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Five State Tax Policy Changes That Would Modernize Laws and Ease Administration and Compliance

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Council On State Taxation

As the 2023 state legislative sessions are progressing in earnest, legislators should seize the opportunity to fix or continue to fix issues that challenge tax professionals, taxpayers, and state tax administrators. This article focuses on five policy recommendations to modernize state tax laws, ease administration, and improve compliance:

1) Provide at least one month after the federal extended deadline for corporate taxpayers to file state income tax returns;

2) Provide a 30-day safe harbor for personal income tax filing obligations of traveling employees and corresponding withholding obligations of their employers;

3) Improve taxpayer reporting of federal tax adjustments, including partnership adjustments, by incorporating the Multistate Tax Commission model legislation collaboratively developed with other national tax associations;

4) Participate partially or fully in the Streamlined Sales and Use Tax Agreement; and

5) Centrally administer local taxes and fees, such as lodging/accommodation taxes, and improve local (and state as necessary) e-filing and electronic payment processes.

I. PROVIDE AT LEAST ONE MONTH AFTER THE FEDERAL EXTENDED DEADLINE FOR CORPORATE TAXPAYERS TO FILE STATE INCOME TAX RETURNS

Sufficient time to accurately file a corporate income tax return is imperative to fair, efficient, and customer-focused tax administration. Prior to a 2017 federal law change that extended the federal corporate filing deadline from September 15 to October 15 for calendar-year corporate income tax filers, most states allowed corporate taxpayers to file their state returns one month following the September 15 federal extended due date. An inadvertent consequence of the federal law change in 2017 was that over 30 states' extended corporate income return due dates now fell on the same date as the federal extended date. Fortunately, several states have already rectified this problem by extending their corporate income tax return date to fall at least one month after the revised federal extended due date; however, 18 states still impose conflicting due dates. These states are shown in Figure 1.[1]

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COST has a history of encouraging state tax policy makers to improve tax administration through the use of "Administrative Scorecards." These scorecards highlight areas where a state imposes either effective or deficient tax administrative practices. COST's three primary scorecards are: "Best and Worst of State Tax Administration," https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/admin-scorecard-final-may-2020.pdf; "Best and Worst of State Sales Tax Systems," https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/cost-2022-sales-tax-systems-scorecard.pdf; and, in partnership with the International Property Tax Institute, "Best (and Worst) of International Property Tax Administration," https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/2019-international-property-tax-scorecard---final-june-20.pdf.

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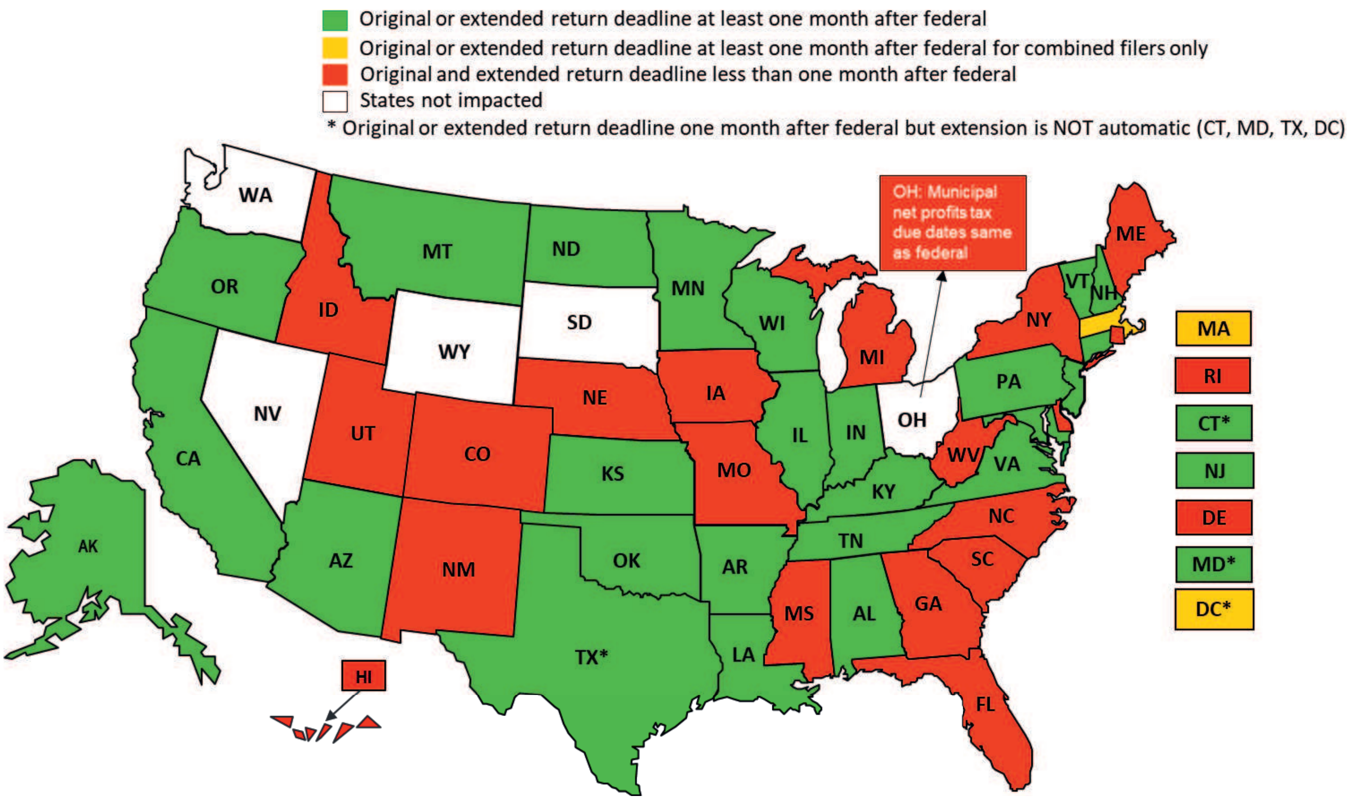
[1] Figure 1 only addresses state corporate income taxes. Extension should be automatic; states that only provide an extension upon request, *i.e.,* not automatically, are also listed.

Figure 1. – States With and Without a One-Month Extension



Sources: figures 1 through 4, Council On State Taxation; figure 5, ''The Efficiency of State Administration of Local Taxes,'' Janelle Fritts and Jared Walczak, Tax Foundation, December 2022.

Because corporate income state tax returns are derived from information computed from federal returns, state returns cannot be accurately completed until after the federal return is completed. We focus on this request for corporate income tax returns because multijurisdictional corporations must make significant adjustments to federal income (*e.g.*, apportionment of that income, application of credits, adjustments for depreciation, and certain federal provisions such as GILTI, etc.) before filing a state corporate income tax return. States that provide taxpayers with an automatic one-month extension after the federal extended deadline are thus rewarded with greatly enhanced accuracy of state returns, thereby easing the burden on tax administrators by reducing the number of amended returns that will be filed. This additional time is also critical for adjustments required under federal tax changes such as the Tax Cuts and Jobs Act of 2017, the Coronavirus Aid, Relief, and Economic Security Act, and the Inflation Reduction Act.

Importantly, any tax liability owed would still be based on the original due dates, including estimated payments. Interest and penalties associated with a late payment would still be owed under existing state law. In other words, resolution of this issue is easily accomplished by automatically extending the due date of the return to avoid late-filing penalties, without a significant impact to a state's revenue stream. While some state tax administrators have indicated they can address abatement of late-filing penalties on a case-by-case basis, this approach creates uncertainty and is not practical to use on an annual basis. Also, corporations required to submit letters of good standing regarding their tax obligations when contracting with state or local governments may be negatively impacted, even when a late filing penalty is abated.

To address this issue, we propose states adopt the following model legislation:

A. For tax years beginning on or after January 1, 20XX, calendar year and fiscal year [taxpayer] returns shall be due no later than one month after the due date established under the Federal Internal Revenue Code, including any applicable extensions granted by the Internal Revenue Service.

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B. No penalty due to late filing shall be incurred by a taxpayer granted a federal extension if its state return is filed no later than one month after the period of time specified in the Federal extension. The [taxpayer] does not need to apply to the [revenue director] for an extension of time within which to file the taxpayer's state return.

II. PROVIDE A 30-DAY SAFE HARBOR FOR PERSONAL INCOME TAX FILING OBLIGATIONS OF TRAVELING EMPLOYEES AND CORRESPONDING WITHHOLDING OBLIGATIONS OF THEIR EMPLOYERS

Both businesses and governments share a common problem when employees travel for work temporarily in states where they are not residents. In nearly half the states, traveling employees incur a personal income tax liability on the first day in a state, and employers trigger a concomitant withholding obligation. Requiring nonresidents to file tax returns for short work stints in each state where they work, and the lack of uniform rules for when states subject nonresidents to personal income taxes, is impractical and inefficient. It also unfairly casts numerous private- and public-sector employees as tax scofflaws because many states' personal income tax withholding and tax filing requirements are impractical for compliance purposes.

Fortunately, many state tax administrators acknowledge strict compliance is not administratively feasible in this area, even agreeing employees in their own agencies are not strictly following other states' laws in this area. However, technically, an employee's temporary work in another state without any withholding on wages can subject the employee and the employer to civil and criminal penalties. Most work travel is of short duration, such as attending a training event or business meeting in a nonresident state. Imposing an income tax for such work burdens the U.S. economy by forcing both employees and employers to comply with a patchwork of confusing, outdated (and at times predacious) nonresident state income tax laws. State laws vary on day thresholds, dollar thresholds based on income earned in the nonresident state, and, in at least one case, a combination of day and income thresholds. This also can impact the ability for an employee to claim a credit for tax paid to another state if the employee's resident state does not similarly impose such a tax.

According to the Federation of Tax Administrators: ''Complying with the current system is . . . indeed difficult and probably impractical.''[2] The problem is unjustly compounded for employees who reside in states that do not impose an income tax because they cannot take a credit on their home state's income tax return for income tax paid to a nonresident state. Effective and efficient tax administration demands a reasonable and uniform threshold among states.

There is a solution to this quagmire. A minimum 30-day threshold — like that provided by laws enacted by Illinois in 2019,[3] and Louisiana[4] and West Virginia[5] in 2021 — would ease unreasonable tax burdens on America's increasingly mobile workforce and their employers. Vermont's Department of Taxes in 2022 changed its guidance to offer a 30-day threshold for nonresident employee withholding only.[6] Providing a uniform, fair, and easily administered law in all states with personal income taxes would help ensure that a fair amount of tax is withheld and paid to states without imposing an undue burden on employees and employers. After 30 days in a nonresident state, an employee would incur income tax from that state and, accordingly, be able to credit the amount paid against the income tax imposed by the resident state.[7]

The 30-day threshold was chosen based on a COST survey of employers and has been the standard in proposed legislation brought before Congress.[8] Because most business travel is shorter than 30 days, this uniform threshold would instantly bring most traveling employees (including government employees) and their employers into compliance. The definition of a ''day'' includes all workdays, regardless of when they occur (*e.g.*, weekdays, weekends, federal holidays, etc.) to count against the threshold. Thus, the 30-day

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[2] Statement of Harley Duncan before the U.S. House of Representatives Committee on the Judiciary, Subcommittee on Commercial and Administrative Law (Nov. 1, 2007).

[3] S.B. 1515, 101st Gen. Assemb. (Ill. 2019). Exceptions are made for certain types of employees — *e.g*., professional athletes, professional entertainers, and qualified production employees (in states that offer certain types of film tax credits based on a nonresident state's income tax earned in the state.

[4] S.B. 157; Louisiana is only providing a 25-day threshold which we hope to extend to a 30-day threshold in the future.

[5] H.B. 2026 (2021 RS).

[6] https://tax.vermont.gov/business/withholding.

[7] A credit would not be required if the resident state does not impose an income tax or does not similarly tax this type of income.

[8] *E.g.*, H.R. 1864, 112th Cong. (2012); H.R. 1129, 113th Cong. (2013–14); H.R. 2315, 114th Cong. (2015–17); H.R. 1393, 115th Cong. (2017–18); S. 4318, 116th Cong. section 403 (2019–20). Sen. Charles E. Schumer, D-N.Y., however, has prevented legislation passed in the U.S. House from being considered in the Senate and opposes efforts to include it as part of a COVID-19 relief package. *See* Jad Chamseddine, *Federal Remote Worker Tax Relief Could be Available by Year's End*, Tax Notes State, Dec. 14, 2020, p. 1205.

threshold is analogous to the "full month of work-days." A threshold shorter than 30 days would result in compliance difficulties because of the need to carve out some types of days (*e.g.*, weekends) or certain types of activities (*e.g.*, attendance at trade shows). A single, comprehensive 30-day threshold is far simpler and thus preferable because it will foster compliance and ease of administration by employees, employers, and states.[9]

In contrast, in July 2011, the MTC adopted its Model Mobile Workforce Statute. North Dakota in 2011 and Utah in 2022 passed legislation enacting the MTC model statute.[10] The MTC statute is more restrictive. An employer is not required to withhold a state's income tax on a nonresident's wages, and a nonresident is not subject to income tax in a state, if (1) the nonresident was in the state for no more than 20 days in a tax year; (2) the nonresident's state of residence offers a similar exemption or does not impose an individual income tax; and (3) the nonresident has no other source of income in the state, (4) the person does not perform real property construction services, and (5) is not a key employee of the employer (by reference to IRC section 416(i)) or, oddly enough, a construction contractor. This essentially excludes an officer of a corporate employer that has an annual compensation of more than $150,000, and the 50 highest-paid employees of a noncorporate employer. We discourage states from using the MTC model *per se* due to these complexities. Instead, we recommend the model provided below.

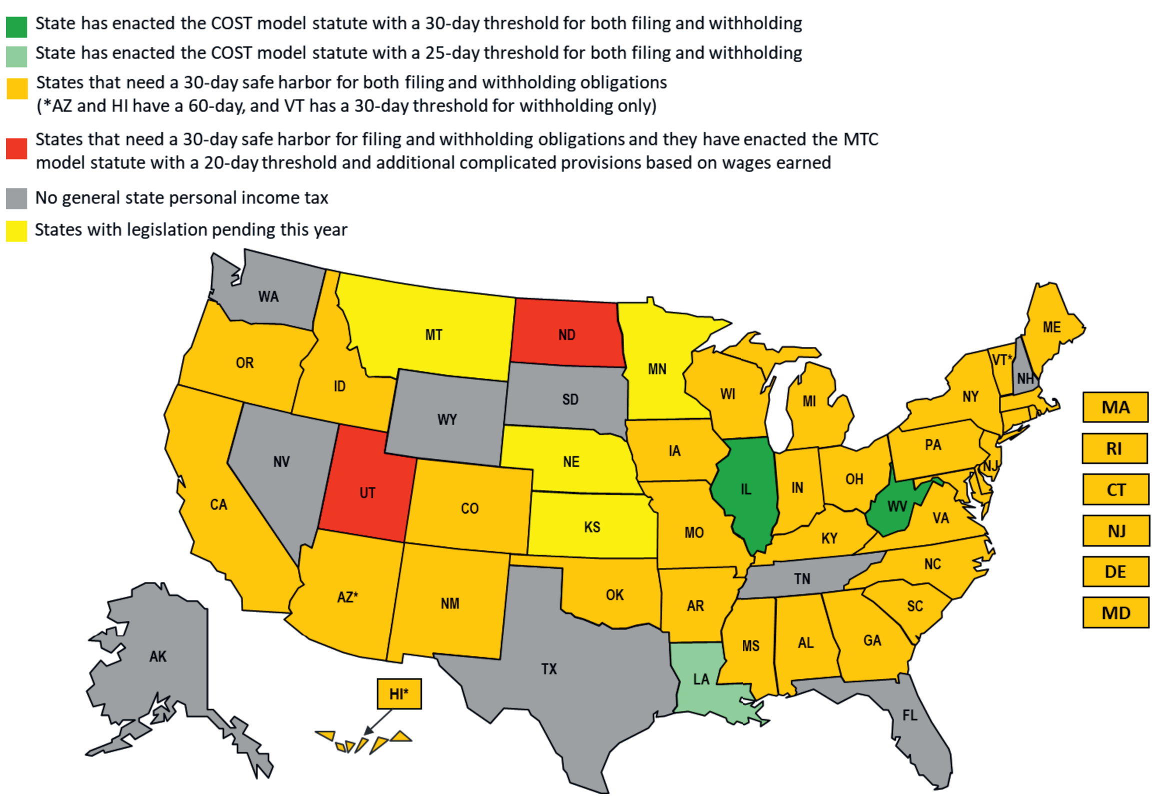
Figure 2 indicates states that have adopted a safe harbor threshold that applies to both employer withholding and the imposition of an income tax on nonresident employees.[11]

[9] This issue is important at the local level in states like Michigan and Ohio that authorize local income taxes.

[10] S.B. 2170, 62nd Legis. Assemb. (N.D. 2011) (reenacting and amending N.D. Cent. Code section 57-38-59.3).

[11] Some states have dollar thresholds, but such thresholds only complicate compliance because when a dollar threshold is exceeded is unclear (*e.g.*, commissions, bonuses, etc.).

Figure 2. – States Filing and Withholding Thresholds



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Relying solely on a reasonable, time-based (rather than dollar-based) threshold eliminates the need for most employees to track travel for tax purposes. When employees travel, they do not think in terms of dollars earned while away from home; instead, they track days on business travel. If a dollar threshold is imposed, it would require employers to track and calculate employee income for all traveling workers, a task that is next to impossible for employees paid partially through bonuses and commissions at the end of the year. A reasonable time-based threshold (30 days) would allow employers to better analyze employee travels and improve compliance for employees who travel to a nonresident state for significant periods. It eliminates complexities of calculating bonuses, commissions, and other deferred benefits to comply with a dollar threshold. A dollar threshold nullifies the potential compliance gains from a uniform rule.[12] It would also require employers to coordinate payroll systems with payments made to employees by third parties. Third-party payments may include sick or disability payments, supplemental retirement pay, and various types of stock compensation and relocation benefits, all of which may be considered wages to the employee. It is extremely challenging (and impractical) for employers to track and incorporate supplemental wages generally paid outside an employer's payroll system and add that information to internal payroll systems. And lastly, while a day is the same everywhere, the concept of income is defined differently in every state. A dollar threshold would thus either require a model definition of income — which would significantly alter state tax statutes — or require employees to research specific state statutes where they expect to travel to calculate earnings on a complex per-diem basis.

For the reasons discussed above, the following is model legislation we propose states adopt to address this issue.

Nonresident Withholding and Reporting Threshold Draft Legislation

[Section 1]

(A) As used in this section:

(1) "Professional athlete" means an athlete who performs services in a professional athletic event for compensation.

(2) "Professional entertainer" means a person who performs services in the professional performing arts for compensation on a per-event basis.

(3) "Public figure" means a person of prominence who performs services at discrete events, such as speeches, public appearances, or similar events, for compensation on a per-event basis.

(4) "Qualified Production employee" means a person who performs production services of any nature directly in connection with a state qualified [film, television, or other commercial video production] for compensation, provided that the compensation paid to such person are qualified expenditures under [state's incentive program], and that such compensation is subject to withholding as a condition to treating the compensation as a qualified production expenditure.[1]

[1] A "production employee" exception is optional, based on whether it is needed to avoid undercutting a state's film, television, or other commercial video production incentive program.

(5) "Time and attendance system" means a system through which an employee is required, on a contemporaneous basis, to record the employee's work location for every day worked outside the state where the employee's employment duties are primarily performed and which is designed to allow the employer to allocate the employee's compensation for income tax purposes among all states in which the employee performs employment duties for the employer.

(B)(1) Compensation, as defined under [state statute cross-reference], paid to a nonresident individual is exempt from the tax levied under [state statute cross-reference] if all of the following conditions apply:

(a) The compensation is paid for employment duties performed by the individual in this state for thirty or fewer days in the calendar year;

(b) The individual performed employment duties in more than one state during the calendar year;

(c) The compensation is not paid for employment duties performed by the individual in the individual's capacity as a professional athlete, professional entertainer, public figure, or qualified production employee; and

(d) The nonresident individual's state of residence: i) provides a substantially similar exclusion, or ii) does not impose an individual income tax, or iii) the individual's income is exempt from taxation by this state under the United States Constitution or federal statute.

(2) Except as otherwise provided in this division, an employer is not required to withhold taxes un-

[12] Employees frequently receive stock commissions, relocation benefits and other benefits such as personal use of a company car that generate income. These supplemental wage payments are based on factors not related to salary and cannot be estimated before the end of the year.

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der [state statute cross-reference] from compensation that is paid to an employee described in division (B)(1) of this section. If, during the calendar year, the number of days an employee spends performing employment duties in this state exceeds the thirty-day threshold described in division

(B)(1)(a) of this section, an employer shall withhold and remit tax to this state for every day in that calendar year, including the first thirty days on which the employee performs employment duties in this state.

(C) The [revenue department] shall not require the payment of any penalties or interest otherwise applicable for failing to deduct and withhold income taxes as required under [state statute cross-reference] if, when determining whether withholding was required, the employer met either of the following conditions:

(1) The employer at its sole discretion maintains a time and attendance system specifically designed to allocate employee wages for income tax purposes among all taxing jurisdictions in which the employee performs employment duties for such employer, and the employer relied on data from that system.

(2) An employer maintaining records under subsection (1) shall not preclude an employer's ability to rely on an employee's determination under subsection (3).

(3) The employer does not maintain a time and attendance system, and the employer relied on the employee's annual determination of the time the employee expected to spend performing employment duties in this state, provided, however, that the employer did not have (a) actual knowledge of fraud on the part of the employee in making the determination and (b) provided that the employer and the employee did not collude to evade taxation in making the determination.

(D) For purposes of this section, an employee shall be considered present and performing employment duties within this state for a day if the employee performs more of the employee's employment duties in this state than in any other state during that day. Any portion of the day during which the employee is in transit shall not be considered in determining the location of an employee's performance of employment duties. However, if an employee performs employment duties in a resident state and in only one nonresident state during one day, such employee shall be considered to have performed more of the employee's employment duties in the nonresident state than in the resident state for such day.

[Section 2]

The enactment by this act of [state code section] applies to taxable years beginning on and after January 1, 202X.

[Section 3]

If any provision of this act, or the application of such provision to any person or circumstance, is held to be unconstitutional, then the remainder of this act, and the application of the provisions of such to any person or circumstance, shall not be affected thereby.

III. IMPROVE TAXPAYER REPORTING OF FEDERAL TAX ADJUSTMENTS BY INCORPORATING THE NEW MTC CONSENSUS MODEL

Beginning in tax year 2018 (*i.e.,* partnership returns on Form 1065 filed in 2019) and following an audit, the IRS default process is to assess and collect tax from a partnership (entity) rather than the partnership's partners.[13] A partnership may still opt to push out audit adjustments to its partners, requiring the partners to report and pay any additional tax due. Although states conform to the IRC to derive taxable income, the states generally impose their own independent assessment and refund provisions. Thus, most states need to enact legislation to efficiently collect tax following an audit under the new federal partnership audit regime.

This federal change creates an opportunity for states to improve processes for reporting IRS adjustments for all taxpayers (including individual and corporate taxpayers). Fortunately, the MTC formed a workgroup several years ago and worked with other national tax associations that address state tax issues such as COST, the American Institute of CPAs, and the Tax Executives Institute to comply with the federal law changes for partnerships and improve the MTC's prior 2003 reporting model. Approved in 2018, and recently revised at the MTC's meeting in November 2020, the new MTC Model Statute (MTC Consensus Model) should be used by state legislatures

[13] Bipartisan Budget Act of 2015, Pub. L. No. 114-74. The intent of the changes was to address issues with the collection of tax through multiple tiered partnerships. Over a 10-year period it was estimated to raise approximately $10 billion. Partnerships had an option to elect into the new audit regime pre-2018; however, few partnerships made that election.

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to improve taxpayers' reporting of federal changes.[14] Importantly, while the MTC Consensus Model extensively addresses the new federal partnership audit regime, it includes equally important procedures that apply to all taxpayers required to report their federal tax changes to the states.[15]

States conforming to the entire MTC Consensus Model prevents taxpayers from submitting multiple amended returns to a state before an IRS audit for a tax period is truly final (*e.g*., serial reporting). A state should provide at least 180 days for the federal adjustment to be reported to the state. Further, when the general state statute of limitations is closed, any corresponding state adjustment should be limited to the change at the federal level. Providing at least 180 days is the gold standard. Both COST's policy position and the MTC Consensus Model recommend that states allow taxpayers 180 days, and by mutual agreement with the state revenue agency, extend that period for more complicated filings.[16] Finally, if a taxpayer fails to report federal changes to a state, it raises the question of how long the statute of limitations period remains open. Absent fraud, many state laws limit tax assessments to a set period after the reporting of the final federal determination (*e.g*., six years). These issues are addressed in the MTC Consensus Model.

The format to report a federal adjustment to a state should not be overly complicated. States should allow taxpayers to use spreadsheets to ease taxpayer compliance and simplify state tax administration (especially for complex returns). States should include the MTC Consensus Model's *de minimis* provision, which does not require a taxpayer to file if the adjustment is below a set threshold (*e.g*., less than $50 additional tax due or refunded).[17] Taxpayers that are confident additional state tax will be due pending an IRS audit to a state should be able to easily make estimated payments before a final determination. This practice benefits the state by accelerating revenue collection and benefits taxpayers by allowing them to reduce interest and penalties on any additional tax owed. Again, the MTC Consensus Model addresses all these issues.

To account for constitutional limitations imposed on states, the state reporting requirements under the MTC Consensus Model appropriately differ from federal procedures. Procedurally, rather than imposing the same default method used at the federal level (*i.e.,* in which the partnership pays), the default under the MTC Consensus Model is essentially status quo. The default at the state level requires the partnership to notify the state and its partners of a federal adjustment within 90 days of final determination, but its partners must report and pay tax due on an adjustment within 180 days of that final determination. However, a partnership can elect to pay any additional tax for its partners within 180 days of the final determination. Tiered partnership structures are also addressed, requiring all audit adjustments to be reported within 90 days of the final federal deadline of the audited partnership for those tiered partners. Notably, the MTC Consensus Model includes a provision that allows a state partnership representative to differ from the federal partnership representative; an automatic 60-day extension for partnerships with thousands of partners (K-1 reports); and a provision that allows taxpayers and the state revenue agency, by mutual agreement, to use an alternative reporting or payment process.

The MTC Consensus Model's provisions, both for reporting of general IRS changes and those specific to IRS partnership audits, should be enacted by the state legislatures. See Figure 3. Ultimately, the more widespread the adoption of the MTC Consensus Model, the more efficient voluntary compliance will be for taxpayers and state revenue agencies.

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[14] The new MTC Consensus Model is available on the COST website, at https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/costs-proactive-legislative-initiatives/proposed-model-rar-statute-technical-corrections-final.pdf.

[15] Some states have focused on only applying the changes to address partnerships; however, the MTC Consensus Model as a whole addresses the reporting of federal tax changes for all taxpayers including statute of limitation issues, waivers, estimated payments, etc.

[16] The MTC Consensus Model also addresses entities that file combined or consolidated returns as a group. The "trigger" for the final determination date does not occur until the IRS completes its audits for a tax period that covers all members of that group.

[17] This could also address reporting changes for foreign taxes under IRC section 905(c) to prevent multiple state reporting of federal changes that have little to no impact on state tax liabilities.

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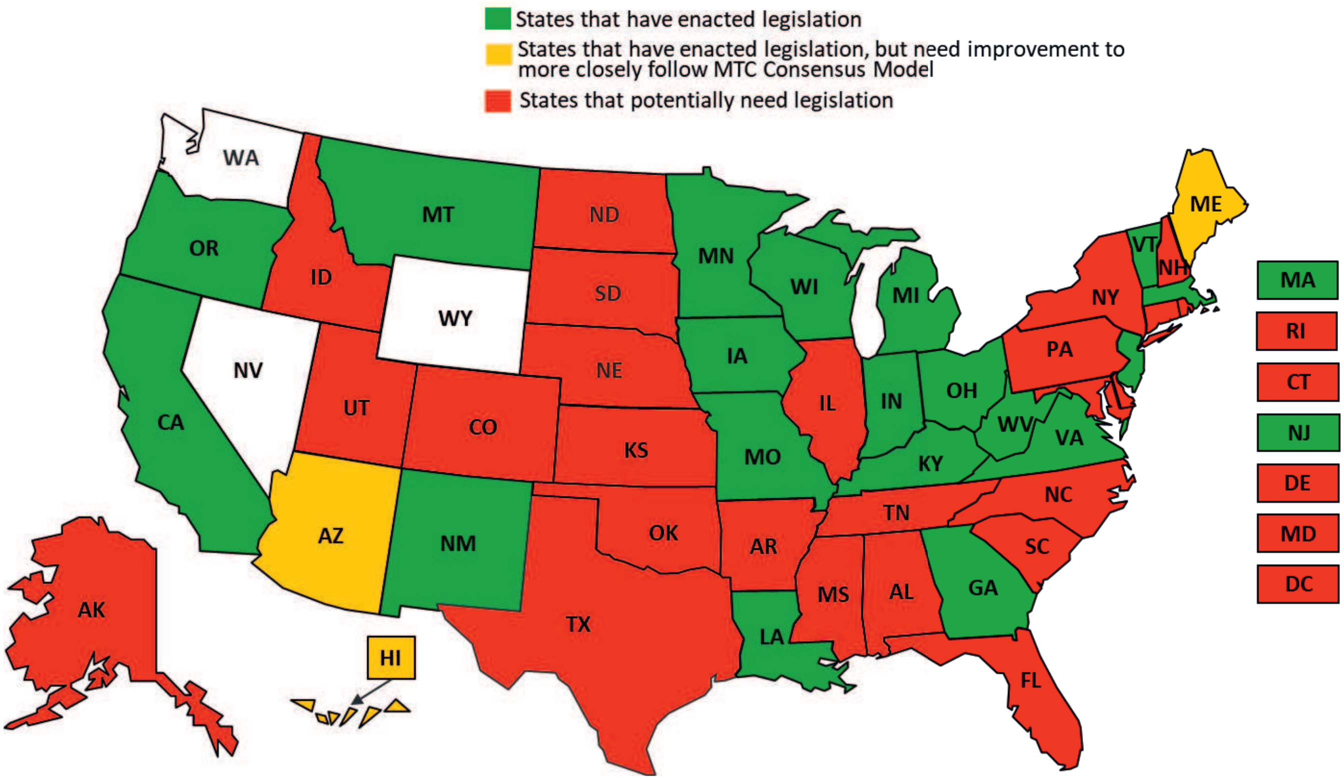
Figure 3. – States' Enactment of MTC Consensus Model



IV. PARTICIPATE PARTIALLY OR FULLY IN THE SSUTA

COST has actively participated in the Streamlined Sales Tax Project since its inception. For large and small sellers, more statewide uniformity is needed to efficiently collect and remit state sales and use taxes (and applicable local sales and use taxes). As a result of the U.S. Supreme Court's *Wayfair* decision in 2018, all sales tax states have adopted some form of economic nexus (*e.g.*, over $100,000 in sales to purchasers in a state)[18] to subject sellers without a physical presence in their state. However, nonparticipating Streamlined Sales Tax States have largely ignored a key feature noted by the Court in *Wayfair*: the reduced burdens on taxpayers achieved through full membership by a state in the SSUTA.[19] Regardless of whether reducing undue burdens is a constitutional requirement, state revenue administrators and legislatures should seek to improve their sales and use tax structures to improve administration and compliance with those taxes.[20]

In December 2022 COST issued its second scorecard that evaluates and grades state administration of sales tax systems. Although participation in the SSUTA was only one of many features of state sales tax administration evaluated,[21] SSUTA states fared

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[18] While COST supports the dollar threshold for states asserting economic nexus for sales tax purposes, it does not recommend the states' use of a transactional threshold because it can inefficiently (to both businesses and the states) pick up de minimis sales and is difficult for some sellers to calculate. South Dakota introduced legislation this year, S.B. 30, that would eliminate its 200-transaction threshold.

[19] *South Dakota v. Wayfair Inc*., 585 U.S. ___, 138 S. Ct. 2080 (2018). The Court noted that "South Dakota affords small merchants a reasonable degree of protection. The law at issue requires a merchant to collect the tax only if it does a considerable amount of business in the State; the law is not retroactive; and South Dakota is a party to the Streamlined Sales and Use Tax Agreement." *Id.* at 2098.

[20] For more information on the inefficient and ineffective U.S. sales tax system, see Frieden and Lindholm, *U.S. State Sales Tax Systems: Inefficient, Ineffective, and Obsolete*, Tax Notes State, Nov. 30, 2020, p. 895.

[21] Frieden, Nicely, and Nair, *The Best and Worst of State Sales Tax Systems*, COST (Dec. 2022), https://www.cost.org/

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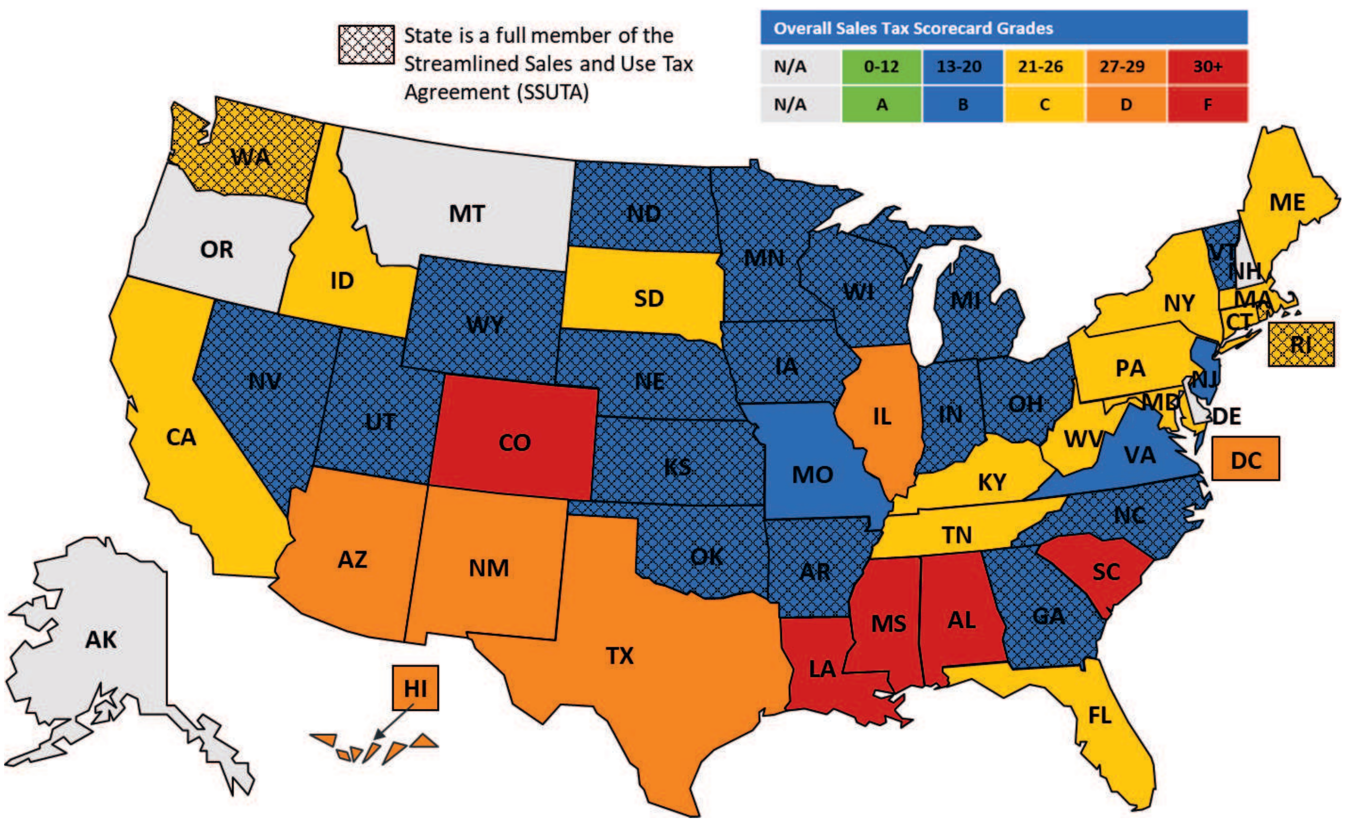
much better overall.[22] The following chart shows how SSUTA states compared to non-SSUTA states.

globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/cost-2022-sales-tax-systems-scorecard.pdf.

[22] States also need to consider making their marketplace facilitator laws, as warranted, to more closely follow the National Conference of State legislatures model, https://www.ncsl.org/Portals/1/Documents/Taskforces/SALT_Model_Marketplace_Facilitator_Legislation.pdf?ver=2020-01-30-122035-320. COST recently adopted a policy position on the importance of uniformity with the states' marketplace facilitator laws, available at https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/marketplace-faciliator-laws-policy-statement-final-june-2020.pdf.

Figure 4. – SSUTA States and COST Scorecard Overall Grades



Ideally, states that do not participate in SSUTA should take steps to become full-member states. Besides providing uniformity, participation in SSUTA brings together state tax administrators, state legislators, and the business community to interact and resolve sales and use tax issues that affect multiple states. Acknowledging that full compliance with SSUTA may take some time, the SSUTA Governing Board created a process for nonmember states to participate in assisting sellers to collect state sales and use taxes by providing Certified Service Provider (CSP) services (with states reimbursing some of those costs) and use of SSUTA's central registration system.[23] Often referred to as ''Streamlined Light,'' the benefits of a nonparticipating state initiating these services include: (1) reducing undue burdens; (2) providing similar CSP approval/reimbursement/audit processes; (3) allowing states to work together on sales tax issues; and (4) increasing uniformity.

Importantly, Congress may revisit this area. June 2022, the U.S. Senate Finance Committee held a hearing addressing the impact of the *Wayfair* decision.

[23] Streamlined Sales Tax Governing Board, ''Nonmember State Participation in Streamlined,'' https://www.streamlinedsalestax.org/docs/default-source/miscellaneous/nonmember-state-participatione532c93f98474a0aa273f65014dd31d2.pdf?sfvrsn=43f69c86_6.

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Small businesses and a consultant assisting small businesses with collecting and remitting the states' sales/use taxes raised concerns with the lack of uniformity and the cost of compliance. The federal Government Accountability Office (GAO) also issued a report in November 2022, after interviewing multiple interested parties (including COST), noting the lack of uniformity and cost incurred by businesses from states using inconsistent definitions, thresholds, and processes.

The following model legislation was approved by the SSUTA Governing Board to help non-SSUTA states craft legislation to increase their participation in the SSUTA:[24]

Model Utilizing Streamlined Sales and Use Tax Services Act

Definitions.

"Central Registration System" means the central registration provided by the Governing Board pursuant to Article IV of the Streamlined Sales and Use Tax Agreement.

"Certified service provider" means an agent certified by the Governing Board to perform the seller's sales and use tax functions as provided for under the Governing Board's contract with such providers.

"Governing Board" means the Streamlined Sales and Use Tax Agreement's Governing Board, including its various committees that address certified service provider and central registration services and issues.

Authorization.

The [Department] is authorized to consult and contract with the Governing Board, and other states as necessary, to allow sellers to use the Governing Board's certified service providers and central registration services, and as necessary, work jointly with other states to accomplish these ends.

1) Provide and maintain an electronic, downloadable database of all sales and use tax rates for the jurisdictions in this state that levy a sales or use tax.

2) Provide and maintain an electronic, downloadable database that assigns the addresses and zip codes in the state to the applicable taxing jurisdictions.

3) Complete the Streamlined Sales and Use Tax Agreement's Taxability Matrix and Certificate of Compliance, noting how the State's sales and use tax law follows or deviates from those requirements.

The [Department] shall also work with the Governing Board to:

1) Establish and provide a certification process to allow certified service providers to receive compensation, similar to that for the Governing Board's full member states. Non-SSUTA states may have a different compensation structure solely to account for additional complexities in collecting and remitting this State's sales and use tax due to not being a Governing Board full member state.

2) Enter into a contractual relationship with the Governing Board and/or the Governing Board's certified service providers. At a minimum, the contractual relationship shall address:

A. The responsibilities of the Governing Board, certified service providers, and the sellers that contract with the certified service provider related to liability for proper collection and remittance of sales and use taxes.

B. The responsibilities of the Governing Board, certified service providers, and the sellers that contract with the certified service provider related to record keeping, auditing, and the protection and confidentiality of taxpayer information.

C. The method and amount of compensation to be provided to the certified service provider by this State for the services the certified service provider provides to certain sellers.

3) The [Department] is authorized to pay annual dues to the Governing Board, not to exceed the dues calculation that would be owed if the State was a Governing Board full member state.

4) [State adds any necessary language to comply with the State's purchasing and contract laws here.]

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[24] The full model is available on the SSUTA website, https://www.streamlinedsalestax.org/docs/default-source/miscellaneous/model-act-for-nonmember-state-participationfbe3b70b50e5420eb4eecac8cd652e7c.pdf?sfvrsn=7457c968_6.

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5) The [Department] shall also comply with the Governing Board's requirements to use the Board's central registration system and is authorized to enter into a contract consistent with the requirements imposed on the Governing Board's full member states.

Relief from Liability.

1) Sellers and certified service providers are relieved from liability to the state for having charged and collected the incorrect amount of sales or use tax resulting from the seller or a certified service provider relying on 1) erroneous data provided by the state in its rate and boundary databases, or 2) erroneous data provided by the state concerning the taxability of products and services as provided in the Taxability Matrix.

2) Sellers and certified service providers are relieved from liability to the state for having charged and collected an incorrect amount of sales and use tax resulting from the seller or certified service provider relying on certification by the [Department] of the accuracy of the certified service provider's tax rules and automated systems.

Effective Date. This act shall be effective on X date.

V. CENTRALLY ADMINISTER LOCAL TAXES AND IMPROVE LOCAL (AND STATE AS NECESSARY) E-FILING AND ELECTRONIC PAYMENT PROCESSES

The COVID-19 pandemic was a wakeup call to the importance of efficient e-filing and electronic payment systems both at the state and local levels. While many state revenue agencies have vastly improved their e-filing systems to make uploading documents and accessing multiple accounts easier, the systems used by many local governments remain deficient. For example, a payment processor for several lodging entities noted that it must file over 1,000 paper (hard copy) local lodging returns each reporting period. Property taxes, which are mostly locally administered, are also a problem.

The ability to file all returns and remit payments at a state centralized location would be ideal. Increasingly, efforts are underway by policymakers seeking to expand marketplace facilitator collections of local taxes and fees (*e.g*., lodging taxes). Such collections should not be required unless the state has a central administration system which a taxpayer can use to register and remit the local taxes and fees.[25] Additionally, the local taxes and fees should have the same tax base and provide adequate time before imposing the collection of local taxes and fees. If central administration of a local tax and fee is not possible, there should be no marketplace facilitator collection requirement and the local governments should be required to implement efficient e-filing and payment systems. This is particularly important with lodging taxes and property taxes. The systems should allow taxpayers to file tax returns (including property tax renditions), make payments, and initiate the filing a tax appeal. While this will require an investment in technology, the improved efficiency in processing filings and payments creates a win-win situation for both tax administrators and taxpayers.

The process to file tax disputes and conduct hearings at the state and local level also must be modernized to allow electronic filing of appeals (on an elective basis) and to provide taxpayers the option of using virtual hearings after the pandemic. Allowing taxpayers and practitioners an election (not mandatory) to submit an appeal electronically helps mitigate issues they face over timely filing of an appeal and helps simplify and standardize the filing of an appeal. Traps for the unwary, such as the requirement to provide appeal notices to multiple parties, should also be eliminated. While in-person meetings should still be an option in the future, it is efficient for all parties when audit and appeal hearings are held virtually in a protected environment.

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[25] For more information on this issue, *see* "*Locally Administered Sales and Accommodations Taxes: Do They Comport With Wayfair?*" available at: https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/local-study.pdf.

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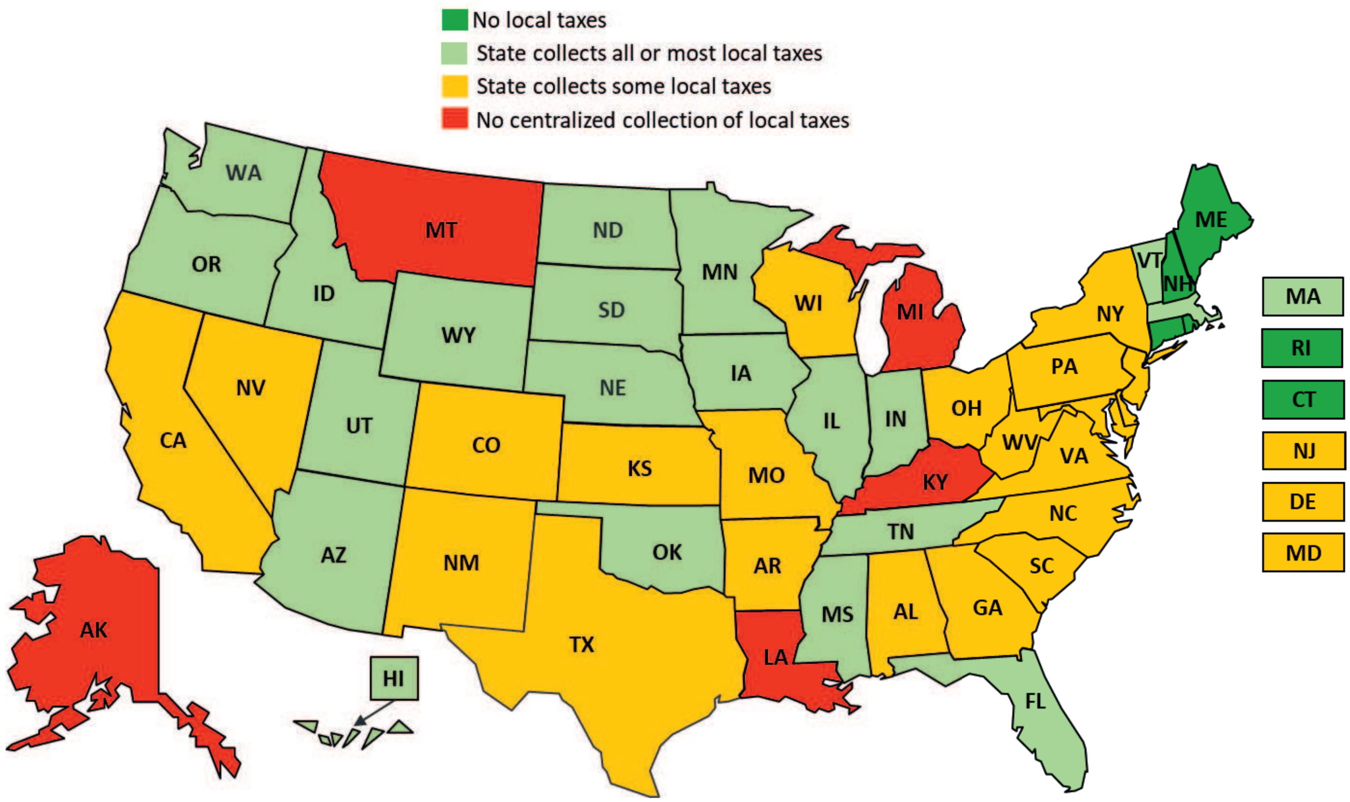
Figure 5. – Centralized Collection of Local Taxes



CONCLUSION

We have policy recommendations to modernize state tax laws, ease administration, and improve compliance. Similar to past years, COST anticipates that 2023 and 2024 will be busy legislative years with state and local government officials addressing many tax issues. We look forward to working with state chambers of commerce, other taxpayer associations, state and local tax officials, state legislators, and other interested parties to address and enact these and other initiatives this year.

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