

September 14, 2020

The Honorable Dustin Burrows
Chairman, House Ways & Means Committee

**INTERIM CHARGE NO. 1.3 –
CONDUCT ACTIVE OVERSIGHT OF ALL ASSOCIATED RULEMAKING....TO ENSURE INTENDED
LEGISLATIVE OUTCOME OF ALL LEGISLATION...**

I, as a Member of TexasCityServices LLC at 2840 Keller Springs, STE 102, Carrollton, TX 75006 and as a representative of numerous Texas municipalities, transits, and special sales tax purpose districts and as a Texas sales tax practitioner of nearly 40 years, ask the Interim Committee as it debates this charge, to please consider the following facts as they relate to the Texas Comptroller's recent changes to 34 Texas Tax Administrative Code "Rule" 3.334:

- 1) ***Rule 3.334 at a minimum negates the monetary positive impact of HB 1525 of the 86th Legislature on Texas local sales tax revenues and likely results in an overall loss to Texas localities of at least \$100MM and quite possible greater than \$200MM.¹ This will also result in a direct reduction to the state budget anywhere from \$2MM to \$4MM.²***
- 2) Any change to destination sourcing, even one limited to only certain transactions as is Rule 3.334, will be extremely costly to Texas businesses. It is ***estimated to cost business at a minimum of \$30MM annually with a one-time cost to build software interfaces approaching \$3B*** to automate the tax decisions necessary to comply with Rule 3.334.³ If the business elects "manually" make its sales tax decisions on a transaction by transaction basis, we estimate a minimum of at least an extra hour monthly in ***sales tax compliance cost to Texas businesses annually 7.2MM man hours or an additional minimal cost of \$108MM annual cost to Texas businesses will likely be incurred.⁴*** It is extremely unlikely that any business would spend only one hour to comply with Rule 3.334's complexity, ***so actual business time and costs will likely far exceed \$108MM annually.***
- 3) ***Any change to destination sales taxes in Texas, including those found in Rule 3.334 violates the US Supreme Court's guidance issued in Complete Auto Transit v. Brady.*** The US Constitution's Commerce Clause is not the controlling doctrine for transactions within a single state's on boundaries; however, the US Supreme Court's logic and fairness tests for transactions between states is equally applicable to transactions between Texas localities. In determining the application of a state's tax, the Court asked four questions:
 - a. Is there "sufficient connection" between a business and the taxing jurisdiction to warrant a tax's imposition?
 - b. Is the taxing jurisdiction only getting "its fair share" of the proposed tax?
 - c. Does the tax treat "similar situated business businesses differently"?
 - d. Is the proposed tax "fairly related to the services provided" by the taxing

jurisdiction imposing the tax?

Rule 3.334 fails all four test questions:

- a. “Sufficient connection?” – Under current Rule 3.334 a business must collect or consider all 1,500+ local sales taxes when internet, or traveling sales persons may be involved, even in those Texas jurisdictions it has no activity (its’ the customer’s activity) that gives rise to the additional business’ tax collection burdens.⁵
- b. “Fair share?” – Non-Texas “remote sellers”, as defined in 86th Legislature’s HB 2153, may elect a single local use tax rate. In-state businesses are being treated differently, and in a far more costly manner than non-Texas businesses. In-State business are forced to comply by Rule 3.334’s complexities and costs in determining the over 1,500 different local sales taxes, while non-Texas sellers can elect a single combined local tax rate, and forgo the added burdens of Rule 3.334 compliance.
- c. “Difference between similarly situated business?” – Again, in-state sellers are being treated significantly different (and worse from a cost of compliance prospective) than that out-of-Texas sellers due to the 86th Legislature adoption of HB 2153.
- d. “Fairly related to the service provided?” - Under Texas Tax Codes 111, 151 and 321 the business collecting/remitting the sales tax is “the taxpayer”, not the purchaser. Accordingly, requiring remittance of a local sales tax where the taxpayer receives no services is in violation of this provision. While customer’s do receive services from the location from which shipments are received, in-state sellers located in other Texas localities do not. However, the seller’s location is left to provide services (water, sewer, police, fire, roads, infrastructure, etc.) to the seller while the customer’s locality receives the benefit of the tax.

- 4) **Rule 3.334 effective in October 2021, will significantly increase Comptroller workload** as almost all sections of 34 Tax Administrative Code “Rules” will need be revoked and reissued. Many of the published opinion letters and tax guidance publications will need to be suspended and reissued. Furthermore, the Comptroller has no audit procedures adopted to investigate sales functions and/or fulfillment operations, business function/operations that under Rule 3.334 are critical in determining proper local sales taxes.

Summary

Rule 3.334 not only nullifies any local sales tax gains resulting from the passage by the 86th Legislature of HB 1525; it also significantly increases business and state compliance costs, and violates the logic used by the US Supreme Court in determining tax fairness between taxing jurisdictions.

The Committee should recommend to the Comptroller that Rule 3.334 be suspended and rewritten to reflect the actual intent of Tax Code Sec. 321 and provide guidance to the Comptroller on the Legislative Intent behind the critical definitions included in Tax Code Sec. 321. To the extent, if



any, there is unfairness in the Tax Code, it is the Legislature's duty to address in the 87th Legislative Session the reasons giving rise to the unfairness.

The requested brevity by the Committee of this submission prevents me from including all the documentation supporting the facts discussed above. However, I have provided links via footnotes to the documents supporting these facts and encourage the Committee to review these substantiated facts and call/e-mail me with any questions.

Thank you for this opportunity, and please call me at (972) 814-6574 or e-mail me at kylekasner@cityservices.us with any questions.

Sincerely,



Kyle Kasner

¹ The Comptroller in 2020 changed 34 Tax Administrative Code "Rule" 3.334 to redefine place of business with the results in a change from origination to destination sourcing of local sales taxes in many types of transactions, (<https://www.sos.state.tx.us/texreg/archive/January32020/Proposed%20Rules/34.PUBLIC%20FINANCE.html#58>). Tax Code 321.002 "includes any location at which three or more orders are received by the retailer during a calendar year." Comptroller Rule 3.334 ignores this broad definition, and instead prohibits internet orders and salespersons from being considered as giving rise to places of business even if the business has but a single location in Texas or the World. The Rule 3.334 change also incorporated the 86th Legislature's HB 1525. House Bill 1525 was estimated by the Comptroller to increase local sales tax in 2020 by nearly \$100MM annually (<https://capitol.texas.gov/tlodocs/86R/fiscalnotes/html/HB01525F.htm>).

However, in Rule 3.334 the Comptroller combined HB 1525 with its place of business definitional changes, claiming the combination was "revenue neutral." This loss of \$100MM revenue gain to no gain can only result if HB 1525's \$100MM gain was offset by the place of business definitional change's loss of \$100MM. This \$100MM loss must be a result of the change from origination to destination sourcing of local tax in only certain transactions. Analysis of over 300 business who sell only to other business (B2B) indicates that loss for shipments to OCL businesses could easily double what the Comptroller estimated in the then Rule 3.334. A request for support concerning these estimates were not responded to by the Comptroller.

² The Comptroller charges a 2% service charge on any local tax collected on behalf of any jurisdiction in the State of Texas. If there is a reduction in local tax collected there is a direct 2% reduction of tax collected by the State of Texas.

³ Per the Texas Comptroller's published sales tax permit listing there are over 750,000 sales tax permitted locations in Texas with over 600,000 being but a single place of business in Texas (<https://data.texas.gov/Government-and-Taxes/Active-Sales-Tax-Permit-Holders/jrea-zgmq/data/>). Per Avalara, the least expensive software application capable of destination sales tax, initial costs of software is \$50 annually (<https://www.avalara.com/us/en/products/sales-and-use-tax/avatax/avatax-pricing.html>). Six hundred thousand single places of businesses at \$50 software cost per business is \$30MM in added costs for compliance for Texas businesses. In addition, the Avalara product does not allow for the necessary inputs required by the new Rule 3.334 (internet vs. point of sale, sales office vs traveling sales office, in house inventory fulfillment vs. 3rd party drop ship supplier, etc.). It is estimated to build these interfaces into any sales tax decision software will be at a minimum \$5,000 per single location business, or a one-time software interface business cost of compliance of \$3B. Businesses with multiple locations and sales order/fulfillment systems will face interface costs in excess of \$100,000. While I was the lead sales tax partner at Pricewaterhouse Coopers Dallas we often had interface projects of over \$1MM per business.

⁴ Small businesses with but a single location in Texas (estimated at 600,000 as explained above) have greatly expanded their delivery capabilities since Covid-19 in an effort to stay competitive (i.e. what restaurant, laundry, liquor store, or grocery store doesn't provide deliveries today?) Assuming one hour of extra compliance as a result of Rule 3.334 each month for Texas small businesses results in an additional 7.2MM employee hours for all small business (600,000*12*1). Seven million two hundred

thousand employee hours at \$15 (“living wage”) an hour results in \$108MM in additional costs to Texas businesses to come to compliance.

⁵ [https://comptroller.texas.gov/economy/fiscal-notes/2016/may/local-taxes.php#:~:text=In%20Texas%2C%20local%20sales%20taxes,%2Dpurpose%20districts%20\(SPDs\)](https://comptroller.texas.gov/economy/fiscal-notes/2016/may/local-taxes.php#:~:text=In%20Texas%2C%20local%20sales%20taxes,%2Dpurpose%20districts%20(SPDs))

