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Credit for Sales and Use Taxes Paid to Other State and Local Jurisdictions

Draft Issue Paper

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Background: In early 2008 SLAC began working on the sourcing of services rules. In conjunction with that effort the business participants wanted each sourcing rule to include provisions for credit for taxes paid to other jurisdictions. Since there are no provisions in the SSUTA for requirements of member states regarding credit for tax paid, (except Section 313.A.4.) a separate workgroup was formed in 2008 to draft an amendment to the SSUTA relating to credit for taxes paid to other jurisdictions, instead of including language in each sourcing rule. The group discussed the scope of work and developed 2 principles:

- Taxpayers should not be subject to taxation in multiple states on the same transaction
- Tax administration with respect to credits should be as simple as possible

In July 2010 a survey was sent to states to determine what use taxes are imposed in a state and its local jurisdictions, obtain language from each state’s statutes and rules regarding credit for tax paid, and what are the state’s requirements for receiving credit for taxes paid.

Issues: The purpose of this document is to identify the issues relating to the allowance of credit for the state and/or local sales and/or use tax paid in one member state against the sales and/or use tax due on the subsequent storage, use, or other consumption of that same product in another member state. There are numerous issues that arise when discussing this topic and even more issues when a transaction involves both a member state and a nonmember state, such as the proper sourcing of the transaction.

A summary of the issues included in this paper has been provided to the executive committee to assist with defining the scope of the amendment to the Agreement.

Issues

(1) Which taxes are intended to be covered by a proposed amendment (tax on retail sale, subsequent use tax when moved to another state, both, other)?

Purchasers need to know when credit for a sales, use or similar tax that they paid in one state on a retail sale may be used to offset a sales, use or similar tax that is due in a state where the product is subsequently stored, used, or otherwise consumed.

Sales, use, or similar taxes may be paid by the purchaser at various times including being paid:

- by the purchaser to the seller at the time of the sale;
- directly to the state due to the fact that the purchaser provided its direct pay permit to the seller;
- directly to the state by the purchaser because the purchaser purchased the items from a retailer that was not registered to collect the tax in that state.

All of the above scenarios may occur with regard to a retail sale of a product. Sellers need to be assured purchasers are not disadvantaged because the seller is collecting the sales or use or similar tax subject to the requirements of the Agreement. Purchasers need to know what credit for tax paid on the retail sale is available in the member states to comply with their reporting and payment requirements under each of these scenarios in the member states.

In addition to covering credit for tax paid on the retail sale of a product, requests have been made to include in the proposed amendment provisions requiring member states to uniformly provide credit for use tax paid in a state by the purchaser on the storage, use, or other consumption of property and services against the subsequent storage, use or other consumption of the property and services subsequently moved to another state.

Workgroup Recommendation on (1): In order to provide uniformity among the member states regarding taxes subject to the requirements of the Agreement it is recommended that the amendment to the SSUTA address (enter recommendation).

(2) Legally due and owing requirement – what does it mean to be legally due and owing?

States were surveyed to obtain information concerning credit for tax paid and the states current laws and rules. The 23 states responding to the survey all indicated that their states laws required, for purposes of receiving credit for tax paid to another jurisdiction, that the tax must be legal, legitimate, proper or lawful and all 23 states indicated the tax must have been paid to the other jurisdiction. If the tax was not paid, the states do not allow credit.

Are taxes paid to the other jurisdiction required to be “legally due”, “legally due and paid”, “legally imposed”, or some similar phrase in order to allow credit?	AR, IA, IL, IN, KS, KY, MA, MI, MN, NC, NJ, NV, RI, SD, TN, UT, VT, WA, WI, WV,WY	23
Legally imposed	AR, IA, MN, TN, UT, WA	6
Properly due and paid	IL	1
Paid	IN	1
Lawfully/legally paid	KY, WI, WV	3
Lawful obligation to pay & paid	RI	1
Imposed under law...due and Paid	MI	1
Subject to a tax	KS	1
Legally due and paid	MA, NC, NE, NJ, VT, WY	6
Legitimately paid	NV	1
Legally levied and paid	OH	1
Previously paid / liability to another state	SD	1

The workgroup discussed using the following criteria for determining if the tax was properly and legally imposed:

- The retail sale in member states must be sourced in accordance the SSUTA.
- The state and local jurisdiction to which the retail sale is sourced imposes tax on the retail sale of the product or on the storage, use or other consumption of the product.
- The other state and its local jurisdictions’ statutes do not provide for an exemption, credit, or refund of tax on the retail sale or storage, use or other consumption of the product.

- The tax must have been paid to the other jurisdiction. No member state provides credit for any tax that was not paid to another state.
- No member state provides credit for tax paid in another jurisdiction if the purchaser recovered or could have recovered the tax.
- No member state indicated credit was available if the tax was paid in error in the other state but was no longer refundable (i.e. expiration of the statute of limitations for receiving a refund).

An additional question included in the survey focused on tax paid to another jurisdiction on a retail sale that was “sourced in accordance with the Agreement.” Most of the states responding to the survey indicated they would consider “sourced in accordance with Agreement” (Section 310) to mean the tax was legally due in that jurisdiction if they also imposed their tax on that particular product.

Workgroup Recommendation on (2): The Credit Workgroup recommends for purposes of the amendment that “properly and legally imposed” language be included in the amendment and that such phrase means,

- 1) the other jurisdiction’s statutes provide for the imposition of the tax on the retail sale or on the storage, use, or other consumption of the product;
- 2) there is no exemption or credit available in the other jurisdiction on the retail sale or on the storage, use, or other consumption of the product; and
- 3) the tax amount is not recoverable or could not have been recovered from the other jurisdiction by that purchaser at any time.

The workgroup also recommends that language should be included in the proposed amendment to specially indicate the retail sale was “sourced in accordance with the Agreement.”

Finally the workgroup recommends that the amendment include language to indicate the tax must have been “paid” to the other jurisdiction.

(3) Sourcing differences when both member and non-member states are involved

Different states have different rules for determining the location to which a particular transaction is sourced. Member states are required to source transactions in accordance with the SSUTA.

Except as permitted by Section 313.A.4. of the SSUTA, if a sale is properly sourced to the purchaser’s business address contained in the seller’s books and records, the purchaser’s address obtained during the consummation of the transaction, or the location from which the property was shipped because none of the other sourcing rules could be applied, are member states allowing a purchaser credit against their sales or use tax due for the tax paid to the seller? Including language in the proposed amendment to specifically address a member state’s requirement that credit for tax paid on a retail sale that is “sourced in accordance with the Agreement” be granted, will provide clarity for member states, sellers, and purchasers.

However, nonmember states are not required to follow the sourcing hierarchy provided in the SSUTA. Therefore, consideration needs to be given to address when a member state is required to allow credit for taxes paid on a transaction that takes place in a nonmember state using that

nonmember state’s laws but which may be sourced in accordance with the SSUTA to a member state.

Member states

Credit for the sales or use tax paid on a retail transaction that was properly sourced in accordance with the SSUTA should be allowed. Sellers should not be disadvantaged as a result of any requirement to collect a member state’s tax and the purchaser’s should be allowed this credit. When a transaction is sourced in accordance with Section 310 of the SSUTA and the tax was “properly and legally imposed” by the jurisdiction to which the retail sale was sourced, then credit for the tax paid should be allowed against a subsequent sales or use tax due in another member state, except as provided in Section 313.A.4. of the SSUTA.

Nonmember states

When a purchaser purchases a product from a seller located in a state that is not a member of the SSTGB should the Agreement include requirements of the member state regarding credit for tax paid to the nonmember state or is that beyond the scope of the Agreement? For example, a nonmember state may subject sales of tangible personal property to tax in its state when title to the property passes in the state, while a member state would source the sale under the SSUTA (i.e., where the purchaser “receives” the property). These differences between member and nonmember states exist today.

Workgroup Recommendation on (3): The Credit Workgroup recommends that, except as permitted by Section 313.A.4. of the SSUTA, for transactions involving only member states,

- 1) if the sale was properly sourced in accordance with the requirements of the SSUTA;
 - ~~1)2)~~if the tax was “properly and legally imposed” by the state to which the retail sale was sourced; and
 - ~~1)3)~~if the tax was paid by the purchaser to the seller;
- the member state must allow a credit against any subsequent sales or use tax due the member state on the storage, use, or other consumption of the product.

With respect to transactions between member and nonmember states, the workgroup recommends adding the following language to the amendment.

Nothing in this section shall limit any purchaser’s right under local, state, federal or constitutional law or a state’s obligation thereunder, to receive or provide a credit for sales or use taxes legally due and paid to other jurisdictions.

(4) Sales price differences

Under the Agreement, member states have the option to exclude from sales price delivery charges, installation charges, trade-in credit, and services necessary to complete the sale. For example, it is not uncommon for a purchaser to purchase a product in a state that includes installation charges in its definition of “sales price” and “purchase price” and subsequently move that product to another state. The other state may or may not include installation charges in its “sales price” or “purchase price” definitions.

Should the Agreement include:

- (a) a requirement that member states allow a credit for the total tax paid on the retail sale price of a product in one member state that includes items that are optional in the definition of sales price against the subsequent storage, use, and other consumption in another member state that excludes items that are optional from its definition of purchase price; or
- (b) an option for a state to reduce the amount of credit for the tax paid on the purchase price of the product for the differences in the definition of sales price between the member states provided the election is clearly noted in the member state's taxability matrix?

Workgroup Recommendation on (4): The Credit Workgroup recommends that (insert recommendation)

(5) Tax owed but not paid to first state and subsequent state now wants the tax – who gets the tax and under what circumstances?

As indicated in (1) above, the tax must have been paid to receive credit for tax paid to another jurisdiction. No member state provides credit for tax that was not paid to another state. No member state provides credit for tax paid in another jurisdiction if the purchaser recovered or could have recovered the tax. No member state indicated credit was available if the tax was paid in error in the other state but is no longer refundable (i.e., expiration of the statute of limitations for receiving a refund)

In addition, whether the scope of the amendment to the Agreement is to include requirements of member states for credit for use tax paid by the purchaser on the storage, use or other consumption of personal property and services against use tax due in another state when the product was subsequently moved to another state for storage, use or other consumption in that state has not been determined.

Nothing in the amendment is intended to prevent a state from providing credit for tax paid in areas not covered by the amendment or on terms and conditions more favorable to a seller or purchaser. Language is also being included to clarify that nothing in the amendment shall limit any purchaser's right under local, state, federal or constitutional law or a state's obligation thereunder, to receive or provide a credit for sales or use taxes properly and legally imposed and paid to other jurisdictions.

Questions have been raised regarding what if a purchaser does not pay a legally imposed use tax to a state and a second state in which the property was subsequently moved to for storage, use, or other consumption assesses use tax. Does the first state have to now allow a credit for the use tax assessed and paid in the second state against the use tax due in their state? In the alternative, if the purchaser goes back and pays the use tax in the first state, does the second state now have to credit and/or refund up to the amount of tax due in the second state for use tax paid to the first state. In addition, what happens if the statute of limitations is tolled in the second state for purposes of receiving a credit or refund?

Workgroup Recommendation on (5): The Credit Workgroup recommends that (insert recommendation).

(6) Credit for local taxes

In 2008 the credit workgroup began by reviewing Article V of the Multistate Tax Compact which has been adopted by 20 states.

Each purchaser liable for a use tax on tangible personal property shall be entitled to full credit for the combined amount or amounts of legally imposed sales or use taxes paid by him with respect to the same property to another State and any subdivision thereof. The credit shall be applied first against the amount of any use tax due the State, and any unused portion of the credit shall then be applied against the amount of any use tax due a subdivision.

Should the Agreement include a requirement for member states with no local jurisdictions that impose sales or use tax to:

- (a) only allow credit for the state sales or use tax paid to the other state;
- (b) allow credit for both state and local jurisdiction sales or use tax paid to another state; or
- (c) indicate whether both state and local tax credit is allowed on their taxability matrix?

Member states are not prohibited from having local jurisdiction tax rates under the Agreement. The survey conducted by the workgroup indicates the majority of states, whether or not they have local jurisdictions that impose sales and use tax, grant credit against their state and local use tax for sales and use tax paid to other states and local jurisdictions in those states. However, three member states, Indiana, Kentucky, and West Virginia, do not have local jurisdictions that impose sales and use tax and do not grant credit against their state use tax for sales or use tax paid to local jurisdictions outside of their state.

Workgroup Recommendation on (6): The Credit Workgroup recommends credit for tax paid on a retail sale include credit for the state and, if any, local tax on the retail sale that is paid or collected by the seller. The three member states that do not currently grant credit for tax paid to local jurisdictions may propose an alternative that allows them to maintain their current practice.

(7) Allocation of credit between state and local taxes –

In addition to the question concerning credit for local taxes paid, the workgroup considered whether there should a specific requirement for allocation of the credit between state and local tax paid. Article V of the Multistate Tax Compact provides the following, “The credit shall be applied first against the amount of any use tax due the State, and any unused portion of the credit shall then be applied against the amount of any use tax due a subdivision.”

The work group members felt that this was beyond the scope of the Agreement and a state decision. Leaving this matter up to the states does not burden sellers or purchasers as long as credit for the full amount of state and local taxes paid by the purchaser, up to that amount of tax due, is given.

Workgroup Recommendation on (7): The Credit Workgroup recommends that allocation of the credit for tax on the retail sale against the purchaser's state and local use tax liability should be governed by state law.

(8) Installment Sales

Some states impose their tax on installment sales based on when the sale takes place while others imposed their tax on installment sales using the cash basis and tax each payment as it is made. What happens when a product purchased in an installment sale is moved from a state that imposed its tax when the sale took place to a state that imposes its tax based on when each installment payment is made and vice-versa?

Workgroup Recommendation on (8) – The Credit Workgroup recommends that (insert recommendation).

(9) Credit for tax paid on purchase by seller against tax charged on sale by seller (real property after installation in one state and tangible personal property in another state)

Some states treat a transaction as a sale to an end user and consumer while other states treat that same transaction as a sale that the state has authorized as a sale for resale. For example, installation of tangible personal property to real property that is treated as a sale to an end user and consumer in one state while another state treats the same transaction as a purchase for resale. Should the Agreement include a requirement to give credit against a state's sales tax on the retail of a product for the tax paid on the purchase of that same product?

Generally, the state workgroup members felt this was beyond the scope of the Agreement and opposed including a requirement in the Agreement. They also indicated a transaction that is the purchase of a product and a subsequent transaction that is for the sale of the same product are two separate and distinct transactions.

Workgroup Recommendation on (9) – The Credit Workgroup recommends that the following provisions be included in the Agreement

1) Credit may be limited by a state to tax paid on the retail sale of a product that is subjected to use tax imposed by the member state on the storage, use or other consumption of such product.

~~1)2)~~ Nothing in this section prohibits a member state from providing credit on terms and conditions more favorable to a purchaser than the terms required by this section.

~~1)3)~~ Nothing in this section shall limit any purchaser's right under local, state, federal or constitutional law or a state's obligation thereunder, to receive or provide a credit for sales or use taxes legally due and paid to other jurisdictions.

(10) Issues specific to leases and rentals

The discussion concerning credit for tax paid that is “sourced in accordance with the Agreement” identified separate issues related to the lease or rental of tangible personal property. The workgroup decided to include a separate provision in the amendment to specifically address credit for tax paid with regard to leases or rentals of tangible personal property. The SSUTA contains separate sourcing provisions for retail sales and for leased tangible personal property and the SSUTA does not require member states to impose tax on the lease of tangible personal property in the same manner.

While the Agreement provides for a uniform definition of lease or rental and uniform sourcing rules for leases or rentals of tangible personal property under Section 310.B, states are not required to impose the tax on the lease or rental of tangible personal property at the same time. In general states impose their tax on each periodic payment, on the entire amount of the lease payments (lump sum or accelerated basis), or on the purchase price of the property by the lessor. Leased property moved from one state to another state that impose the tax at different times on the lease payments or on the purchase of tangible personal property for lease may result in the lessor collecting sales tax on the leased personal property in two states.

In March of 2011 the workgroup surveyed the states to determine at what time the state imposes tax on the lease or rental of tangible personal property and what credit for tax paid is provided by the states when the primary property location of the property moves to its state. The survey indicates some states do not allow credit for tax paid:

- on the lease payments where tax was imposed on a lump sum or accelerated basis against periodic payments subject to tax in its state when the property is relocated to its state,
- on the acquisition of the property against the periodic payments subject to tax in its state when the property is relocated to its state.

(a) Should the Agreement include:

- i) a requirement to allow credit for the full amount of the tax paid to the lessor on a lump sum or accelerated basis in one state against sales or use tax imposed in another state on each periodic payment after the primary property location of the leased property was moved to the second state;
- ii) a requirement to allow credit for only a prorated portion of the tax paid upfront on a lump sum or accelerated basis against the tax due on the amount of the lease payments made subsequent to the movement of the primary property location of the leased property to the second state; or
- iii) an option to do either (i) or (ii) above, but require each state imposing tax on the lease payments to indicate the allowance for credit for tax paid on their taxability matrix?

An additional question regarding credit for tax paid results if a state requires a lessor to pay sales or use tax to their state on the acquisition of tangible personal property that will be leased or rented. When the leased property is taxed at the time of acquisition and the property is subsequently relocated to a state that imposes its tax on each lease payment, the lessor must collect tax on the lease payments in the second state.

(b) Should the Agreement:

- i) Include a requirement to allow a credit for sales or use tax paid on the acquisition of the tangible personal property that will be leased against the sales or use tax due on the lease or rental payments in the second state.
- ii) Not have a requirement to allow a credit for tax paid by the lessor on the acquisition of the personal property that will be leased.
- iii) Require states to indicate in their taxability matrix if the state allows credit for tax paid by the lessor on the acquisition of property against sales or use tax due on the lease or rental payments subsequent to the relocation of the property in the state.

Workgroup Recommendation on (10)(a): The Credit Workgroup recommends that (insert recommendation)

Workgroup Recommendation on (10)(b): The Credit Workgroup recommends that (insert recommendation)

Other Questions: In addition to the issues identified above, various business community members have also indicated they would like to have the following issues addressed in the proposed amendment or interpretive rule:

- An interpleader provision which would be invoked if two or more Member States assert that the tax is due to them on the same transaction. *State Response:* The SSTGB should not get involved in deciding which state is entitled to the tax. In addition, the SSUTA and corresponding rules should be drafted clearly so that there is no question as to when a state must allow credit for tax paid to another jurisdiction.
- Purchasers should be entitled to a credit for the tax they paid, even if it was not legally due to the state in which it was paid. *State Response:* This issue is covered in part in (5) above. The states do not believe credit should be required if the tax paid was not legally due in the state where it was paid.
- A presumption should be made that the tax was paid if the purchaser was audited. *State Response:* This should be determined on a state-by-state basis.
- Credit for tax paid in error if the tax is not refundable by the other state. *State Response:* This issue is covered in part in (5) above. The states do not believe credit should be required if the tax paid was not legally due.
- Credit for tax paid by the purchaser directly to the state. *State Response:* This issue is covered in part (1) above with regard to tax on a retail sale. Whether the scope of the amendment includes credit for use tax paid in a state by the purchaser on the storage, use, and consumption of property and services against the subsequent storage, use and consumption of the property and services subsequently moved to another state has not been decided.
- Provisions which prioritize the purchaser's liability for tax. *State Response:* This issue is covered in part in (1) and (5) above. Whether the scope of the amendment includes credit for use tax paid in a state by the purchaser on the storage, use, and other consumption of property and services against the subsequent storage, use and other consumption of the property and services subsequently moved to another state has not been decided.
- Provisions allowing credits for tax paid to states by direct pay permit holders. *State Response:* This issue is determined on a state-by-state basis based on each state's requirements.

The expected goals of this workgroup are to: (1) recommend an amendment to the SSUTA relating to the allowance of credit against a member state's tax for tax paid to other jurisdictions; and (2) draft an interpretive rule that contains examples of how the proposed amendment would apply in various factual situations to insure consistent application.