STREAMLINED SALES TAX MITIGATION

SCOPE AND OBJECTIVES

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STATE OF WASHINGTON
JOINT LEGISLATIVE AUDIT AND REVIEW COMMITTEE

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Why a JLARC Study of Streamlined Sales Tax Mitigation?

In 2007, the Legislature enacted legislation (SSB 5089) to conform to the multi-state Streamlined Sales and Use Tax Agreement. The Streamline Agreement is intended to harmonize state tax codes and facilitate collecting sales tax on interstate transactions. The legislation took effect July 1, 2008.

As part of the 2007 legislation, the Legislature included provisions to mitigate negative impacts to revenue collections for local taxing jurisdictions. The Legislature also directed the Joint Legislative Audit and Review Committee (JLARC) to review these mitigation provisions in 2010. The purpose of the study is to determine to what extent the provisions compensate jurisdictions that experienced a loss in local sales tax revenue.

Mitigating Losses of Local Sales Tax Revenue

Sourcing Change Caused Sales Tax Revenue Losses for Some Local Jurisdictions

Sales tax ***sourcing*** rules determine the taxable location of a sale and which jurisdiction is entitled to local sales tax. Prior to becoming a full member of the Streamline Agreement, Washington retailers sourced sales tax based on a delivery's point of ***origin***. For example, a couch delivered from a warehouse in Kent to a home in Seattle would be sourced to Kent, and Kent would receive the local sales tax from that purchase.

Full members of the Streamline Agreement are required to use a delivery's ***destination*** as the sales tax source. Therefore, in July 2008, Washington changed its sourcing statutes to conform to the Streamline Agreement. Thus Seattle now receives local sales tax for the delivery of a purchase sent to Seattle from Kent. This sourcing change shifted the distribution of sales tax around the state. As a result, some local jurisdictions experienced a loss in local sales tax revenue.

DOR Estimated the Losses of Local Taxing Jurisdictions

The Legislature directed the Department of Revenue (DOR), in consultation with an advisory committee, to determine the impact of the sourcing change to local jurisdictions. For the first year, DOR estimated the gains or losses for each jurisdiction by comparing tax returns with the previous year. For subsequent years, DOR uses one-fourth of the loss estimated in the initial year as the ***quarterly loss*** for each local jurisdiction.

Local Losses Are Offset by Interstate Revenue Gains

Some out-of-state retailers have voluntarily registered with the Streamline Agreement. These registered retailers collect and remit sales tax for purchases delivered to Washington. DOR monitors this new source of sales tax revenue, which is known as ***voluntary compliance revenue***. Each quarter, DOR subtracts the local portion of voluntary compliance revenue from estimated quarterly losses in order to determine the ***net loss*** for each local jurisdiction.

Local Jurisdictions Receive State Mitigation Payments

Local jurisdictions receive mitigation payments each quarter for the net loss due to the sourcing change. Mitigation continues until DOR determines that a local jurisdiction no longer experiences a net loss. To date, the state has made seven quarterly payments to 153 local jurisdictions, totaling over $47 million.

Study Scope

As directed by statute, JLARC will review to what extent the Streamline Agreement mitigation provisions compensate the local taxing jurisdictions impacted by the change in sourcing. JLARC staff will solicit input from DOR's mitigation advisory committee, which includes representatives from impacted local jurisdictions, the Office of Financial Management, and fiscal committee staff.

Study Objectives

The study will analyze the effect of the mitigation provisions by addressing four key questions:

1) Does the Department of Revenue determine local losses consistent with statutory provisions?
2) Do the distributions made to local jurisdictions equal the net loss as determined by the Department of Revenue?
3) To what extent do the distributions compensate local jurisdictions for the impact of the sourcing change?
4) How have other Streamline Agreement member states addressed impacts to local jurisdictions due to sourcing changes?

Timeframe for the Study

Staff will present the preliminary report at the December 2010 JLARC meeting and the final report at the January 2011 meeting.

JLARC Staff Contact for the Study

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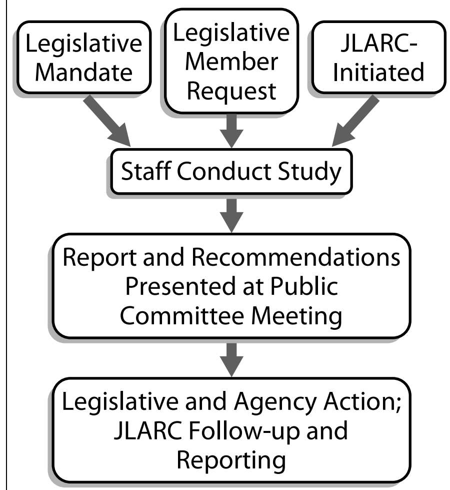
JLARC Study Process



Criteria for Establishing JLARC Work Program Priorities

- Is study consistent with JLARC mission? Is it mandated?
- Is this an area of significant fiscal or program impact, a major policy issue facing the state, or otherwise of compelling public interest?
- Will there likely be substantive findings and recommendations?
- Is this the best use of JLARC resources? For example:
  - Is JLARC the most appropriate agency to perform the work?
  - Would the study be nonduplicating?
  - Would this study be cost-effective compared to other projects (e.g., larger, more substantive studies take longer and cost more, but might also yield more useful results)?
- Is funding available to carry out the project?