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March 19, 2013

House Co-Chair Patricia M. Widlitz
Senate Co-Chair John Fonfara
Finance, Revenue and Bonding Committee
300 Capitol Avenue
Hartford, Connecticut

Dear Chairs, Vice-Chairs, Ranking Members and Members of the Finance, Revenue and Bonding Committee.

I submit this testimony in support of **Senate Bill 1110: An Act Concerning the Collection and Remittal of Sale and Use Taxes.**

My name is William Comiskey and I am a partner in the State and Local Tax practice group of Hodgson Russ LLP, a law firm with offices in across New York State and in Florida. I am based in the Albany office, located at 677 Broadway in the city of Albany.

I currently represent taxpayers involved in audits and tax controversies before the New York Department of Taxation & Finance. In addition, because I believe completely in the solution they offer, I am pleased to say that Pay My Taxes, LLP, a company that offers sales tax vendors an easy and sensible way to avoid sales tax issues by establishing an escrow account to safeguard and segregate collected sales taxes through their credit card processing bank, is one of my clients and that I have helped the company in its efforts to introduce its product to state tax administrators. I am here today at their suggestion.

Most relevant for today, prior to joining Hodgson Russ in 2010, I served as New York's top tax enforcement officer - the Deputy Commissioner for Enforcement at the New York State Department of Taxation & Finance - where I was in charge of the State's tax audit, collection and criminal enforcement operations.

I have seen the way that New York administers its sales tax laws from both sides - as a tax administrator and as an attorney representing businesses and individuals facing tax audits and prosecutions and struggling with compliance issues.

Respectfully, I urge this Committee to approve Senate Bill 1110 and to authorize the Commissioner of Revenue Services to take all necessary steps to curb sales tax noncompliance

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and to ensure that all sales tax dollars collected by Connecticut's merchants are remitted to the State. By empowering the Commissioner of Revenue Services to both examine the scope of the problem of sales tax noncompliance and to implement needed reforms, Connecticut will have positioned itself to greatly increase sales tax revenues through the adoption of reforms that will harmonize modern banking and electronic technologies with well-recognized principles of law.

As a tax administrator with New York's Department of Taxation & Finance, my office tackled sales tax noncompliance with unprecedented energy.

Why?

Because we recognized that sales tax noncompliance is an enormous problem that costs New York many hundreds of millions of dollars each year – money that had been collected from New York's citizens but that merchants had simply not remitted to the State. We were galvanized too by the recognition that sales tax noncompliance was widespread, especially in some areas of industry where the State had little or no third-party information regarding a vendor's sales activities, and that honest and compliant vendors were operating as a result at an unfair competitive disadvantage.

There is every reason to believe that similar noncompliance is happening here and that Connecticut's citizens are also being shortchanged by sales tax vendors who collect but do not remit Connecticut's sales taxes.

It has been estimated that the national sales tax delinquency rate is 5%, a number that I personally believe is low. Assuming it is on the mark, however, given Connecticut's annual sales tax collections of approximately \$3.2 billion, the annual sales tax gap in Connecticut is in the area of \$160 million, a staggering amount that I am sure every member of this Committee agrees is completely unacceptable. Another number that provides a glimpse of the magnitude of the problem is the amount of uncollected sales tax receivables that have been identified as a result of state tax audits – more than \$200 million according to an October 31, 2011 report of the Connecticut Department of Revenue Services for the fiscal years 2009 and 2010.

Some states have undertaken their own sales tax gap studies and their findings confirm that states are suffering staggering losses from sales tax noncompliance. Minnesota, for example, reported that it lost approximately \$178 million in unpaid sales taxes in 2000. California has estimated that its annual sales tax gap (not including its use tax gap) exceeds \$1 billion, a number that is high given California's relative size but one that gives some evidence of the magnitude of the issue.

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Simply stated, all states – Connecticut included – are losing essential revenues because vendors are not complying with state tax laws. New York and other states have pursued solutions that have involved greater enforcement, enhanced penalties, and investments in data collection and analysis designed to reveal underreporting and noncompliance. All of these steps will help reduce the sales tax gap but, in my opinion, they alone are not enough.

True reform will only come when states realign their systems to recognize and build upon the fiduciary role that merchants play in sales tax administration and then harness the power of modern banking and computer technology to make the collection and remittance of sales tax revenues seamless, painless for the merchant and simple for the state. Fully integrated technology based on sound principles of fiduciary obligations holds the promise of revolutionary change that can end the widespread abuse that exists in sales tax administration.

First, a word about the need for states to fully define the role of the vendor as a fiduciary. I am convinced that meaningful increases in sales tax compliance will only come when vendors are required to treat the sales tax dollars that they collect as money that does not belong to them. It will only come when vendors are expected to act as the fiduciaries they are and when they actually live up to their obligations as fiduciaries. It will only come when they are required to segregate and safeguard the states revenues they collect by depositing those funds upon receipt into escrow accounts that they cannot access except to pay the money over to the state.

When states allow vendors to hold on to the state's money for months at a time, use that money for any purpose and commingle it into their general business or personal accounts, how can anyone be surprised that when vendors spend that money and don't have it when it comes time to file their sales tax returns? I have encountered sales tax vendors who insist, wrongly, that the money they collected is theirs until they are required to pay it over. That is a mindset that New York administrators have only recently begun to challenge in their publications, which now stress (for the first time) that vendors are fiduciaries and that they should not use the sales taxes they collect for their own purposes. But the message has been slow to reach vendors.

Mandatory sales tax escrow accounts based on commonly understood concepts of fiduciary responsibility must be the foundation of any serious effort at sales tax reform. New York has passed laws to empower its Commissioner to require *delinquent* vendors to open and maintain escrow accounts to segregate collected sales tax revenues and to pay over the taxes shortly after receipt. The Commissioner has reported that the Department is using these tools more than ever and that they are having an impact to improve compliance by troubled vendors.

That is a promising start, but it does not go nearly far enough since it only applies to delinquent vendors known to the Department. It does not reach the tens of thousands of noncompliant vendors who have not been discovered by the Department and who fly under the audit radar.

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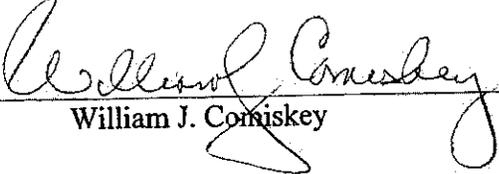
Consider. All lawyers, including those who are most scrupulous in their adherence to their fiduciary and ethical obligations, are required to maintain separate escrow accounts to protect money that they hold that is not theirs. The escrow account is a mechanism that helps prevent all lawyers from "borrowing" their client's money. It prevents noncompliance and is a constant reminder that the money they hold does not belong to them.

So too, requiring all vendors – delinquent and non-delinquent alike -- to have an escrow account will help prevent vendors from slipping into delinquency by removing the temptation to use the state's money for their own purposes.

I have seen too many good people succumb to that temptation and end up in serious trouble with the State. We need a better system.

And escrow accounts do not have to be burdensome. In fact, as my clients are discovering when they are introduced to the Pay My Taxes product, banks like First Data that process their customer's credit cards can (and will) segregate and preserve collected sales taxes in separate accounts with no burden or cost on the vendor. These accounts actually relieve merchant obligations and stress because the earmarked money never becomes available to the merchant. Sales tax compliance becomes automatic and simple. It is happening today for some merchants who are lucky enough to learn of the service. It should become the way of doing business for all vendors.

Thank you.


William J. Coniskey