

Department of Finance and Administration

Legislative Impact Statement

Bill: HB2085

Bill Subtitle: TO DISTRIBUTE A PORTION OF THE SALES AND USE TAX COLLECTED FROM SELLERS THAT DO NOT HAVE A PHYSICAL PRESENCE IN THE STATE TO THE STATE HIGHWAY AND TRANSPORTATION DEPARTMENT FUND.

Basic Change :

Sponsor: Representative Rye

HB2085 provides for a distribution of sales and use tax revenues that are received from sellers having no physical presence in Arkansas.

The provisions of the bill would be effective on the first day of the calendar quarter following the effective date of the act. Beginning on the effective date, DFA would begin determining the amount of sales and use taxes that are collected from sellers that have no physical presence in Arkansas. The sales and use taxes collected from these sellers would be deposited with the first fifteen million dollars (\$15,000,000) being deposited as state general revenues with amounts received after meeting the fifteen million dollar (\$15,000,000) threshold being deposited to the State Highway and Transportation Department Fund.

The bill also deletes existing code provisions regarding the distribution of sales and use tax revenues that would be received from sellers having no physical presence in Arkansas from the date Federal law is adopted authorizing the collection of state and local sales taxes. Provisions deleted from the Code include those that would reduce the state sales and use tax rate on food and food ingredients and the provisions that would reduce income taxes for filers subject to the 4.5% income tax rate.

Revenue Impact :

FY2018 --- Sales and use tax general revenues collected from out-of-state sellers having no physical presence in Arkansas would be changed beginning on the anticipated effective date of the act (October 1, 2017) with the first fifteen million dollars (\$15,000,000) continuing to be deposited to State General Revenues with all monies received after meeting the threshold being deposited to the State Highway and Transportation Department Fund. If revenues exceed the \$15,000,000 threshold amount during FY2018, the revenues would then be deposited for Highways which may result in reduced State General Revenues during FY2018 compared to the previous fiscal year. The revenues from out-of-state sellers having no physical presence in Arkansas who have been collecting and remitting the Arkansas sales taxes during previous years which would have been deposited to General Revenues would change during FY2018 after meeting the \$15,000,000 threshold amount and would then be deposited for Highways. The amount of General Revenue reduction in FY2018 is not known.

Taxpayer Impact :

Revenues being received from out-of-state sellers having no physical presence in Arkansas will be distributed in the manner as outlined in the bill. Consumers purchasing products from out-of-state sellers that are collecting Arkansas sales taxes will have no change.

Resources Required :

Modifications to DFA's cash receipts and accounting systems will require modification. Resource costs associated with the changes have not been determined.

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Resources will be expended to contact the more than 16,000 existing out-of-state sellers requesting information regarding their status of having physical presence in Arkansas and updating DFA's tax registration information to reflect their response in order to have information for future depositing of their remitted sales tax revenues.

Time Required :

A period of six months is estimated by DFA to modify the cash and accounting systems and the DFA tax registration and tax reporting system to allow for the compiling of the additional taxpayer information related to their status of not having physical presence in Arkansas in order to account for the revenues in the manner required. Requesting and receiving responses from the exiting 16,000 out-of-state sellers regarding their physical presence status in Arkansas may not be complete during the six month time frame dependent of taxpayer timely response to the information request.

Procedural Changes :

DFA would have to contact all currently registered out-of-state sellers collecting sales and use taxes and request information as to their status as being required to collect and report or if the company deems themselves as not having a physical presence and their tax reporting is on a volunteer basis. Modification of DFA's tax registration system will be required to provide for an out-of-state seller who registers to collect Arkansas sales and use taxes to indicate if they are registering as the result of having nexus with Arkansas and are required to collect the Arkansas taxes or are registering to collect tax on a volunteer basis having no physical presence in the state.

Other Comments :

DFA has no knowledge as to the out-of-state sellers that have or do not have physical presence in Arkansas and cannot make the distribution of revenues as provided without gathering significant information from out-of-state registered sellers.

Information indicating physical presence is not provided by sellers registering to collect Arkansas sales and use taxes. Even if sellers would have been required in the past to indicate if they had physical presence at the time of registration, a business may create nexus after the initial registration in multiple ways. Physical presence is established by an out-of-state vendor not only by having property located in the state but also when making sales to Arkansas purchasers by soliciting sales through salespersons, solicitors, representatives or consignees who are soliciting sales while in Arkansas. Since October 2005, when Arkansas became a member of the Streamlined Sales Tax Governing Board, 3,254 out-of-state sellers have registered to collect Arkansas state and local sales taxes when making sales to Arkansas consumers through the terms and requirements of the Streamlined Agreement. At the time of their Streamlined registration, most of the sellers were volunteering to begin collecting Arkansas taxes. Since their registration, Arkansas does not have data for the Streamlined registrants as to their possible nexus-creating activities since their initial registration. DFA has approximately 75,000 registered businesses that collect and remit Arkansas state and local sales and use taxes. Of the total registrants, more than 16,000 are out-of-state sellers collecting and reporting in the same manner as the in-state sellers. To acquire the necessary information to implement the bill, DFA would have to

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contact all of the out-of-state sellers and request information as to their physical presence status. The accuracy of the "no physical presence" information acquired could not be verified without a field audit and if the out-of-state seller does not provide the information, DFA could not include the seller's data in the calculations regardless of their status.

The bill does not exclude existing tax collections from currently registered out-of-state sellers having no physical presence in Arkansas from the distribution change. Transfers to the State Highway and Transportation Department Fund will occur if the existing general revenue collections from these sellers exceed the fifteen million dollar (\$15,000,000) threshold. If they do exceed \$15,000,000 as of the effective date of the act, a loss to state general revenues will occur.

The bill is not clear as to the distribution change occurring on the effective date of the act. After the first fifteen million dollars (\$15,000,000) is deposited to state general revenues, it is unclear whether the remaining revenues deposited to State Highway and Transportation Department Fund to be future collections are for an indefinite period of time or whether or not it is the intent of the bill for the fifteen million dollar (\$15,000,000) threshold to be a threshold met each fiscal year with the remainder collected during the year to go to highways. The bill should be amended to provide clarity for the deposits across multiple years.

Sales and Use tax revenues received by DFA are deposited to general revenues upon receipt. A transfer to the State Highway and Transportation Department Fund could only occur after the tax returns from the out-of-state sellers are processed with error corrections completed each month. The Education Excellence Trust Fund receives an amount equal to 14.14% of the prior year's sales tax general revenues. If sales taxes are deposited to general revenues and subsequently transferred to the State Highway and Transportation Department Fund, it is not clear if the initial general revenues deposits from the out-of-state sellers with no physical presence that are subsequently transferred to Highways are to be excluded from the calculation. If not excluded, during the fiscal year following the transfer to Highways, the Educational Excellence Trust Fund would receive 14.14% of the amount before the transfer and general revenues would be shorted.

Legal Analysis :

HB 1965 amends existing law in relation to the distribution and use of certain sales and use tax revenues from remote sellers. The bill repeals existing provisions regarding the use of sales and use tax revenues from remote sellers concerning the income tax levied on individuals, trust, and estates, and the sales and use tax levied on food and food ingredients. The bill eliminates existing provisions which allow the DFA Director to determine whether federal law authorizes the state to collect sales and use tax from remote sellers. The bill further amends existing law concerning the disposition of taxes, interest, and penalties, by authorizing funds in excess of fifteen million dollars (\$15,000,000) received from remote sellers to be deposited into the State Highway and Transportation Department Fund. The effective date of this amendment is the first calendar quarter following the effective date of this act.