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Business Airs Fears Over Purchaser Use Tax Issues at SST Meeting

By Dave Buehler © 2006, CCH Incorporated

While work on the Streamlined Sales and Use Tax (SST) Agreement thus far has focused largely on sellers and getting computerized collection systems running to collect sales tax on remote sales, attention recently has turned toward the other side of the transaction: purchasers and use tax liability.

The Agreement protects sellers who engage the services and utilize the software of a Certified Service Provider (CSP). The CSPs are to be audited and held liable for under-collecting, not the sellers who hire the CSPs. If the published rate is wrong, certain "hold harmless" provisions come into play. However, business leaders expressed their concern about the flip side of sales: will purchasers be granted similar "hold harmless" status?

The SST State and Local Advisory Council met March 7-8, 2006, in Atlanta, allowing state and local government officials and members of the business community to air concerns. The meeting was somewhat novel in focusing on issues concerning purchaser use tax as well as the topic of audits in general.

Purchaser Use Tax

Business wants protections for purchasers, who could later be audited by individual states on the same transactions on which the CSPs were audited. That creates a problem concerning exactly how a purchaser may prove in its books and records that it relied on the published rates. Perhaps, it was suggested, purchasers could prove reliance on published rates by demonstrating that they had downloaded the rates each month. "If the rate is wrong for sellers, it's wrong for purchasers," stated Susan Haffield, PricewaterhouseCoopers.

The theme of purchaser use tax being audited surfaced repeatedly during discussions of other topics during the conference. Business suggested that while, in some instances, purchasers may owe the use tax, purchasers could be protected from related penalties and interest.

A memorandum presented by interested members of the business community pointed to, among other issues, the fact that, while sellers' issues are being addressed, an area that needs development is the effect of the Agreement on purchasers. The paper notes that many of the Agreement's provisions generally either shift the burden to the purchaser or remain silent with respect to the purchaser. "As a result, the purchaser's compliance burden and audit exposure could be *increased* under the Agreement—a result not contemplated by the Streamlined Sales Tax Project or by business during development of the project," the paper states. Further, audit procedures for use tax have not been formulated in the Agreement. Federal legislation would likely require such

procedures. Purchasers need protections, too, given that sellers are protected by relying on state-supplied information.

“Businesses are concerned with states auditing both the seller and the purchaser on the same transaction,” the memo continues. “If a seller is registered and audited, the buyer should not be held liable for tax on those transactions.” As a solution to this problem, some in business suggested at the meeting that the Governing Board should provide a master list of audited SST sellers. Transactions involving listed sellers could be removed from a use tax audit.

Crafting Audits

Some business representatives assert that what the Agreement contains concerning audits will prove critical to its success. “This is going to be a key area to the Agreement,” said Richard Prem, Amazon.com.

A major and often repeated concern of business was whether tax officials would audit the seller, then go back and audit the purchaser. Also, a need for clarity exists as to how sampling for audits would be conducted. Overlap of audit periods was another problem cited.

Still, a huge gain came for business taxpayers when representatives of the states agreed to let business representatives participate in the process of shaping the audit process. “This is fantastic news,” Stephen Kranz, Council On State Taxation (COST), later commented. “From now forward, they (state administrators) will have open meetings about audits, and in the audits they will also consider implications for business purchasers.” However, state administrators did not appear to be willing to go as far as business in granting hold-harmless protection to purchasers, he said

Exemption Certificates

Will Yancey, PhD., CPA, from Texas, raised the issue of maintaining exemption certificates for SST audits. He said many large chain retailers who use their own software, Model 3 and Model 4 sellers under the Agreement, will not have computerized copies of exemption certificates. Often walk-up customers will hand a paper exemption certificate to such retailers when making a purchase at a store, for example, an office supply store or a construction supply store. Store managers will staple the paper certificate to an invoice for retention. With audits every three to four years, that means maintaining millions of pieces of paper.

Taxpayers should only be required to keep records as is their practice in the ordinary course of business, Yancey maintained. This means that these retailers should not be forced to computerize their exemption certificate archives. Individual retail locations generally keep this paper on site for about four to 14 weeks. The states, then, should show up within the retention period to audit.

Taxability Matrix

Also discussed was the taxability matrix. Business representatives called for a supplemental matrix of more detail, listing each state and what they tax or exempt. The

fear of being held liable for tax when uncertainty exists, perhaps about a new product, would be a likely deterrent to attracting companies to volunteer under the Agreement.

But talk of shielding taxpayers from tax liability on items that are in a gray area as far as taxable status, was confronted by R. Bruce Johnson, Utah State Tax Commission. “I have a real problem extending indemnity to things not listed,” Johnson said. “I don’t want to extend indemnity to what someone *thinks* is exempt.” He offered as an example American flags, which in some states are exempt. What if a T-shirt has a flag on it, and a seller assumes that the shirt is exempt. Should that seller be offered safe harbor? “No,” Johnson asserted.

Ohio, Texas Amendments

A particularly contentious debate arose in discussions of amendments to the Agreement proposed by Ohio and Texas. The Texas amendment was offered by Utah, since Texas is not a member of the Governing Board. Both proposals show reluctance to part with origin-based sourcing of sales tax in favor of destination-based sourcing, as called for by the Agreement. Ohio suggests a single statewide rate option for interstate sales that could not exceed the highest combined state and local tax rate in any jurisdiction in the state.

Members of the business community decried these proposals as an unnecessary complication rather than simplification of sales tax compliance. “The real simplification would have been one rate,” said Warren Townsend, Wal-Mart Stores, Inc. Stephen Olivier, ChevronTexaco, stated, “This is a big step backward. I just see this as adding hurt to the taxpayer.”

Beth Ann Kendzierski, Apria Healthcare, noted that a customer could be invoiced at different tax rates depending on whether her company delivered from an in-state location or out-of-state location. “If we present our national accounts with an invoice with two rates, that’s not going to fly,” Kendzierski stated. “Why don’t you make the effort to make it truly simplified instead of maintaining the status quo?”

Paul Goodman, Society of American Florists, spoke on behalf of 26,000 small businesses. “It’s the intrastate issues that are plaguing the florists,” Goodman said.