HB 1183

HD2, SD1

L E G I S L A T I V E

TAXBILLSERVICE

126 Queen Street, Suite 304 TAX FOUNDATION OF HAWAII Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: MISCELLANEOUS, Streamlined sales and use tax

BILL NUMBER: HB 1183, SD-1

INTRODUCED BY: Senate Committee on Economic Development and Technology

BRIEF SUMMARY: Adds a new chapter to the law to set out sections of HRS chapter 237 which establish transactions subject to the __ general excise tax rate.

Adds a new chapter to the law to set out sections of HRS chapter 238 which establish transactions subject to the__ use tax rate.

Adds a new chapter to the law to set out sections of HRS chapter 237 which establish transactions subject to the__ general excise tax rate. The measure delineates provisions governing commissioned sellers of insurance to replace references to agents, general agents, subagents, or solicitors with the term "insurance producers."

Adds several new sections to HRS chapter 237 to establish sourcing rules to determine when a product or service is taxed, including telecommunication services. The measure delineates provisions defining "direct mail" and how the sourcing of direct mail transactions will be ascertained.

Adds a new section to HRS chapter 237 to allow a seller to take a deduction from taxable sales for bad debts.

Adds several sections to HRS chapter 255D to establish provisions relating to the determination of the proper general excise or use tax rates between different tax jurisdictions, rounding on tax computations, amnesty for registered sellers who pay, collect, or remit general excise or use taxes in accordance with the terms of the streamlined sales and use tax agreement, tax rate changes by a county, certified service provider, confidentiality of records, liability for uncollected tax and rate changes, and customer refund procedures.

Amends HRS sections 237-8.6 and 238.2.6 to prohibit a county to conduct an independent audit of sellers registered under the streamlined sales and use tax agreement.

Amends HRS section 237-24.3 to redefine the term "prosthetic device."

Establishes a committee to oversee the department of taxation's implementation, administration, and compliance of the streamlined sales and use tax agreement. The committee shall be administratively attached to the department of taxation. Requires the committee to hold meetings to carry out this act and serve as the state's official delegation to the streamlined sales and use tax governing board when establishing the state's criteria for compliance.

Permits the department of taxation to seek technical assistance with legal professionals that have a background and practice in taxation. Allows the department of taxation to secure services in an expeditious manner as soon as possible. The legislative reference bureau shall assist the department of taxation or contractor in drafting any legislation.

This act shall take effect when the state becomes a party to the streamlined sales and use tax agreement; provided that: (1) the amendments made to HRS section 237-9 by this act shall not be repealed when that section is reenacted on June 30, 2014, pursuant to section 13(3) of Act 134, SLH 2009; (2) the amendments made to HRS section 237-24 by this act shall not be repealed when that section is reenacted on December 31, 2013, pursuant to section 4, Act 70, SLH 2009; and (3) the amendments made to HRS section 237-24.3 by this act shall not be repealed when that section is reenacted on December 31, 2014, pursuant to section 4, Act 239, SLH 2007, as amended by section 5, Act 196, SLH 2009, as amended by section 1 of Act 91, SLH 2010.

EFFECTIVE DATE: July 1, 2050

STAFF COMMENTS: The Streamlined Sales Tax Project's Model Agreement and Act is a project undertaken with other states that is intended to simplify sales and use tax administration as it relates to multiple sales and use tax rates, definitions, and taxing jurisdictions.

Goals of the project include the establishment of a single sales tax rate, uniform definitions of sales and use tax terms, requiring states to administer any sales and use taxes, and a central electronic registration system to allow a seller to register to collect and remit sales and use taxes for all states.

At the national level, there appears to be a number of difficulties in the negotiations and unanimous agreement is far from reality. Before jumping on the band wagon, lawmakers should exercise care as it should be remembered that Hawaii does not have a sales tax as found in other states. To the contrary, the general excise tax, while viewed as a sales tax, is a far cry from the retail sales tax structure found on the mainland.

The 2005 legislature had approved a measure to direct the department of taxation to identify issues that need to be resolved to effectuate the orderly enactment and operation of a streamlined sales and use tax based on the Streamlined Sales Tax Project's Model Agreement and Act. The act also repealed the streamlined sales and use tax advisory committee council which was to consult with the department of taxation on the implementation of the streamlined sales and use tax agreement in Hawaii. When this measure was sent to the governor, the governor vetoed it due to the repeal of the advisory council, unrealistic deadlines in the measure, and concerns of allowing a third party to access confidential tax return information. A special session of the legislature overrode the governor's veto and the measure passed as Act 3 of the Special Session of 2005.

Basically the measure attempts to turn Hawaii's gross receipts tax imposed for the privilege of doing business in Hawaii into a retail sales tax structure with respect to where the tax is imposed. Much of the bill is devoted to separating the wholesale imposition of the tax from the retail and then reworking where the tax is applied otherwise known as "sourcing." The general excise tax, as we know it today, would be radically changed to accommodate the format adopted by the Streamline Sales Tax Project (SSTP).

What is not evident in the measure is that by participating in the consortium known as the SSTP, Hawaii businesses will be required to collect the sales taxes of other states when purchases are made by residents of that state. The cost of collecting, accounting, and remitting those taxes will add even more overhead costs to operating a business in Hawaii. So why is there such enthusiasm on the part of the legislature to participate in the SSTP? Lawmakers have been promised hundreds of millions of dollars that could be had if the state would just participate in the project. The suggestion came to the 2001-2003 Tax Review Commission on the recommendation of their consultant who was already an advocate of the project.

Of course, no thought was given to how this would affect Hawaii businesses and what additional costs there would be. Given the fact that Hawaii businesses will now have to operate in a different mode insofar as the general excise/SSTP sales tax, will lawmakers compensate businesses for undertaking the collection of other state's retail sales taxes? Indeed, the law being proposed in this measure is a hybrid of the current general excise tax law and a retail sales tax. It retains the two-tiered wholesale/retail system and keeps the tax imposed on services as well as on business-to-business transactions. So the measure attempts to have the best of both worlds - to force other states to collect our general excise tax while retaining the pyramiding features of the general excise tax. This is a major change in the state's largest source of general fund revenues. Care should be taken in making this transition as it could alter not only the past interpretation of the general excise tax, but it may also have a major impact on the revenue producing capacity of the tax.

One of the key issues still under discussion amongst the members who have already signed on is "where" does the sale occur. For a number of the larger states like California, Illinois, and Texas which have much at stake since they are states that manufacture goods shipped to other states, the sourcing rules they adopted use "origin" based rules, that is the tax that is imposed at the place from which the goods are shipped and not where the purchaser takes possession. The proposed bill here is ambiguous, at best, as in some cases being origin based as long as the purchaser takes possession of the goods at the place of the business but provides, on the other hand, for the taxation at the address to which the goods are delivered. It is this destination rule that causes the most problems for businesses as they must now deal with a plethora of rates depending on the number of states from which they receive orders for their goods.

While some states may elect destination, there is no doubt that the larger states will elect origin sourcing as they are probably net exporters of goods. That being the case, Hawaii residents will probably end up paying the Illinois or California sales tax on their purchases from out-of-state vendors and in the long run, the purported windfall will turn into a disaster for Hawaii. Under current law, the use tax would otherwise have been due on those sales and while it has been difficult to enforce and collect on individual sales, more of an effort should be placed on the collection of the use tax where Hawaii already has jurisdiction.

Again, a main area of concern is whether the states can afford the streamlined system itself. Given the promises that have been made and not delivered upon such as the software that is supposed to facilitate the collection and remittance of the various states' sales taxes, to the promise to pay the cost of funding the administrative structure of the governing board, it appears that all of these are promises with no intent to make it happen. As such, it is premature for Hawaii to jump on the throttling locomotive engine that appears to be headed for a brick wall. This proposal needs more discussion in the interim and further clarification as well as a discussion with taxpayers who must carry out the duty of the actual

collection.

Curiously, this is what the 2005-2007 Tax Review Commission recommended, that until the member states of the SSTP agreement come to a definitive conclusion, it is premature for Hawaii to jump on board. With this latest development, it appears that Hawaii will be a net loser as its residents will end up paying other state's sales taxes.

While the proposed measure attempts to conform Hawaii's general excise and use tax laws to the streamlined sales and use tax agreement, due to its complexity and technical aspects, it is questionable whether members of the legislature are qualified to determine whether this measure will be sufficient to comply with the Streamlined Sales and Use Tax Agreement.

In 2006 a bill that would adopt the streamline sales tax agreement was introduced and nearly passed the legislature but for a small glitch in the closing moments of the session. This, despite the fact that the State Auditor had a consultant assess the revenue potential of participating in the project. Instead of the hundreds of millions of dollars the promoters of the project had promised, the consultant estimated that Hawaii would benefit at the very least by about $10 million and at the most $50 million.

At the same time, when the department of taxation was asked what it estimated it would cost the department to implement the project for Hawaii, the price tag was set at $15 million. Thus, it came as no surprise that when the Tax Review Commission looked at the issue, the decision was a no brainer, Hawaii would stand to gain about $10 million in revenue, but it would cost the state $15 million to implement. And that doesn't include the cost to businesses in Hawaii that would be required to collect the sales taxes of other states.

So the Commission's advice to the legislature and administration was to wait. In its recommendation it was noted that "the largest states (by economic size) have failed to sign on to the project, jeopardizing the chances of becoming an effective vehicle for collecting the Use Tax. Until the Project shows greater promise of producing results, it is premature for Hawaii to incur the expense to join it."

In 1992, in *Quill Corp. v. North Dakota*, the U.S. Supreme Court reaffirmed that the power of states to impose taxes on interstate commerce is limited by their geographic border. Although some academics resent this "physical presence rule," it remains the law of the land and is essential to prevent revenue officials from wreaking havoc on national markets by reaching beyond their borders for tax revenues. Since no working alternative to the physical presence rule has been developed, abandoning it would result in states harming themselves by harming the whole.

The SSTP was formed in reaction to *Quill*, though not necessarily to create an alternative to the physical presence rule. The SSTP is a working group of revenue officials and experts with the stated purpose of bringing simplicity and uniformity to sales taxes in the United States. (The governance structure raises some questions of democratic accountability and whether SSTP receives or seeks genuine public input.) Member states must adopt reforms to align their tax code with the SSTP. The hope is that simple and uniform sales tax statutes will allow the collection of interstate sales taxes without placing burdens on interstate commerce.

Simplicity and uniformity are both important goals, but the SSTP has, at best, mixed success in achieving them. There are nearly 8,000 sales taxing jurisdictions in the United States, each with their

own bases and rates, and the enormous complexity involved in tracking borders and changes is a huge stumbling block to state efforts to impose taxes on online sales.

While the SSTP has made some progress on uniformity (they have succeeded, for instance, in a single accepted definition of "candy"- something everyone defined differently before), the SSTP appears to be giving up the effort on simplicity. At their New Orleans meeting in July 2008, for instance, the SSTP panel was asked if any effort was being made to reduce the number of sales taxing jurisdictions, and/or to align them with 5-digit zip codes. "No and no," were the short, but honest answers.

Rather than requiring that states simplify before reaching out beyond their borders to tax out-of-state companies, the SSTP seems content to let states continue the status quo. One panelist noted that far from requiring substantial reforms, "States still get to do 99.9% of what they want to do" under the SSTP agreement. This demonstrates either disingenuousness or how little the SSTP recognizes that many existing sales taxes are in need of substantial reform.

The SSTP already abandoned the notion of taxing like transactions alike when they adopted "destination sourcing" for online sales, but permitted states to adopt "origin sourcing" for intrastate sales. This, in effect, requires Internet companies to collect sales taxes based on where their customer is located, but allows brick-and-mortar stores to collect sales taxes based on where the store is located. In this way the SSTP prevents a level playing field between Internet businesses and brick-and-mortar businesses.

Coupled with the SSTP's non-worry about reducing the number of jurisdictions (they spoke optimistically of providing maps of sales tax jurisdictions, having rejected even aligning jurisdictions with 9-digit zip codes), full implementation of the SSTP, at this time, without serious reforms, could result in a serious and inequitable burden on e-commerce.

Another recent example involves clothing taxes. The SSTP requires that all states have a uniform definition of clothing, and tax all of it (or none of it) at the same rate. Minnesota did so, but then imposed a "separate" fur tax on fur sales. Rather than recognizing this as an end-run around tax uniformity, the SSTP upheld Minnesota's action.

The SSTP is attempting to persuade Congress to permit SSTP member states to begin collecting sales taxes on online purchases, premised on the belief that the SSTP's simplification and uniformity mission has been accomplished. **The SSTP has not accomplished its mission**. The SSTP should look again at serious simplification efforts before declaring themselves a success and seeking to expand state taxing power.

States should be willing to adopt uniform definitions worked out by the SSTP so as to reduce transaction costs between state statutes. However, the ability of any state to collect sales tax on online transactions is wholly dependent on the willingness of other states to simplify their laws and adopt uniform definitions as well. It is also dependent on the creation of a working alternative to the physical presence standard that provides certainty and prevents multiple taxation. Neither the wholesale adoption nationwide of uniform sales tax statutes, nor the development of a working alternative that provides the certainty needed for long-term investment, are likely in the foreseeable future.

For these reasons, lawmakers and other states should understand that SSTP membership does not lead to a sudden influx of free tax money. In any event, this money will come from Hawaii residents and should be looked at as a tax increase notwithstanding the existing liability under the use tax laws. The SSTP's goals are good ones, but their success is mixed at best, and whatever effect it has will not be seen in the short-term.

A few years ago, a similar measure was vetoed by the governor. In her veto message, she stated that the "bill is objectionable because it would abdicate the authority of the state to establish, administer, and change its general excise tax structure; grants amnesty to certain taxpayers, absolving them of the requirement to pay taxes due the state, and treats out-of-state vendors more favorably than in-state vendors." She further stated that in order to comply with the Streamline Sales and Use Tax Model Agreement and Act (SSUTA), the state and each county would have to establish a single tax rate and once the state participates in the SSUTA, the state must certify to a national governing board that the state's law complies with the SSUTA and may relinquish control over the state's ability to determine its own tax revenue collections. The governor also had concerns about the provision of the SSUTA requiring the state to pay out-of-state vendors for collecting Hawaii taxes since the taxes the state would be receiving would be reduced by the collection fee paid to the out-of-state vendor, thereby giving out-of-state vendors an unfair advantage since local businesses are not compensated for collecting and paying required taxes.

The long and short of this measure is that it is nothing more than a tax increase that will probably end up benefitting other states if the majority of states adopt "origin" based sourcing and continuing a tradition of passing the cost to administer and complying with the proposal on to businesses in Hawaii, adding yet another nail in the coffin for businesses in Hawaii. It is certainly a reflection of the lack of understanding of Hawaii's unique general excise tax and how generous it is in producing revenues for the state.

Digested 3/29/11

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March 30, 2011

The Honorable David Y. Ige, Chair
Senate Committee on Ways and Means
State Capitol, Room 211
Honolulu, Hawaii 96813

RE: H.B. 1183, H.D.2, S.D.1, Relating to the General Excise Tax

DECISION MAKING: Wednesday, March 30, 2011, at 9:00 a.m.

Aloha Chair Ige, Vice Chair Kidani and Members of the Committee:

I am Craig Hirai, a member of the Subcommittee on Taxation and Finance, submitting written comments on behalf of the Hawai'i Association of REALTORS® ("HAR"), the voice of real estate in Hawai'i, and its 8,500 members. HAR **supports** H.B. 1183, H.D.2, S.D.1, Relating to the General Excise Tax, which adopts amendments to Hawaii tax laws to implement the Streamlined Sales and Use Tax Agreement.

The Report of the 2001-2003 Tax Review Commission states that Hawaii would potentially achieve not only the benefit of better definitions, uniformity, and certainty, but also increase tax compliance by interstate vendors (primarily mail order and e-commerce merchants) who agree to pay state taxes under the Streamlined Sales Tax Project. The Report goes on to state that because of Hawaii's uniquely broad based General Excise and Use Tax system, by joining the Streamlined Sales Tax Project, Hawaii may be able to better maintain the viability of its broad revenue base.

The Report of the 2005-2007 Tax Review Commission, however, states that while the Commission believes that the goal of coordinating the collection of taxes on interstate sales, such as via the internet, is desirable, and that Hawaii should remain involved in discussions on the Streamlined Sales Tax Project, the Commission did not think that Hawaii should make a formal commitment yet.

HAR believes that the procedures set forth in Section 32 of H.B. 1183, H.D.2, S.D.1, should help alleviate some of the concerns of the 2005-2007 Tax Review Commission, and that H.B. 1183, H.D.2, S.D.1, should eventually level the playing field for local merchants who must deal with the high cost of doing business in Hawaii and still compete with mail order and e-commerce merchants from outside of the State.

Mahalo for the opportunity to submit written comments.

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Senator David Y. Ige, Chair
Senator Michelle Kidani, Vice Chair
Committee on Ways and Means
State Capitol, Honolulu, Hawaii 96813

HEARING Wednesday, March 30, 2011
9:30 am
Conference Room 211

RE: HB1183, HD2, SD1, Relating to the General Excise Tax

Chair Ige, Vice Chair Kidani, and Members of the Committee:

Retail Merchants of Hawaii (RMH) is a not-for-profit trade organization representing about 200 members and over 2,000 storefronts, and is committed to supporting the retail industry and business in general in Hawaii.

RMH supports HB1182, HD2, SD1, which adopts amendments to Hawaii's tax laws to implement the Streamlined Sales and Use Tax Agreement.

Through our affiliation with the National Retail Federation, the world's largest retail trade association, and a major participant in the Streamlined Sales Tax Project, RMH has watched the development and progress of this program over the past nine years and has supported Hawaii's initiatives to participate in the multi-state discussions.

As electronic commerce continues its dramatic increase, traditional brick and mortar retailers, which are required by law to collect taxes for government, experienced further erosion of their sales base to remote sellers, which, under most circumstances, are not subject to tax mandates. The Streamlined Sales and Use Tax Project will level the playing field. The unfair disadvantage our local small businesses are experiencing leads to less commerce at brick-and-mortar establishments that most certainly affects Hawaii tax revenues and Hawaii employment. In light of the newly developed free "Tax Cloud" system to support collections, we are assured that implementation will eliminate any costly burden on small businesses.

The reality is that the State of Hawaii has huge liabilities and unfunded mandates that cannot be satisfied without additional revenue or cutting essential services. It is more than reasonable to collect a tax that's already due before instituting new taxes on everyone. Tax revenue generated from online sales can be used to pay down deficits and get Hawaii back on track toward fiscal responsibility.

Retailers nationally are encouraged that current initiatives in Congress, primarily The Main Street Fairness Act, hold greater promise to ameliorate this unfair situation, and there is consensus that this legislation will be enacted soon. This measure makes the necessary amendments to Hawaii tax laws to facilitate our compliance.

We respectfully request that you pass HB1183, HD2, SD1. Thank you for your consideration and for the opportunity to comment on this measure.

Carol Pregill, President

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From: mailinglist@capitol.hawaii.gov
Sent: Tuesday, March 29, 2011 9:26 AM
To: WAM Testimony
Cc: tammy@internetalliance.org
Subject: Testimony for HB1183 on 3/30/2011 9:30:00 AM
Attachments: NCSL_Task_Force_Letter_on_affiliate_nexus.pdf

Categories: Green Category

Testimony for WAM 3/30/2011 9:30:00 AM HB1183

Conference room: 211
Testifier position: support
Testifier will be present: No
Submitted by: Tammy Cota
Organization: Internet Alliance
Address:
Phone:
E-mail: tammy@internetalliance.org
Submitted on: 3/29/2011

Comments:
We support HB 1183 as amended to be a Streamlined Sales Tax bill (not as introduced which proposed an affiliate nexus tax). Also see two attachments to this letter.

Tammy Cota, Executive Director
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Cell: 802-279-3534
Email: tammy@internetalliance.org
Web: www.internetalliance.org

March 30, 2011

Honorable David Ige, Chair
Senate Ways and Means Committee
Hawaii State Capitol, Room 215
Honolulu, HI 96813

Honorable Marcus Oshiro, Chair
House Finance Committee
Hawaii State Capitol, Room 306
Honolulu, HI 96813

Dear Senator Ige and Representative Oshiro:

I am the executive director of the Internet Alliance (IA), a national organization of consumer companies that provide goods and services via the Internet. The IA's mission is to build consumer confidence and trust in the Internet so that it may become the leading global marketing medium of this century.

The IA is writing to express support for HB1183 SD1. This bill proposes that Hawaii implement the Streamlined Sales and Use Tax Agreement (SSUTA). The IA believes this is a more practical, and legal, approach than SB1355 HD1 (nexus).

The IA opposes the creation of a nexus standard for taxing out-of-state businesses based on their local affiliate agreements or require an out-of-state business to file information with the state about Hawaii customers' purchases. This bill will not raise any revenue for the state and in fact in-state businesses will suffer. Faced with an obligation to collect the tax, out-of-state businesses will simply cut off ties with in-state affiliates and eliminate any debate about the nexus standard. There will be no additional revenue for Hawaii. In fact, such a tax could reduce state revenue, eliminate in-state jobs and drive business and consumer dollars out of state.

Also, the Direct Marketing Association (DMA) just won a landmark preliminary injunction in federal court through a lawsuit it filed against a similar tax notice law that passed in Colorado, which is explained in more detail in the attachment.

Instead of passing an affiliate nexus tax, Hawaii should take the advice of organizations such as the National Conference of State Legislatures (NCSL) Task Force on State and Local Taxation of Telecommunications and Electronic Commerce who sent the attached letter to every legislature advising against enacting nexus taxes. The task force letter also urges states to consider adopting SSUTA. For more information about NCSL's position,

please feel free to call Neal Osten at 202-624-8660 or email him at neal.osten@ncsl.org. He would be happy to discuss the issue with you in more detail.

In summary, the IA believes creating a new affiliate nexus tax is unconstitutional and bad policy that would harm the state's economy and in-state local affiliates, and creating an annual notice to the state violates the Commerce Clause of the United States Constitution. Therefore, the IA urges you to reject the nexus tax and instead adopt the SSUTA.

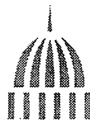
Thank you for taking the time to consider our position. Attached you will find more detailed reasons for advancing SSUTA and rejecting the nexus tax. Please contact me if you would like to discuss this issue further or have questions.

Sincerely,

Tammy Cota

Tammy Cota

cc: Senate Ways and Means Committee members
House Finance Committee members



NATIONAL CONFERENCE *of* STATE LEGISLATURES

The Forum for America's Ideas

Don Balfour
Senator
Georgia Senate
President, NCSL

Nancy Cyr
Senior Legal Counsel
Nebraska Legislative Research Office
Staff Chair, NCSL

William Pound
Executive Director

February 2, 2010

Dear Legislative Leader:

We are writing in our capacity as Co-Chairs of the National Conference of State Legislatures Executive Committee Task Force on State and Local Taxation of Communications and Electronic Commerce to bring to your attention an effort by some to collect sales taxes on online transactions by the adoption of "affiliate nexus" legislation. NCSL has led the effort over the past ten years to simplify the collection of sales and use taxes through the Streamlined Sales and Use Tax Agreement and we believe that compliance with the Agreement will provide the states the best opportunity to require collection of all out-of-state sales taxes.

NCSL believes that the effort for states to consider compliance with the Streamlined Sales and Use Tax Agreement is critical in preserving states' ability to raise revenues independent of the federal government. Failure to address structural problems with our sales and use taxes invites Congress to impose its own consumption tax, either in the form of a national sales tax or a value added tax.

There is some confusion among state policymakers that has been fueled by national press reports that the streamlined sales effort and the "affiliate nexus" issues are one and the same. This is not the case. The streamlined sales tax effort will lead to a level playing field where all remote sellers – on line, catalog, or otherwise – are required to collect and remit taxes to the customer's state just as your in state sellers. The "affiliate nexus" issue targets only a small subset of remote sellers that pay commissions to in-state "affiliates" that advertise the seller through the affiliate's web sites. As a result, the "affiliate nexus" bills target only one marketing channel and would not solve the larger problem that the streamlined sales tax effort is trying to address.

Twenty-three states have already enacted legislation to participate in the streamlined sales tax effort and over 1100 out of state sellers have started to collect previously uncollected sales taxes for these states. As of December 31, 2009, these states have received over $500 million in previously uncollected sales tax revenue. NCSL has been working with Congress and the Administration to enact legislation that would give states that comply with the Streamlined Sales and Use Tax Agreement the authority to require all out-of-state sellers to collect those states' sales taxes. When the federal legislation is enacted, states will finally have the ability to close the sales tax collection loophole which is estimated to cost states $23 billion.

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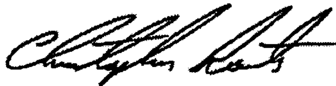
We are very concerned that effort by some to bypass the streamlined sales tax process with these online affiliate nexus laws will distract from the goal of solving the nexus issue once and for all through the Agreement and federal legislation. Furthermore, pending litigation over the constitutionality of the affiliate nexus approach threatens to make it only more difficult for the coalition of Main Street retailers, NCSL, and other groups to convince Congress to pass federal legislation endorsing the Agreement.

Thank you for your consideration of our request. If you have questions or would like additional information about the streamlined sales tax effort, please contact us or Neal Osten, in NCSL's Washington office at neal.osten@ncsl.org.

Sincerely,



Representative Christopher Rants, Iowa — Delegate Shelia Hixson, Maryland
Co-Chairs, NCSL Executive Committee Task Force on State and Local Taxation of Communications & Electronic Commerce

Reject SB 1355 (Nexus)

Affiliate Nexus Bad for Hawaii

SB 1355 proposes to expand "engaging" in business to include the sale of tangible personal property by a person soliciting business through an independent contractor or other representative if the person enters into an agreement with a resident of Hawaii, under which the resident, for a commission or other consideration, directly or indirectly refers potential customers, whether by a link on an internet website or otherwise, to the person.

This language is modeled after a flawed New York law that passed in 2008. The fact that the New York nexus tax generated revenue is an anomaly. In New York, one large retailer chose not to cut off affiliate relationships but only did so to have standing to challenge the law. Most experts believe the law will ultimately be struck down. The basis of the suit is that physical presence, or nexus, is necessary for states to compel companies to serve as tax collectors as the U.S. Supreme Court ruled in 1992 (see Quill Corp. v. North Dakota, 504 US 298 (1992)).

Evidence from two other states that passed similar laws - Rhode Island and North Carolina - shows that the laws actually reduced revenue, eliminated jobs and drove business and consumer dollars out of state.

Former General Treasurer Frank T. Caprio said "the affiliate tax has hurt Rhode Island businesses and stifled their growth, as they've been shut out of some of the world's largest marketplaces, and [it] should be repealed immediately." In fact, the Rhode Island legislature is currently considering a repeal of this law (see R.I.HB 5115).

In the past two years, at least 14 states looked at this very issue and **rejected it**. Those states are California, Connecticut, Hawaii, Iowa, Kentucky, Maryland, Mississippi, Nevada, New Mexico, Oklahoma, Tennessee, South Carolina, Vermont and Virginia.

Annual Notice Bad for Hawaii

The annual notice section is just as legally problematic as the affiliate nexus tax. This section would require an out-of-state business not collecting and remitting the excise tax to provide an annual statement to the Department of Taxation, which must include the names of residents located in Hawaii, the date of the sale, the zip code of the shipping address of each sale and the dollar amount of each sale.

The Direct Marketing Association (DMA) just won a landmark preliminary injunction in federal court through a lawsuit it filed against a similar notice law that passed in Colorado. The ruling prohibits the State of Colorado from enforcing its controversial new law, H.B. 10-1193, that would have required out-of-state companies to report to the state the names, addresses, and purchase amounts of their customers.

The IA agrees with the DMA who rightly argued that the law violates the Commerce Clause of the United States Constitution by (a) imposing discriminatory obligations upon out-of-state retailers that do not apply to in-state Colorado retailers, and (b) unduly burdening interstate commerce under principles set forth by the Supreme Court in Quill Corp. v. North Dakota, 504 U.S. 298 (1992).

The Court accepted these arguments in finding that the DMA had a likelihood of success on both Commerce Clause counts, and concluded that out-of-state retailers subject to the new law would suffer irreparable harm if enforcement of the statute were not barred.

The preliminary injunction effectively suspends the law while the litigation continues and until the Court makes a final ruling regarding the law's constitutionality. The notice requirement contained in the Hawaii nexus bill would likely face similar litigation.