected the information, how it used the information, and whether it disclosed the information to signatory states. A provider also would have to provide the necessary technical, physical, and administrative safeguards to protect personally identifiable information from unauthorized access and disclosure.

A provider's retention of personally identifiable information would be limited to exemption claims because of a consumer's status or intended use of the goods or services purchased, to investigations of fraud, and to the extent necessary to ensure the reliability of the provider's technology.

The bill specifies that this privacy policy would be subject to enforcement by signatory states' attorneys general or other appropriate authorities.

If personally identifiable information were retained for limited purposes by or on behalf of the signatory states, in the absence of exigent circumstances, individuals would have to be given reasonable notification of that retention and afforded reasonable access to their own data, with a right to correct inaccurately recorded data. If anyone other than a signatory state sought to discover personally identifiable information, then, in the absence of exigent circumstances a reasonable and timely effort would have to be made to notify the individual of the request.

The agreement would not enlarge or limit the signatory states' authority to do any of the following:

- Conduct audits or other review as provided under the agreement and state law.
- Provide records pursuant to a signatory state's freedom of information act, disclosure laws with governmental agencies, or other regulations.
- Prevent, consistent with state law, disclosures of confidential taxpayer information.
- Prevent, consistent with Federal law, disclosures or misuse of Federal return information obtained under a disclosure agreement with the Internal Revenue Service.
- Collect, disclose, disseminate, or otherwise use anonymous data for governmental purposes.

Other Provisions

The bill provides that the payment, collection, and remittance of the sales and use taxes would be subject to the provisions of the General Sales Tax Act and the Use Tax Act. If there were a conflict between those Acts and the bill, the provisions of the bill would prevail.

The bill specifies that the agreement authorized by it would bind and inure only to the benefit of this State and the other signatory states. No person, other than a signatory state, would be an intended beneficiary of the agreement. Any benefit to a person other than a signatory state would be established by the law of this State and the other signatory states and not by the terms of the agreement.

The bill provides that a person would not have any cause of action or defense under the agreement because of the State's approval of the agreement. A person could not challenge, in any action brought under any provision of law, any action or inaction by any department, agency, or other instrumentality of the State or any political subdivision of the State, on the ground that the action or inaction was inconsistent with the agreement.

The bill also specifies that a law of this State, or the application of a law, could not be declared invalid as to any person or circumstance on the ground that the provision or application was inconsistent with the agreement.

The bill provides that implementation of any condition of the agreement in the State, whether adopted before, at, or after the State's membership in the agreement, would have to be by an action of the State.

Legislative Analyst: G. Towne

FISCAL IMPACT

The fiscal impact of this bill cannot be identified at this time. While the State is currently not collecting anywhere from \$100 million to \$300 million in sales and use taxes from taxable Internet and mail order transactions, this bill by itself would not solve this collection problem. This bill does, however, propose a major step toward possibly solving this problem. Under the bill, the State would be allowed to join a multistate compact whose intended purpose would be to simplify and streamline the sales and use taxes among the states and to develop a uniform collection process that would not be burdensome to businesses or consumers. The scope of this potential compact among the states, as outlined in the bill, could require Michigan eventually to make changes in its

sales and use tax bases, particularly in regard to adopting uniform definitions of particular goods and services, which could have both positive and negative fiscal impacts. In addition, the State also would potentially have to eliminate its current special reduction in the tax rate, from 6.0% to 4.0%, granted on residential use of electricity, natural gas, and home heating fuels. Any additional sales and use tax revenue that this bill would eventually help collect would primarily benefit the School Aid Fund, local revenue sharing, and the General Fund/General Purpose budget. About 73% of the sales tax is earmarked to the School Aid Fund and most of the remaining sales tax revenue is distributed to local governments. The use tax is distributed to the School Aid Fund (33%) and the General Fund/General Purpose budget (67%).

The Department of Treasury would need to acquire the capacity for electronic acceptance of tax registration information and the electronic collection of sales and use taxes. The Department estimates this cost at \$2 million. The first \$1 million of this cost was included in the FY 2000-01 appropriation to the Department of Treasury. The remaining \$1 million is requested in the appropriation for FY 2001-02.

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.