



Legislative UPDATE

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Comptroller Proposes Internet Sales Tax Sourcing Rule Changes

In response to the United States Supreme Court decision in *South Dakota v. Wayfair* (2018) and recent *Wayfair*-related legislation passed during the 2019 legislative session, the Texas comptroller published [proposed rule changes](#) in the Texas Register today. Of particular importance to Texas cities, the proposal would change the sales tax sourcing of certain internet marketplace purchases to the destination city.

How will these changes affect your community? Each city will need to analyze how the proposed rule changes will impact their sales tax revenues because every city will be affected differently. Some cities stand to lose potentially significant amounts of sales tax revenue because of the change to how internet orders are sourced, while others would potentially see net gains of sales tax revenue.

The *Wayfair* opinion concluded that state and local sales taxes may be collected from remote sellers that have no physical presence in a state. In order to fully implement *Wayfair*, the Texas legislature passed two bills during the 2019 legislative session:

- H.B. 1525 requires an online marketplace (e.g., Ebay, Amazon, or Walmart) to collect sales taxes on marketplace sales instead of potentially requiring each individual seller on that marketplace to do so. Additionally, it requires the sales taxes associated with marketplace sales to be sourced to the *destination* to which the marketplace goods are shipped.
- H.B. 2153 gives remote sellers the option to either: (1) collect and remit the actual sales taxes owed based upon the shipping destination; or (2) collect a simplified “single local

use tax rate” of roughly 1.75 percent on all sales. Remote sellers who collect the single local use tax rate send the money to the comptroller, who remits the revenue to local taxing entities based upon their existing proportion of the local sales tax base.

The comptroller’s proposal makes changes to 34 Texas Administrative Code Section 3.334, which deals generally with local sales and use taxes. Many of the changes will not significantly alter the collection of city sales and use taxes. Other changes are quite beneficial to Texas cities. For instance, the proposal generally requires sellers to collect local use taxes, a burden that currently falls on the purchaser of goods under certain circumstances.

However, the proposed change affecting orders made on the internet could significantly alter the sales tax base in some Texas cities. The comptroller proposes to add Section 3.334(c)(6), which states that “internet orders are not received at a place of business of the seller in Texas.” This statement represents a shift from the current rule, which generally provides that, when an internet order is received by a seller at a place of business in Texas, the sale is consummated at the place of business at which the order is received. The new rule is intended to address the current difficulty of identifying exactly where internet orders are received.

Under the current rule, sales taxes on internet orders made by Texas residents can potentially be sourced to the community in Texas where a given place of business is located. Under the *proposed* rule, sales taxes on internet orders made by Texas residents wouldn’t automatically be sourced to the community where the place of business is located. Instead, sales tax sourcing would vary depending on the following considerations:

- Is the internet order placed using the seller’s device? Under the proposal, if a purchaser places an order for a taxable item with a seller using the internet on a computer or device of the seller at the seller’s place of business in Texas, the sale is consummated at that place of business, regardless of where the order is fulfilled. (This provision would not apply to an order placed on the internet using the *purchaser’s* device.)
- Is the internet order fulfilled from a place of business of the seller in Texas? Under the proposal, except for the scenario above when an internet order is placed using the seller’s device, if a seller fulfills an internet order at a location that is a place of business of the seller in Texas, the sale is consummated at the place of business where the internet order is fulfilled.
- If the internet order is fulfilled from a location in Texas that is not a place of business of the seller in Texas, the sale is consummated at the location in Texas to which the order is shipped or delivered, or at which the purchaser of the item takes possession. In other words, the sales taxes are sourced to the destination to which the order is delivered.
- If the internet order is fulfilled from a location outside of Texas, the sale is not consummated at a location in Texas. However, in accordance with the *Wayfair* opinion, local use taxes are due and sourced to the destination to which the order is delivered.

Some cities have relied for years upon sales taxes being sourced to their city from internet orders within the state under the current rule structure. Further, some cities may have entered into sales tax rebate incentive agreements with businesses under Chapter 380 of the Local Government Code with the understanding that sales taxes from internet orders would be sourced to those cities. Acknowledging this issue, the comptroller's rules provide that the new internet order rules would not apply to sales of taxable items for internet orders made by a seller who entered into a Chapter 380 economic development agreement before September 1, 2019. The grandfathering provision would remain effective until December 31, 2022, at which point the new internet order rules would apply, assuming they are finally adopted.

Comments on the proposal may be submitted to Teresa G. Bostick, Director, Tax Policy Division, P.O. Box 13528, Austin, Texas 78711-3528. Comments must be received no later than 30 days from the date of publication of the proposal in the *Texas Register*. The earliest possible date of adoption is February 2, 2020. Individual cities with concerns about the new rules should express those concerns through the comment process.

Please contact Bill Longley, TML Legislative Counsel, with questions at bill@tml.org or (512) 231-7400.

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