Approved: March 22, 2004
Date

MINUTES OF THE SENATE ASSESSMENT AND TAXATION COMMITTEE

The meeting was called to order by Chairman David Corbin at 10:45 a.m. on March 18, 2004 in Room 519-S of the Capitol.

All members were present.

Committee staff present:
Chris Courtwright, Legislative Research Department
Martha Dorsey, Legislative Research Department
Gordon Self, Revisor of Statutes Office
Shirley Higgins, Committee Secretary

Conferees appearing before the committee:
Richard Cram, Kansas Department of Revenue
Mark Ciardullo, Kansas Department of Revenue

Others attending:
See Attached List.

Senator Corbin called the Committee's attention to the minutes of the March 16 meeting. Senator Donovan moved to approve the minutes of the March 16, 2004, meeting, seconded by Senator Goodwin. The motion carried.

Senator Corbin opened the continued discussion on **SB 532** concerning sales tax remittance credit, income tax credit, and waiver of penalty and time for returns and payment of tax. He called upon Richard Cram, Kansas Department of Revenue, to present information requested at the March 16 meeting regarding different annual caps and discount percentages.

Mr. Cram distributed copies of a proposal for destination-based sourcing sales tax credit. (Attachment 1) He explained that, as suggested by Senator Donovan, the discount would be structured so that it would go only to those retailers affected by destination sourcing, and it would only be based on the sales that were sourced outside the location where the business is located. He explained that retailers would by paid 2% of the tax they remitted not to exceed a certain cap. Mr. Cram then distributed copies of a table showing figures for discounts of 2%, 3%, and 4% with different annual caps. (Attachment 2) He explained that a retailer would file their return and report the sales to the different jurisdictions. The Department would then identify which sales were sourced outside the taxing jurisdiction where the business is located. On a quarterly basis, the Department would calculate the discount and then pay it back to the retailer. After four payments are made, the Department would determine whether they were above or under the cap.

Mr. Cram noted that approximately 2,000 of 14,000 businesses have currently implemented destination sourcing. He explained that the fiscal numbers shown in the calculations assume that all businesses affected by destination sourcing would be implementing it and would be reporting their destination sourced sales. Initially, the fiscal note would be smaller because only a small number of businesses have implemented destination sourcing. He noted that the figures include all filers–annually, quarterly, monthly–who are doing destination sourcing. The Department believes that the bulk of those impacted will be the monthly filers.

Senator Donovan commented that the fiscal notes reflect that the proposal would not reward those retailers that are not hurt at all by destination sourcing and would only reward those being adversely affected. In his opinion, a 2% discount is too low. He believes the reimbursement should be sufficient to convince retailers that the state will help them make a conversion to destination sourcing, looking towards the time when the Streamlined Sales Tax goes into effect for all retailers, at which time the percentage could be reduced.

Senator Taddiken and Senator Lee expressed their concern that starting at a higher rate and then later dropping it back will give the impression that something is being taken away. They support starting at the intended level and phasing in people rather than raising and lowering the rate. Senator Corbin observed that it is easier to raise than to it is to lower.

Senator Donovan suggested that the discount rate start at least at 4% because the intent is to reimburse retailers with small increment sales in most cases. He contented that, if the initial number is not high enough for the "little guys," they will not consider the payment to be enough to be worth the trouble. In his opinion, an initial higher percentage is necessary to demonstrate to small retailers that destination sourcing is a beneficial program even though it is a long-range program. For the Committee's information, he asked Hal Hudson, National Federation of Independent Businesses, to express his opinion of the proposal. Mr. Hudson answered that NFIB believes that it is a reasonable place to start.

Senator Lee moved to amend **SB 532** to reflect a 2% discount with an annual cap of $15,000 to become effective January 1, 2005, seconded by Senator Oleen.

Committee discussion followed as to whether the discount should begin at 2% or 4%. Senator Lee reiterated he opinion that 2% is a good place to start, noting that neighboring states give a 2% discount. Although she agreed that 4% would be a better incentive to comply, she expressed her concern that the legislature would change the language in the future to provide that it will not be reduced.

As a compromise to help small businesses, Senator Journey offered a friendly amendment to allow a 4% discount for the first $1,000 cap and reduce the discount to 2% up to a cap of $10,000 for the balance of any further reimbursement. Senator Lee had no objection to Senator Journey's suggestion. Discussion followed regarding the calculation of the reimbursement. Joan Wagnon, Secretary, Department of Revenue, confirmed that a staggered rate would change how the Department would administer the discount and would make the Department's calculation more complex. Senator Corbin commented that Senator Journey's suggestion would create more confusion for the retailer. In response, Mr. Hudson stood to acknowledge Senator Journey's attempt to help small business. However, he noted the difference between Senator Lee's motion and Senator Journey's suggestion is $20 a year. He agreed with Senator Corbin that it would not be worth the confusion to the retailer. Senator Donovan asserted that the easy way to handle it for small businesses is to do the higher percentage with the understanding written into the law that the state will reimburse a percentage of the destination sourced tax revenue. And then, once all sales are included, it becomes a different tax under a different reimbursement rate. He maintained that the simple answer is to start with 4% with a cap of $5,000 or $10,000 a year. In response, Senator Lee observed that she fears that, if the rate is lowered from 2% to 4% in a few years, retailers will lead a march on the Capitol complaining that their fees have been cut in half. Senator Oleen commented that 4% will produce expectations that are going to be difficult for the state to fund.

Mr. Cram noted that a technical amendment is needed in the draft he presented to the committee. The word "credit" should be inserted to clarify that the discount would be either a credit or a payment, depending on the circumstances.

Upon a call for a vote on Senator Lee's motion, the motion carried with Senator Donovan voting "No."

Staff clarified for Senator Donovan that the original bill has a one-time $500 credit for quarterly and monthly filers. Senator Donovan noted that small business groups have indicated to him that a one-time $500 payment is not looked at as a benefit. Reimbursement is looked at as a fair exchange for the work done by retailers to collect taxes, and it is an ongoing benefit. He noted that the fiscal note on the $500 credit is about $3 million.

In response to committee questions, Secretary Wagnon clarified that **SB 532** provides for an income tax credit, not a refundable credit. She noted that, if the Committee would want it to be refundable, the Department would recommend that it be refunded from the sales tax fund.

Senator Corbin commented that **SB 532** was his idea as a possible solution. However, it has not been very well received by certain groups, and it has become more confusing than it should. Therefore, he has lost interest in it. He thanked the Committee for the time and work put into consideration of the bill.

Mark Ciardullo, tax specialist for the Department of Revenue, presented an overview of the retailers' compensating (use) tax as requested by Senator Oleen at a previous meeting. (Attachment 3) He explained that the use tax is a companion tax to the sales tax, the purpose of which is to impose the same tax burden on any consumer that purchases an item out of the state of Kansas and delivered into the state for use,

consumption, and storage.

His overview includes the following topics: Taxation of Remote Sales, Exemptions, Credit for Taxes Paid to Another State, General Credit, Reciprocal Credit, No Credit, Collection of Use Taxes, Place of Business, Solicitation of Business by Representatives, Actual Enforcement Policies, Mandatory Registrants, Voluntary Registration, Individual Customers, Income Tax Reporting and Use Taxes, Cooperative Enforcement Efforts, Use Tax Leakage and Loss of Business to Other States, and Sales for Delivery outside the State. In conclusion, Mr. Ciardullo noted that the use tax remains the weak link in state sales tax administration, and the object of the Streamlined Sales Tax Project is to shore up the weak link as much as possible.

Senator Oleen noted that there are people who are honest and willing to report purchases on which compensating use tax is due. She asked if the Committee had an interest in suggesting the insertion of a line item on the state income tax form to report compensating use tax due. Senator Corbin noted that the suggestion has been made before. However, adding a line item makes the form lengthy. Mr. Ciardullo commented that either a line item or a separate form could be used to report compensating use tax due.

The meeting was adjourned at 12:00 p.m.

The next meeting is scheduled for March 22, 2004.

SENATE ASSESSMENT AND TAXATION COMMITTEE
GUEST LIST

DATE: March 18, 2004

NAME	REPRESENTING
Steven Brunkan	KS Dept of Revenue
Mark Ciardullo	KS Dept of Revenue
Charellitta Lewis	
Larry R Baer	LKM
George E Petersen	Ks Taxpayers Network
Deann Williams	KMCA
Ann Durkes	DOB
Hal Hudson	NFIB/KS
Mike Klein	The Salvation Army
Charlie Keller	Hein Law Firm

Proposal for Destination-based Sourcing Sales Tax Credit

Except as otherwise provided and effective _________, retailers who: (1) are required to file returns and remit retailer's sales or compensating use tax, and (2) report and remit local retailer's sales or compensating use tax to multiple taxing jurisdictions in this state on their returns as a result of the destination-based sourcing provisions enacted effective July 1, 2003 at K.S.A. 2003 Supp. 79-3670 et seq., are entitled to a payment, not less than quarterly, from the retailer's sales and use tax refund fund and the local retailer's sales and use tax clearing fund of an amount equal to 2% of the state and local retailer's sales or retailer's compensating use tax remitted by such retailer to the department of revenue during the prior calendar quarter and which is attributable to taxable sales by the retailer sourced and reported on the return to local taxing jurisdictions within this state and outside the local taxing jurisdiction where the retailer's business premises are physically located, or if the retailer is located in a county in which only the county sales or use tax exists or no local sales or use tax exists, outside the county where the retailer's business premises are physically located. Such quarterly payments shall not exceed in total more than $____ in any calendar year, based on the prior four quarters. Retailers that are telecommunications providers pursuant to K.S.A. 2003 Supp. 79-3603(b), as amended, utilities providers pursuant to K.S.A. 2003 Supp. 79-3603(c), as amended, cable, community antennae and other subscriber radio and television service providers pursuant to K.S.A. 2003 Supp. 79-3603(k), as amended, telephone answering service , mobile telecommunication service, beeper service or other similar service providers pursuant to K.S.A. 2003 Supp. 79-3603(t), as amended, shall not be eligible to receive any such payment.

Richard Cram, KDOR

Senate Assessment & Taxation
3-18-04
Attachment 1

Discount to destination sourced filers and sourced sales only with annual cap

Discount %	Annual Cap	Total	State	Local	sgf
		(dollars in millions)			
2%	$ 15,000	$ 2.35	$ 1.76	$ 0.59	$ 1.68
2%	$ 10,000	$ 2.23	$ 1.67	$ 0.56	$ 1.59
2%	$ 5,000	$ 1.98	$ 1.49	$ 0.49	$ 1.42
2%	$ 2,000	$ 1.61	$ 1.20	$ 0.41	$ 1.14
2%	$ 1,000	$ 1.30	$ 0.98	$ 0.32	$ 0.93
2%	$ 500	$ 0.98	$ 0.74	$ 0.24	$ 0.71
3%	$ 15,000	$ 3.34	$ 2.51	$ 0.83	$ 2.39
3%	$ 10,000	$ 3.14	$ 2.35	$ 0.79	$ 2.24
3%	$ 5,000	$ 2.75	$ 2.06	$ 0.69	$ 1.96
3%	$ 2,000	$ 2.16	$ 1.62	$ 0.54	$ 1.54
3%	$ 1,000	$ 1.67	$ 1.26	$ 0.41	$ 1.20
3%	$ 500	$ 1.20	$ 0.90	$ 0.30	$ 0.86
4%	$ 15,000	$ 4.27	$ 3.20	$ 1.07	$ 3.05
4%	$ 10,000	$ 3.97	$ 2.98	$ 0.99	$ 2.84
4%	$ 5,000	$ 3.43	$ 2.57	$ 0.86	$ 2.45
4%	$ 2,000	$ 2.61	$ 1.95	$ 0.66	$ 1.86
4%	$ 1,000	$ 1.96	$ 1.42	$ 0.54	$ 1.35
4%	$ 500	$ 1.35	$ 1.01	$ 0.34	$ 0.96

Discount to all filers, using a annual cap

Discount %	Annual Cap	Total	State	Local	sgf
		(dollars in millions)			
2%	$ 15,000	$ 26.88	$ 20.16	$ 6.72	$ 19.21
2%	$ 10,000	$ 25.48	$ 19.11	$ 6.37	$ 18.21
2%	$ 5,000	$ 22.71	$ 17.03	$ 5.68	$ 16.23
2%	$ 2,000	$ 18.50	$ 13.88	$ 4.63	$ 13.22
2%	$ 1,000	$ 14.89	$ 11.17	$ 3.72	$ 10.64
2%	$ 500	$ 11.22	$ 8.42	$ 2.81	$ 8.02
3%	$ 15,000	$ 38.23	$ 28.67	$ 9.56	$ 27.32
3%	$ 10,000	$ 35.88	$ 26.91	$ 8.97	$ 25.65
3%	$ 5,000	$ 31.45	$ 23.59	$ 7.86	$ 22.48
3%	$ 2,000	$ 24.65	$ 18.49	$ 6.16	$ 17.62
3%	$ 1,000	$ 19.13	$ 14.35	$ 4.78	$ 13.67
3%	$ 500	$ 13.70	$ 10.28	$ 3.43	$ 9.79
4%	$ 15,000	$ 48.75	$ 36.56	$ 12.19	$ 34.84
4%	$ 10,000	$ 45.23	$ 33.92	$ 11.31	$ 32.33
4%	$ 5,000	$ 39.22	$ 29.42	$ 9.81	$ 28.03
4%	$ 2,000	$ 29.78	$ 22.34	$ 7.45	$ 21.29
4%	$ 1,000	$ 22.44	$ 16.83	$ 5.61	$ 16.04
4%	$ 500	$ 15.46	$ 11.60	$ 3.87	$ 11.05

Senate Assessment + Taxation
3-18-04
Attachment 2

KANSAS

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE
POLICY AND RESEARCH

KATHLEEN SEBELIUS, GOVERNOR

Testimony to the Senate Committee on Assessment and Taxation
Mark D. Ciardullo, Tax Specialist

March 18, 2004

Retailers' Compensating (Use) Tax

Chairman Corbin and Members of the Committee:

When the states first imposed their sales taxes, they were concerned about the potential loss of revenue from out-of-state purchasing, to which the sales tax, as such, could not be applied for constitutional reasons. In 1935, California and Washington developed the expedient of imposing use taxes upon the initial use of goods purchased outside the state and brought in for use in the state. Such practice had previously been upheld by the courts with respect to gasoline taxes. The U.S. Supreme Court upheld the Washington use tax in the case of Henneford v. Silas Mason Co., Inc., that the tax was imposed not upon interstate commerce, as such, but upon the privilege of use after interstate commerce was completed. Had the tax not been upheld, there would have been serious consequences for the states. With, the powers to impose the use tax upheld, later cases have centered on the power to collect tax from out-of-state vendors. Due/Mikesell.

Use tax is imposed on the use, storage or consumption of tangible personal property in the State. K.S.A. 79-3703. It applies to goods purchased outside the State. The use tax complements the sales tax. Use tax was developed to safeguard State sales tax revenues from erosion by purchases of goods outside the State, and to protect local merchants from loss of business to border and other States that either have no sales tax or whose sales tax rate is lower than that of the merchant's State. Hellerstein & Hellerstein, ¶ 16.01.

Taxation of Remote Sales

The purchaser is obligated to pay use tax to the State of residence on out-of-state purchases. Except for businesses subject to regular audits, unless the out-of-state retailer collects use tax from the purchaser and remits it to the State, as a practical matter, it will not be paid. The viability of both the sales and use tax depends primarily upon the collection, reporting and remittance functions that retailers perform. In order for States to obtain an acceptable compliance rate on payment of use tax on remote sales to consumers, out-of-state retailers must be obligated to collect and remit use tax on those sales.

Senate Assessment + Taxation
3-18-04 Attachment 3

Under Kansas law, an out-of-state retailer "doing business" in Kansas is obligated to collect and remit use tax on its sales to consumers in Kansas. K.S.A. 79-3705c. However, United States Supreme Court decisions have restricted the constitutional power of the States to subject interstate sales to sales or use tax. In *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), the Supreme Court held that the Commerce Clause bars a State from imposing a use tax collection duty on an out-of-state seller with no physical presence (nexus) in the State. Thus, an out-of-state merchant has no legal obligation to collect use tax on its sales to customers located in another State, if the sale is conducted by telephone, mail order, or in recent times, the Internet, and if the out-of-state merchant has no physical presence in that State.

Physical presence, or nexus, is established if the out-of-state retailer has agents, employees or a facility permanently located in the State. Temporary presence can be sufficient to establish nexus under certain circumstances (such as frequent deliveries into the state). However, this is currently a heavily litigated area of the law.

State governments and local merchants have long been concerned about the fact that mail-order consumer retail sales by out-of-state merchants essentially escape use tax. The rapid growth of remote retail sales over the Internet has heightened those concerns.

EXEMPTIONS

Property brought into Kansas by a nonresident of Kansas for his or her use for less than 60 days.

Property brought into Kansas purchased other than at retail.

Property brought into Kansas purchased at retail, and on which a legal sales or use tax in excess of the Kansas rate has been paid.

Property brought into Kansas that would not have been subject to Kansas sales tax, if the property had been purchased in Kansas.

CREDIT FOR TAXES PAID TO ANOTHER STATE

Initially, most states did not give credit for sales tax that had been paid to another state, and therefore, there was potential double taxation. The principal difficulty arose with goods used by a business firm in one state and then transferred to another state. Inevitably, complaints were raised about this treatment, and some states began to provide credit. The trend increased sharply in the mid-1960s as a result of a report and subsequent federal legislation proposed by a subcommittee of the U.S. House Judiciary Committee. As a consequence, credit is now given for sales tax paid other states with relatively few exceptions:

GENERAL CREDIT

States give credit for sales tax paid to another state, whether or not the other state does.

RECIPROCAL CREDIT

Eighteen states-Alabama, Colorado, Georgia, Kentucky, Louisiana, Massachusetts, Michigan, Nebraska, New Jersey, New York, North Carolina, North Dakota, Oklahoma, Pennsylvania, South Dakota, Texas, and Vermont - provide credit for sales tax paid to those states that also provide credit.

In view of the States imposing a "brought in" tax include: Arizona, Arkansas, Georgia, Hawaii, Kansas, Louisiana, Maryland, Missouri, New York, North Dakota, Oklahoma, Pennsylvania, Tennessee, Washington, and Wisconsin. Mississippi taxes "the privilege of using."

NO CREDIT

Nevada had provided credit for sales tax paid states that were members of the Multi State Tax Compact, but when Nevada withdrew from the compact in 1981, this ended credit; Nevada was convinced that Utah and Idaho were taking advantage of the state by obtaining tax revenues from shipments for use in Nevada.

COLLECTION OF USE TAXES

Use taxes are collected from those out-of-state vendors who are required by the state to register and collect use taxes, from out-of-state vendors who are under no legal obligation to collect tax but register voluntarily, and from the purchaser in the state. In general, the out-of-state vendors can be required to register as use tax vendors and collect and remit tax constitutionally, without violating the Due Process Clause of the Fourteenth Amendment and the Interstate Commerce Clause, only if sufficient nexus exists between the state and these firms. Nexus may arise from several sources.

PLACE OF BUSINESS

Vendors who have any places of business within the state, such as a store, office, warehouse, or display room, are required to register and collect tax on all sales for delivery into the state, even if they are made independently of the local place of business. The courts have sanctioned this rule since the earliest days of use taxes. It was specifically upheld in two Iowa cases in 1941 involving mail-order sales by firms also in retail business in the state.

SOLICITATION OF BUSINESS BY REPRESENTATIVES

Most states require registration of firms that solicit business in the state by representatives, salesmen, agents, or independent firms soliciting orders for the firms. This power was upheld in a series of Supreme Court cases.

ACTUAL ENFORCEMENT POLICIES

States differ materially in enforcing their use tax laws. This section examines mandatory registrants, mail-order firms, voluntary registration, individual customers, income tax reporting and use taxes, and cooperative enforcement efforts.

MANDATORY REGISTRANTS

Most states make at least some effort to ensure that out-of-state firms subject to the registration requirement register and collect tax, but they differ in the zeal with which they pursue the objective. Many such firms are noted in the audits of in-state firms. Purchase invoices indicate out-of-state suppliers from which the firm is buying, and checks are then made to see if they are subject to the registration requirement or are registered.

VOLUNTARY REGISTRATION

All states find that some out-of-state vendors register voluntarily even though not required to do so, and some states have waged an active campaign to increase the number of voluntary registrants. These firms fall into two groups: supply firms of a wide variety of types, and department stores in nearby states. Supply firms include those serving manufacturers, other forms of business, and professionals: medical, dental, and so on. Many supply firms are willing to register to avoid having their customers file use tax returns and pay tax or possibly incur substantial penalties for not doing so. Not infrequently, customers will urge their suppliers to register and collect tax.

This same consideration does not apply, however, to department stores and other retailers selling to the public or to farm supply firms, since their customers are not subject to sales tax audit. Few, therefore, have registered voluntarily, except through strong efforts of the states. A number of states have actively encouraged them to register, in some cases offering concessions, often an agreement not to audit for use tax in years before registration, or the understanding that returns will be filed only when there is liability to report. Others apply a certain amount of pressure, such as a threat to follow their delivery trucks and assess their customers. Some states extend the compensation discount to these collections as an inducement to register, collect, and remit.

INDIVIDUAL CUSTOMERS

States also vary in their efforts to require payment from individual purchasers. Two groups are systematically controlled: business firms subject to sales tax audit and purchasers of motor vehicles that must be registered. Because of limited audit coverage, not all business purchases are caught, but at least they are potentially subject to control.

Most states make no effort to catch individual purchasers on goods bought outside the state. Administrators regard any effort as not worth the trouble. Commonly, tax will have been paid to the other state, and little or no revenue loss is involved.

There are, however, exceptions:

Other registered items: In states where certain other expensive items are registered, check is frequently made and the customer billed, or the tax collected with registration:

Boats: California, Kentucky, Maine, Maryland, Michigan, Missouri, and New Jersey
Planes: Kentucky, Maine, Maryland, and Wyoming Snowmobiles: Vermont
General: Arizona and Tennessee

New Jersey is especially aggressive in checking for boats; the department operates three boats (obtained in enforcement actions) that it uses for frequent checking of its marinas, with considerable revenue yield. Kentucky, however, has received little cooperation from marinas in its land-based enforcement visits.

Farm equipment: A number of states attempt to discover out-of-state purchases of farm machinery, particularly when neighboring states do not tax it. These are now very expensive items and the amount of tax is substantial. California, Iowa, Nebraska, and Utah particularly note efforts to reach these items. Various methods are used, including ones also applied to other large-item purchases-recording of chattel mortgages and liens (Maine, Utah), property tax rolls (Utah, Washington), truck weigh stations and observation by compliance officers.

Check at truck weigh stations: A few states systematically check trucks at weigh stations near the borders. Wyoming has a program of checking all bills of lading on trucks to determine destination of major items. Small delivery trucks are not stopped.

Customs: States make use of information from U.S. Customs offices at border. In the past there was not always complete willingness to cooperate on the part of U.S. Customs. A more recent effort has been the audit of federal customs declarations filed by returning overseas travelers. In these programs, auditors physically review individual declarations from residents of their state, identify large purchases, and send use tax bills.

Contractors: A number of states give particular attention to out-of-state contractors performing contracts within the state, using Dodge Reports and other sources.

Self-Audits: Some states have made direct taxpayer mailings, explaining the use tax law and asking the taxpayer to review records to determine whether use tax liability might be owed.

INCOME TAX REPORTING AND USE TAXES

A number of states collect use tax directly from purchasers by linking the use tax to the state income tax reporting system. Two approaches are used. First, states enclose in the individual income tax re porting booklet that is mailed to taxpayers a use tax return with instructions for filing it. Second, states place a use tax reporting line on the income tax return itself, with instructions on how the owed amount would be computed. The line usually appears on returns filed by individuals only, but Indiana has the line on corporate returns as well

Yields from these reports are not large, although the direct costs of adding the lines and instructions are modest.

COOPERATIVE ENFORCEMENT EFFORTS

States have developed interstate agreements for cooperative enforcement of their sales and use tax to improve voluntary vendor compliance and to aid use tax enforcement activities. The efforts include publicity about use tax obligations, encouragement of in-state retailers to register for use tax collection in other states, exchange of audit information (in an audit, the state gathers a list of sales sent out of state without tax and sends the list to the destination state), and distribution of questionnaires to businesses to identify retailers who should be registered in the state.

USE TAX LEAKAGE AND LOSS OF BUSINESS TO OTHER STATES

If the use tax were fully effective, sales tax would not cause loss of business to other states, certainly so long as the tax is confined to consumer goods, except possibly through migration of population or industrial activity, which are rather remote possibilities. But since use taxes are not fully effective, the fear has been that some business will be diverted to retailers or mail-order sellers located beyond the borders of the state. The problem has, of course, diminished as the sales tax has spread. Now a person can buy tax-free in fewer places. Two of these states, Alaska and Montana, are so remote as to be of little consequence. However, some differences in coverage and rates may lead to diversion, plus purchases by mail or for delivery in another state.

SALES FOR DELIVERY OUTSIDE THE STATE

Most states exempt from tax all sales for delivery outside the state. Arizona and Mississippi tax such sales when the sale itself has been made within the state. If the order comes from outside the state and delivery is made to a point outside the state, the state cannot apply its tax under court interpretation of the interstate commerce clause. The more usual policy of exempting all such sales is preferable. Taxation of sales for out-of-state delivery either takes revenue that is rightfully due the other state or, in a few instances, may result in double taxation. As noted, Washington and North Dakota exempt over-the-counter purchases by residents of other states with no sales or use tax (only Oregon for Washington).

CONCLUSION

The use tax remains the weak link in state sales tax administration. The objective of the Streamlined Sales Tax Project is to shore up the weak link, as much as possible. From the state's standpoint, leakage of revenue occurs, primarily on mail-order sales by the catalog type of mail-order house or Internet retailers not operating retail stores and electronic ordering, retailers doing some casual mail-order business, and to some extent by purchase of consumer durables for delivery in the other state. The states can reach motor vehicles, other registered items, purchases through the large mail-order houses also having stores in the state, and purchases by business firms subject to audit (though many of these purchases are not caught).