

**Minutes of Sales Tax Simplification Governing States
Inaugural Meeting
November 28-29, 2001
Salt Lake City, Utah**

The initial session of the governing states was held at the Salt Lake City Marriott Downtown, 75 S. West Temple, Salt Lake City, Utah on November 28-29, 2001. The terms “governing” and “implementing” used in these minutes have the same meaning. “Governing” was used in the meeting materials. “Implementing” was used in the rules adopted at the meeting. The *Rules of Procedure, Streamlined Sale Tax Implementing States* will be issued separately from this document.

Delegates

The following state delegates participated in the meeting.

Arkansas

Mary Cameron, Department of Finance and Administration

District of Columbia

Stephen P.B. Kranz, Committee on State Taxation

Florida

Marshall Stranburg, Department of Revenue

Illinois

David Vite, Illinois Retail Merchants Association

Tim Bramlet, Taxpayers Federation for Illinois

Indiana

James Turner, Department of Revenue

Kentucky

Charlotte Quarles, Revenue Cabinet

Louisiana

Representative Bryant Hammett

Cynthia Bridges, Secretary, Department of Revenue

Raymond Tangney, Department of Revenue

Maryland

Senator Patrick Hogan

Delegate Sheila Hixson

Kevin Hughes, Governor's Office

Steven M. Cordi, Deputy Comptroller, Comptroller of Treasury

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Michigan

Senator Diane Byrum
Senator Joanne Emmons
Representative James Koetje
Representative Nancy Quarles
June Summers Haas, Bureau of Revenue, Department of Treasury
Doug Roberts, Department of Treasury
Nancy Taylor, Department of Treasury
Lucille Taylor, Legal Counsel to the Governor

Minnesota

Matthew G. Smith, Commissioner, Department of Revenue

Nebraska

Mary Jane Egr, Tax Commissioner, Department of Revenue

Nevada

Dino DiCianno, Department of Taxation

North Carolina

Charles Collins, Department of Revenue
Sabra Faires, Department of Revenue

North Dakota

Rick Clayburgh, Tax Commissioner, Office of State Tax Commissioner

Oklahoma

Representative Clay Pope
Jerry Johnson, Member, Tax Commission
Thomas Kemp, Chairman, Tax Commission

Tennessee

Senator William Clabough
Representative Matthew Kisber
Ruth Johnson, Commissioner, Department of Revenue

Texas

Senator Troy Fraser
Representative Dennis Bonnen
John Keel, Director, Legislative Budget Board
Billy Hamilton, Deputy Comptroller of Public Accounts

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Utah

Senator Lyle W. Hillyard
Representative Wayne A. Harper
R. Bruce Johnson, Commissioner, State Tax Commission
James Olsen, Utah Retail Merchants Association

Wisconsin

Diane L. Hardt, Department of Revenue

Wyoming

R.M. (Johnnie) Burton, Director, Department of Revenue

Participants

The following additional individuals attended the meeting

California

Pedro R. Reyes, Deputy Policy Director, California Assembly
Beth Ann Kendzierski, Tax Director, Apria Healthcare, Inc.

Colorado

Jeff Dale, Policy Specialist, National Conference of State Legislatures
Joel Harris, Policy Analyst, Office of Governor Owens
Stacey Sprinkle, Director, Federal & State Tax Policy, Verizon Wireless

Connecticut

Joseph Ercolano, Director, Government Affairs, Pitney Bowes

District of Columbia

Ken Beier, Project Manager, Multistate Tax Commission
René Blocker, Deputy Director, Multistate Tax Commission
Katherine M. Breaks, Manager, KPMG LLP
Dan Bucks, Executive Director, Multistate Tax Commission
Joseph R. Crosby, Legislative Director, Committee on State Taxation
Harley T. Duncan, Executive Director, Federation of Tax Administrators
Jason Lumia, Director, Economic Development & Commerce Committee,
National Governors' Association
Ellen B. Marshall, Legislative Consultant, Multistate Tax Commission
Neal Osten, Senior Committee Director, National Conference of State Legislatures
Maureen Riehl, Vice President, National Retail Federation
Frank Shafroth, Director, State-Federal Relations, National Governors' Association
Carl Tubbesing, Deputy Executive Director,

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National Conference of State Legislatures

Graham Williams, Policy Associate, National Conference of State Legislatures

Georgia

Bernard Rothman, Senior Vice President, First Data Corporation

Hawaii

Nathan Chee, Department of Taxation

Richard Chiogioji, Department of Taxation

Idaho

Jake Hoffman, IT Policy Analyst, Idaho Tax Commission

Dan John, Tax Policy Manager, Idaho Tax Commission

Illinois

Glen Bower, Director, Department of Revenue

Terry Charlton, Staff Attorney, Department of Revenue

Russ Davis, National Director, Legislative Affairs, Sears, Roebuck and Company

Kentucky

Robert W. Cox, Deputy Executive Director, Governor's Office for Economic Analysis

Dr. James R. Ramsey, State Budget Director

Louisiana

Dirk Thibodeaux, Attorney, Louisiana House of Representatives

Maryland

Ryan Bishop, Department of Legislative Services, Maryland General Assembly

Massachusetts

Jon W. Abolins, Vice President, Tax & Government Affairs, Taxware 2002

Minnesota

Don Trimble, Assistant Commissioner, Department of Revenue

Larry Wilkie, Director, Business Tax, Department of Revenue

Paul A. Wilson, Fiscal Analyst, House of Representatives

Nebraska

Thomas J. Gillaspie, Administrator - Legal Services, Department of Revenue

New Jersey

Deborah Bierbaum, Director, External Tax Policy, AT&T

New York

Senator Steve Saland, President, National Conference of State Legislatures

Pennsylvania

Annabelle Canning, Executive Director, Federal and State Tax Policy,
Verizon Wireless

Dick Eppleman, Director, Government Markets, Vertex, Inc.

South Dakota

Representative Richard "Dick" Brown

Fred Baatz, Senior Research Analyst, Legislative Research Council

Texas

John Heleman, Revenue Analyst, Texas Comptroller of Public Accounts

Eleanor Kim, Assistant Director of Tax Administration,
Comptroller of Public Accounts

Wayne Zakrzewski, Assistant General Counsel – Tax, J. C. Penney Company, Inc.

Utah

Senator Curt Bramble

Senator Howard A. Stephenson

O. William Asplund, Assistant Director,
Office of Legislative Research and General Counsel

Gary Cornia, Chair, Utah Tax Review Commission

Bryant R. Howe, Research Analyst,
Office of Legislative Research and General Counsel

W. Val Oveson, Managing Director, Pricewaterhouse Coopers LLP

Rebecca L. Rockwell, Associate General Counsel,
Office of Legislative Research and General Counsel

Vermont

Scott Mackey, Kimbell, Sherman & Ellis

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Virginia

Dennis Brown, Vice President, State Government Relations,
Equipment Leasing Association

Steve Lodge, Vice President, Legislative Affairs,
National Confectioners Association

Thomas E. McMahon, Senior Vice President and Chief Counsel,
National Automatic Merchandising Association

Becky Sullivan, Staff Vice President, Government Relations,
International Council of Shopping Centers

Washington

Tremaine Smith, Program Manager, Department of Revenue

Wyoming

Senator Bob Peck

Representative John J. Hines

Representative Patricia Nagel

Opening Session

Welcoming Remarks

The meeting was opened by Senator Steve Saland of New York, President of the National Conference of State Legislatures. He explained that the first day of the session will explain 'how we got here' and the second day is set aside for organizing efforts of the governing states. These efforts can include rules and procedures, timeframe, and goals. He congratulated the delegates from twenty states and the District of Columbia for participating in this truly historic gathering. He recognized the sales tax simplification efforts of governors, tax administrators, and legislators--starting in 1999 in Boston; and expressed thanks to the National Governors' Association (NGA), the National Conference of State Legislatures (NCSL), the Federation of Tax Administrators (FTA), and the Multistate Tax Commission (MTC) for support of these activities.

Senator Saland cited base shrinkage as the major problem with the sales tax. In the 1930s, the sales tax was not difficult for merchants to collect and consumption of services was not a significant feature of the economy. However, by the 1970s, services increased their share of economic activity and remote sales became more prevalent. Thus, sales taxes were applied to a smaller share of consumer expenditures. The new threat to the sales tax is e-commerce, which is expected to cost the states \$13 billion in revenue in 2001 and \$45 billion by 2006.

Keynote Address

Dr. Charles McLure of Stanford University delivered the keynote address. He introduced the topic by recalling a dream where travelers, who were bound for Salt Lake City, entered a clearing, followed by a strange beast that kept nipping at their heels. The beast was a centipede-like creature, representing the U.S. economy. The travelers have a choice of three paths: 1) the Great Swamp, which consists of current sales and use tax systems, 2) Terra Firma, which incorporates the features of an ideal sales tax system, and 3) the Lesser Bog, which consists of the Streamlined Sales Tax Project (SSTP) proposal.

Dr. McLure then described the major features of the Great Swamp by indentifying the complexities faced by single-state vendors. He then went on to describe the additional complexities faced by multistate vendors. He added that while large mail order firms might be able to handle the complexity, small remote vendors—of which there are potentially many in electronic commerce—would be hard-pressed to handle the complexity. In addition to complexity, Dr. McLure notes the economic distortions and inequities of the Great Swamp. He further noted the origin of state sales tax systems in the Great Depression. In this environment, a myriad of state and local requirements and taxation of goods, and exemption of services, was not a problem. In closing his description of the Great Swamp, Dr. McLure noted that the states had 25 years, since the Bellas Hess decision in 1967, to simplify their sales taxes. Instead, they continued to force vendors to trudge through the Great Swamp. In 1992, the Supreme Court provided directions, in Quill, on how to escape from the swamp. If the states act accordingly, with simplification efforts, he predicted that “either the Congress or the Court itself may eliminate the physical presence test.”

Dr. McLure then prescribed how to “drain the swamp” by defining the rules of the ideal system. They are:

- If a product is sold to consumers, it is subject to tax.
- If a product is sold to business, it is exempt.
- States would administer local sales and use taxes, using procedures that would allow vendors to identify the local jurisdiction of destination (e.g., based on zip codes).
- These rules would apply equally to local merchants and to remote vendors, subject to a de minimis rule.

- The legal framework and administrative procedures of all states would be identical. (Some of these features, which cannot be discussed in detail, might follow the outlines of the SSTP proposals.)
- Multi-state “one-stop” administrative procedures (e.g., for registration, filing tax returns, payment of tax) should be employed to the extent possible.

Under this system states would retain full sovereignty over the choice of state sales tax rates and could allow local autonomy over local rates. This system would be ‘compliance-friendly’ since it eliminates virtually all the complexity of the current sales tax swamp. The system also has the advantage of eliminating economic distortions and inequities. While Dr. McLure acknowledged that the ideal system would entail some loss of state sovereignty, it would retain state (and local) control over tax rates.

Moving on to SSTP, Dr. McLure noted that the project had made amazing progress in achieving simplification, but that it would not reach Terra Firma. He noted that the SSTP draft requires uniformity of the state and local tax bases in each state; by comparison, the NCSL draft would allow local tax bases to deviate from the state base.

In reference to the Internet Tax Freedom Act, Dr. McLure asked whether simplification is worthwhile when there is no assurance of removal of a physical presence standard by the Congress or the Supreme Court. He stated that the answer is a resounding yes. He added that the revenue implications of nexus standards may be significant, but the primary issue is one of economic neutrality and fairness.

Dr. McLure closed by citing the success of the European Union in adopting the value added tax almost 40 years ago. He said that the U.S. states will have to resist the temptation to merely tinker in ‘politics as usual’ and go the full nine yards.

Opening Remarks

Utah Governor Michael Leavitt, past Chairman of the National Governors’ Association provided an historical perspective on creating governing arrangements, and cited the need for compatible regulatory and fiscal regimes--if the states are to be viable entities in a global economy. The governor pointed out that in 1785, the new country, under the Articles of Confederation, had no federal court system, multiple currencies, and disputes over the status of Vermont. Potential trading

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partners did not view the states as a unified system. But from these limitations, a unified national government emerged--with retention of state powers in the 10th Amendment. The Governor pointed out that we have a similar challenge today—to create a system of transaction taxes that is viable in the 21st century. He further pointed out that a changing world also poses challenges for regulation of insurance and medical practice where 50 sets of regulation or licensure can pose impediments to interstate commerce. He cited the example of surgery performed over the Internet, which may require the surgeon to be licensed in the state where the operation is performed. He stated that there are two clear options here—a federal takeover, or a system of state regulation that is not a burden on interstate commerce.

For the state tax area, the governor pointed out that the current system is unsustainable. He put forth a scenario where retailers have three cash registers. One of the cash registers collects sales tax on cash transactions. The second cash register provides for use of credit cards and purchases via the Internet. The third is the same as #2, but with no sales tax collection. Obviously, the first cash register would not get much business and register #3 would capture most of the sales. He pointed out that the alternative to state action is to have the Internal Revenue Service take over the sales tax, with a resulting shift in power from the states to the federal government. He emphasized that a streamlined system must be elegantly simple and should consist of a single sales tax base per state. He recognized the political challenge of achieving one base per state and other simplification measures, but noted the reduced friction that accompanies simplified requirements, which could save businesses about \$4 billion per year.

The governor concluded by stating that the U.S. is ahead of the European Union in creating a seamless market, but that both unions are working on the same set of issues. He predicted that the system that figures out the best version of federalism will become the predominant economy of the 21st Century.

Governor Leavitt and Dr. McLure then took questions. Senator Emmons of Michigan pointed out that these reforms cost the states a lot of money, particularly if business activity is exempted from transactions taxes. Dr. McLure pointed out that Michigan could probably sell a lot more cars if business inputs were not taxed. That is, Michigan is currently disadvantaged relatively to the European Union and Japan regarding tax treatment of manufactured exports.

Representative Pope of Oklahoma made the point that a credit for business transactions would work only where other taxes are high. He explained that in Oklahoma, “all of our taxes are low.” Dr. McLure responded that credits, in the

case of a VAT or sales tax credit, are only against the same type of tax. They work in the same way as payroll tax credits; that is, the credit is only against payroll taxes.

Joel Harris, representing the Governor of Colorado, pointed out that his state's chief executive, was one of three governors supporting the permanent extension of the Internet Tax Freedom Act. He added that taxation of remote sellers was taxation without representation. In response, Governor Leavitt pointed out that sales and use taxes are imposed on the consumer and that taxation without representation is not an issue here. He clarified that businesses are required to collect the tax—this was the mechanism established when sales taxes were introduced in the 1930s. He added that the objective, with the streamlined sales tax, is to treat all taxpayers alike, and that we either have reform, or we can say goodbye to the sales tax. Dr. McLure added that many companies, such as sellers of alcoholic beverages and tobacco products, do have representation in the destination state; thus, this was not a sensible argument.

Sales Tax Administration in a Global Economy

Harley Duncan, Executive Director of the Federation of Tax Administrators, then moderated a panel consisting of Dan Bucks, Executive Director of the Multistate Tax Commission, Richard Prem of Amazon.com, Paul Allen of Franklin Covey, Inc., and Wayne Zakrzewski of J.C. Penny Company, Inc. The first topic was tax registration. Mr. Prem noted that registration requirements, which potentially apply for hundreds of state and local entities, are a rude awakening for expanding companies. Mr. Zakrzewski added, that if this is the only thing the implementing states take care of, that it will be a vast improvement. Mr. Bucks explained the MTC Nexus Program, which invites companies to come forward and commence sales tax responsibilities--adding that physical presence tests are not always clear. In response to a question, there was also discussion of implications of sales tax nexus for other taxes.

Mr. Duncan then introduced the next topic--taxability determinations. There was discussion of the difficulties with product definitions, sales tax holidays, and caps and thresholds. There was disagreement on the panel on the merits of sales tax holidays, but concurrence that sales tax holidays under uniform guidelines would be better than the current situation. The problems of adopting software to frequently changing and nonuniform taxability standards was cited, as well as the difficulty of inexperienced customer service representatives making taxability determinations. A comment from the audience was that under most VAT regimes, consumers must apply for refunds.

On tax rate determinations, the panelists noted many challenges, including, the lack of correspondence of zip codes and tax jurisdictions, and senior discounts. The private sector panelists explained that they risk sanctions if they do not collect at the highest rate applicable in a zip code-defined geographic area. They also explained the need for lead-time in adjusting to tax rate changes.

Panelists also explained the range of return and remittance requirements. For example Tennessee requires separate filing in each jurisdiction. In Florida, all returns are submitted to the State, but there is no consolidated return. Mr. Duncan explained the administrative simplification would also lead to audit simplification.

Mr. Bucks concluded the panel with a history of sales tax simplification efforts. He also explained that the more the states adopt the sales tax to the needs of interstate commerce, the more likely the Supreme Court will support the extension of the sales tax to remote vendors.

NCSL and NGA Perspectives on Sales Tax Simplification

The first lunch speaker, Frank Shaffroth, Director of State-Federal Relations for the NGA, emphasized that this is the last, best chance to fix the sales tax problem. He cited the success of tax reform at the federal level in the 1980s—this seemed like an insurmountable task, but participants overcame the obstacles and developed a significant tax agreement.

The second lunch speaker, Representative Matt Kisber of Tennessee, is co-chair of the NCSL Executive Committee Task Force on State and Local Taxation of Telecommunications and Electronic Commerce. This group began its life in 1999 to provide input to the Advisory Committee on Electronic Commerce. Representative Kisber noted, that while there was a good deal of consensus, there were a number of issues important to a streamlined system that still need to be decided, such as uniform definitions, rounding rules, bad debt provisions, caps, thresholds and holidays. He concluded his remarks by stating that a product should be drafted and before the states in late 2002.

Report on the Recommendations of the Streamlined Sales Tax Project

Dan Bucks reconvened the meeting and commended Dianne Hardt, of the Wisconsin Department of Revenue, and Charles Collins, of the North Carolina Department of Revenue, for their outstanding work as co-chairs of the SSTP. Mr.

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Collins noted that not many people expected the project to get this far when it commenced its work in March 2000.

After an overview of the project history and organization, Mr. Collins and Ms. Hardt reviewed the recommendations of the project. These consist of the SSTP Act, the SSTP Interstate Agreement, and uniformity features. The uniformity features are:

- Uniform Sourcing Rule for All Transactions (including gifts)
- Standardized Geographic Coding System for Local Rates
- Local Rate Simplification
- Uniform Required Notice and Limited Frequency of Rate Changes (including annexations)
- Uniform Product Codes for Exemptions by Product Category
- Uniform Definitions
- No or Minimal Sales Tax Returns or Reporting Requirements for Participating Sellers
- Central, One-Stop Registration System
- Simplified Exemption Administration for Use and Entity Exemptions
- Uniform Treatment of Bad Debts
- Systems Checks of Sellers and Minimal Exposure to Audits (under no return/no audit option)
- Uniform Audit Procedures for Calculation Services or Vendors
- State and Local Taxes Remitted at State Level Only, with State Responsible for Distributing Funds to Local Governments
- Voluntary Registration Not a Factor in Determining Nexus for Income or Other Taxes; and Terms and Conditions for Past Liability Relief
- Uniform Rounding Rules
- Privacy Protections
- Joint Certification of Software
- State Compensation for System.

Ms. Hardt and Mr. Collins also reviewed several works in progress:

- Joint Cost of Collection Study
- Technology Issues, including the pilot project
- November 2001 Issue Papers
 - ◊ Bad Debts
 - ◊ Direct Pay Permits
 - ◊ Vending
 - ◊ Candy
 - ◊ Soft Drinks

- ◇ Multiple Points of Use
- ◇ Confidentially
- ◇ Uniform Sourcing
- Future Issue Papers
 - ◇ Rounding
 - ◇ Multiple Tax Rates
 - ◇ Uniform Returns
 - ◇ Caps and Thresholds
 - ◇ Lease and Rental
 - ◇ Bundling
- Definitions
 - ◇ Food
 - ◇ Prepared Food
 - ◇ Tangible Personal Property
 - ◇ Drugs and Medical Equipment

Proposed Rules

Carl Tubbesing, Deputy Executive Director of NCSL, then reviewed a set of proposed rules for the implementing states. He emphasized that this was an initial suggestion or starting point for the rules for the implementing states. It was decided, by voice vote, to hold the Thursday morning session as a public meeting. Johnnie Burton, Director of the Wyoming Department of Revenue, asked about the relationship of the SSTP to the Implementing States. Mr. Tubbesing responded that he expected the Implementing States to continue to rely on the SSTP. The meeting closed for the day at 4:20 P.M.

Organizing the Governing States

Senator Saland opened the meeting at 8:40 A.M. on Thursday morning. Governor Leavitt participated throughout the morning. The state participants discussed and voted on a series of amendments to the Rules of Procedure for the Streamlined Sales Tax Implementing States. All amendments and the final rules were passed by a unanimous voice vote. A copy of the Rules is available from National Conference of State Legislatures.

June Haas of Michigan nominated Bruce Johnson of Utah as the executive branch representative who will serve as co-chair. This was accepted by a unanimous voice vote. Senator Emmons of Michigan nominated Representative Matt Kisber of Tennessee as the legislative representative to serve as co-chair. This was accepted by a unanimous voice vote.

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Following a break, Governor Leavitt thanked the group for coming to Utah. He followed with a suggestion and request. Reflecting on the experience of the SSTP project, he said there has not been enough communication between SSTP participants, and legislators and governors. He stated that it is very important for participants push their way into the awareness of their governors. Governor Leavitt added that participants should not view themselves as business people or tax administrators or legislators—that they should view themselves as representatives of their states. He concluded by stating that this effort can be a template for other areas where the states can be full players in the federal system—and that these areas are rightly within the fundamental role of the states.

Senator Saland then commented that the group has a very aggressive time line. He emphasized there is a lot of work to do, but that “we also have a common understanding.” He added that the private sector is important and we need the assistance of the private sector in communicating with legislators. Representative Kisber concurred and asked the private sector delegates of the Implementing States to think about ways in which they could act as liaisons between the business community and the Implementing States.

Bruce Johnson commented that this is an exciting and historic opportunity—and that time is of the essence. He reemphasized Governor Leavitt’s comments that participants are representing their states. In addition, he recognized that is natural for small groups to form, but that it is important that everyone be involved and receive full notice of activities.

Representative Kisber stated that Charles Collins has offered to put together a document, discussing issues that the group needs to address. Bruce Johnson added that attendees needed to review their briefing books and realize why some approaches were rejected. June Haas asked that participants receive the Charles Collins document prior to their next meeting, which will be in late January or early February 2002, and preferably on a Friday/Saturday following a proposed SSTP meeting. NCSL and MTC made commitments to assist the project’s distribution of documents on a website—either the existing SSTP website, or an alternate website. Participants in the meeting will be polled for their contact information and preferred means of contact (email/fax). The meeting was adjourned at 11:10 A.M.

Respectfully Submitted

Ken Beier
Multistate Tax Commission