Streamlined Sales and Use Tax Agreement and Certified Service Providers

By: Rute Pinho, Chief Analyst
Evelyn Wisnieski, Principal Budget Analyst
March 29, 2019 | 2019-R-0101

Issue

Briefly explain the statutory changes that would be necessary for Connecticut to (1) join the Streamlined Sales and Use Tax Agreement (SSUTA) and (2) contract with certified service providers (CSPs) to collect and remit Connecticut sales tax on behalf of remote sellers. What is the potential revenue impact of these changes?

Summary

SSUTA is a multi-state agreement designed to simplify and modernize sales tax collection and administration and to promote compliance by, and reduce costs for, retailers making sales in multiple states. (OLR report 2018-R-0182 provides an overview of the agreement and its member states.) The agreement's main goal is to improve tax collection on remote sales by minimizing administrative costs and burdens on such retailers. One of the ways it seeks to do so is by certifying agents (i.e., CSPs) to perform all of the seller's sales and use tax functions. The CSP model is designed to make it easier for sellers operating across multiple states to comply with each state's sales tax collection and remittance obligations by outsourcing these responsibilities to specialized companies.

Connecticut would need to make major revisions to its sales and use tax law in order to join SSUTA and contract with CSPs, including (1) simplifying its sales and use tax rates, (2) eliminating price-based tax exemptions, (3) adopting uniform definitions for taxable and exempt items and other key

tax terms and (4) allowing CSPs to retain a percentage of sales tax collected and remitted on behalf of remote sellers.

The revenue impact of Connecticut joining SSUTA depends on (1) the uniform sales tax rate adopted and (2) how taxable goods and services are redefined for purposes of complying with the agreement. Below we provide two scenarios, prepared by the Office of Fiscal Analysis (OFA), illustrating the potential revenue impact; one yields $188.8 million in additional FY 20 revenue and the other yields $271.6 million. The revenue impact of requiring the Department of Revenue Services (DRS) to contract with a CSP is indeterminate.

SSUTA

Connecticut would need to make extensive changes in its sales and use tax laws to comply with SSUTA. We highlight three of the most significant changes below and provide two scenarios that illustrate the potential revenue impact of these changes.

Simplifying Rates

SSUTA generally prohibits member states from (1) having multiple state sales and use tax rates on tangible personal property or services or (2) applying tax rates that are based on the value of the transaction or item. However, it carves out exceptions for sales and use taxes imposed on (1) food, food ingredients, and drugs (which may be subject to an additional rate) and (2) other specified commodities and property, including energy (e.g., natural gas, gasoline, and electricity), fuel used to power vehicles and watercraft, motor vehicles, aircraft, watercraft, and modular or manufactured homes (SSUTA, §§ 308 & 323).

These restrictions would require Connecticut to amend its tax structure to eliminate or replace its multiple tax rates. Table 1 lists the state's various sales and use tax rates that currently apply.

Table 1: Connecticut's Sales and Use Tax Rates

Rate	*Basis*
6.35%	Gross receipts from the sale, rental, or leasing of tangible personal property and rendering of specified services
7.75%	• Most motor vehicles with a sales price of more than $50,000 • Jewelry with a sales price of more than $5,000 • Articles of clothing or footwear or handbags, luggage, umbrellas, wallets, or watches with a sales price of more than $1,000
4.5%	Sale of a motor vehicle to a nonresident member of the U.S. armed forces serving on active duty in Connecticut
1%	Computer and data processing services

9.35%	Rental or leasing of a passenger motor vehicle for a period of 30 days or less
2.99%	Sales and purchases of vessels, motors for vessels, and trailers used for transporting a vessel
11%	Room occupancy in a bed and breakfast establishment
15%	Room occupancy in a hotel or lodging house

Although SSUTA may provide some latitude for Connecticut to remove some of these taxes from under the sales and use tax structure and impose them as separate excise taxes (some member states have done so with their room occupancy taxes, for example), SSUTA explicitly prohibits states from imposing a replacement tax on any good or service defined in the agreement that effectively circumvents the agreement's intent (§ 334).

Eliminating Price-Based Exemptions

SSUTA authorizes member states to enact entity-based, use-based, and product-based exemptions, as long as the exemptions are consistent with any applicable product definitions established in the agreement's Library of Definitions (§ 316). It generally prohibits states, however, from using price-based exemptions. The exceptions are for clothing and sales tax holidays. SSUTA member states may impose a cap or threshold of $110 or more on clothing items that either provides that (1) the entire sales price of the item is taxable if it is over the specified threshold or (2) only the portion of the sales price over the threshold is taxable (§ 323). They may also establish a sales tax holiday during which items priced below a specified threshold are exempt from tax (§ 322).

Connecticut currently has several price-based sales tax exemptions that would need to be repealed if the state joined SSUTA. These include exemptions for:

1. items costing $20 or less sold by certain nonprofit organizations and schools (CGS § 12-412(26));
2. the first $2,500 of funeral expenses (CGS § 12-412(55)); and
3. sales of certain gift shop items for $100 or less by nursing homes, rest homes, residential care homes, convalescent homes, or adult day care centers 12-412(56)).

Enacting Uniform Definitions

SSUTA member states must agree to use the common definitions established in the agreement's "Library of Definitions" and not deviate from uniform definitions for taxable and exempt items and services and administrative terms (§ 327). This means that Connecticut, in joining SSUTA, would need to amend its sales and use tax statutes and related administrative rules and regulations in order to incorporate the agreement's definitions. This includes definitions for key tax terms, such as "sales price" and "lease or rental," and product definitions, such as "clothing," "digital products," and "food and food products."

Estimated Fiscal Impact

The revenue impact of Connecticut joining SSUTA will depend upon (1) the uniform sales tax rate adopted and (2) how taxable goods and services are redefined for purposes of complying with the agreement.

Below we provide a baseline and two scenarios to illustrate the potential impact of joining SSUTA. All of the estimates are annualized for FY 20. Scenario 1 applies a uniform tax rate to all categories of sales. Scenario 2 applies a uniform tax rate to all categories of sales, but excludes rental cars and room occupancy. Each scenario also calculates the revenue neutral decrease in the sales tax rate that can be accommodated without negatively impacting revenue to the state.

Please note that this analysis considers the revenue impact to all funds in aggregate. Any policy change adopted will impact the funds that receive a portion of sales tax collections, including the General Fund, the Special Transportation Fund, and municipal revenue sharing account beginning in FY 22 when the transfer is scheduled to resume. There may also be an impact to the Tourism Fund and regional planning incentive account if the room occupancy taxes or rental car taxes were to be amended by an enacted policy.

Baseline. The baseline estimate shown in Table 2 estimates FY 20 sales and use tax revenue under current law (i.e., presuming Connecticut does not adopt SSUTA and there are no other tax policy changes).

Table 2: Baseline Estimate

Category	*Total Rate*	*FY 20 Revenue (All funds)*
General Sales Tax	6.35%	$4,499,100,000
Luxury Sales Tax	7.75%	85,100,000
Rental Car Sales Tax	9.35%	23,900,000
Room Occupancy Tax	15.00%	130,300,000
Bed & Breakfast Occupancy Tax	11.00%	*
Computer and Data Processing	1.00%	50,900,000
Motor Vehicles Sold to Active Duty	4.50%	1,800,000
Boat Tax	2.99%	2,500,000
	Total	**$4,793,600,000**

*The B&B Occupancy Tax estimate is assumed within the Room Occupancy Tax.

Tax Exemptions. For purposes of both scenarios described below, we eliminated the tax exemptions listed in Table 3 in order to comply with SSUTA requirements. The total impact of eliminating these exemptions and applying the 6.35% tax rate to all these goods and services is $11.5 million annually.

Table 3: Eliminated Tax Exemptions

Tax Exemptions	FY 20 Estimate
Monthly charges of $150 electricity	$3,300,000
Items under $20 sold by nonprofits	50,000
Vending machines less than $0.50	50,000
Gold, silver, antique coins	50,000
First $2,500 of funeral expenses	6,300,000
Items under $100 sold by nursing homes	50,000
Machinery exemption of 50%	1,700,000
Total	**$11,500,000**

Scenario 1. The scenario in Table 4 applies the 6.35% rate to all of the categories of sales listed in the baseline table above. The full impact to the state is estimated to be **$188.8 million in FY 20**. The revenue neutral rate in this scenario is **6.10%.**

Table 4: 6.35% Rate Applied to All Sales

Scenario 1a: All Rates at 6.35%

Category	Tax Rate	State Revenue Impact
One Sales Tax Rate	6.35%	177,600,000
Tax Exemptions Eliminated		11,200,000
Uniform Definitions		Minimal
	Total Impact	**188,800,000**
Scenario 1b: Revenue Neutral Rate Decrease		
Less: Rate Decrease on Base	6.10%	(196,200,000)
	Total (Net) Impact	**(7,400,000)**

Scenario 2. The scenario in Table 5 applies the 6.35% rate to all of the categories of sales listed in the baseline table but excludes the room occupancy (hotels, lodging houses, and bed and breakfasts) and rental car taxes. The full impact to the state is estimated to be **$271.6 million in FY 20**. The revenue neutral rate in this scenario is **6.00%.**

Table 5: 6.35% Rate Applied to All Sales Except Room Occupancy and Rental Car Taxes

Scenario 2a: All Rates at 6.35% (excl. Room Occupancy, Rental Car)

Category	Tax Rate	State Revenue Impact
One Sales Tax Rate	6.35%	260,400,000

Tax Exemptions Eliminated		11,200,000
Uniform Definitions		Minimal
	Total Impact	**271,600,000**
Scenario 2b: All Rates at 6.35% (excl. Room Occupancy, Rental Car)		
Less: Rate Decrease on Base	6.00%	(270,700,000)
	Total (Net) Impact	**900,000**

Certified Service Providers (CSPs)

Overview

CSPs are private companies certified under SSUTA to perform sales and use tax functions for remote sellers. According to the Streamlined Sales Tax Governing Board's website, the board currently contracts with six CSPs (Accurate Tax, Avalara, Exactor, Sovos, TaxCloud, and Taxify by Sovos).

CSPs generally do not charge sellers for their services for SSUTA member states. Rather, member states pay the CSP for providing its services at no charge to sellers who voluntarily come forward to collect and remit sales tax in the state (i.e., volunteer sellers). They do so by allowing the CSP to retain a percentage of the sales tax reported and paid on time to the state on behalf of each volunteer seller. It appears that Connecticut's sales and use tax law would need to be amended to allow this type of payment structure.

CSPs do not work exclusively with SSUTA member states. At least one state, Pennsylvania, has announced plans to certify service providers on its own to help remote sellers in sales tax registration, collection, reporting, and remittance.

Fiscal Impact

Requiring the DRS to contract with a CSP may result in revenue gain to the extent that it captures any delinquent, underreported, or underpaid taxes due to the state that otherwise would not be collected. However, the revenue impact is anticipated to be minimal because (1) the CSP may collect taxes that would have otherwise been remitted by the retailer and (2) existing law already allows DRS to more broadly enforce sales tax collection from retailers (PA 18-152).

The state would also incur a cost for the CSP's services, depending on the provider chosen and the contracted terms. The net fiscal impact to the state is therefore indeterminate.

RP:kl