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Streamlined Sales Taxes

A proposed amendment to the “delivery charge” definition in the Streamlined Sales and Use Tax Agreement could resolve a long-standing dispute over the taxation of postage by states. In this article, author Melanie Hill of Dow Lohnes Price Tax Consulting Group explains the proposal and why it may be a win-win for both states and the direct mail industry.

Large-Scale Streamlined Sales Tax Dispute Resolution: ‘Reverse Toggle’ May Resolve Debate Over Postage Taxation

By MELANIE C. HILL

The Business Advisory Council (BAC) to the Streamlined Sales Tax Governing Board has proposed an amendment to the “delivery charge” definition in the Streamlined Sales and Use Tax Agreement (SSUTA) that is viewed as a compromise on the issue of taxation of postage, a source of contention within the streamlining effort since October 2006.

The amendment—which has been dubbed “the reverse toggle”—is sponsored by Wyoming, West Vir-

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ginia, and Utah, with the joint support of those elected representatives and tax administrators in each state. If the governing board adopts the amendment, it will have timely resolved a hotly contested issue that could otherwise prove to be a liability when the board seeks support for federal streamlining legislation.

The BAC compromise protects states’ rights by allowing the taxation of delivery services on mail while restoring the pre-SST landscape, wherein postage on mail was not commonly regarded as a taxable delivery charge regardless of the method of payment to the postal service. Some leaders in the State and Local Advisory Council (SLAC) assert that the SSUTA now includes postage on mail as part of the tax base if the service provider’s permit or meter account is used to transfer the funds to the U.S. Postal Service and that such a result can *only* be avoided if the state legislature passes a special exemption for delivery charges on direct mail. This view is far from universal, and the uniform language, when coupled with a rigid interpretation, denies

states the right to recognize the application of agency and contract law to individual facts and circumstances.

LACK OF UNIFORMITY

States within the project do not now interpret the delivery charge definition in a uniform manner, a problem which leaves thousands of printers, commercial mailers, and direct mail users at risk for owing past tax on postage should the matter be resolved administratively by the board in the manner that the SLAC proposes. Such a result can only lead to nonuniform tax administration and/or protracted dispute resolution. Many printers, mailers, and direct mail users already view the complex sourcing rules as a disruption to interstate commerce, and the taxation of postage is an added controversy which could be placed on the steps of the U.S. Capitol. These issues can be resolved by the governing board if stakeholders on both sides focus less on winning the current debate and focus more on supporting a prospective resolution.

The direct mail industry acknowledges that one state participating in the project routinely taxed postage on mail as a delivery charge prior to passing its SST legislation; however, it is illogical for the board to interpret its uniform language for *all* states to reflect the treatment by this single state. Furthermore, there is *not a single state* participating in the streamlined system which has previously imposed tax on postage for delivery of business correspondence, invoices, and statements. Since this type of mail is squarely within the direct mail definition, the current debate highlights an even greater discrepancy between states' historical sales tax treatment and the position adopted by SLAC. The SST drafting protocol is supposed to be based on proposing language which reflects *mainstream* treatment by the participating states while providing maximum simplicity and uniformity.

After months of negotiations, it is clear that this issue will not be resolved as a matter of interpretation. A dispute over a matter of interpretation of this scale will create winners and losers in a public debate where both sides lose if either side loses. Thus, a proactive dispute resolution based on a prospective compromise will create winners on both sides while allowing individual stakeholders latitude to resolve issues related to interpretation of the SSUTA's current delivery charge definition. This is the background upon which the "reverse toggle" proposal rests.

REVERSE TOGGLE EXPLAINED

The "reverse toggle" is a compromise in that it does not resolve the current debate as to whether postage is part of the sales price in any given state; the current treatment is left for resolution on a state-by-state basis. However, what the "reverse toggle" does provide is a prospective resolution which will result in uniform treatment and clarity in legislative intent. The "reverse toggle" simply restores the presumption that postage on mail is not part of the sales price of printed material or mailing services and reflects the mainstream viewpoint prior to the SSUTA. However, the proposal does not take the taxation of delivery services on mail or correspondence completely off the table; it clearly provides that states may enact a specific imposition of tax on delivery of mail or business correspondence. In the wis-

dom of Solomon, it will result in uniform treatment within two years without creating winners or losers under the current delivery charge definition.

The "reverse toggle" proposal cannot be fully appreciated without an understanding of the current delivery charge definition in the SSUTA. Industry asserts that the current delivery charge definition does not apply to postage on mail when procured by a mailing agent through its meter or permit account. For example, it defines "delivery" as those charges for delivery to a *location designated by the purchaser*. Thus, the delivery charges to ship a box of brochures to an advertiser clearly falls within the delivery charge definition, both current and proposed. Conversely, the delivery of a million pieces of mail to a million different locations is clearly not delivery to a location specified by the purchaser.

In addition, title to material manufactured as a custom print job typically passes at the printer's loading dock; it is a questionable proposition to regard the subsequent delivery of mail by the postal service as a delivery charge by the printer on the sale of printed material. The postal service is not delivering the original print job manufactured by the printer; the postal service is delivering individual pieces of mail which have undergone additional mailing services subsequent to the print manufacture job. Therefore, the delivery of mail by the postal service should not be regarded as a delivery charge as part of the sales price of the print manufacture job.

Furthermore, the current delivery charge definition applies to *charges by the seller*; the industry contends that a charge by the postal service for the delivery of mail is not a charge by the seller. The printer is, at most, merely facilitating the mail owner's purchase of postage from the postal service. The printer is not assessing a shipping and handling charge that includes a mark-up on postage for delivery services provided by the postal service, nor is the printer "reselling" postage. As used in the SSUTA, a *charge by the seller* would presumably include an element of profit since most sellers are in business to achieve a profit on their business activities. The printer realizes no profit on the postage charges assessed separately by the postal service for its services, and in states which impose a gross receipts tax on the seller, the printer would "go in the hole" if tax were imposed on postage.

DEPARTURE FROM PAST PRACTICE

It is a common industry practice for the direct mail user to pay postage in advance directly to the postal service in the form of a check made out to the postmaster. In such cases, it is a dramatic departure from historical tax practice to include a direct payment to the postmaster as part of the taxable sales price of printed material, yet that is what some states are asserting through the SLAC position. While the printer accounts for the postage used in the mailing by providing a copy of the postal service's official, certified postage statement, an accounting of fiduciary funds between a principal and its agent should not result in tax imposition on such funds.

The governing board is not likely to adopt an interpretative ruling on the current delivery charge definition because, while any one of the above reasons may be determinative in a given state, the board is not likely

to agree on a single determinative factor which will be accepted by all states. By its nature, a uniform interpretation of the current delivery charge definition with regard to the delivery of mail will be elusive because a uniform interpretation imposes a rigidity which does not address each state's judicial and administrative history with regard to agency and contract law.

The "reverse toggle" removes the steam building on both sides seeking to win this debate in favor of a prospective resolution. With the future delivery charge definition in place, it is much more likely that individual states and taxpayers will be able to resolve disputes under the current definition using facts and circumstance determinations or individual state tax administrative policy (rather than administrative policy imposed by the board).

The direct mail industry clearly views the "reverse toggle" as a compromise. It is a significant compromise for some constituents who simply believe that it is unconstitutional to impose tax on a check made out to the postmaster general. The direct mail trade associations' original proposal attempted to require the board to recognize mailing agency in the payment of postage, which would have resulted in a unilateral win. This is an additional compromise that mailing agency is not part of the "reverse toggle" proposal. Clearly, the direct mail industry is conceding significant territory in accepting the "reverse toggle" proposal; however, the trade associations representing the industry recognize that compromise is necessary when resolving issues of this scale. The benefits of prospective resolution and clear legislative intent justify the compromise.

COMPROMISE REQUIRED

If a compromise between the parties is to be achieved, members of the SLAC need to meet the industry part way. The most commonly cited reason for not supporting the "reverse toggle" is that there is no dispute to resolve: states may pass an exemption if they choose not to tax the delivery of mail when postage is paid through a printer or mailer. As long as states deny that a problem exists, it will not be resolved; an issue of this magnitude will not simply "go away." Many states have chosen to stay out of the issue since they have passed an exemption and have no issue within their state borders. While this is understandable, it clearly minimizes the debate and ignores the impact of this un-

resolved issue on the success of the project as it goes for federal approval.

Members of the SLAC should start by recognizing that the industry has compromised its position by accepting the "reverse toggle." Members of the SLAC could then measure the amount of compromise they are willing to accept in an effort to move this issue off the table. The "reverse toggle" is a good place to start. For those states that have adopted the exemption, the "reverse toggle" amendment is of little significance; it will have no fiscal impact and will be little more than an item imbedded in "clean-up" legislation. Some states may argue that it is difficult to get even innocuous "clean-up" legislation passed; the validity of this argument is greatly reduced given that the SLAC is proposing its own delivery charge amendment for December. States that have not passed the exemption and are not interpreting the current delivery charge definition as a tax imposition on the delivery of mail will be able to pass the "reverse toggle" with no fiscal impact.

Another position cited by some states is that the tax administrators believe that postage on mail is taxable under the current delivery charge definition, and they don't relish asking the legislature for a specific imposition statute. While this is a legitimate concern for the tax administrators, in reality, it puts the issue squarely in the hands of the legislature where it rightly belongs. If the legislature chooses to enact the "reverse toggle," it would have no fiscal impact if the state's tax administrative policy has been to interpret the current agreement as including postage on mail in the tax base as a delivery charge. While this may be viewed as a compromise for these states, it is nonetheless a revenue neutral statute change. In reality, there are very few states in this position and the "reverse toggle" does not prevent these states from taxing delivery charges on mail. The "reverse toggle" proposal removes the argument that states' rights to tax delivery of mail are being trampled because it clearly provides states with exactly that right.

CONCLUSION

The industry is conceding a blanket prohibition against tax on mail delivery; the states are conceding a presumption that mail delivery is taxable as a delivery charge. Neither side is winning the current debate, but both sides will win if the issue is resolved prospectively and legislatively through the enactment of the "reverse toggle."