



TAXATION AND BUDGET REFORM COMMISSION

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Staff Analysis and Economic Impact Statement

Measure: SR 17

REFERENCE:

ACTION:

Sponsor: Finance & Taxation Committee

1. FTC
2. GPSC

Favorable
Pre-Meeting

Subject: Streamlined Sales and Use Tax
Agreement

- 3.

Date: January 24, 2008

I. Summary:

Statutory Recommendation 17 brings Florida law into compliance with the provisions of the Streamlined Sales and Use Tax Agreement (Agreement) and enables the state to petition for membership in the Agreement.

The Streamlined Sales Tax Project's legislation includes two components necessary to accomplish the project's goals. First, states would adopt enabling legislation referred to as the Uniform Sales and Use Tax Administration Act ("Act"). The Act allows a state to enter into an agreement with one or more states to simplify and modernize sales and use tax administration. The Act does not require any amendments to a state's sales and use tax law.

Secondly, states would amend or modify their sales and use tax laws to achieve the simplifications and uniformity required by the participating states working together. The project refers to this legislation as the Streamlined Sales and Use Tax Agreement ("Agreement"). A state is in compliance with the Agreement if the effect of the state's laws, rules or regulations, and policies is substantially compliant with each of the requirements of the Agreement.¹

CP 18 will accomplish the first step in the process by requiring the legislature to enact enabling legislation. If passed, SR 17 will enact the second step in the process by providing implementing legislation to conform state tax laws to other states' laws under the pact agreement.

¹ Streamlined Sales Tax Project, *Executive Summary*, at <http://www.streamlinedsalestax.org>. (Last visited January 2008).

II. Present Situation:

Sales and Use Taxes

Florida is among the 45 states and the District of Columbia that impose sales and use taxes. Florida is also among the eight states that do not have a personal income tax and rely heavily on sales tax collections to fund government operations.

The state sales tax rate of 6 percent is imposed on the cost or price of tangible personal property or a service at the moment it is sold to a purchaser.² The seller or dealer is required to collect the sales tax from the purchaser at the time of the sale.³ The dealer must remit the sales taxes collected to the Florida Department of Revenue.⁴ “The overall purpose of the use tax is to recoup sales tax revenues that the state would lose when goods purchased out-of-state are brought into Florida for use here.”⁵ “A use tax ordinarily serves to complement the sales tax by eliminating the incentive to make major purchases in states with lower sales taxes; it requires the resident who shops out-of-state to pay a use tax equal to the sales tax savings.”⁶

States’ attempts to enforce the use tax by requiring out-of-state firms to collect taxes from customers led to the 1967 U.S. Supreme Court decision, *National Bellas Hess, Inc. v. Illinois*, 386 U.S. 753 (1967). In the case, the court ruled that states lack the authority to compel out-of-state firms to collect use taxes unless those firms have “nexus” in the state. Nexus was defined by physical presence, having an office or store, owning property, or employing workers in a state. The court decision was rooted in the Commerce Clause of the U.S. Constitution which gives Congress jurisdiction over issues involving interstate commerce. The court said that imposing a tax collection obligation on out-of-state sellers would impose an “undue burden” on interstate commerce. *National Bellas Hess* was reaffirmed by the U.S. Supreme Court in *Quill Corp. v. North Dakota*, 112 S.Ct. 1904 (1992). In the *Quill* decision, the court cited the complexity and fluidity of sales tax structures from state-to-state as an undue burden on remote sellers and interstate commerce.

Electronic Commerce

According to the U. S. Department of Commerce, the United States had more than 210,080,067 Internet users as of November 2006. In November 2007, the Census Bureau reported that the estimate of retail e-commerce for the third quarter of 2007 was \$34.7 billion. Total retail sales for the quarter were estimated at \$1,020.4 billion and e-commerce sales in the third quarter accounted for 3.4 percent of total retail sales.⁷

² Section 212.06(1) (a), F.S.

³ Section 212.06(3)(a), F.S.

⁴ Section 212.11, F.S.

⁵ *Kuhnlein v. Department of Highway Safety and Motor Vehicles*, 646 So. 2d 717, 722 (Fla. 1994).

⁶ *Minneapolis Star and Tribune Co. v. Minnesota Comm’r of Revenue*, 460 U.S. 575, 581-582 (1983).

⁷ U. S. Census Bureau, *U.S. Census Bureau News*, November 19, 2007, at:

<http://www.census.gov/mrts/www/ecommm.html> (Last visited January 11, 2008).

Based on the increasing use of the Internet for purchases, the inability of states to collect online sales taxes can have a dramatic effect on state and local revenues.

Streamlined Sales Tax Project

The Streamlined Sales Tax Project was organized by the National Conference of State Legislatures (NCSL) Executive Committee's Task Force on State and Local Taxation of Telecommunications and Electronic Commerce in March 2000. The project is an effort, with input from state governments, local governments and the private sector, to simplify and modernize sales and use tax collection and administration. Section 213.27(8), F. S., authorizes the Department of Revenue to enter into contracts with public or private vendors to develop and implement a voluntary system for sales and use tax collection and administration.⁸

In 2001, the NCSL Executive Committee endorsed the Uniform Sales and Use Tax Administration Act and the Streamlined Sales Tax Agreement. States that adopted the Uniform Sales and Use Tax Administration Act, or had their governors issue similar authorizations, were authorized to participate in the next phase of discussions with other states to develop a multi-state, voluntary, streamlined system for the collection and administration of state and local sales and use tax.

There are 42 states and the District of Columbia involved in the project. Thirty-four states and the District of Columbia had their legislatures enact enabling legislation. These states, including Florida, make up the Streamlined Sales Tax Implementing States (SSTIS). Twenty-two states, as of January 2008, have passed compliance legislation conforming to the Streamlined Sales Tax Agreement and are members of the governing board. States with full membership are Arkansas, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, New Jersey, North Carolina, North Dakota, Oklahoma, Rhode Island, South Dakota, Vermont, West Virginia, and Wyoming. Associate member states are Nevada, Ohio, Tennessee, Utah, and Washington.

The goal of the Streamlined Sales Tax Project is to establish a Streamlined Sales Tax System with:

- Uniform definitions within tax laws. Legislatures choose what is taxable or exempt in their state and agree to use the common definitions for key items in the tax base.
- Rate simplification. States will be allowed one state rate and a second state rate in limited circumstances (food and drugs). Each local jurisdiction will be allowed one local rate.
- State level tax administration of all state and local sales and use taxes. Businesses will no longer file tax returns with each local government that conducts business in a state. Each state will provide a central point of

⁸ Section 213.27(8), F.S.

administration for all state and local sales and use taxes and the distribution of the local taxes to the local governments.

- Uniform sourcing rules. The states will have uniform rules to determine which jurisdiction will tax a transaction.
- Simplified exemption administration for use- and entity-based exemptions. Sellers are relieved of the “good faith” requirements that exist in current law and will not be liable for uncollected tax.
- Uniform audit procedures.
- State funding of the system. To reduce the financial burdens on sellers, states will assume responsibility for funding some of the technology models.

III. Effect of Proposed Changes:

Statutory Recommendation 17 brings Florida into compliance with the provisions of the Streamlined Sales and Use Tax Agreement (Agreement) and enables Florida to petition for membership in the Agreement. States are required to have sales and use tax laws compatible with other states as set forth in the Agreement.

Aside from tax administration issues, the most significant issues in this measure relate to changes to the definitions and the replacement of the bracket system with a rounding methodology to compute tax due on amounts less than one dollar.

By conforming definitions in Florida’s sales tax law with the Agreement, some transactions that are currently exempt from tax may become taxable and some transactions that are currently taxable may become exempt.

Subsection (2) of s. 212.08, F.S., provides for medical exemptions. With the adoption of the Agreement’s medical definitions, the following items will be treated differently than they are under current law:

- Items no longer exempt unless sold with a prescription:
 - Hypodermic syringes;
 - Artificial eyes and limbs, orthopedic shoes, and crutches;
 - Lithotripters; and
 - X-ray opaques used in connection with medical x-rays of humans or animals.
- Items newly exempt:
 - Chemical compounds and test kits for the diagnosis and treatment of nonhuman disease, illness or injury; and
 - Cosmetics and toilet articles sold as an over-the-counter drug or with a prescription.

Under current Florida law, all non-100 percent juice drinks are subject to sales tax, while 100 percent fruit juices are exempt. In the measure, the term “soft drinks” is defined as nonalcoholic beverages that contain natural or artificial sweeteners. Soft drinks do not

include beverages that contain milk or milk products, soy, rice, or similar milk substitutes, or greater than 50 percent of vegetable or fruit juice by volume. As a result of this change in definition, fruit juices containing 50 percent or more juice will become exempt from the sales tax.

Under current Florida law, all candy is subject to sales tax. In the measure, candy is redefined to mean a preparation of sugar, honey, or other natural or artificial sweeteners in combination with chocolate, fruits, nuts, or other ingredients or flavorings in the form of bars, drops, or pieces. Candy does not include any preparation that contains flour and requires no refrigeration. This definition will result in candy containing flour becoming exempt from the sales tax and certain chocolate products used for baking becoming taxable.

Under current law, ice cream, frozen yogurt, and similar frozen dairy or nondairy products sold in cones, small cups, or pints, and popsicles, frozen fruit bars, or other novelty items are taxable. In order to comply with agreement definitions, these items will become exempt under this measure.

Compliance with the Agreement requires the Legislature to repeal the brackets for calculating the amount of tax due for sales amounts of less than one dollar. Under the agreement, the brackets must be replaced with a conventional rounding methodology. The state will lose some revenue as the result of the rounding methodology. Under the rounding methodology, taxes of \$0.005 are rounded up to the next cent. Taxes of less than \$0.005 are rounded down to zero.

Under current Florida law, the brackets for the collection of the state sales tax are as follows.

- (a) On single sales of less than 10 cents, no tax shall be added.
- (b) On single sales in amounts from 10 cents to 16 cents, both inclusive, 1 cent shall be added for taxes.
- (c) On sales in amounts from 17 cents to 33 cents, both inclusive, 2 cents shall be added for taxes.
- (d) On sales in amounts from 34 cents to 50 cents, both inclusive, 3 cents shall be added for taxes.
- (e) On sales in amounts from 51 cents to 66 cents, both inclusive, 4 cents shall be added for taxes.
- (f) On sales in amounts from 67 cents to 83 cents, both inclusive, 5 cents shall be added for taxes.
- (g) On sales in amounts from 84 cents to \$1, both inclusive, 6 cents shall be added for taxes.
- (h) On sales in amounts of more than \$1, 6 percent shall be charged upon each dollar of price, plus the appropriate bracket charge upon any fractional part of a dollar.

Under the brackets, for example, the state collects \$0.05 on a \$0.67 sales transaction. Under the rounding methodology ($.06 \times \$0.67 = \0.0402), the state will collect \$0.04 on a \$0.67 sales transaction.

Other changes to Florida Statutes include:

- Amending or creating definitions to comply with the Agreement for “certified service provider;” “computer;” “computer software;” “delivery charges;” “direct mail;” “electronic;” “lease,” “let,” or “rental;” “seller;” “Model 1 seller;” “Model 2 seller;” “Model 3 seller;” “sales price;” and “tangible personal property.” The definition of “sales price” is revised to include all delivery charges.
- Limiting the \$5,000 cap on discretionary sales surtax to the sale of motor vehicles, aircraft, boats, motor homes, manufactured homes, and mobile homes. In addition, specifying the time at which changes in surtaxes may take effect; providing the criteria for determining the situs of certain sales; providing for databases to identify taxing jurisdictions; and providing criteria to hold purchasers liable or harmless for failure to pay the correct amount of taxes.
- Providing the criteria for determining the location of transactions involving tangible personal property, digital goods or services, and for the lease or rental of tangible personal property. The recommendation also requires purchasers of direct mail to use the direct mail forms.
- Authorizing the executive director of the Department of Revenue to maintain and publish a taxability matrix in a format approved by the governing board; and providing the circumstances under which a seller, certified service provider, or purchaser is held harmless from tax, interest, and penalties resulting from relying on erroneous data provided by the state in the taxability matrix.
- Providing amnesty, with some exceptions, for uncollected or unpaid sales or use tax to a seller who registers to pay or collect and remit applicable sales or use tax on sales made to purchasers in this state in accordance with the terms of the Agreement. For the amnesty to apply, the seller must not have been registered with the Department of Revenue in the 12-month period preceding the effective date of the state’s participation in the Agreement.
- Providing for Simplified Sales and Use Tax registration, certification, liability, and audit. A seller that registers under the agreement agrees to collect and remit sales and use taxes for all taxable sales into the member states. When registering, the

seller may select a model 1, model 2, or model 3 method of remittance or other method allowed by law to remit the taxes collected.

“Model 1 seller” means a seller that has selected a certified service provider as its agent to perform all the seller’s sales and use tax functions.

“Model 2 seller” means a seller that has selected a certified automated system to perform part of its sales and use tax functions, but retains responsibility for remitting the tax. “Model 3 seller” means a seller that has sales in at least five member states, has total annual sales revenue of at least \$500 million, has a proprietary system that calculates the amount of tax due each jurisdiction, and has entered into a performance agreement with the member states which establishes a tax performance standard for the seller. A certified service provider is the agent of a model 1 seller with whom the certified service provider has contracted for the collection and remittance of sales and use taxes, and is liable for sales and use tax due each member state on all sales transactions it processes for the model 1 seller. A model 2 seller that uses a certified automated system remains responsible and is liable to the state for reporting and remitting tax. A model 3 seller is liable for the failure of the proprietary system to meet the performance standard. The executive director of the Department of Revenue may certify a person as a certified service provider and a software program as a certified automated system. In addition, the department may establish one or more sales tax performance standards for model 3 sellers.

- Providing the effective date of state rate changes for services covering a period starting before and ending after the statutory effective date. The new rate applies to the first billing period starting on or after the effective date for rate increases. The new rate applies to bills provided on or after the effective date for a rate decrease.
- Providing for notice of state rate changes. A sales and use tax rate change imposed under ch. 212, F.S., is effective on January 1, April 1, July 1, or October 1. The Department of Revenue must provide notice of such rate change to all affected sellers 60 days before the effective date of the rate change.
- Revising the procedures by which a dealer may obtain a credit or refund of taxes paid on the unpaid balance of worthless accounts. Dealers, including both dealers required to file federal income tax returns and those who are not required to file the returns, may claim a credit or tax refund when they would be eligible for a bad debt deduction for federal income tax purposes. When the claim for credit exceeds the amount of sales taxes due in a period, a refund claim may be filed within 3 years of the due date of the return in which a bad debt could first be claimed.

- Deleting the provisions that determine whether certain leases or rentals of motor vehicles for a period of less than 12 months are taxable in Florida.
- Providing a procedure for a purchaser to obtain a tax refund of tax collected by a dealer. A purchaser must make a written request for a tax refund to dealers. The request must contain all information necessary to determine the validity of the claim. A purchaser may not take any action against a dealer to secure the refund until 60 days after the dealer's receipt of the request for a refund.
- Deleting the requirements of the current method of calculating taxes (brackets) and requiring that the tax computation be carried to the third decimal place and rounded to the next whole number, if the third decimal place is greater than four.
- Providing tax exemptions for food and food ingredients and dietary supplements. Food and food ingredients included as exempt from tax are bakery products, if sold without eating utensils. Bakery products include bread, buns, biscuits, bagels, croissants, pastries, doughnuts, Danish, cakes, tortes, pies, tarts, muffins, bars, cookies, and tortillas.

Dietary supplements are any product that supplements the diet and contains a vitamin, a mineral, an herb or botanical, or an amino acid. "Prepared food" products and tobacco are not exempt from tax. Prepared food includes sandwiches sold for immediate consumption and a combination of hot and cold food items, and food sold with eating utensils provided by the seller. Prepared food does not include food that is only cut, repackaged, or pasteurized by the seller, eggs, fish, meat, and poultry.

The tax exemption does not apply to "soft drinks." Soft drinks are defined as nonalcoholic beverages that contain natural or artificial sweeteners. Soft drinks do not include beverages that contain milk or milk products, soy, rice, or similar milk substitutes, or greater than 50 percent of vegetable or fruit juice by volume. Therefore, fruit juices containing 50 percent or more juice are exempt from the sales tax. The tax exemption also does not apply to candy. Candy is defined as a preparation of sugar, honey, or other natural or artificial sweeteners in combination with chocolate, fruits, nuts, or other ingredients or flavorings in the form of bars, drops, or pieces. Candy does not include any preparation that contains flour and requires no refrigeration. Therefore, this definition will result in candy containing flour becoming exempt from the sales tax.

- Providing for medical exemptions. Items exempt from sales tax include any drug; any durable medical equipment, mobility enhancing equipment, or prosthetic device; hypodermic needles; over the counter drugs; hearing aids; dental prostheses; funerals; and chemical compounds and test kits used for the diagnosis

or treatment of disease, illness, or injury intended for one time use. Chlorine is not exempt from tax when it is used for the treatment of water in swimming pools.

IV. Constitutional Issues:

A. Constitutional or Legislative Matter:

The proposed revisions to the Florida Statutes can be accomplished legislatively.

B. Other Constitutional Issues:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

Implementing the Streamlined Sales and Use Tax will enhance Florida's sales and use tax by reducing the costs of collecting and remitting state and local sales and use taxes. However, the fiscal impact of the collection and remittance of sales and use taxes by mail-order and e-commerce businesses that do not currently collect taxes for Florida is indeterminate.

The Economic and Demographic Research Office has not conducted an estimating conference to determine the fiscal impact of this statutory recommendation. However, during the 2005 Legislative Session, the Revenue Estimating Conference adopted estimates for a similar measure, CS/SB 56. The estimates were reviewed by issue and the revisions in definitions of "medical exemptions," "fruit drinks," and "ice cream" resulted in a loss of sales tax revenue. The conference results also indicated that changing the method used to calculate sales taxes from brackets to rounding will have a negative impact on sales tax revenue, and changing the definition of "sales price" to include delivery charges will result in an increase in sales revenue.

Streamlining Fiscal Impact (millions of dollars)
CS/SB 56

Issues	State		Local		Total	
	Cash	Recurring	Cash	Recurring	Cash	Recurring
Rounding	(16.5)	(39.5)	(3.4)	(8.3)	(19.9)	(47.8)
Fruit Drinks with 50% or more juice	(1.0)	(2.4)	(0.2)	(0.5)	(1.2)	(2.9)
Frozen Dairy and non-dairy	(3.6)	(8.5)	(0.7)	(1.7)	(4.3)	(10.2)
Medical Exemptions	(1.2)	(2.9)	(0.2)	(0.6)	(1.4)	(3.5)
Delivery Charges	5.5	13.4	1.2	2.8	6.7	16.2
Candy/Food	2.5	5.9	0.5	1.3	3.0	7.2

B. Private Sector Impact:

If Florida becomes a participant in the pact, some currently uncollected use taxes may be paid at point of sale, which could cause consumers to pay more for remote sales purchases.

C. Government Sector Impact:

Voluntary collection of use taxes at point of sale by remote sales vendors may increase the amount of use tax remitted to the state.

A key feature of the Streamlined Sales Tax System is that states are responsible for funding some of the technology models; therefore, there may be an associated cost to the Department of Revenue. Estimates of the cost to the department are not available at this time.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.