

These resolutions are to be voted on in 2008 for a period to end in 2011

Resolution One Consider State and Local Tax Systems When Making Federal Policy Changes

Under the U.S. Constitution both federal and state governments have the right to establish their own, separate systems of taxation. Income tax systems in 41 states, the District of Columbia and New York City have been developed in coordination with the federal income tax system, and fundamental aspects of the state and local income taxes, including the definition of income, allowable deductions, third-party reporting, and compliance, are heavily dependent on the federal income tax.

This system of income tax conformity has effectively created a tax base and tax system that is in many ways integrated and is effectively shared between the federal government and other income tax jurisdictions. This both eases the burden of compliance on taxpayers and simplifies administration for all parties.

Additionally, 45 states, the District of Columbia and New York City balance their tax portfolio by imposing a consumption tax, which has no direct federal counterpart. For most, this is a retail sales tax or a gross receipts tax. These taxes have different rates and bases.

A number of factors, including the fiscal condition of the federal government, the broadening reach of the alternative minimum tax and the expiration of earlier tax reductions, will occasion a substantial policy debate in the U.S. about fundamental reform of the federal tax system. Alternatives often mentioned include elimination or substantial revision of the corporate income tax, adoption of a value added or other national consumption tax, and substantial simplification and “flattening” of the personal income tax. The nature of the current income tax system means that changes to federal tax laws will often have a substantial fiscal and administrative impact at the state and local level. The alternative federal systems that are commonly mentioned each have substantial impacts of states and other taxing jurisdictions ranging from effective elimination of business income taxes to a substantial involvement in consumption taxation – an area heretofore largely left to state and local governments.

The interaction of federal and sub-national tax systems and the impacts on states and localities is evident in some of the recent federal policy changes, including the phase-out of the federal estate tax, broadening of allowable deductions for retirement contributions and broadening the depreciation allowance for businesses.

Failure to take into account the fiscal, administrative and policy implications for states and localities of such changes leads to nonconformity and considerable new complexities and recordkeeping burdens for taxpayers and tax professionals. Such failure also affects the state and local tax infrastructure, compliance programs and levels of service to taxpayers. Such failure can also lead to the effective preemption of state and local tax bases and lost opportunities to

leverage improvements in the overall tax system by considering sub-national and federal structures as an interrelated system. There are often alternative ways to achieve changes to federal policy that minimize or eliminate any need for states and localities to make adjustments to their own tax systems and thus keep the federal, state and local systems in harmony.

Policy

The Federation of Tax Administrators (FTA) supports Congressional efforts to formally and carefully consider the positive and negative impact of potential federal tax measures on state and local income tax systems, including generation of revenue estimates. Congress is encouraged to identify federal tax actions that can lead to nonconformity and to estimate the impact of those actions. States, local governments with income taxes and taxpayers should work in concert to educate Congress on the effects of federal changes that force states and localities to reduce conformity and to jointly seek the creation of procedures that will reduce or eliminate the need for such state and local action.

Finally, because states and localities have extensive experience in the administration of consumption taxes, FTA asks Congress to take advantage of their expertise when considering any new federal consumption tax.

This resolution shall automatically terminate three years after the Annual Business Meeting at which it is adopted, unless reaffirmed in the normal policy process.

Resolution Two Business Activity Tax Nexus Legislation

Background

Business activity taxes are levied by states and some localities for the privilege of doing business in or earning income within the taxing jurisdiction. These include corporate income taxes, gross receipts taxes, business license taxes, franchise taxes, business and occupation taxes, and insurance premiums taxes.

Decisions by the U.S. Supreme Court allow a taxing jurisdiction to tax business activities within the jurisdiction if there is a substantial nexus between a commercial entity and the taxing jurisdiction. A number of state courts have held that the taxed entity need not have a physical presence in the taxing jurisdiction in order to be subject to a business activity tax, and the Supreme Court has specifically stated that it has not applied a physical presence requirement to the imposition of business activity taxes.

In the 110th Congress, The Business Activity Simplification Act (S. 1726 and H.R. 5267) (BATSA) were introduced by Senators Charles Schumer (D-N.Y.) and Mike Crapo (R-Idaho) and Reps. Rick Boucher (D-VA.) and Bob Goodlatte (R-VA.). The bills require that a business have certain types of physical presence in a taxing jurisdiction before being subject to a business activity tax. The bills substantially expand P.L. 86-272 by: (a) expanding the range of activities defined as protected “solicitation” under the Act; (b) broadening the reach of the Act to include not only sales of tangible personal property, but to include sales of all forms of property, including intangible and digital property; and (c) extends the types of taxes covered by the Act to all forms of business activity tax and not just corporation net income taxes. The bills substantially narrow a jurisdiction’s authority to tax entities operating in the jurisdiction, reverses years of judicial precedent, and create tax-planning opportunities, especially for large businesses, to eliminate taxation of revenues earned within a state or locality.

FTA member agencies and other state and local officials have consistently resisted enactment of legislation such as H.R. 5267 and S. 1726 for several reasons:

- It represents a substantial reversal of current law.
- It would allow many companies to engage in tax planning and structuring in order to avoid substantial amounts of tax in their domicile state and the jurisdiction in which they do business by changing their business form, but not the nature of the income-producing activities. In particular, larger companies would be able to transfer intangible assets to holding companies incorporated in no-tax or low-tax jurisdictions and to isolate their physical assets and confine their activities in certain jurisdictions to those protected by the expanded P.L. 86-272 in a fashion that substantially minimizes their tax burden.
- The legislation would impose the largest unfunded tax preemption mandate ever estimated by the U.S. Congressional Budget Office, a revenue loss of \$3 billion per year within three years.
- The legislation favors out-of-state businesses over in-state businesses. It would allow a large corporation that can conduct business online to go into a jurisdiction electronically

and exploit the market i without being subject to the taxes that in-state businesses are required to pay.

- The expansion of P.L. 86-272 is unwarranted and runs counter to the direction that business operations are taking.

Policy

The Federation of Tax Administrators strongly opposes any legislation that would restrict a state's constitutional authority to tax entities doing business in a state. The Federation opposes any legislation that would establish a physical presence nexus requirement for the imposition of state and local business activity taxes.

This resolution shall automatically terminate three years after the Annual Business Meeting at which it is adopted, unless reaffirmed in the normal policy process.

Resolution Three

Strengthening the Jenkins Act and Contraband Cigarettes Trafficking Act

Background

State and local tobacco tax enforcement is hindered by the illicit transportation of cigarettes between states and nations to avoid the proper payment of taxes.

The Jenkins Act, at 15 U.S.C. §§375-378, is a federal statute that requires anyone selling cigarettes in interstate commerce to report those sales to the tobacco tax administrator for the jurisdiction into which the sales are made. The Contraband Cigarette Trafficking Act, at 18 U.S.C. §2341-2346, makes it a federal crime to distribute or purchase "contraband cigarettes," a stated quantity of cigarettes that bear no evidence of payment of applicable cigarette taxes.

FTA members have long sought to strengthen the provisions of the Jenkins Act and the Contraband Act to better assist enforcement of state and local tobacco taxes by, for example, expanding the scope of those statutes to include tobacco products other than cigarettes and lowering the threshold of the CCTA. Bills have been introduced periodically in Congress that would effectuate some of the changes to the Jenkins Act and the Contraband Act sought by the states, including, for example, S. 1177, entitled the "Prevent All Cigarette Trafficking Act" or "PACT Act," which was introduced in the 108th Congress and would have: given states the authority to require the collection of tax on any "delivery sale," defined as any interstate sale in which the order is submitted by telephone, mail or the Internet, or the cigarettes are delivered by mail or other delivery service; allowed state attorneys general to sue to enforce the act; lowered the threshold for what constitutes contraband under the CCTA from 60,000 cigarettes to 10,000; and prohibited the sale of cigarettes into a state that had signed the Master Settlement Agreement that were not in compliance with the MSA.

The extension of the Patriot Act signed into law on March 9, 2006 contained a section amending the CCTA in several ways that should prove helpful to state and local tobacco tax administration, including: reducing the quantity of cigarettes necessary to be considered contraband from 60,000 to 10,000; adding smokeless tobacco, at a quantity of over 500 consumer-sized cans, to what can be considered contraband; allowing state and local governments to sue to enjoin a violation of the Act; and changing the penalties for violations, and

State and local tobacco tax enforcement could be further benefited by the provisions of the PACT Act, as noted above, that were not included in the recent amendments to the CCTA, including the requirement of collection of state and local taxes on delivery sales, and the prohibition of sales of cigarettes that were not in compliance with the MSA, as well as other provisions, such as the prohibition on the mailing of cigarettes, as contained in S. 1027, the PACT Act introduced in the 110th Congress on March 29, 2007.

Policy

The Federation of Tax Administrators should continue to work with the members and with Congress to arrive at legislation that would enhance the state and local enforcement of their tobacco taxes by strengthening the requirements of the Jenkins Act and CCTA, as well as authorizing the collection of taxes on remote sales of cigarettes and other tobacco products not

protected by tribal sovereignty, prohibiting the sale of cigarettes not in compliance with the MSA, restricting the means of delivery of remote sales under certain circumstances, and providing for the tracking and tracing of cigarettes and other tobacco products at the federal level through their distribution chains, and other measures to enhance the enforcement of federal excise taxes that do not interfere with and can support state and local enforcement efforts.

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Resolution Four

Taxation and Withholding of Wages Earned in Multiple States

Background

The fundamental principle of individual income taxation is that income is taxable where it is earned or where the services giving rise to the income are performed. In addition, the state of a taxpayer's residence may tax all income regardless of where earned, but is generally required to offer a credit for taxes paid to other states to assure that income is not subject to multiple taxation. This is the same tax policy embraced by the U.S. government and by all other income-taxing governments.

As U.S. work patterns shift to increasingly include interstate commuting, telecommuting and multistate travel, more workers find themselves with tax obligations to more than one jurisdiction. Likewise, employers are faced with an increased responsibility for withholding income taxes for multiple jurisdictions. State and local laws and practices vary with respect to de minimis thresholds for withholding. There also is variance in enforcement programs aimed at compliance among persons (and their employers) who are temporarily in the jurisdiction.

As introduced in the 110th Congress, H.R. 3359, the Mobile Workforce State Income Tax Fairness and Simplification Act, would authorize a state or locality to impose an income tax liability and a withholding requirement only when a nonresident has performed services in the jurisdiction for at least 60 days in a calendar year. The bill contains an exception for professional athletes and entertainers.

In its review of H.R. 3359 and in various discussions with proponents of the bill, FTA made several points.

- H.R. 3359 represents a substantial preemption and intrusion into state tax authority;
- While FTA recognizes concerns regarding the administrative burdens imposed by current practices, the 60-day threshold is well beyond a level necessary to deal with the vast majority of individuals who would be temporarily in a jurisdiction.
- H.R. 3359 would substantially disrupt the current tax system in favor of a system based on taxation by the resident jurisdiction.
- H.R. 3359 would substantially disrupt the revenue flows in certain states, particularly New York State because of its economy and its previous and current compliance programs in the area.
- A simple "days threshold" will expose some jurisdictions to substantial revenue disruptions; a "dollar threshold" that would limit the exposure of the states should also be applied.
- Independent state action is a viable and preferred substitute for federal legislation.

The impact of H.R. 3359 will undoubtedly fall most heavily on New York State because of its economy and its tax compliance programs. As with the FTA at large, New York is mindful of the issues involved in complying with the current law. It will be undertaking a review and analysis of the issue with a view toward recommending a state-level solution to the issue.

Policy

The ability to tax income where it is earned is fundamental to state tax sovereignty and state and local income tax systems. Moreover, this ability is absolutely necessary in our federal system, where a state may choose to not employ an income tax. FTA, however, recognizes the administrative and compliance burdens imposed on individuals and employers under current arrangements and are willing to explore options for addressing those burdens for employees who are in a jurisdiction for limited periods of time. In short, the issue comes down to arriving at an appropriate balance between administrative simplification and adherence to standard tax policies and avoiding the disruption of state and local revenue flows. FTA does not support H.R. 3359 as introduced.

FTA will assess any federal legislative measures in this area against the following criteria: (1) Recognizing that the benefits of federalism will impose administrative burdens on commerce, is there disinterested evidence that the administrative burden and complexity posed by current state and local practices is impeding the growth of commerce? (2) Does the proposed preemption address issues of simplification and complexity? (3) Can meaningful simplifications and uniformity be achieved through state action? (4) Would preemption disrupt state and local revenue flows and tax systems? (5) Would preemption cause similarly situated taxpayers to be taxed differently; specifically, does the proposal create advantages for multistate and multinational businesses over local business? (6) Does the preemption support sound tax policy? (7) Does the preemption create unknown or potential unintended consequences? (8) Have state and local tax authorities and taxpayer representatives together agreed to a beneficial change in federal law?

In addition, FTA makes the following specific comments on H.R. 3359 and similar legislation.

- Since New York State is the most significantly affected state and since it is undertaking a review of the issue, federal legislation should not proceed until proponents of H.R. 3359 have worked with New York State officials to resolve the issue at the state level. Further, Congress should also take account of constructive action by other states on this issue before proceeding with legislation.
- Based on its review and analysis, FTA believes an appropriate resolution of the issue should, at a minimum, meet the following criteria:
 - The action should be clearly limited to wages and related remuneration earned by nonresident employees. FTA believes it is not inappropriate to use presence and time in a taxing jurisdiction to govern the taxation of wages and related remuneration earned by a nonresident in a taxing jurisdiction. However, the legislation must also be clear that it is not intended to impair the ability of states and localities to tax non-wage income earned from the conduct of other economic activities in the taxing jurisdiction.
 - The action should provide that a state or locality may impose income tax liability on and a withholding obligation with respect to the wage and related remuneration of a nonresident if the nonresident is present and performing services in the jurisdiction for 20 or more days in a calendar year.
 - Alternatively, the threshold could be formulated as limiting state and local income taxation (and withholding) to those nonresidents present and performing services in

- the jurisdiction for 30 days or more in a calendar year, unless the individual earned in excess of \$250,000 in wages and related remuneration in the prior year in which case the threshold would be 15 days in the jurisdiction.
- The action should provide that all persons paid on a “per event basis” are excluded from the coverage of the bill.
 - The action should provide for the allocation of a day to a nonresident jurisdiction when services are performed in the resident jurisdiction and another jurisdiction in a single day.
 - The action should cover wages and remuneration earned within a jurisdiction in a calendar year so as to not disrupt taxation of any deferred amounts. It should not, however, impair the ability of states and localities to tax income arising from the conduct of other economic activities in the taxing jurisdiction.
 - The effective date of any action should be delayed until the beginning of the 2nd calendar year following enactment to allow sufficient time for implementation by state and local governments and affected employers.

Acceptance of a standard that a nonresident be present and performing services in a jurisdiction for the purposes outlined above should not be interpreted to imply that FTA considers that a physical presence standard is in any way an appropriate standard for establishing jurisdiction to tax in other contexts, particularly for the imposition of business activity taxes on entities doing business in a state. As outlined in Resolution No. 3 (2008), FTA is firmly opposed to federal legislation that would establish a physical presence nexus standard for the imposition of business activity taxes.