

THE FEDERAL TAX AUTHORITY[®]

PREPARED TESTIMONY SUBMITTED FOR THE RECORD
OF THE PENNSYLVANIA SENATE
FINANCE COMMITTEE PUBLIC HEARING REGARDING
**REQUIREMENTS FOR COLLECTING SALES TAX
ON TRANSACTIONS OVER THE INTERNET**

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TESTIMONY BY
R. DAVID L. CAMPBELL

CHIEF EXECUTIVE OFFICER, THE FEDERAL TAX AUTHORITY

I. PREAMBLE

Before I get started, I would like to thank Chair Mike Brubaker, Vice Chair Jane M. Earll, and the other distinguished members of the Finance Committee for providing this forum so that your constituents and members of the business community can voice their perspectives and opinions on proposed legislation regarding the collection of sales tax on internet transactions (and, presumably, other remote transactions such as mail order and telephone order).

II. BACKGROUND

For the record, my name is David Campbell. I am the chief executive officer of the Federal Tax Authority, or FedTax, founded in 2008. We are a Washington State Limited Liability Company with operations in Washington, Connecticut, and Kansas. Our management team includes highly experienced professionals who have been directly involved in building some of the most recognizable brands in e-commerce, including MasterCard, Google, WebMD, Microsoft, Expedia, and American Express. FedTax.net has been designated a Certified Service Provider by the Streamlined Sales Tax Governing Board specifically for our TaxCloud service, which I will discuss further in a moment.

III. PURPOSE

My purpose today is to urge you to adopt legislation that would update Pennsylvania's tax laws sufficiently to enable Pennsylvania to effectively collect sales tax on *all* retail commerce occurring within its borders, whether via a local or a remote retailer. Enacting such legislation is very important to alleviate the imbalance being felt by local retailers across the state, as increasingly they are seeing consumers browse their stores and ask clerks questions, only to go home and buy from online retailers to save on sales tax. Over time, the vanishing sales tax revenue has hurt not only the state, which is losing the sales tax proceeds, and local retailers, who are losing business, but even Pennsylvania residents themselves, as the loss of sales tax revenue has resulted in dramatic cuts to local services, including police, firefighters, and schools.

One option being presented today is affiliate nexus legislation, also known as the "Amazon tax." Affiliate nexus laws dictate that any retailer with in-state affiliates that bring in a certain amount of revenue has nexus in that state and therefore must collect sales tax for that state. The problem with affiliate nexus legislation, however, is that it's often ineffective: because such legislation hinges entirely upon an *elective* marketing

practice, online retailers have shown themselves more than willing to simply end their affiliate programs in states with affiliate nexus laws, ultimately hurting affiliates (many of which are small businesses) that rely on those programs for income. It is possible that *some* income may be generated through affiliate nexus legislation, but the recent experiences of North Carolina and Rhode Island strongly suggest the possibility of a grimly different outcome.

In our opinion, a better option is available to Pennsylvania: to adopt legislation conforming to the Streamlined Sales and Use Tax Agreement (SSUTA). As you may know, the goal of SSUTA is to simplify the administration of sales and use tax, making it easier for states to collect the tax due them. (More details on SSUTA can be found at <http://streamlinedsalestax.org>.) Twenty-four states are currently members of SSUTA, and more are joining all the time—forty-four states, including Pennsylvania, have been participating in SSUTA since its inception in 2000.

In addition, by adopting SSUTA legislation Pennsylvania would send a clear message to Washington, DC, that state-by-state efforts are an imperfect solution to this national problem. Rather, it is time for federal action to correct the growing inequity between local retailers that have to collect sales tax and online retailers that do not. It's time to shift the burden of calculating, reporting, and remitting tax on online purchases from individual consumers to online retailers. It's time for local communities to start receiving the sales tax revenue they are due, so they can stop cutting services for lack of funds. It's time to recognize that collecting sales tax on online purchases is fair, easy, and the right thing to do. It's time to pass the Main Street Fairness Act.

IV. BACKGROUND ON THE STREAMLINED SALES AND USE TAX AGREEMENT

I will restrain myself from a detailed description of the history and many accomplishments achieved by SSUTA in order to yield that analysis to Mr. Christopher Rants, who is also scheduled to testify before your committee today. Instead I will just briefly describe SSUTA. It is the result of the cooperative efforts of forty-four states, the District of Columbia, local governments, and the business community, and it aims to make collecting sales tax easy and simple in order to enable Congress to finally pass legislation allowing states to require out-of-state retailers to collect sales tax.

SSUTA achieves this goal by reducing or eliminating most, if not all, of the costs and administrative burdens of collecting sales taxes, through:

1. **Simplifying common definitions**, so that the tax category “candy,” for instance, means the same thing in all states
2. **Standardizing critical sales tax data**, such as sales tax rates, tax base definitions, and jurisdictional boundary definitions, so they can be consistently applied in all states
3. **Standardizing reporting procedures**, so that retailers don't have to submit different sales tax returns in each state

These measures are intended to ensure that neither retailers *nor* states expend an undue amount of resources to collect sales tax. As of January 2011, twenty-four states have met most or all of the legal and infrastructure requirements to become SSUTA members, and more states are currently moving to adopt these measures.

V. THESIS

As I am sure many in attendance today will agree, the collection of sales tax on internet transactions is important for Pennsylvania for numerous reasons, no matter which method (or methods) is enacted. My goal today is to discuss and preemptively refute the two main arguments you are likely to hear in opposition to these proposals:

1. A remote retailer with no operations within Pennsylvania would find it far too difficult to keep track of all of the state's tax rules.
2. Even if technology does make it possible to keep track of all of Pennsylvania's tax rules, sales tax management systems are prohibitively costly to acquire and difficult to implement, making them well out of the reach of small businesses.

These two arguments can be boiled down to one idea: For out-of-state retailers, collecting sales tax is prohibitively complex and costly.

This idea can be traced back to the 1967 Supreme Court ruling in *National Bellas Hess v. Illinois Department of Revenue*. In its majority opinion, the court ruled that “the **many variations in rates** of tax, in allowable **exemptions**, and in administrative and **record-keeping requirements** could entangle National's interstate business in a virtual welter of complicated obligations to local jurisdictions” (emphasis added). You may notice that the three main goals of SSUTA, mentioned earlier, are designed to alleviate precisely these three concerns.

I frequently cite this quote because it summarizes the ruling's basis in complexity and burden, which has rippled forward to today and created a tidal wave of unanticipated consequences. This ruling has shielded all out-of-state retailers from the obligation to collect sales tax, based purely on the notion that it would be too complex and place too much of a burden on businesses—and perhaps it would have, in 1967. That was the year the floppy disk was invented at IBM. It was also one year before Gordon Moore and Robert Noyce started a microprocessor company named Intel, and one year before Dr. Larry Roberts published a plan to develop ARPANET, which laid the foundation for the internet we know today.

Clearly, the world is a very different place today, forty-four years after the Supreme Court's ruling in *Bellas Hess*. Today, auction sites like eBay and music services like iTunes easily manage millions of items for sale at any given moment. Today, keeping track of a few thousand local tax rates is no longer an insurmountable technical or administrative burden. The basis for the *Bellas Hess* ruling no longer applies.

Modern technology, including the sales tax management service offered by my company, has made it easy for retailers to collect sales tax for any state in the U.S. I am proud to say that our service, TaxCloud, enables any retailer of any size to easily collect sales tax and comply with all the provisions of *either* form of legislation under consideration by this committee today. The old objections no longer apply. Collecting sales tax for any state is not difficult. It's easy, and it costs retailers nothing.

VI. CERTIFIED SERVICE PROVIDERS

Recognizing that technology is the key to making it easy for any retailer to collect sales tax for any state and that technology providers are well-positioned to provide retailers with automated systems to collect and remit

sales tax, the Streamlined Sales Tax Governing Board established a certification process whereby technology providers have their systems tested and verified by each of the SSUTA member states. Upon successful completion of this process, these companies earn the title of "Certified Service Provider" (CSP) and are authorized to perform *all* of a retailer's sales tax functions. Due to the logistical complexity of the certification process (it takes about a year of coordinated efforts among all member states to certify a CSP), companies may apply to become CSPs only during a brief application period every other year.

I am pleased to say that our company, FedTax, was designated a Certified Service Provider on July 1, 2010. In addition, although we initially built TaxCloud to be a SSUTA-certified service, merchants can also use it to comply with affiliate nexus requirements—in fact, it's being used in both ways by internet retailers today. Finally, we are currently the only company that is providing its sales tax services at **absolutely no cost** to retailers.

VII. MAKING SALES TAX CALCULATION AND COLLECTION EASY

As a Certified Service Provider under SSUTA, we handle every aspect of sales tax calculation, collection, and remittance for our clients. Our TaxCloud service calculates, in real time, the sales tax due on any transaction. It also determines whether an item is tax-exempt and automatically integrates changes and updates to tax codes, rates, and jurisdictions—for every jurisdiction in the nation. Finally, TaxCloud keeps track of all collected sales taxes to be remitted by retailers, generates detailed state-by-state reports, and for SSUTA states even files the sales tax returns and remits tax payments to all applicable jurisdictions.

What's more, TaxCloud is extremely **easy** for anyone to use. Most retailers are able to set up TaxCloud in less than 20 minutes, and it can be integrated into virtually any accounting or e-commerce shopping cart system. In short, we're offering a service that handles all sales tax management obligations for retailers at absolutely no cost to them.

The very existence of TaxCloud refutes the primary argument of those who say that collecting sales tax on remote purchases would be burdensome for small businesses, that it is too costly and time-consuming. It is difficult to see the merits of this argument when a free service is available that handles every aspect of sales tax management at absolutely no cost to retailers. With no complicated tax rules to figure out, no returns to prepare, no fees to pay or costly software to install, it's difficult to understand what burdens the collection of sales tax would impose on small businesses. TaxCloud costs nothing and takes very little time to monitor and operate. A business of any size, even a sole proprietorship, would have no trouble collecting sales tax with TaxCloud or a similar sales tax management service.

VII. CONCLUSION

By enacting legislation to extend the definition of nexus or (preferably) to conform to SSUTA, Pennsylvania would be taking a much-needed step toward closing its budget gap and recovering hundreds of millions of dollars in uncollected sales tax. (According to a recent study at Carnegie Mellon University, Pennsylvania loses between \$264 million and \$398 million every year in uncollected sales tax.¹) Federal legislation such as

¹ Strauss, Robert P. "The Impact of Not Collecting Sales and Use Taxes from Internet Sales into Pennsylvania," 2011. http://standwithmainstreet.com/sites/standwithmainstreet.com/files/pa_impact_study.pdf

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the Main Street Fairness Act, which is expected to be introduced in Congress shortly, would enable SSUTA member states—and *only* SSUTA member states—to require all retailers to collect sales tax.

In the past ten years, the percentage of revenue that localities receive from sales tax has dropped dramatically. That sales tax revenue pays for schools, police, and other local initiatives and priorities, and with the loss of sales tax revenue, funding for local communities is being cut everywhere. This trend cannot be considered a coincidence—as more and more consumers go online, less and less funding goes to locally approved initiatives. By enacting legislation that ultimately allows it to join SSUTA or affiliate nexus legislation, Pennsylvania will take an important step toward ensuring that much-needed revenue is returned to its communities, secure in the knowledge that with CSPs like FedTax and sales tax management services like TaxCloud, any retailer can easily calculate and remit sales tax for every jurisdiction in the country—at no cost to the retailer.

True, enacting such legislation is just a first step toward resolving the unfair practice of requiring local small businesses to collect sales tax while not requiring the same of larger, and frequently more technologically sophisticated, out-of-state retailers. It's only a first step, but it's a crucial one. Momentum on this issue is building, and Pennsylvania now has the opportunity to send a message to Congress that the problem of uncollected sales tax, which affects nearly every state in the nation, needs a national solution. The best way to send this message is to introduce and enact legislation to require online retailers with Pennsylvania affiliates to collect sales tax or (preferably) to join the Streamlined Sales and Use Tax Agreement.

Thank you once again for allowing me this opportunity to express our support.



R. David L. Campbell

Chief Executive Officer

The Federal Tax Authority (FedTax)