PIONEER OPPORTUNITY

As the COVID-19 Pandemic Spurs Consumer Shift to E-Commerce, the Massachusetts Sales Tax Collection System Deserves Renewed Scrutiny

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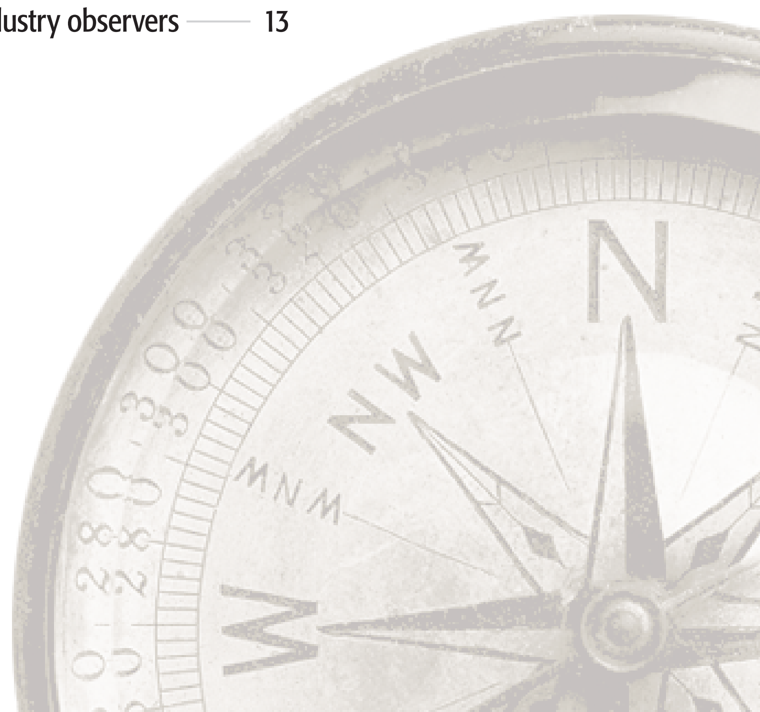

Introduction

The COVID-19 pandemic has created twin crises in Massachusetts. The first is the public health crisis that has resulted in over 100,000 confirmed cases of COVID-19 and over 7,000 confirmed deaths as of May 31st, 2020.[1] The second is the economic crisis that has forced thousands of Massachusetts businesses to close their doors to employees, customers, and the public, causing 38.8 percent of the Massachusetts workforce to file unemployment claims as of May 23, 2020.[2]

For Massachusetts state government leaders, COVID-19 has caused a steep, unforeseen mid-year drop in state revenue from income, corporate, capital gains, and sales taxes; MBTA fare revenue; and casinos and the lottery. As state government leaders scramble to find ways to continue funding essential services, provide local aid to cities and towns, and make contractually obligated payments on public debt and collective bargaining agreements, they should consider enacting a bill pending in the current legislative session that would modernize and speed up sales tax collection from large-scale internet retail sellers without affecting hard-pressed small and medium sized retailers.

Governor Baker has offered a "tax modernization" proposal that has the potential to increase both short- and long-term sales tax collection. Now is the time for Massachusetts to do two important things: 1) join 19 other states in requiring large-scale retailers to accelerate sales tax remittance; and 2) require credit card processors to remit sales taxes on purchases from large volume retailers with annual sales of $10 million or more directly to the Massachusetts Department of Revenue.

Governor Baker has offered a "tax modernization" proposal that has the potential to increase both short- and long-term sales tax collection.

Before the pandemic, the sales tax accounted for approximately 23 percent of Massachusetts' total annual tax revenue, but the decline in retail sales over the past 10 weeks has created a crisis for state leaders here and in other sales tax-dependent states across the country. According to the U.S. Census Bureau's Advance Monthly Sales for Retail and Food Services Survey released on May 15, retail and food services sales revenue in the U.S. declined by 21.6 percent in a month-to-month comparison of April 2019 and April 2020.[3] The Census Bureau does not report state-by-state monthly data on retail and food services sales revenue, but the Massachusetts Taxpayers Foundation (MTF), which has a long history of producing authoritative state revenue estimates, recently projected that state sales tax revenue will decline by $2.037 billion from the January 2020 state benchmark of $7.425 billion, a decrease of 27.4 percent.[4] MTF projects a total decline in state tax revenue of $6 billion from the $31.15 billion January 2020 benchmark, a decrease of 19.3 percent. According to the MTF forecast, more than one-third of the expected plunge in Massachusetts tax revenues will come from a decline in sales tax collections.

Sales of retail goods and food services plummeted in Massachusetts and across the U.S. after state governments imposed social distancing directives and ordered non-essential businesses to close. In Massachusetts, Governor Charlie Baker declared a state of emergency on March 10, 2020 and banned all public gatherings of more than 25 people five days later. On March 23, the governor expanded his ban to include all public gatherings of more than 10 people and issued an emergency order requiring that all non-essential businesses close their facilities to workers, customers, and the public. Safety measures such as these, while essential to protect the lives and health of employees and the general public, have had a particularly devastating impact on brick-and-mortar retail businesses across the country.

Figure 1 presents sales revenue data released by the U.S. Census Bureau on May 15 that compares April 2019 and April 2020 monthly retail and food services sales in the U.S. by category.[5] It shows that retailers other than non-store retailers experienced a 27.8 percent drop in sales in April 2020 compared to April 2019, while non-store retailers increased sales by 21.6 percent.

Figure 1. Comparison of April 2019 and April 2020 monthly retail and food services sales, non-store retailers vs. all other retailers

Source: U.S. Census Bureau, Pioneer Institute analysis

Figure 2 presents advance monthly sales for retail and food services in the month of April from 2010 to 2020, as estimated by the U.S. Census Bureau. The chart compares the cumulative growth in sales of non-store retailers with that of all other retailers in April of each year. As shown, non-store retailers experienced a cumulative increase in sales of 182.5 percent from April 2010 to April 2020, while all other retailers experienced a decrease in sales, including a $125.3 billion decrease from April 2019 to April 2020. Owing to this sudden drop in sales, U.S. retail and food services sales in April 2020 were $4.0 billion less than in April 2010 when non-store retail sales are excluded.

Figure 2. Cumulative growth of April retail and food services sales, 2015 to 2020, non-store retailers compared with all other retailers (millions)

Year	Non-store Retailers (sales)	All other retailers (sales)	Non-store Retailers (cumulative growth)	All other retailers (cumulative growth)
2010	27,745	329,525	0.0%	0.0%
2011	30,737	350,036	10.8%	6.2%
2012	33,173	366,742	19.6%	11.3%
2013	35,344	376,924	27.4%	14.4%
2014	38,277	395,371	38.0%	20.0%
2015	41,698	400,902	50.3%	21.7%
2016	45,323	407,711	63.4%	23.7%
2017	51,389	423,946	85.2%	28.7%
2018	57,804	438,163	108.3%	33.0%
2019	64,475	450,821	132.4%	36.8%
2020	78,383	325,563	182.5%	-1.2%

Source: U.S. Census Bureau, Pioneer Institute analysis

Before the COVID-19 pandemic began, retail sector analysts had already been forecasting tough times ahead for brick-and-mortar retailers because of online shopping. In January 2020, credit insurance company Euler Hermes wrote, "The U.S. has lost more than 56,000 stores, or 10.7%, of its discretionary retail footprint since 2008, despite healthy spending on discretionary consumer goods. Employment data depict a similarly gloomy picture, with 670,000 net job destructions since 2008 (-9.6%). For one job created in e-commerce, four and [a] half jobs are lost in traditional discretionary retail."[6] Euler Hermes "estimates that continued e-commerce penetration could eliminate another 500,000 jobs and 30,000 retail establishments by 2025."[7]

The Census Bureau released its April advance monthly retail sales report on May 15, 2020.[8] Shortly thereafter, CNBC Markets Editor Patti Domm wrote, "April retail sales plunged a shocking 16.4% [from March], worse than the 12.3% expected by economists, but one category was higher: online sales. Analysts say the divide between online merchants and brick-and-mortar stores is growing, and a trend toward restructuring and consolidation is being accelerated by the coronavirus crisis." She quoted Diane Swonk, chief economist at Grant Thornton, as follows: "It's an acceleration of a trend. It speeded up by two to four years the restructuring in retail."[9] She also quoted Michael Arone, chief investment strategist at State Street Global Advisors as follows: "If you look at this retail number this morning, what's already happened with folks like Neiman Marcus and what's likely to happen with J.C. Penney . . . the pandemic has accelerated the major shakeup in the industry. It's basically expected to happen much quicker."

For one job created in e-commerce, four and [a] half jobs are lost in traditional discretionary retail.

Forrester Research Inc., an American market research company that provides advice on existing and potential impact of technology, projected in a webinar on April 23, 2020 that E-commerce will be 25 percent of total retail sales in the U.S. by 2024.[10] It stated, "COVID-19 has become a brutal accelerator agent of digital transformation trends that were already underway. Research indicates that it takes 66 days or roughly two months for a behavior to become an automatic habit. That is roughly how long most countries have been in various stages of lockdowns."[11]

While Massachusetts brick-and-mortar retailers hope for a rapid "v-shape" recovery, as do state government leaders who depend on sales tax revenue from retail sales, some economists are pessimistic. "When we look at the department stores, specialty stores, specialty hard goods, specialty soft goods, we do not see this getting back to the 2019 level until 2023 at best. There are a lot of these stores that are going to go under," Greg Buzek of IHL Group, a global research and advisory firm specializing in technologies for the retail and hospitality industries, said in a webinar on May 7, 2020.[12] Buzek, Founder and President of IHL, presented the following forecast of the recovery of U.S. Department Stores, specialty hard goods, and specialty soft goods.[13]

What can Massachusetts do to address its sales tax shortfall without further burdening small and medium size retailers?

Governor Baker's proposed FY2021 budget includes four outside sections (48–51) related to "tax modernization" that could provide effective mechanisms to speed up and improve sales tax collection. They can best be understood as two proposals—a phase one proposal for advance payment of sales taxes and a phase two proposal for real-time sales tax collection. In the following sections, we summarize these two proposals and advocates' and opponents' arguments for and against the proposals. We conclude with our recommendations.[14]

Phase one of Governor Baker's proposal, beginning on July 1, 2020

Under current law, retailers are required to file a return for each month, remitting sales tax collected until the 20th day of the following month.

Under Governor Baker's proposal, the Department of Revenue (DOR) commissioner would be authorized to promulgate regulations to require retailers that collected more than $100,000 in sales taxes or taxes on accommodations and meals (hereinafter referred to as "sales taxes") in the previous 12 months to make a preliminary remittance of taxes. If the legislature approves the proposal, the administration has signaled that sales taxes collected during the first three weeks of the month would have to be remitted in the final week of the same month. Remittance for the final week and reconciliation of the monthly filing would continue to occur in the following month. Phase one would only impact the largest 10 percent of businesses, which account for 90 percent of sales tax revenue.[15]

Under current law, retailers are required to file a return for each month, remitting sales tax collected until the 20th day of the following month.

Phase two of Governor Baker's proposal, beginning on July 1, 2023

Under current law, merchants are the parties solely responsible for collecting and remitting sales/meals/occupancy taxes to DOR. Under the governor's phase two proposal, merchants would be required to identify the sales tax component of sales transactions to third-party payment processors and the processors would be required to remit such taxes to DOR. Currently, when a retail customer swipes a credit or debit card in a store or enters one online to make a purchase, a third-party payment processor requests authorization for the purchase amount from the credit or debit card company. If the purchase is authorized, the third-party payment processor approves the transaction and subsequently processes batch payment from the credit/debit card's sponsoring financial institution to the merchant's bank account, after deducting fees due to the third-party payment processor, credit card brand, and financial institution, which typically range from 1.5 to 3.5 percent.[16] In doing so, the third-party payment processor remits any sales, meals, or occupancy taxes included in the transaction to the merchant's bank account, not to DOR.

By means of explanation, the DOR wrote that "starting October 1, 2019, there are new Massachusetts sales and use tax collection requirements that apply to out-of-state "remote" sellers and marketplace facilitators ("marketplaces"), such as Amazon, Walmart, Etsy, and eBay. Remote sellers must collect tax on sales of tangible personal property or services into Massachusetts when they have Massachusetts sales that exceed $100,000 in a calendar year. Marketplaces must collect tax on behalf of third parties ("marketplace sellers") selling on the marketplace when the marketplace's total Massachusetts sales (including those facilitated on behalf of marketplace sellers and those made directly by the marketplace on its own behalf) exceed $100,000 in a calendar year."[17]

According to Avalara.com, as of February 3, 2020, more than 30 states [including Massachusetts] have adopted marketplace facilitator laws that shift the burden of tax collection to the marketplace facilitator. Avalara.com writes, "If you sell via an online marketplace such as Amazon, Etsy, or Walmart, you need to understand a new breed of sales tax regulations that focus on marketplace sales—marketplace facilitator laws. Marketplace facilitator laws impose an obligation on the marketplace facilitator to collect and remit sales tax on behalf of marketplace sellers…. These laws are significant because they shift the obligation to collect and remit sales tax from the seller to the platform that facilitates the sale (the marketplace facilitator)."[18]

A brief description of the current settlement process for credit and debit card transactions currently in use by virtually all U.S. merchants is as follows:

1. A customer makes a credit/debit card purchase
2. The vendor accepts credit/debit card as payment
3. The payment processor sends the transaction to a credit brand (Visa, MasterCard)
4. The issuer of the credit card, i.e. a bank, pays the credit card brand
5. The card brand bills the customer
6. The issuer receives payment[19]

Opponents estimate the one-time cost of implementing the governor's proposal would be more than $1.2 billion, including $418 million for retailers, $99 million for telecommunication providers, and $700 million for payment processors. Recurring annual costs, they estimate, would exceed $28 million.[20]

Proponents argue that the cost to retailers would be minimal since no hardware changes would be necessary to alter or replace existing point-of-sale (POS) card-reading devices and that costs to other parties would be far less than opponents claim.

Opponents base their cost estimates primarily on the fact that credit and debit card authorization and transaction processes currently performed by third-party payment processors do not capture information about sales tax or individual items purchased. Implementing a change to do so, and to facilitate a system whereby third-party payment processors would remit sales taxes to DOR, would be complicated, expensive, and burdensome for merchants, third-party processors, and credit/debit card issuers, they argue. Opponents state that currently, when a customer swipes a credit or debit card at a merchant's place of business, third-party payment processors do not receive information from the merchant identifying which items or services are being purchased, whether the purchased items are subject to sales/meals/occupancy taxes in any jurisdiction, or whether sales/meals/occupancy taxes are included in the total sale amount, but instead include only the total transaction amount and data identifying the credit and debit card.

Supporters of the governor's proposal refute opponents' claims that its implementation would be overly complicated, expensive, or burdensome. They argue that merchants already employ point-of-sale systems that instantaneously determine whether items are subject to sales tax, include sales tax in the total transaction amount, and delineate the sales tax amount on the sales receipt. They argue that since merchants already capture real-time electronic records of sales taxes charged in each transaction, as required by DOR regulations, opponents are exaggerating the technical difficulty of electronically transmitting the same information to third-party payment processors. Supporters argue that two recent pilot tests of real-time sales tax collection have demonstrated that the sales tax modernization initiative would not impose additional burdens on merchants, especially small ones. They also argue that major third-party payment processors currently offer products to corporate customers that include sales tax data for each transaction.[21]

They argue that merchants already employ point-of-sale systems that instantaneously determine whether items are subject to sales taxes.

Governor Baker's phase two proposal would authorize the DOR commissioner to promulgate regulations requiring all vendors accepting credit and debit card payments in Massachusetts to separately identify tax and non-tax amounts of charges when requesting payment from third-party payment processors. Under this proposal, the third-party payment processors would no longer remit the sales, meals, or occupancy taxes to the retailer, but instead to Massachusetts DOR.

Arguments in favor of phase one of the governor's proposal

The current statutory timetable for remittance of sales, meals, and occupancy taxes to Massachusetts DOR was established at a time when retailers used manual cash registers and mechanical adding machines, compiled records in paper ledgers, and remitted payment to DOR by mail with paper checks.[22] Advancements in electronic data processing and electronic fund transfers have obviated the need for protracted remittance timetables, especially for high-volume retailers that employ modern automated technology. According to the Council on State Taxation, as of April 2018, 19 states already require advance payment of sales taxes (see Appendix A).[23]

Current Massachusetts law (M.G.L. c. 62C, § 5) requires that businesses with sales/use tax liabilities file returns and make payments electronically.[24] Therefore, the proposed acceleration of the remittance schedule does not create a technological challenge.

However, because those liabilities are not automatically remitted to the DOR, large-volume retailers earn interest on sales tax balances during the period that the retailers retain the sales taxes. Retailers earn interest on retained sales taxes for up to 50 days less the lag time of receiving payment from third-party payment processors on credit and debit card purchases. By implementing a preliminary remittance schedule, the Commonwealth of Massachusetts would get the money sooner, allowing it to earn interest on sales taxes remitted sooner. The Baker administration estimates that phase one will result in a one-time revenue boost of $306 million.[25]

Arguments against phase one of the governor's proposal

The Retailers Association of Massachusetts has been critical of several aspects of the proposal, notably its "vague language" that gives the DOR a lot of discretion in passing regulation on sales tax remittance, which would allegedly result in a significant regulatory burden on "thousands of retailers and restaurants."[26] Massachusetts is also one of 22 states and D.C. that do not compensate vendors for collecting and remitting sales taxes, perhaps contributing to the existing perception that the state is insufficiently business-friendly (see Appendix B).[27]

Large-volume retailers earn interest on sales tax balances during the period that the retailers retain the sales taxes.

Arguments in favor of phase two of the governor's proposal

Perhaps the most appealing attribute of an automated sales tax collection process would be the elimination of unnecessary government expenses. Taxjar.com claims that such a system "dramatically reduces the cost of compliance for the states to claim their revenue" by tightening enforcement of sales tax laws.[28] Estimates of sales tax revenue in Massachusetts that goes uncollected every year range as high as $800 million, and some tax law experts believe a more immediate DOR collection system would help reduce this figure.[29]

Opponents often argue that implementing this system would be prohibitively expensive and risky, especially under the original timeline of the governor's proposal. However, other observers have found the concept to be not only technologically feasible but also necessary to reform an outdated tax collection system.

In one example, over 65% of sales tax revenue originates from debit and credit card purchases that could potentially transmit electronic transaction data very shortly after the purchase is made. Instead, "current sales tax collection methods are not making use" of this impressive technology, according to STAC Media.[30]

Complicating factors such as the rate of the sales tax in a given jurisdiction and whether the product sold is subject to the tax are only minor hurdles. STAC Media also claims that "when a Merchant's POS system is initially setup it is configured to know the Merchant's sales tax nexus and as a result it will recognize to which proper tax table it refer[s] for specific transactions…The capability to calculate the sales tax on individual line items is built into the POS."[31]

Perhaps the strongest evidence of the system's feasibility is its implementation during two test cases, one in New York and one in Massachusetts. Owners of the New York City restaurant that participated in the pilot study stated that they "have not seen any evidence from the 2 years of testing and application that the sales tax modernization initiative would impose additional burdens on merchants—especially small ones. In fact, from our experience it appears that it lessens the burden on the small business owners as it reduces the 2–3 days a month spent trying to determine the proper sales tax payments."[32]

The Massachusetts restaurant's owner echoed many of these sentiments, in particular citing that "no changes were made to the Purchase of Sale system" and "bifurcation [of sales tax amounts] can be accomplished at a payment processer level with ease."[33]

Arguments against phase two of the governor's proposal

Opponents of the governor's 2017 proposal for "real time" sales tax collection include the Associated Industries of Massachusetts, Greater Boston Chamber of Commerce, Massachusetts Taxpayers Foundation, National Federation of Independent Business, Retailers Association of Massachusetts, Massachusetts Bankers Association, Massachusetts Food Association, BJ's Wholesale Corporation, Mastercard, American Express, Bank of America, Capital One, Electronic Transactions Association, National Conference of State Legislators Association Special Task Force, First Data, Staples, Verizon, and others (see Appendix C).[34]

Crucially, a core element of this opposition is a denial of the technological feasibility of implementing the automated sales tax collection system. First Data Corporation, the largest payment processor in the payments industry, claims that industry actors cannot "know what types of items were purchased, whether they were taxable or non-taxable, whether cash-back was received, whether a sales tax holiday is occurring, etc." under the current system.[35] Other agencies, including the Massachusetts Bankers Association and the Card Coalition, argue that the current system's "routing only [of] the necessary information required to authorize a transaction" would render the supposed efficiency of an automated system irrelevant.[36]

A core element of this opposition is a denial of the technological feasibility of implementing the automated sales tax collection system.

While the technological feasibility of an automated system deserves more scrutiny, a more uniform complaint among industry representatives is the anticipated regulatory burden of the system on retailers and, ultimately, the public. The Greater Boston Chamber of Commerce noted that "even if the technology is available, installing new technology infrastructure at virtually every brick-and-mortar retailer in the state will have costs for both businesses and consumers."[37] The National Conference of State Legislatures' Task Force goes further, anticipating additional efforts required of state administrators under the new system, contrary to the claims of its supporters.[38]

A 2017 State Tax Research Institute report found that the additional costs to businesses of an automated sales tax collection system would total billions of dollars, even while the Massachusetts Taxpayers Foundation expressed alarm that the governor's proposal contained insufficient detail to allow businesses to adapt to and anticipate the magnitude of the potential changes.[39]

In stakeholder responses to the governor's proposal, this alarm was often expressed in the context of the unprecedented nature of the phase two requirements. In one way or another, several observers, including the Massachusetts Taxpayers Foundation, Associated Industries of Massachusetts, and BJ's Wholesale Club, anticipated the prohibitive costs involved in "developing unique technology for a Massachusetts-only change in the sales tax remittance procedure" that "does not exist anywhere else in the United States and therefore would need to be created from scratch."[40]

BJ's Wholesale Club even made a brief, alternative proposal in which the state would "require each taxpayer to remit an advance payment for the following month with each month's return, based on the prior year's sales."[41] It then went on to point out the precedent for such legislation in several other states, including Pennsylvania, Florida, North Carolina, and Ohio, and to cite the supposed benefits of leaving the sales tax collection procedure "100% within the control of the taxpayer."[42]

Moreover, the organization Americans for Tax Reform disputes the alleged fiscal benefits of an automated sales tax collection system, citing "the fact that it generates no new revenue for state government" as "explaining why no state has seen fit to institute this mandate."[43] A complete lack of impact on state coffers seems unlikely given a Boston University researcher's argument that an automated system would reduce gaps in sales tax enforcement in Massachusetts.[44] Still, it's worth noting that private corporations and industry-affiliated nonprofits are not the only actors inclined to oppose the governor's proposal.

A law enacted in July 2019 by the State of New Hampshire, Chapter 280 of the Acts of 2019, would require "foreign taxing jurisdictions (aka, other states) to provide written notice to the New Hampshire Department of Justice at least 45 days prior to conducting examinations of sellers in New Hampshire, imposing sales and use tax." Further, "should the [N.H.] Department of Justice conclude that a foreign taxing authority is creating an undue burden on interstate commerce, or is violating any provision of the U.S. or New Hampshire constitutions or any other federal or state law, it may bring civil action in the name of the state against such person or state."[45] New Hampshire's legislative action can be understood as an attempt to thwart the enforceability of the Commonwealth's accelerated sales tax proposal, and thereby mediate the economic impact the Commonwealth has on merchants in the Granite State, in which there is no sales tax.

Conclusions

Phase one of Governor Baker's proposal, for advance payment, makes sense and is entirely feasible. According to the Council on State Taxation, as of April 2018, 19 states already require advance payment of sales taxes, while Massachusetts does not. Advancements in electronic data processing and electronic fund transfers have obviated the need for protracted remittance timetables, especially for high-volume retailers that would be impacted by the advance payment regulations since virtually all of them employ modern automated technology. Currently, Massachusetts law under (M.G.L. c. 62C, § 5) requires that businesses with sales/use tax liabilities file returns and make payments electronically. Therefore, the proposed acceleration of the remittance schedule does not create a technological challenge.

New Hampshire's legislative action can be understood as an attempt to thwart the enforceability of the Commonwealth's accelerated sales tax proposal.

Phase two of Governor Baker's proposal (real-time sales tax collection) makes sense and is entirely feasible for a subset of transactions—i.e., those involving marketplace facilitators such as Amazon, Walmart, Etsy, eBay, and other high-volume internet sellers as designated by the commissioner of DOR.

As currently drafted, the governor's phase two proposal would, effective July 1, 2023, require all vendors accepting credit and debit card payments in Massachusetts to be subject to real-time sales tax collection.[46]

In light of the many arguments offered by opponents of real-time sales tax collection, particularly those pertaining to potential undue hardship and expense that would be placed on small and medium-sized local retailers, the Institute suggests that the legislature initially undertake a scaled-down approach by implementing the governor's phase two proposal solely regarding highly sophisticated large-scale sellers—i.e., those with annual sales of $10 million or more.

Advocates of the governor's plan argue that opponents' claims are greatly exaggerated about the technical difficulty and expense of implementing real-time sales tax collection. Advocates have presented results of two pilot tests of the governor's proposal that they say demonstrate that opponents' claims are unfounded. One way to find out whether the governor's proposal would work without placing a potential hardship on local small and medium-sized sellers is to implement it only on high-volume internet sellers and market facilitators.

This would allow state officials and all parties of interest to gain experience and address unforeseen problems in effectuating this requirement. By implementing this in a scaled-down manner, the Commonwealth would be able to ascertain how much it improves Massachusetts' collection of sales taxes from remote sellers. If this new sales tax collection requirement is successfully implemented, the Commonwealth would be better able to determine whether it makes sense to expand its application.

These large-scale retailers and market facilitators have the technical capacity to identify tax and non-tax amounts of charges when requesting payment from third-party payment processors. Under this scaled-down approach, third-party payment processors serving high-volume internet marketplace facilitators and other large-volume retailers would remit sales tax daily to Massachusetts DOR, but local retailers would not be subject to the same requirement.

On October 1, 2019, Massachusetts joined 30 other states in requiring marketplace facilitators to collect sales taxes from remote sales they facilitate. By virtue of this new requirement, out-of-state sellers utilizing marketplace facilitators are required, effective October 1, 2019, to collect sales taxes. By implementing the governor's phase two proposal on these market facilitators, DOR would have an additional enforcement tool.

Another advantage of the governor's phase two proposal is that it would facilitate efficient collection of sales taxes from out-of-state sellers, particularly from New Hampshire retailers that use marketplace facilitators. The state of New Hampshire has recently adopted legislation aimed at preventing Massachusetts from enforcing its newly adopted sales/use tax requirements on out-of-state sellers.

Appendix A: List of state policies requiring advance payments of sales taxes[47]

Name of State	Regulatory Requirements	Citation
Arizona	Sellers owing over $1M per year must make an advance payment each June.	ARS § 42- 5014(D)
Arkansas	Sellers with $200,000 in sales per month must make bimonthly advance payments (amounting to 80 percent of tax due).	ACA § 26-52-512; AC r.77(D)
California	Sellers with a monthly estimated tax of >$17K must make advance payments.	CRTC § 6452
Florida	Sellers must make advance payments. Payment is due with the return for the prior month.	FS § 212.11.
Georgia	Sellers owing $60,000 or more in the prior year, excluding local sales taxes, must make advance payments of 50% each month by the 20th day of period.	GCA § 48-8-49(b)(2)
Illinois	Sellers owing > $20,000 per month must make advance payments four times per month.	35 ILCS § 120/3.
Iowa	Advance payments must be made depending on filing frequency (more than $60k per year requires 2 monthly payments).	IC § 423.31
Kansas	Sellers > $40K per year must make advance payments based on the first 15 days of each month w/prior month's return due date.	KSA § 79- 3607(a)
Michigan	Sellers must make multiple advance payments.	MCL § 205.56(2)(b).
Minnesota	Sellers owing $250,000 or more during the previous year must make advance payments.	MS § 289A.20, subd. 4(b).
Mississippi	Sellers averaging > $50,000 monthly must make one advance payment each June that equals 75% of the current June's liability or 75% of the prior June's liability.	MCA § 27-65-33.
Missouri	Sellers owing $10,000 or more every 6 months must make 4 advance payments per month.	RSMo § 144.081; 12 CSR 10-104.030(3).
New Jersey	Sellers owing $30,000 or more in the prior year must make monthly advance payments	NJAC 18:24-11.2(a)-(c); NJRS § 54:32B-17(b).
New York	Sellers owing more than $500,000 per year must make advance payments.	NYTL § 10(b)-(c).
North Carolina	Sellers owing $20,000 or more per month must make advance payments w/prior month's return.	NCGS § 105-164.4(16)(b2).
Ohio	Sellers > $75K per year must make monthly advance payments w/ prior month's return.	ORC § 5739.122.
Oklahoma	Sellers owing $30,000 or more per year must make advance payments.	68 OS § 1365(D).
Pennsylvania	Sellers remitting $25,000 or more for the third quarter of preceding year must make advance payments.	72 PS §§ 7217(a), 7246, 7247.
Virginia	Sellers with $2.5M or more in yearly sales must make a June advance payment.	VC § 58.1-615

Appendix B: List of states that compensate vendors for collecting and remitting sales taxes[48]

Name of State	Share and Conditions of Vendor Compensation	Citation
Alabama	5% of the first $100 tax due, and 2% of remaining tax due (capped at $400 per month).	AC § 40-23-36; AAC r.810-6-4-.03
Arizona	1% of tax due (capped at $10,000 per calendar year).	ARS § 42-5017.
Arkansas	2% of tax due (capped at $1,000 per month). Separate caps for local collections.	ACA § 26- 52-503.
Colorado	3.33% of tax due.	CRS § 39-26-105(1)(C) (II)(A).
Florida	2.5% of tax due for sellers who report via electronic means only (capped at $1,200 per reporting period).	FS § 212.12(1)(a).
Georgia	3% of tax due on the first $3,000 of total sales and use taxes reported, and 0.5% of portion exceeding $3,000.	GCA § 48-8-50(b).
Illinois	1.75% per calendar year.	35 ILCS §§ 105/9, 110/9, 115/9, 120/3.
Indiana	0.73% for sellers < $60,000 in tax liability in prior year, 0.53% for sellers with tax liability between $60,000 to $600,000, and 0.26% for sellers > $600,000.	IC § 6-2.5-6-10(b).
Kentucky	1.75% < $1,000, then 1.5% of the remainder on each return ($50 cap per reporting period).	KRS § 139.570.
Louisiana	0.935% of the tax due (capped at $1,500 per month).	LSA § 47:306(A)(3)(a).
Maryland	1.2% on the first $6,000 and 0.9% on the remainder (capped at $500 per period).	MCA, Tax-Gen. § 11-105.
Michigan	0.5% of the tax due monthly at a rate of 4% (capped at $20,000 per month).	MCL § 205.54(1)(a).
Mississippi	2% of tax due (capped at $50 per month and $600 per calendar year).	MCA § 27-65- 33(1).
Missouri	2% of tax due.	RSMo § 144.140.
Nebraska	2.5% of tax due (capped at $3,000 per month).	NRS § 77-2703(2) (d).
Nevada	0.25% of tax due.	NRS §§ 372.370(1), 372.355.
New York	5% of taxes due (capped at $200 per reporting period). Sellers filing monthly returns or subject to PrompTax are not eligible for the credit.	NYTL § 1137(f); TB-ST-925 (11/10).
North Dakota	1.5% of tax due (capped at $110 per return).	NDCC § 57-39.2- 12.1(1)
Ohio	0.75% of tax due per return.	ORC § 5739.12(B)(1).
Pennsylvania	1% of tax due (capped at $25 for monthly filers, $75 for quarterly filers, and $150 per semi annual filers).	72 PS § 7227.
South Carolina	2%-3% (capped of $3k or $10k per year).	SCC § 12-36-2610.
South Dakota	1.5% of tax due (capped at $70 per return).	SDCL 10-45-27.2.
Tennessee	No vendor comp. except a limited comp. for out-of-state sellers.	TCA § 67-6- 509.
Texas	0.5% of tax due on a timely return. Additional 1.25% on prepayment amount.	TTC § 151.423. TTC § 151.424.
Utah	1.31% of tax due per month.	UC § 59-12- 108(2)(c).
Virginia	Very limited vendor comp. which does not apply to sellers w/> $240,000 in yearly liability	23VAC10-210-485
Wisconsin	0.5% of liability (capped at $1,000 per reporting period).	WS § 77.61(4)(c).
Wyoming	1.95% of the first $6,250 and 1% of the remainder (capped at $500 per month).	WS § 39-15- 107(b)(xi).

Appendix C: Selected quotes on automated sales tax collection from notable industry observers

Americans for Tax Reform

"The significant costs that a Real Time sales tax collection mandate would impose on businesses, coupled with the fact that it generates no new revenue for state government, are key factors explaining why no state has seen fit to institute this mandate."[49]

Associated Industries of Massachusetts

"AIM has received feedback from several members whose initial estimated cost of compliance, by June 1, would require tens of millions of dollars of investments. These estimates do not consider the annualized operational and compliance costs… Based on high level estimates compliance would include the following: Hardware/Software Modifications, Accounting Support, Sales Tax Support and Increased costs for third-party processors…. This system would require financial institutions to purchase and implement expensive software programs in order to (1) interface with vendors to obtain daily reports on Massachusetts tax charges; (2) to interface with the Department of Revenue to remit tax on a daily basis; (3) to create new sales tax remittance reports to track sales tax remitted each day; (4) implement new daily sales tax remittance procedures to ensure that tax is remitted each day (something that does not exist anywhere else in the United States and therefore would need to be created from scratch); (5) implement new systems to generate monthly tax remittance reports and returns to submit to Massachusetts; and (6) implement new systems and procedures to generate monthly tax remittance reports to provide to each customer—potentially encompassing tens of thousands of businesses each month for large processors. (7) There will be increased costs for the third-party processors to support sales tax audits which would require skilled expertise that the processor may not have on staff."[50]

BJ's Wholesale Club

In its submission in opposition to the governor's 2017 proposal for daily tax remittance by third-party payment processors, BJ's Wholesale Club strongly recommended as an alternative that Massachusetts retailers remit an advance payment of sales taxes for the following month with each month's return. BJ's wrote: "One such alternative, which we would strongly recommend, would be to simply require each taxpayer to remit an advance payment for the following month with each month's return, based on the prior year's sales. This requirement, or one similar, is a fairly common practice already in several states in which we do business, including Pennsylvania, Florida, North Carolina, and Ohio. This advance payment method is easy to compute, reconcile and track, requires no incremental costs other than the lost time value of money, and most importantly, is 100% within the control of the taxpayer, as opposed to an unrelated, third party payment processor."[51]

Boston Herald

"In 2017, lawmakers agreed to go along with Baker's suggestion to accelerate sales taxes—if the Department of Revenue determined a new system could be feasibly adopted by June 2018. The agency subsequently found financial benefits and described it as an achievable goal with current technology. But the scale and complexity made it tough to promise by the deadline without big costs and risks."[52]

"Boston University professor Richard Ainsworth, a comparative tax law specialist, claims the state could collect nearly all of the estimated $600 million to $800 million sales tax revenue that's lost every year by mandating businesses use software that tracks each transaction and immediately send the data to the Department of Revenue."[53]

Card Coalition

A national trade association representing the payment card industry claimed that "simply put, real-time sales tax collection does not work. Companies that would be subject to such a requirement have not been required to do this in any other state and their business operations are not configured to do so. In the U.S., there are an estimated ten million merchant locations, more than a dozen payment card networks, hundreds of payment processors, and over 8,000 card-issuing financial institutions. The infrastructure that facilitates electronic payment transactions transmits data between retailers, payment networks, and card issuers, transmitting thousands of transactions per second every hour of every day. Payment processors and payment networks send and receive these authorization messages as single units of code, routing only the necessary information required to authorize a transaction. Because neither payment processors nor payment networks see details around the goods purchased, they have no ability to identify the appropriate sales tax that should be applied to the transaction."[54]

CPApracticeadvisor.com

A New Hampshire law enacted in July 2019 (Chapter 280 of the Acts of 2019) would "[make] other states jump through hoops" on collecting out-of-state sales taxes, according to CPApracticeadvisor.com.[55] Entitled "An Act providing for protection of private customer information and rights of New Hampshire remote sellers in connection with certain foreign sales and use taxes," the new law requires "foreign taxing jurisdictions" (aka, other states) to provide written notice to the New Hampshire Department of Justice at least 45 days prior to conducting examinations of sellers in New Hampshire, imposing sales and use tax." Further, "should the [N.H.] Department of Justice conclude that a foreign taxing authority is creating an undue burden on interstate commerce, or is violating any provision of the U.S. or New Hampshire constitutions or any other federal or state law, it may bring civil action in the name of the state against such person or state, and all that that entails… The action may be brought in any court of competent jurisdiction. The bill also authorizes New Hampshire remote sellers to file an action in any court of competent jurisdiction in the event they're 'subject to collection, audit, or examination by a foreign taxing authority in connection with alleged sales tax collection or remission obligations.'"[56]

Cronin Group

A Massachusetts restaurant owned by Cronin Group participated in a pilot of actual real-time sales tax remittance in 2016. In the pilot, sales taxes were remitted to a secondary account using a merchant account on a First Data third-party processor platform. The owner said that "no changes were made to the Purchase of Sale system" and "bifurcation [of sales tax amounts] can be accomplished at a payment processer level with ease."[57]

First Data Corporation

First Data Corporation, the largest payment processor in the payments industry, submitted input to DOR in 2017 explaining their opposition.[58] It wrote, "When merchandise is scanned at checkout, the retailer's cash register captures individual purchase items and the sales tax amount, but that data is not transmitted to the payment processor during the initial card authorization, nor during the later settlement of the transaction when money is taken from the consumer's card account at the bank and deposited into the merchant's bank account. Only the total transaction amount is provided from the cash register to the point of sale terminal (where the debit or credit card access device is swiped, dipped, or tapped). In other words, for debit or credit card transactions, the payment processor does not know what types of items were purchased, whether they were taxable or non-taxable, whether cash-back was received, whether a sales tax holiday is occurring, etc…. [F]or a payment processor to comply with the sales tax outlined in [the governor's proposal], additional data fields would need to be added to the transaction data stream that would allow the retailer to key in or electronically capture the sales tax amount separately from the total transaction amount."[59]

Greater Boston Chamber of Commerce

"Third-party payment processors would have to significantly transform the present infrastructure in order to make electronic payment transactions. Even if the technology is available, installing new technology infrastructure at virtually every brick-and-mortar retailer in the state will have costs for both businesses and consumers. And compliance challenges not only affect physical infrastructure: making an almost immediate transfer of sales tax payments could affect crucial cash flows that allow businesses to pay vendors and employees. The effects on cash flow could be particularly significant for smaller businesses. Mandating same day sales tax remittance would also add to an increasing number of items that place Massachusetts's businesses at a competitive disadvantage compared to their counterparts nationwide. Massachusetts would be the only state to require an accelerated sales tax remittance infrastructure, making the costs of compliance—both financial and administrative—isolated to businesses located here."[60]

Massachusetts Bankers Association

"Under the current system, banks, payment processors and payment networks send and receive these authorization messages as single units of code, routing only the necessary information required to authorize a transaction. Because these messages do not include all of the details about the goods purchased, banks and others in the payments system do not have the ability to identify the appropriate sales tax that should be applied to the transaction."[61]

Massachusetts Taxpayers Foundation

"The accelerated sales tax remittance . . . would require fundamental changes to the operations of thousands of businesses involved in debit and credit card processing because these transactions are enabled by interconnected global technology platforms. [R]etailers will face significant cost in purchasing or developing new point-of-sales technology to properly account for which items are subject to tax and which are tax exempt so that third party processors can distinguish between the two in order to remit the proper amount of tax on each transaction. Retailers would bear these costs, and the necessary staff training, after having transitioned to "chip reading" technology very recently. Banking and card-processing companies will incur significant costs related to developing unique technology for a Massachusetts-only change in the sales tax remittance procedure. This will involve renegotiating thousands of contracts with retailers and other vendors to reflect the new responsibilities for remitting sales tax. Insurance policies will also have to be revised to cover this new liability. These amended agreements will need to address a host of issues, most notably liability for unpaid tax obligations and how to reconcile returns, exchanges, gift cards and other ancillary issues stemming from these transactions. At present, it's not possible to quantify the full cost of making these changes because the proposal lacks sufficient details. However, it is clear that the contemplated change fails to meet any standard of cost effectiveness for impacted businesses."[62]

Morso Restaurant

Owners of the New York City restaurant that participated in the pilot study stated: "We have not seen any evidence from the 2 years of testing and application that the sales tax modernization initiative would impose additional burdens on merchants—especially small ones. In fact, from our experience it appears that it lessens the burden on the small business owners as it reduces the 2–3 days a month spent trying to determine the proper sales tax payments."[63]

National Conference of State Legislatures

The National Conference of State Legislatures' Task Force on "real-time" remittance stated in a letter to legislators: "Based on that panel and previous staff level meetings it became clear to Task Force members and staff that while the goal of expedited sales tax remittance is admirable, the proprietary patented process being promoted as "real time" sales tax collection raises significant challenges, creates additional burdens for both retailers and state administrators, imposes new burdens on business not currently involved in the sales tax collection process, and thus is not a process that this Task Force could recommend to the states."[64]

National Federation of Independent Business

"Our biggest concern with real-time sales tax collections is who will cover the cost of an entirely new system. Banks? Small shops and restaurants? One thing is clear; the expense eventually will be passed along to consumers."[65]

Retailers Association of Massachusetts

"The vague language would have allowed the Department of Revenue (DOR) to, by regulation, mandate a "preliminary remittance of sales tax" be made to the Commonwealth by thousands of retailers and restaurants. RAM strongly opposed those provisions to make changes in the current sales tax remittance process, and expressed our extreme concern to both the House and Senate. RAM lobbying on this issue paid off in that the proposal was not included in either the House or the Senate budget."[66]

"Currently, retailers collect and remit all sales tax to the state, and they are responsible for the accuracy, reconciliation and auditing of their payments and accounts. That process would continue under this proposal for all purchases made not using a third party credit or debit card, such as purchases made using cash, gift cards, checks, store brand cards, and split tender transactions. However, a second payment system would need to be built to accommodate the state's "real-time" collection and remittance process for transactions involving third party credit and debit cards. Retailers, credit card companies, processors and the DOR would incur hundreds of millions of dollars in new expenses to build out and maintain a new system—costs that would be passed onto consumers and taxpayers—in a process that, if even possible at all, would take years to implement." – Retailers Association of Massachusetts[67]

STAC Media

"Since more than 65% of sales tax revenue is collected through purchases made by debit or credit cards the tax portion of the transaction is readily accountable and collectable. However current sales tax collection methods are not making use of cutting edge technology resulting in ineffective collection processes and inordinately long collection times."[68]

"The capability to capture the exact tax amount of each transaction has existed since the advent of Commercial, Corporate and Purchasing cards from all of the different Card Brands for over 15 years…. Credit card companies do not need to know the taxing jurisdiction because when a Merchant's POS [point of service] system is initially setup it is configured to know the Merchant's sales tax nexus and as a result it will recognize to which proper tax table it refer[s] for specific transactions. Companies like Avalara and Vertex provide these tax tables to POS developers…. Issuers and Merchant Banks would not be involved. Only the institution providing the settlement services (typically the processor) would be the one to handle the remittance. . . .The system would be able to recognize sales of items that are exempt from tax, or sales of intangible items such as gift cards, or tips at restaurants, etc. The capability to calculate the sales tax on individual line items is built into the POS. Companies like Vertex and Avalara provide these tax tables to POS companies as a service."[69]

"The technological feasibility of the Sales Tax Modernization Initiative has been demonstrated through two pilots, one that lasted for two years at a small business in New York City [Morso Restaurant], and one that was performed at a restaurant during the 4th quarter of 2016 in Massachusetts for a week. In each case, while the business was in operation, amounts were identified for sales tax obligations and were successfully remitted daily to secondary accounts that were established as proxies for State receiving accounts."[70]

State Tax Research Institute

"To comply with this change, retailers, banks and payment processors would need to spend billions to upgrade software and hardware."[71]

Taxjar.com

"By placing the onus of sales tax on the facilitator (rather than the seller), these laws enable the states to force compliance across the entire state, and it dramatically reduces the cost of compliance for the states to claim their revenue. A marketplace facilitator is a business or organization that contracts with third parties to sell goods and services on its platform and facilitates retail sales. Marketplace facilitators enable these sales by listing the products, taking the payments, collecting receipts, and in some cases assisting in shipment. When we refer to marketplace facilitator laws, we're talking about legislation surrounding the sales tax responsibilities of these facilitators."[72]

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About Pioneer

Pioneer Institute is an independent, non-partisan, privately funded research organization that seeks to improve the quality of life in Massachusetts through civic discourse and intellectually rigorous, data-driven public policy solutions based on free market principles, individual liberty and responsibility, and the ideal of effective, limited and accountable government.

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