STATE TAXES AND ECONOMIC TURMOIL

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by

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Coming Today in this Presentation

• Principles of a Good Tax System
• Economic Turmoil: Opportunity or Armageddon?
• Economic Stimulus: Are we there yet?
• Federal legislation affecting state taxation: Good, Bad or Ugly?
• The Fundamental Problem
Principles of a “Good” Tax System

- Taxes should be adequate to provide an appropriate level of those goods and services best provided by the public sector, such as education, public safety, and transportation.
- Taxes should do the least harm to the private economy.
- Tax bases should be as broad as possible so that tax rates can be as low as possible.
- Taxes should not only be fair and equitable towards individuals and businesses similarly situated, but also they must be perceived as fair by taxpayers. Individuals with the same income level should bear the same or similar tax burden. Businesses engaged in similar commercial activities should be subject to the same level of taxation.

Principles of a “Good” Tax System (2)

- Taxes should not be costly for government to administer and should be easily understood by taxpayers so as to maximize taxpayer understanding and minimize taxpayer compliance costs.
- Taxes should be evaluated on the basis of the impact of all taxes levied on taxpayers, not just a single tax or tax rate.
- Deviations from sound tax policy in pursuit of economic development, social, or other goals should be well-reasoned and implemented only when established tax policies are not significantly undermined and the results of such deviations can subsequently be evaluated.
State Revenue Performance by Tax

Sales Tax Revenues: Some Reports from the States

- down 8.63% from February 2008
- 1.2% below
- down 10.3%
- down about 5%
- down about 8 percent
- down 6.9%
- down in February from the previous February by 11.2%
- YTD we’re down about 5%
- down 7.9% from February 2008
- down 18.5% from February 2008
Economic Turmoil: Opportunity or Armageddon for the States?

- State Tax Revenues are Declining – Deficits are Prohibited
- Corporate Income: UDITPA Revision, Combined Reporting, Single Sales Factor, Incentives, De-Coupling, Penalties
- Reserves: Draw down
- Tax Increases: Tobacco, Sin, Fees, “Temporary” fixes, Amnesty
- Spending Cuts: Layoffs, Furloughs, Salary reductions
- Federal Funds Flowing to States: To take or not to take?

Tax Provisions Affecting States in the Economically Stimulating Legislation

- 5 year (currently 2 year) NOL carry-back for 2008 losses; limited to companies with annual revenues of less than $15 million; companies that receive TARP bailout money from Treasury are not eligible.
- Deduction for sales taxes paid on purchase of new motor vehicles; the deduction taken by non-itemizers will not flow through to most existing state tax codes; the deduction taken by itemizers will.
- Businesses that buy equipment and make investments in plants can expense up to $250,000 directly from their tax liabilities.
- The 50 percent bonus depreciation deduction for qualified property is extended by one year, applying to property placed in service before 2010 and in a few cases 2011.
Congress to the States: “We’re from Washington and we’re here to help you.”

- Main Street Fairness Act
- Business Activity Tax Simplification Act
- Permanent Internet Tax Freedom Act of 2009
- Mobile Workforce State Income Tax Fairness and Simplification Act
- State & Local Taxation of Electronic Commerce
- Cell Tax Fairness Act
- State Video Tax Fairness Act
- Hotels, Rental Cars, Energy: all need help from DC

Main Street Fairness Act
(S. 37; H.R. 3396, 110th Congress)

- State that simplifies its sale and use taxes may require sellers not physically present in the state to collect and remit that state’s use tax
  - Congress consents to the Streamlined Sales and Use Tax Agreement
  - Legislation is independent, but similar to the Streamlined Sales Tax Agreement

- Expanded jurisdiction is provided only to “Member States under the Streamlined Sales and Use Tax Agreement” §4(a)(1)
**Business Activity Tax Simplification Act**
(S. 1726; H.R. 5267, 110th Congress)

- Nexus Criteria: Employees in state for more than 14 days
- Tangible personal property in state for more than 14 days
- All business activity taxes, not just net income taxes, are covered
- All solicitations, not just those for tangible personal property, are protected
- Not just solicitation, but qualitative de minimis activities, such as information gathering, visiting vendor, attending media event, are protected
- Only if in-state person is performing market-related activities and has only one “principal”

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**Permanent Internet Tax Freedom Act of 2009** (S. 43, 110th Congress)

- 2009 Act would make the Internet Tax Freedom Act Amendments Act of 2007 permanent
- Introduced January 6, 2009 and referred to Committee on Finance

**Current law:**

- Prohibits state and local taxes on charges for Internet access through November, 2014
- Continues the grandfather protection for taxes in place prior to 1998
- Provides that taxes may not be imposed on intermediate purchases of telecommunications by ISPs after June 30, 2008
- Provides that gross receipts-based taxes in MI, TX, WA, and OH are not considered taxes on Internet access
Mobile Workforce State Income Tax Fairness and Simplification Act
(H.R. 3359, 110th Congress)

- Employers required to withhold (and employee only taxable) in only states and localities:
  - Where employee resides, and
  - Where employee is physically present performing duties for more than 60 days during a taxable year (retroactive for taxability for year once threshold reached)
- New Legislation that is expected to be introduced is likely to have a 30 day threshold

State Video Tax Fairness Act of 2008
(S. 3418; H.R. 3679)

- Prevents the states from imposing tax at a higher "net tax rate" on one form of multi-channel video programming distribution services compared with another form of multi-channel video programming distribution services.
- The bill is primarily aimed at states that impose a sales tax on satellite operators’ comparable gross receipts, but do not impose a similar tax on cable operators’ comparable gross receipts
More Federal “Help”

- Cell Tax Fairness Act (H.R. 5793; S. 3249)
- Discriminatory State Taxes for Automobile Vehicle Renters (H.R. 2453)
- Energy Infrastructure Tax Fairness Act (H.R. 5558)
- Hotel Reservations Online Intermediaries Protection and Local Tax Evisceration Act

Taxation and Public Trust

- “Tax reform means, Don't tax you, don't tax me. Tax that fellow behind the tree.”
  - Senator Russell B. Long
- Simultaneous Belief: Robust public goods and services and low or no taxes.
- Result: We believe the system used to raise funds for those public goods – our tax system – is unfair.
- Solution: Deferral, Obfuscation, Crisis Management
Questions / Follow-up

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“Taxes are what we pay for civilized society”
Campaña General de Tabacos v. Collector, 275 U.S. 87, 100
Justice Oliver Wendell Holmes,