National Retail Federation
The Voice of Retail Worldwide

Testimony of the
National Retail Federation
And
J. C. Penney Corporation, Inc.

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H.R. 3396: Sales Tax Fairness and Simplification Act of 2007

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Good morning Chairwoman Sanchez, Ranking Member Cannon and members of the Committee. My name is Wayne Zakrzewski, and I am the Vice President and Associate General Counsel for Tax for J. C. Penney Corporation, Inc. ("JCPenney") Today I am here to testify in favor of Mr. Delahunt's bill, H.R. 3396, the Sales and Use Tax Fairness Act of 2007, both on behalf of JCPenney and our national trade association, the National Retail Federation together, we urge swift action by this subcommittee to pass this important retail business legislation.

As a representative of JCPenney, I have been an active participant in the Streamlined Sales Tax ("SST") Project since it began nearly eight years ago in early 2000. I currently serve as a member of the Board of Directors of the Business Advisory Council ("BAC") to the Governing Board of the Streamlined Sales Tax Agreement. I also serve as co-chair of the Steering Committee for the Joint Cost of Collection Study ("JCCS").

JCPenney is a multi-state retailer with $20 billion in annual sales made through our stores, direct mail catalog and Internet businesses. Since 2002 our total business has grown from about $17 billion to $20 billion and we are now one of the largest apparel and home furnishing sites on the Internet. While our catalog business has declined by about $0.7 billion dollars since the 2002 level of $1.8 billion, **our Internet business has grown from $400 million to over $1.4 billion dollars –over a three fold increase**. Some of the Internet growth is due in part to a shift from customers who used to shop through a catalog, but it also represents significant growth in the Internet marketplace.

We are here to ask you to level the playing field between sellers that collect sales tax and those who cannot be required to collect the tax because they do business in the community on a virtual rather than physical basis. We remit over $1.2 billion dollars in sales tax annually on our sales whether made through stores, catalog or online. Many of our online competitors do not collect, which gives them a competitive advantage. This is not because they are innovative or provide incremental value to the consumer, but because the states do not have the ability to require collection of a tax that is due from the consumer.

Their competitive advantage exists because the United States Supreme Court has ruled that businesses that are physically present in a state may be required to collect, while sellers who do business in states only on a virtual basis are not required to collect. The Court found that state sales and use tax systems were too complex to justify placing the burden of collection on sellers that were not physically doing business in a state. However, the current system not only places local businesses that provide jobs in the community at a competitive disadvantage, it also burdens consumers because the taxes that go uncollected must be made up by higher overall rates on those sales where collection is required.

We believe there are compelling reasons why Congress should act now to level the playing field and allow states that are members of the SST system to require remote sellers to collect the taxes due from customers in their states.

Primary among those reasons is the success of the states in implementing the SST Agreement. The initial goal of the SST Project was to simplify sales taxes as much as possible and make uniform those things that could not be simplified. The SST Agreement has made tremendous strides by providing for uniform definitions, exemption certificate administration, rounding rules, and returns and remittances rules. The current Agreement provides for uniform destination sourcing and requires states to provide a taxability matrix that both sellers and purchasers can rely on to determine whether the items they sell are subject to tax. The SST Governing Board ("SSTGB") has identified Certified Service Providers ("CSPs") who work with businesses to collect and remit taxes, all at the expense of the states.

These changes represent a significant reduction in the burden imposed by the sales tax system in SST states and there are continued efforts for improvement. If the provisions of the SST Agreement are rigorously adhered to, business benefits by lower costs of collection, states benefit by more accurate collection of their revenue and consumers have taxes more accurately collected at a lower cost, which means prices are less likely to rise. Almost half of the states imposing sales taxes have adopted the SST Agreement. We believe significantly more states would do so if there was federal legislation rewarding this effort by granting SST states authority to require collection by <u>all</u> remote sellers.

Retailers of all sizes, formats and channels support H.R. 3396. With this act, Congress would strengthen the SST Agreement by mandating that certain levels of simplification and uniformity be maintained and providing an enforcement mechanism to assure compliance.

A major stumbling block for Congressional action in the past arose from concerns about the burden that even an SST system would place on small business. That burden is illustrated by the results of the JCCS Study. The JCCS Steering Committee was formed to carry out a joint effort of business and government to determine the cost incurred by all sizes of business for collecting and remitting state and local sales and use taxes.

The results of this effort showed that, under the pre-SST system, the weighted average cost of compliance was 3.09% for all retailers. When broken down by retailer size, the JCCS determined the costs are:

- 2.17% for large retailers (those with sales over $10 billion)
- 5.2% for midsize retailers (those with sales between $1 million and $10 billion)
- ***13.47% for small retailers (those with sales less than $1 million)***.

The JCCS Study demonstrates that tax collection places a significant burden on all retailers and a more significant burden on small businesses in relation to their size. While the SST Agreement provides a significant reduction in the burdens and costs of collecting, many of those involved in the SST process have always recognized that there would be residual complexity that could not be removed through simplification and uniformity measures. The significance of the costs generated obviously makes one hesitate to impose the current system's burden on small business. Further, there is a consensus that the collection requirement should not be imposed on small business under any system without some meaningful protection. This opens the question as to what that protection should be.

One answer to this question has been to call for a small business exemption ("SBE"), also included in H.R. 3396. The small business exception alternative has been much debated, and it has resulted in controversy as to what is the appropriate size business to benefit from such an exception. The JCCS Study provides a starting point for measuring pre-SST costs and a method of resolving the SBE controversy. To the extent some believe the data is old or inaccurate, that data can be refreshed, data gathering methods improved and data can be verified. We believe that **compensation** is the best way to help small business deal with this residual complexity.

Compensation as a solution eliminates some of the arbitrariness created by drawing a single line between large and small business. It truly eliminates the burden on interstate commerce, since any burden on commerce would be recompensed in a mandatory system. Because of this, we believe that there should be compensation for all sellers. We believe this is the best way to deal with the residual complexity in the SST system. Compensation serves the two fold purpose of compensating sellers for their tax collection services and rewarding states for simplifying their tax systems. State officials have expressed concerns about the cost of compensation. It is interesting to note that some of them do not seem at all concerned that they are imposing these costs on businesses today!

In a mandatory system, Congress can provide that the SSTGB set a reasonable level of compensation for all sellers based on the results of the most recently conducted JCCS Study. If the SSTGB is unwilling or unable to resolve this issue of compensation, then the solution should be specified in federal legislation like H.R. 3396, establishing compensation as a minimum simplification feature. As stated above, this mechanism would not only deal with small business concerns, but also provide a carrot and stick enforcement mechanism to measure compliance with current simplification and uniformity requirements, and likewise encourage continued efforts to streamline taxes and reduce costs for all concerned.

In conclusion, JCPenney, the National Retail Federation, and most multi-channel retailers of all sizes support the passage of H.R. 3396. Retailers like JCPenney are working diligently to ensure that the SST Agreement is fair for all sellers, and that SSTGB stays focused on uniformity and simplicity. With Congress's help, passage of H.R. 3396 into law would be the appropriate next step to a modern, fair and responsive sales tax system across all participating states and sellers.

Thank you Madam Chair for the opportunity to present the views of retailers, and I welcome your questions.

The National Retail Federation is the world's largest retail trade association, with membership that comprises all retail formats and channels of distribution including department, specialty, discount, catalog, Internet, independent stores, chain restaurants, drug stores and grocery stores as well as the industry's key trading partners of retail goods and services. NRF represents an industry with more than 1.6 million U.S. retail establishments, more than 24 million employees - about one in five American workers - and 2006 sales of $4.7 trillion. As the industry umbrella group, NRF also represents more than 100 state, national and international retail associations. www.nrf.com

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