

2009 SENATE FINANCE AND TAXATION

SB 2325

2009 SENATE STANDING COMMITTEE MINUTES

Bill/Resolution No. SB 2325

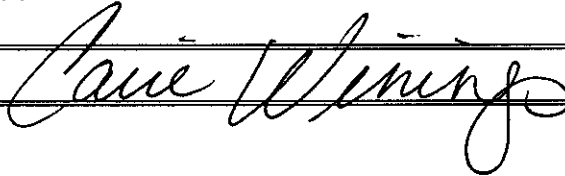
Senate Finance and Taxation Committee

Check here for Conference Committee

Hearing Date: 01/26/2009

Recorder Job Number: 7377

Committee Clerk Signature



Minutes:

Vice Chairman Miller: Opened hearing on SB 2325.

Chairman Cook: Introduced the bill. See attachment #1.

In one sentence we would be modernizing sales tax for the 21st Century.

Senator Oehlke: Have we nailed down vendors to handle the collection?

Chairman Cook: Yes we have. One of the projects goals was to have a third party vendor that could collect and remit a company's sales tax. We have four of them that are licensed and registered with streamline sales tax governing board. There are two types: 1. A Certified Service Provider that the state compensates them. 2. A Certified Automated System and that is a software system that a vendor can buy that is compliant with tax laws.

Myles Vosberg, Tax Commissioners Office: See Attachment #2 for testimony in support of the bill. There were a few clarification questions by the committee on this testimony.

Chairman Cook: Before a state gets approved to be in compliance, the governing board is made up of state legislators, state tax department, and the private sector, and one of the processes of the state being found to be in compliance is that it is reviewed by a group of people to make sure that we pass laws in our state to be in compliance and every year we

have to go through that process, correct?

Myles Vosberg: Correct.

Chairman Cook: And we just went through our review?

Myles Vosberg: It started in the summer and extended through the fall. We had one definition for purposes of communication, telecommunications that we forgot to put in our rule.

Chairman Cook: That will get corrected?

Myles Vosberg: Yes

Chairman Cook: These changes we are going to make, they will go through that same review process, correct?

Myles Vosberg: Correct

Chairman Cook: Has this piece of legislation had any review outside your tax department?

Myles Vosberg: I do not believe so, other than you as the sponsor and the legislative council.

Senator Anderson: Are there other tax departments doing the same thing you are doing?

Myles Vosberg: Yes there are.

Senator Oehlke: The money we have collected so far, the vendor got a percentage of it, right?

Myles Vosberg: That is correct. These figures are net of any compensation.

Senator Oehlke: Is that negotiated by the group of streamlined sales states then, or does each state negotiate an amount?

Myles Vosberg: The governing board enters into a contract with the CSP's and the company that have the software. So they all get the same compensation.

Mike Rud, President, North Dakota Retailers Association: Testified on the record in support of the bill. It would be good for North Dakota.

Chairman Cook: Any further testimony in support?(No), opposed?(No), neutral?(No)

Closed hearing on SB 2325.

Senator Triplett moved a DO PASS.

Senator Anderson SECONDED the motion.

A Roll Call Vote was taken: Yea: 7, Nay: 0, Absent: 0

Senator Cook will carry the bill.

Date: 01/26/09
Roll Call Vote #: 1

2009 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. : 2325

Senate Finance and Taxation Committee

Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Do Pass

Motion Made By Senator Triplett Seconded By Senator Andersch

Senators	Yes	No	Senators	Yes	No
Sen. Dwight Cook - Chairman	✓		Sen. Arden Anderson	✓	
Sen. Joe Miller - Vice Chairman	✓		Sen. Jim Dotzenrod	✓	
Sen. David Hogue	✓		Sen. Constance Triplett	✓	
Sen. Dave Oehlke	✓				

Total (Yes) 7 No 0

Absent 0

Floor Assignment Senator Cook

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

SB 2325: Finance and Taxation Committee (Sen. Cook, Chairman) recommends DO PASS (7 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). SB 2325 was placed on the Eleventh order on the calendar.

2009 HOUSE FINANCE AND TAXATION

SB 2325

2009 HOUSE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2325**

House Finance and Taxation Committee

Check here for Conference Committee

Hearing Date: March 4, 2009

Recorder Job Number: 10152

Committee Clerk Signature

Minutes:

Vice Chairman Drovdal: We will open the hearing on SB 2325.

Senator Dwight Cook: District 34, which is the western upper class suburb to this capital city you are in. **(Testimony 1) (03:27)**

Representative Pinkerton: What can we do to help overturn Quill vs. North Dakota as far as; is there anything legislative that we can do for funding?

Representative Cook: You bet there is. Write your congressmen. It will really help and now is the time to do it. The North Dakota delegation, Senator Dorgan has been a leader in this. He is not a cosigner of the current legislation. I know I have talked personally with him. He is committed to bringing it to the end, to seeing this thing forward. There is just one little issue he has not resolved yet. I think we are getting that worked out, but for anybody that can write our delegation, it would be helpful.

Representative Winrich: Do you have the bill identification in Congress?

Senator Cook: It has not been introduced at this time. It is real close. There was one introduced last year; I think it was SB 46. There was a companion bill in the House. This one

could get introduced we suspect sometime within the next two weeks. There are a lot of things happening right now bringing on the original sponsors of the bill.

Vice Chairman Drovdal: Any other questions of Senator Cook? Seeing none, we thank you for your testimony. Other testimony in favor of SB 2325?

Myles Vosberg, Director of the Tax Administration, Division of the Office of the State Tax Commissioner: (Testimony 2). (05:35) I will just mention that the bill you see before you today represent changes that the governing board of the streamline sales tax committee have made over the last couple of years since we had the last session.

Representative Froelich: On page 7, lines 19-24, can you give me a little better handle on that? There are so many different subdivisions and subsections.

Myles Vosberg: This is the section that deals with where local subdivisions source their sales. In other words, at what point is the sale taxable? ND uses a destination sourcing and so wherever the goods transfer, where the customer takes possession is the point of taxation. What this provision does is allow states to choose to source or tax those sales at the point where the retailer is located, rather than where the goods are delivered to the customer. So unless ND made a change in their law to do that, this particular provision doesn't really impact us. However, it is one of those sections that we have specifically identified in our code and so we are adding it into section 3. It is one of those sections of the agreement; but what all of this language does is it provides the guidelines on what states need to do if they choose to tax those sales at the point where the retailer is located, rather than where the goods are delivered.

Vice Chairman Drovdal: Any other questions?

Representative Pinkerton: On page 18, the last part of section 16, lines 1-14, that deals with transactions of maintenance software agreements, state law currently is that on software agreements, our state law currently conforms with the three sections printed here. Is that correct? Section C in particular.

Myles Vosberg: Section C, that is correct. Section 16 is the language in the streamline agreement that deals with the contracts. Sections 1 and 2 of the agreement are the changes or the additions that we made to our sales tax law to comply with those guidelines and they match what we were already doing. So we did already tax the entire software contract if there was a bundle of service and software together; this just reinforces that.

Representative Pinkerton: Even if the vendor provides documentation that shows some portion is for service and some portion is for upgrades, it makes no difference?

Myles Vosberg: If there is a separate line item on the invoice, then you tax only the prewritten software and not the service; but if they bundle those two together for one price and there is no identification of how much of the price is (cough), then we tax the whole works.

Representative Pinkerton: It has to be on the invoice?

Myles Vosberg: Not necessarily; there could be a contract maybe that lays out those provisions. If there are sales documents of some type, it is not that uncommon for software companies to have a contract that would lay out the provisions that would split it; but when you get the invoice, it is lumped together. We would still acknowledge that contract that is behind the invoice.

Representative Pinkerton: If there is documentation from the vendor that shows the percentage that is for service and the percentage for upgrades, then you would be satisfied with that?

Myles Vosberg: We would accept that, yes.

Vice Chairman Drovdal: Any other questions of Mr. Vosberg? Other testimony in favor of 2325?

Jerry Hjelmstad, ND League of Cities: (17:58) We continue to support this effort to streamline the sales tax and make it possible to collect the sales tax on a national basis.

I will try to answer any questions.

Vice Chairman Drovdal: Other testimony in favor of SB 2325? Seeing none, is there any opposition to SB 2325? Any neutral testimony. Having no neutral testimony, we will close the hearing on SB 2325.

2009 HOUSE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2325**

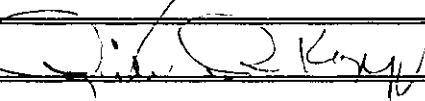
House Finance and Taxation Committee

Check here for Conference Committee

Hearing Date: March 4, 2009

Recorder Job Number: 10157

Committee Clerk Signature



Minutes:

Chairman Belter: We have a motion for a “do pass” from Representative Pinkerton and a second from Representative Brandenburg. Any discussion? **A roll call vote on the “do pass” on SB 2325 resulted in 11 ayes, 0 nays, 2 absent/not voting. SB 2325 will be carried by Representative Drovdal.**

Date: 3/4/09

Roll Call Vote #: 1

2009 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 2325

House FINANCE AND TAXATION Committee

Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Do Pass Do Not Pass Amended

Motion Made By Pinkerton Seconded By Brandenburg

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley R. Betteer	/		Representative Froelich		
Vice Chairman David Drovdal	/		Representative Kelsh	/	
Representative Brandenburg	/		Representative Pinkerton	/	
Representative Froseth	/		Representative Schmidt	/	
Representative Grande	/		Representative Winrich	/	
Representative Headland					
Representative Weiler	/				
Representative Wrangham	/				

Total (Yes) 11 No 0

Absent 2

Floor Assignment Rep Drovdal

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

SB 2325: Finance and Taxation Committee (Rep. Belter, Chairman) recommends DO PASS (11 YEAS, 0 NAYS, 2 ABSENT AND NOT VOTING). SB 2325 was placed on the Fourteenth order on the calendar.

2009 TESTIMONY

SB 2325

Subject: FW: Web Sales Tax

Buying on Web to avoid sales taxes could end soon

By Rachel Metz 1/13/2009

Associated Press

Shopping online can be a way to find bargains while steering clear of crowds - and sales taxes.

But those tax breaks are starting to erode. With the recession pummeling states' budgets, their governments increasingly want to fill the gaps by collecting taxes on Internet sales, which are growing even as the economy shudders.

And that is sparking conflict with companies that do business online only and have enjoyed being able to offer sales-tax free shopping.

One of the most aggressive states, New York, is being sued by Amazon.com Inc. over a new requirement that online companies must collect taxes on shipments to New York residents, even if the companies are located elsewhere. New York's governor also wants to tax "Taxman" covers and other songs downloaded from Internet services like iTunes.

The amount of money at stake nationwide is unclear; online sales were expected to make up about 8 percent of all retail sales in 2008 and total \$204 billion, according to Forrester Research. This is up from \$175 billion in 2007.

Based on that 2008 figure, Forrester analyst Sucharita Mulpuru says her rough estimate is that if Web retailers had to collect taxes on all sales to consumers, it could generate \$3 billion in new revenue for governments.

It's uncertain how much more could come as well from unpaid sales taxes on Internet transactions between businesses. But even with both kinds of taxes available, state budgets would need more help. The Center on Budget and Policy Priorities estimates that the states' budget gaps in the current fiscal year will total \$89 billion.

Collecting online sales taxes is not as simple as it might sound. A nationwide Internet business faces thousands of tax-collecting jurisdictions - states, counties and cities - and tangled rules about how various products are taxed.

And a 1992 U.S. Supreme Court ruling said that states can't force businesses to collect sales taxes unless the businesses have operations in that state. The court also said Congress could lift the ban, which remains in place - for now.

As a result, generally only businesses with a "physical presence" in a state - such as a store or office building - collect sales tax on products sent to buyers in the same state. For instance, a Californian buying something from Barnes & Noble Inc.'s Web site pays sales tax because the bookseller has stores in the Golden State. Buying the same thing directly from Amazon would not ring up sales tax.

That doesn't mean products purchased online from out-of-state companies are necessarily tax-free. Consumers are usually supposed to self-report taxes on these items. This is called a use tax, but not surprisingly, it tends to go unreported.

It hopes of unraveling the complex tax rules - and bringing states more money - 22 states and many brick-and-mortar retailers support the efforts of a group called the Streamlined Sales Tax Governing Board. The group is getting states to simplify and make uniform their numerous tax rates and rules, in exchange for a crack at taxing online sales.

Among other things, participating states need to change how they define things such as "food" and "clothing." For example, one state might now consider a T-shirt clothing and tax it as such, while another might consider it a sporting good and tax it differently.

In response, more than 1,100 retailers have registered with the streamlining group and are collecting sales taxes on items shipped to states that are part of the agreement - even if they are not legally obligated to.

The streamlining board also is lobbying Congress to let the participating states do what the Supreme Court ruling banned: They could force businesses to collect taxes on sales made to in-state customers, even if the businesses don't have a physical presence there.

New Jersey, Michigan and North Carolina are among the largest of the 19 states that have adjusted their tax laws to fully comply with the group's streamlined setup. Washington was the only state to join in 2008, but three more states are close to becoming full members of the group. And Scott Peterson, the group's executive director, expects another seven states - including Texas, Florida and Illinois - to introduce legislation in January that would make them eligible to join.

Undoing the patchwork can be difficult, even if the weak economy increases states' motivation to go after online sales taxes. Similar bills have been introduced in several states and failed, sometimes because of the cost of changing tax laws. New York, for example, decided against joining the streamlining board because it would require extensive revisions to its tax rules.

Besides various states and retailers such as Wal-Mart Stores Inc., Borders Group Inc. and J.C. Penney Co., the National Retail Federation, the industry's biggest trade group, also supports the Streamlined Sales Tax group.

Companies that handle Web sales only have organized as well. NetChoice, whose members include eBay Inc. and online discount retailer Overstock.com Inc., supports the states' tax simplification efforts, but its executive director, Steve DeBianco, says online retailers should have to collect taxes only in states where they have a physical presence.

But what if the meaning of "physical presence" is changed? New York essentially did that in April when its budget included a provision requiring online retailers like Amazon to collect taxes on purchases made by New Yorkers.

The new rule requires retailers to collect sales tax if they solicit business in New York by paying anyone within the state for leading customers to them. Since some Web site operators within New York are compensated for posting ads that link to sites like Amazon, the online retailers would have to collect taxes.

Matt Anderson, spokesman for the New York State Division of the Budget, said the state expects to reap \$23 million during the current fiscal year, which ends March 31, from newly collected online sales taxes.

That's a sliver of the overall state budget for the same period, which is \$119.7 billion. The state faces a revenue gap of \$1.7 billion.

Yet Anderson said the state wants "to level the playing field and end the "unfair competitive advantage" Web-only companies have over brick-and-mortar stores that can't avoid collecting sales taxes.

Amazon complies, and collects sales taxes on shipments to New York. However, Amazon is still fighting the rule. It sued New York in April, alleging its provision is unconstitutional. Amazon also said it is being specifically targeted by the law. The case is pending.

Amazon declined further comment.

Salt Lake City-based Overstock is also suing New York over the law. Unlike Amazon, Overstock is not collecting sales tax in New York, because it ended agreements with about 3,400 affiliates in the state that were being paid for directing traffic to Overstock.com.

The Streamlined Sales Tax group hopes Congress takes up its uniform-tax idea in 2009. Peterson thinks the dismal economy boosts the chances of passage.

But Congress also will be occupied with economic stimulus plans involving bigger pools of money. And Mulpuru, the Forrester Research analyst, notes that for years there has been talk of taxing online retailers.

"It's a legal morass," she said. "In a best-case scenario, it's going to take a while to sort everything out."

#2

TESTIMONY OF THE OFFICE OF STATE TAX COMMISSIONER
BEFORE THE
SENATE FINANCE AND TAXATION COMMITTEE

*Same testimony
& handout given
to House.*

SENATE BILL 2325

January 26, 2009

Chairman Cook, members of the Senate Finance and Taxation Committee, I am Myles Vosberg, Director of the Tax Administration Division of the Office of State Tax Commissioner and I am here today on behalf of the Commissioner to testify in support of Senate Bill 2325.

BACKGROUND

North Dakota has been a member of the Streamlined Sales Tax (SST) Agreement since 2005. As you know, the Streamlined Sales Tax Project has been a joint effort of state and local governments, the business community, tax practitioners, and many trade associations to simplify the sales tax laws in exchange for voluntary collection of sales and use taxes by retailers that have no legal obligation to collect.

Senate Bill 2325 makes the necessary changes for North Dakota to remain in compliance with the Streamlined Sales Tax Agreement. The entire Agreement is adopted by reference in Section 1 of North Dakota Century Code Chapter 57-39.4 except for Articles III and V of the Agreement. Each section of Articles III and V is explicitly adopted in the remaining sections of Chapter 57-39.4. Many of the changes in this bill are amendments and additions to Articles III and V of the agreement. Although some of these changes will not directly impact our administration of the sales tax laws, they are included in N.D.C.C. Chapter 57-39.4 so our law continues to contain these sections of the agreement in their entirety.

Article III is entitled "Requirements Each State Must Accept to Participate" and it identifies concepts and processes that states must comply with to be a member of the agreement. For example, states must: administer all local sales taxes at the state level, participate in a central registration system, and post a taxability matrix to its website. North Dakota's taxability matrix lists each product defined in the agreement and identifies each as taxable or exempt. Article V of the agreement identifies each state's requirement to test software so that it can be certified by the Streamlined Sales Tax Governing Board.

EXPLANATION OF THE BILL

Sections 1 and 2 of bill address the taxability of maintenance contracts for prewritten computer software. Section 1 defines these agreements and section 2 addresses the taxability. North Dakota taxes all mandatory agreements associated with

the purchase of software, optional agreements that include only software updates, and bundles of software updates and support service that are sold for one non-itemized price.

Section 3, 5, and 22 are technical corrections made to previous Streamlined Sales Tax legislation. Section 3 removes obsolete language related to the taxability of freight. Freight charges associated with a taxable sale of tangible personal property are part of the taxable selling price. The location where title passes no longer impacts the taxability of the freight. Sections 5 and 22 correct the definition of prepared food. Food is considered prepared, and therefore taxable, if utensils are provided by the seller – not to the seller as currently stated. Section 5 corrects the sales tax law. Section 22 makes the same correction in the use tax law.

Sections 4 and 21 amend the definition of durable medical equipment. Durable medical equipment and repair parts for the equipment are exempt from sales tax. The addition to this definition clarifies that consumable items used with the equipment are not considered repair parts for purposes of the exemption. Again, section 4 amends the sales tax law and section 21 makes the same change in the use tax law.

Sections 6 through 19 are all changes to Articles III and V of the Streamlined Sales Tax Agreement which are adopted in Chapter 57-39.4 of the Century Code.

- Section 6 provides relief of liability to a retailer that collected sales tax at the incorrect rate if the effective date of a rate change is less than thirty days after the enactment of the change. The relief applies only if the retailer collected tax at the rate in place prior to the change and only for the first 30 days after the date of enactment.
- Section 7 requires states to provide retailers and Certified Service Providers updated databases of information at least thirty days before the first day of a calendar quarter when the change is effective. The databases are 1) a list of all taxing jurisdictions and rates, and 2) a database of all zip codes in North Dakota and the corresponding tax jurisdiction.
- Section 8 allows states to choose where to source florist sales resulting from electronic orders. The sale may be sourced where the order was taken or where the product was delivered.

← where transaction occurs

- Sections 9 and 10 will allow states to elect origin sourcing for intrastate sales if at least five states make the election by January 1, 2010. North Dakota uses destination sourcing to determine where a transaction occurs.
- Section 11 allows any state to elect to use origin sourcing for direct mail delivered in the same state where it originated. Direct mail is a mailing of printed material to addresses on a mailing list at the direction of a purchaser and the recipients are not billed for the materials. North Dakota uses destination sourcing for direct mail.
- Section 12 clarifies that a Certified Service Provider may use personally identifiable information to determine the proper tax jurisdiction of a purchaser.
- Sections 13 and 14 provide additional administrative processes related to sales tax holidays. To date, North Dakota has not provided for sales tax holidays.
- Section 15 requires member states to include information in their taxability matrix about the taxability of digital products and about the administration of sales tax holidays, if any exist.
- Section 16 describes how states characterize components of computer software maintenance contracts as a sale of service or as a sale of prewritten computer software.
- Sections 17 and 18 provide administrative guidelines related to specified digital products and other products delivered electronically if a state chooses to tax any of these products.
- Section 19 clarifies the agreement language regarding each member state's responsibility to review third party software certified by the SST governing board. Each state has the responsibility to test the software to assure the program is correctly determining if categories of products are taxable or exempt. Retailers registering through the central registration system to collect tax in member states may purchase this software to assist in calculating the correct tax on transactions.

Section 20 adds existing sales tax definitions to the use tax laws.

CONCLUSION

This bill will have no fiscal impact. Most of the changes relate to administrative provisions of the Streamline Sales Tax Agreement or are technical corrections to previous legislation. All changes that directly apply to the sales and use tax laws reflect existing administrative practice. The Tax Commissioner's Office respectfully requests favorable consideration on Senate Bill 2325.

Attached is current information regarding sales tax collections remitted by retailers that have registered through the Streamlined Sales Tax central registration system.

Revenue Collections From Streamlined Sales Tax Registrants

October 1, 2005 through December 31, 2008

Period	(1) Not Required to Register in ND	(2) Required to Register in ND	(3) Registered in ND Before 10/01/05	(4) Total Collections From SST Registrants
10/05 - 06/06	\$23,541	\$9,146	\$520,451	\$553,138
07/06 - 09/06	65,723	5,784	322,593	394,100
10/06 - 12/06	145,133	92,623	257,096	494,852
01/07 - 03/07	233,863	79,172	171,041	484,076
04/07 - 06/07	283,164	82,600	218,800	584,564
07/07 - 09/07	314,289	42,548	196,436	553,273
10/07 - 12/07	307,089	105,618	287,591	700,298
01/08 - 03/08	300,969	242,362	184,263	727,594
04/08 - 06/08	216,271	200,525	256,943	673,738
07/08 - 09/08	228,561	199,509	159,806	587,876
10/08 - 12/08	214,928	180,929	493,797	889,654
	<u>\$2,333,530</u>	<u>\$1,240,816</u>	<u>\$3,068,818</u>	<u>\$6,643,163</u>

The revenue in this table was collected and remitted by taxpayers that have registered through the Streamlined Sales Tax (SST) central registration system. Taxpayers that register through the central registration system must collect tax in all SST member states.

(1) Revenue from taxpayers that voluntarily registered and have no obligation to collect North Dakota tax.

(2) Revenue from taxpayers that registered through SST, but have a legal obligation to register and collect North Dakota tax.

(3) Revenue from taxpayers that were already registered in North Dakota and collecting tax before they registered through the SST central registration system.

(4) Total of columns 1, 2, and 3.

SB 2325

Mr. Chairman,

For the record, my name is Dwight Cook, State Senator from District 34 in Mandan.

SB 2325 is our Streamlined Sales Tax compliance legislation. It is that piece of legislation that we see every session to update and further simplify our sales and use tax code so that North Dakota can continue to be in compliance with the Streamlined Sales Tax Agreement. As you know, the development of this act has been and continues to be a joint effort of state and local governments, the business community, tax practitioners and many trade associations. The purpose is to simplify and modernize state sales tax laws, in exchange for voluntary collection of sales and use taxes by retailers that have no legal obligation to collect with the ultimate goal to get Congress to pass legislation that would reverse the Supreme Court decision made in "Quill vs. North Dakota".

Since October 1, 2005, the date this agreement became effective, 1100 remote sellers have voluntarily registered with the central registration created by Streamline. These 1100 retailers have collected and remitted \$6.6 million to the State of North Dakota with over half of that being new money.

The Governing Board now consists of 22 states with 19 being full member states. Congress will soon have before it federal legislation to overturn Quill and the expectation that it will pass is high.

Mr. Chairman, SB 2325 has no fiscal impact. Most of the changes relate to administrative provisions of the Streamlined

SB 2325

Sales Tax Agreement or are technical corrections. All changes that do directly apply to the sales and use tax laws reflect existing administrative practices.

They are simply clarifications in an ever changing and complex world of tangible property that is exploding with many new products every year. It will reduce litigation between the private sector tax attorneys and public sector tax attorneys over what is and what is not taxable. And it needs to pass.