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Legal Q&A

By Bennett Sandlin, TML General Counsel

Sales Tax Sourcing Pop Quiz
(The answers are below—Don't Cheat!)

Streamlined Sales Tax Project Issue:

1. Under current law, a resident of the Town of Texasville goes to an Acme Supply store in Texasville and purchases a chain saw. Which city gets to collect local sales taxes on the purchase?
 - a. Metropolis, where Acme has its state headquarters
 - b. Texasville
 - c. None of the above

2. Under current law, a resident of Texasville drives to an Acme Supply store in Retailville to purchase a chain saw. The chain saw is shipped from the Retailville store back to the man's house in Texasville. Which town gets the sales tax?
 - a. Metropolis, where Acme has its state headquarters
 - b. Retailville, where the chain saw was purchased
 - c. Texasville, where the person lives
 - d. None of the above

3. Under previous proposals of the so-called Streamlined Sales Tax Project, a resident of Texasville goes to an Acme Supply store in Retailville to buy a chain saw. The chain saw is shipped from the Retailville store to his house in Texasville (same as #2 above). Which town gets the sales taxes under the Streamlined model?
 - a. Metropolis, where Acme has its state headquarters
 - b. Retailville, where the chain saw was purchased
 - c. Texasville, where the person lives
 - d. None of the above

Purchasing Office Issue:

4. Under current law, a resident of Texasville calls an Acme Supply store in Retailville to order a chain saw to be delivered to him in Texasville. Acme Supply ships the chain saw to the purchaser in Retailville. Who gets the local sales taxes?
 - a. Metropolis, where Acme has its state headquarters
 - b. Retailville, where the store is located and the call received
 - c. Texasville, where the person lives
 - d. None of the above

5. Prior to 2003, the Town of Cleverton convinced the Acme Construction Corporation to open a small "purchasing office" in Cleverton that contains nothing but a telephone and a single employee. In exchange for opening the office, the Town of Cleverton promised to "rebate" a

portion of any sales taxes collected there back to the company. The purchasing office accepts and processes orders for building materials and supplies for several building projects in the general Cleverton area, including projects inside the boundaries of neighboring towns Closeville and Nextown. The purchasing office consolidates the orders and purchases the materials in bulk from suppliers, then “resells” the materials to the various projects. The materials are delivered to the jobsites by the third-party suppliers. Who gets the sales taxes?

- a. Metropolis, where Acme has its state headquarters
 - b. Retailville, where the suppliers and supplies are located and from which the supplies are shipped
 - c. Nextown and Closeville, where the construction projects are located
 - d. Cleverton, where the single employee took the orders
6. Same question as #5 above, except the sale occurs after 2003. Who gets the sales taxes?
- a. Metropolis, where Acme has its state headquarters
 - b. Retailville, where the suppliers and supplies are located and from which the supplies are shipped
 - c. Nextown and Closeville, where the construction projects are located
 - d. Cleverton, where the single employee took the orders

Warehousing Issue:

7. A resident of Texasville calls the Acme Supply store in Retailville to purchase a chain saw to be delivered to him in Texasville. It turns out, however, that the store is fresh out of the particular model of chain saw the man wants. The store manager calls around and locates the proper chain saw at a warehouse in the Texas town of Shippem. The warehouse in Shippem, incidentally, does not take any order calls from customers. The Shippem warehouse then ships the chain saw to the man in Texasville. Which city gets the sales taxes?
- a. Metropolis, where Acme has its state headquarters
 - b. Retailville, where the call was received
 - c. Shippem, the city from which the chain saw was shipped
 - d. Texasville, where the person lives
8. Same as question #7, except the warehouse in Shippem also takes direct phone orders (though not necessarily from the customer in question). Who gets the sales taxes?
- a. Metropolis, where Acme has its state headquarters
 - b. Retailville, where the call was received
 - c. Shippem, the city from which the chain saw was shipped
 - d. Texasville, where the person lives

ANSWERS TO LEGAL Q&A QUIZ

1. b. **Texasville.** This one’s easy. The store and the purchaser are both in Texasville, so that town clearly “deserves” the sales taxes, which is exactly what Texas law provides.

2. b. **Retailville, where the chain saw was purchased.** Texas law sources the sales taxes to the city that provides the services to the business. (Interestingly, some states give the sales taxes to the city where the item is shipped.)

3. c. **Texasville, where the person lives.** The Streamlined Sales Tax Project is a nationwide effort to make all state sales tax laws appear nearly identical. Once that is accomplished, the theory goes, Congress will be willing to let localities collect sales taxes on certain Internet and catalogue sales. Previous proposals for a uniform set of sales tax laws would have required local sourcing at the place to which goods are shipped. Texas has rejected this idea so far. Recently, there have been indications that the Streamlined Project might tolerate different local sourcing, though this is far from settled. In the meantime, Texas has chosen not to participate in the Project because of this issue.

4. b. **Retailville, where the store is located and the call received.** This one's pretty easy. The fact that the man places his order by phone call instead of in person doesn't change much. The store from which the chain saw is shipped is still the place of business that determines sourcing.

5. d. **Cleverton, where the single employee took the orders.** Prior to 2003, the idea of shifting sales taxes from one city to another merely by opening a "shell" order-taking office, in exchange for sales tax rebates, was dreamed up by clever accountants at some large corporations. A few cities briefly tried this arrangement, but it was outlawed by H.B. 3534 during the 2003 Legislative Session.

6. b. **Retailville, where the suppliers and supplies are located and from which the supplies are shipped.** H.B. 3534 in 2003 returned sales tax sourcing to the city that had the store and shipped the supplies.

7. b. **Retailville, where the call was received.** Now things start to get more complicated! When there's more than one place of business involved in a transaction—typically a store and warehouse arrangement—the general rule is that the place from which the goods are actually shipped gets the sales taxes. For a warehouse to be a "place of business" under the Texas Tax Code, however, the location must receive three or more orders for goods during a year. Since the warehouse in Shippem doesn't take any orders, the sourcing defaults to the Retailville store where the customer's call was received.

8. c. **Shippem, the city from which the chain saw was shipped.** Because the warehouse receives three or more purchase calls a year, it is considered a place of business under the Tax Code. Thus, the general rule that sales taxes are sourced to the place from which the item is shipped is followed. Historically, this distinction is the cause of some consternation for some Texas cities. The city where the supply store is located may feel that it is unfair that a simple change of business practices, such as beginning to receive orders at a warehouse, can trigger the loss of sales taxes from the city that was formerly receiving them. Cities where warehouses are located, on the other hand, believe there is nothing unfair about the practice, since warehouses often require just as many city services as retail establishments. As an organization, TML has historically remained neutral on such complicated sourcing disagreements.