MTC STRATEGIC PLANNING PROJECT - 2014

Marketplace Fairness Act, "single audit" program plan (version 2.0, 5-30-14)

Project description: This project involves development of a high level plan for the MTC to conduct "single audits" on behalf of states in compliance with the Marketplace Fairness Act, should it be enacted. The plan would include the potential for conducting single audits of remote sellers on behalf of all states and local governments collectively, as well as the potential for conducting single audits on behalf of a single state and its subdivisions.

Problem: The current version of the Marketplace Fairness Act (MFA) now pending in Congress requires the states to provide for single audits of remote sellers for all state and local taxing jurisdictions within each state. If the MFA passes, MTC will need to identify the key activities that would need to be in place to assist the states with the single audit requirement and the resources that would be needed in order to provide single audit services to the states. This need will be the greatest for the states that are not participating in the SSUTA. There is also a possibility that MFA could be amended to require a single audit on behalf of all states.

Risks: the MFA could pass at any time. The time for implementation would be short. Current audit resources are committed to our existing audit function, and integrating a new audit service will require thoughtful planning and may require different resources or resource allocation.

Opportunities: MTC could assist the states to comply with MFA. The MTC also has the opportunity to bring many remote sellers into nexus compliance early in the life of the MFA. Also, the single audit requirement in the current version of MFA could be a barrier to enactment, and if MTC has an audit program plan ready, it could assist with gaining support for the MFA in Congress.

Target completion date: December 2014

Issues for review:

<u>MFA Issues</u>
- What are the key elements needed to satisfy the "single audit" requirement for remote sellers under the MFA?
    - Single return filing requirement
    - Status as a "remote seller" – annual minimum remote sales threshold
- What assumptions should be made about the requirements of MFA – what is our common understanding?
- How many "remote sellers" will be subject to the MFA? ***Fewer than 240,000.***
- What substantive issues are most likely to come up in audits under MFA?
- What entity or entities will be the subject of the audit?
    - Multi-corporate groups or single entities?
- Can remote sellers be administered/audited separately from those that are already reporting due to a physical presence?
- What impediments would the "single audit" requirement create to the states' ability to take advantage of the MFA?

- Are there unique issues that affect states that are not participating in SSUTA? ***How to determine that they are in compliance with MFA.***

General Audit Issues
- What would be needed for states to be able to participate in a single audit?
- What would be needed for local governments to be able to participate in a single audit?
    - What special issues exist for states in which local governments have audit authority – IL, PA, LA, CO, AL, AZ (others?)
- What concerns might taxpayers have that should be considered in a "single audit" program design?
- How would the MTC provide policy oversight for this kind of a program?
    - Development of audit policies, practices and procedures;
    - development of audit plans and criteria for audit standards;
    - development of appropriate sampling types and techniques
- How would audit candidates be selected [process and criteria]?
- How would liability (or refunds) be allocated to the state(s) and local governments?
- How to handle audit results that show payments were made to the wrong jurisdiction
- What are the boundaries around what is an "audit" versus what leads up to it and follows from it
- Taxability "matrix" – what is taxable and what is exempt in each taxing jurisdiction for auditors to follow
- Who will be responsible to collect unpaid tax and remit to taxing jurisdictions?
- How do SSUTA participating states currently administer local sales and use taxes?
- What separate issues are there for local tax administration and compliance?
- Would an audit "clearinghouse" model (like IFTA) be useful?
- How would audit results be transmitted to taxpayers, states and local governments?
- What would be the relationship between this program and the SSUTA and CSPs?

Issues Affecting MTC's Audit Program
- What kinds of process changes might be needed to implement a "remote seller single audit" function within the current MTC audit program? ***A "remote seller single audit" function could readily be incorporated into the current MTC audit program. The most significant differences from the current sales tax audit program would probably be audit scope and issues, and size and type of taxpayers.***
- Would this kind of an audit service need to be a separate program from the existing audit function? ***No. This kind of service could be delivered within the current audit program, as a separate function within that program. A "remote seller single audit" function would require a separate fee structure from the current income and sales tax fee structure.***
- What staff resources might be needed to meet the need for "single audits" to be provided for the states? ***An audit supervisor and auditors dedicated to the "remote seller single audit" function.***
- What kind of training would be required for auditors to be able to conduct "remote seller single audits?"
    - Requirements of MFA; state laws and rules; audit techniques
- What would a cost or fee structure for a "remote seller single audit" program look like?

- Are there any legal issues that would affect MTC's ability to offer this kind of service? ***MTC would contract with the states that wanted to use the service, similar to the way associate member states participate in the audit program currently.***
- What technology tools would be needed to conduct "remote seller single audits?" ***Current MTC sampling software could be used.***

Issues Affecting Voluntary Compliance
- What strategies might be developed to assure voluntary compliance by remote sellers? ***Implement a Voluntary Disclosure Program similar to the current program.***
- What MTC staff resources or technology tools might be needed to assist states in maximizing voluntary compliance by remote sellers? ***Depending upon how many remote sellers are subject to MFA and compliance rates, additional staff and technology may be needed.***

Issues Specific to One Audit per Remote Seller (for multiple states)
- Remote sellers may have physical presence nexus in some states – for those states they will also have use tax issues; can audits for these circumstances be done separately under the MFA?
- Taxability matrix and tax rates; different statutes of limitations; confidentiality requirements; appeals processes
  - ***Information exchange agreements may need updating;***
  - ***MTC would need access to sales sourcing databases;***
  - ***Software incompatibility may also be an issue.***
- Who could initiate a "single audit" for multiple jurisdictions? (A state, a group of states, a taxpayer? Can states elect to participate or not?)
- What would be the process and criteria for audit selection?
  - There must be balance and fairness in overall audit selection between remote and in-state sellers (Note – remote sellers need to be put at ease that they are not going to be audited more often than other taxpayers.)
- Remote sellers that are NOT using CSPs may not have electronic records, or may have records in different format (model 1 sellers versus non-model 1 sellers). How can this be dealt with?

Expected outcomes from the project*:*
- High level structure for a single audit program to meet the requirements of MFA, and the needs of affected taxpayers, states and local governments.
- Description of resources needed to implement single audit program.
- List of changes to existing audit and nexus programs that should be considered, if any.
- List of any issues that cannot be resolved until MFA is enacted.

Who should be involved in this project*:*
- Representatives of the states – especially states that have multiple sales tax jurisdictions
- SSUTA members or staff – SSUTA has an audit core team focused on CSP certification
- MTC staff
- Liaison with related MTC projects (example: Uniformity committee)

Additional resources*:*
- SSUTA service providers
- Larger retailers or larger remote sellers – perhaps later in the process after an audit program is designed at a high level

INFORMATION RESOURCES

Topics	Sources
• Central administration of local taxes	TX, WA, TN, WI, AL, NE, SD
• MFA FAQs	Uniformity Committee project
• Streamlined audits (SSUTA states)	SSUTA Web site**
• Private sector input – needs and concerns	Taxpayers, SSUTA BAC
• Current MTC audit structure and program	Steve and Harold
• IFTA structure	IFTA web site
• Local jurisdictions – needs and concerns	
• Non-SSUTA states – needs and concerns	

**SSUTA Web site – Library – all docs – issue papers – draft proposal for single audits; contract compliance audits for CSPs