

# Tax Workshop: Sales and Use & Meals and Rooms Taxes

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# Quick Overview

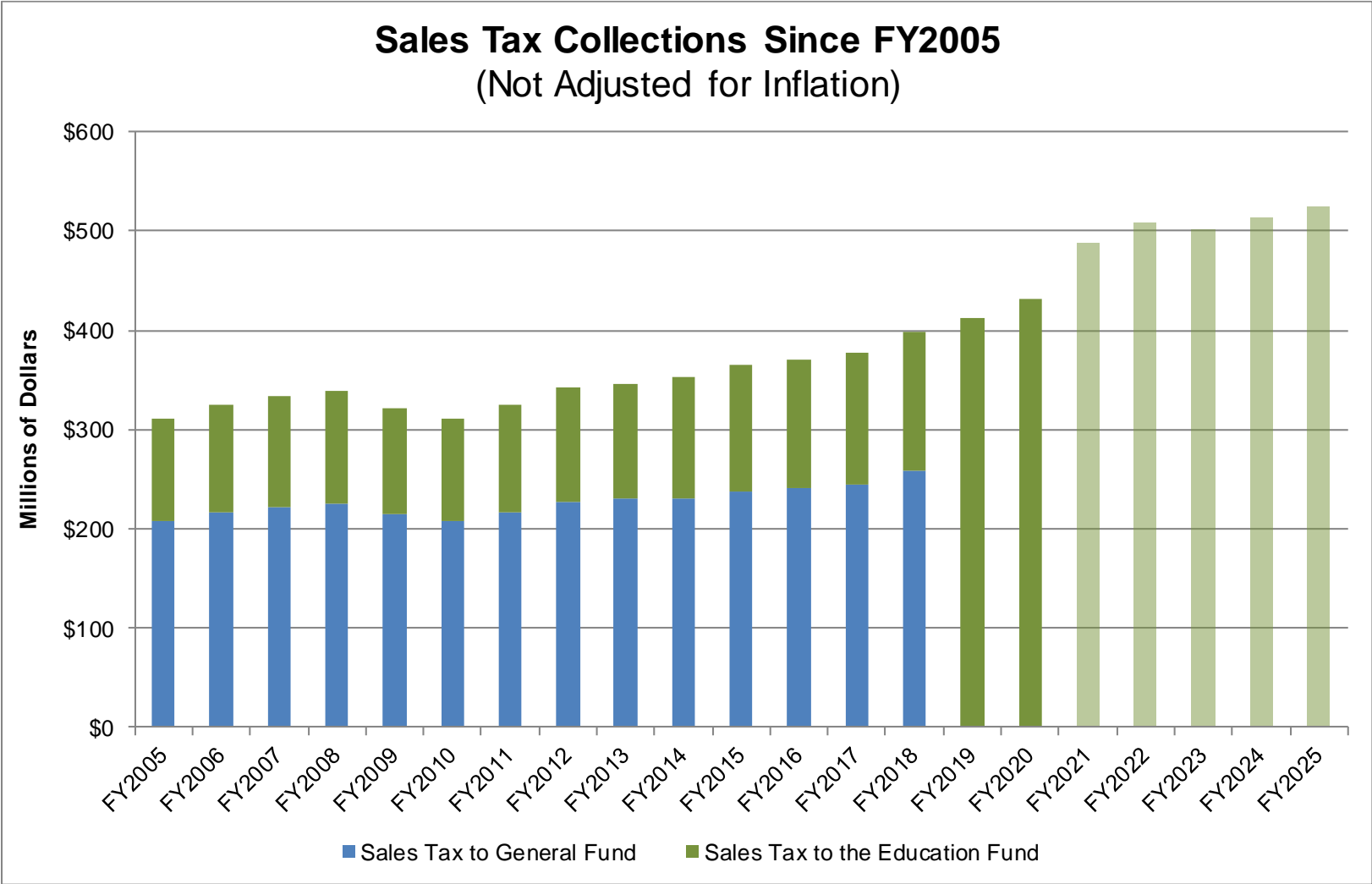
- **Sales and Use tax**

- \$412.5 million in FY2019, \$488.4 million FY2021
- 100% allocated to the Education Fund (new for FY2019)
- 6% charged on retail sales of tangible personal property unless exempted.
- Many exemptions
- Some municipalities have a 1% local option sales tax

- **Meals and Rooms tax**

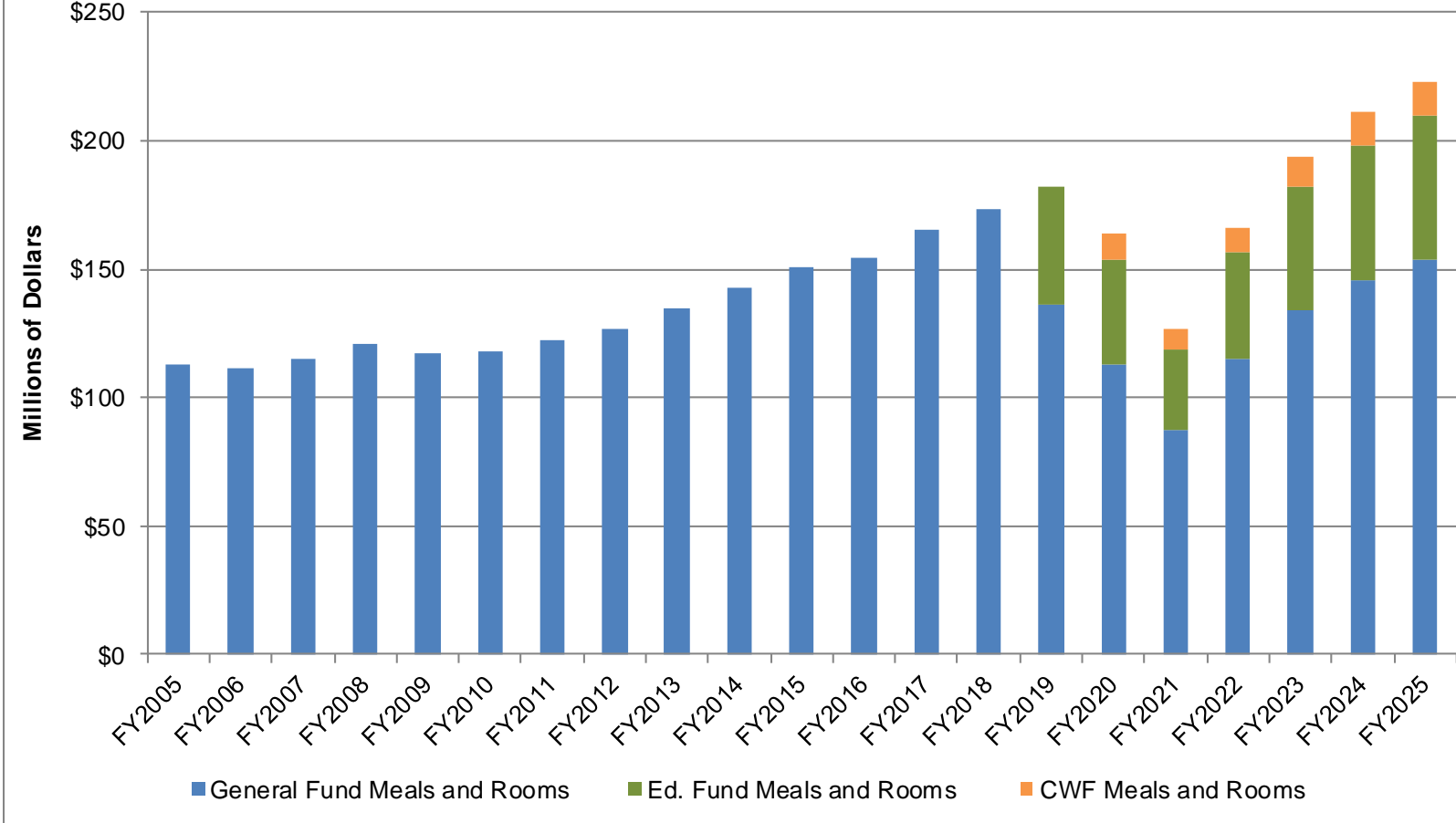
- \$182 million in FY2019, \$126.4 million in FY2021
- 69% to General Fund, 25% to Education Fund, 6% to Clean Water Fund
- 9% on sales of prepared food in restaurants, bars, etc.
- 9% on room rentals, including meeting rooms in hotels
- 10% on sales of alcoholic beverages served in restaurants, bars, etc.
- Some municipalities have an additional local option 1%

# Quick Overview



# Quick Overview

**Meals and Rooms Collections Since FY2005**  
(Not Adjusted for Inflation)



# For another day...consumption taxes

- Excise taxes
  - cigarettes, tobacco and alcohol, motor fuel
- Health care taxes
  - providers, payers, and those who pay Medicaid premiums
- Other consumption taxes
  - fuel tax on retailers of heating oil, propane, kerosene, dyed diesel fuels, natural gas, electricity, and coal
  - solid waste franchise tax
  - electric generating tax
  - solar energy capacity tax

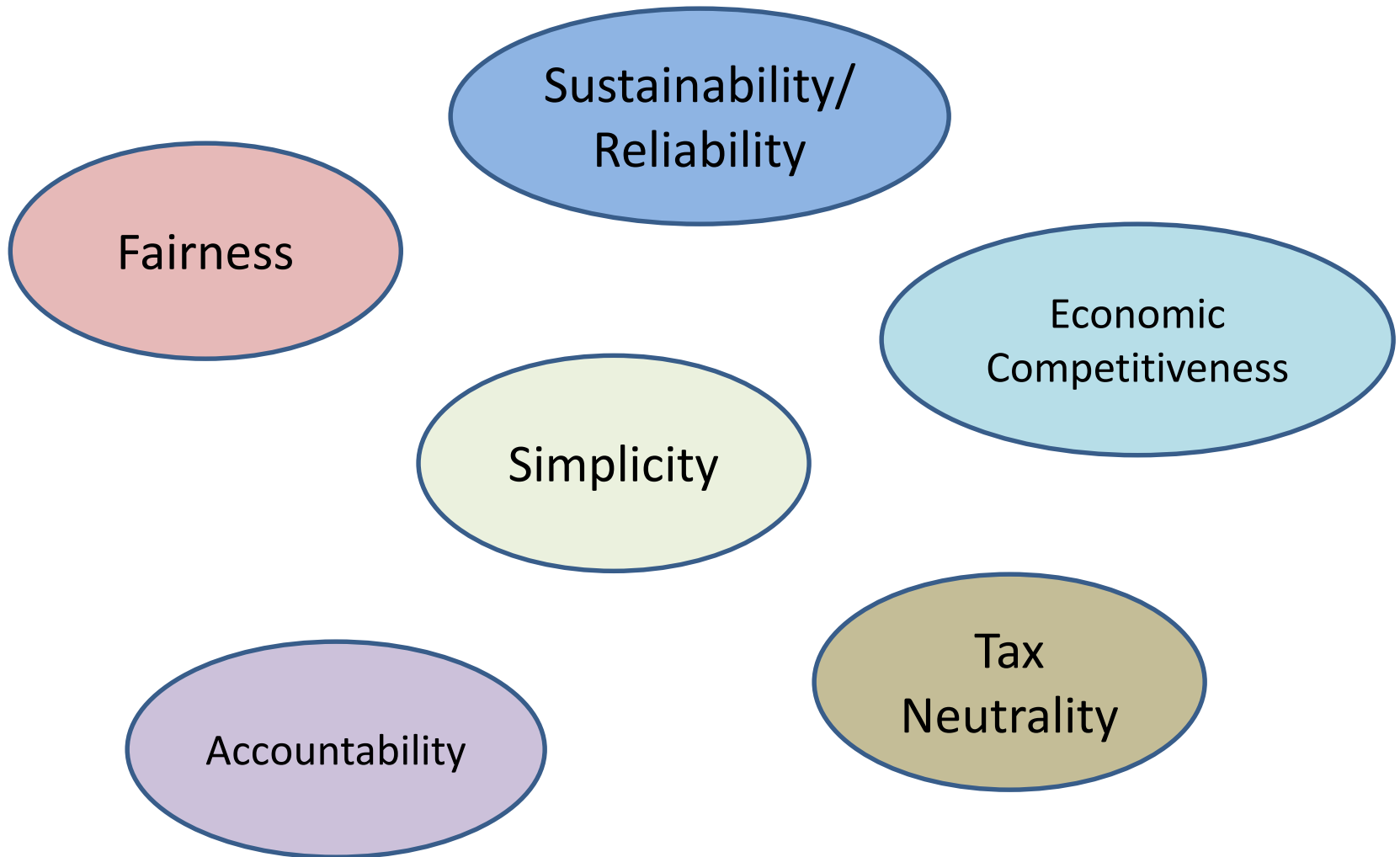
Consumption taxes provided about 32 percent of State revenues in FY2015

## State Revenue Sources for Fiscal Year 2015



State Revenue  
\$3,607.3 Million

# Sales and Use: The 6 pillars



# Reliability and Sustainability

- **Numerous factors impacting reliability**

- **Sales and Use:**

- Economic conditions: historically, large decreases in revenue during the recession
      - Fiscal stimulus during COVID has changed the dynamic
    - Population growth: if population increases, more consumption of goods, more revenue
    - Demographic change: consumers shift consumption patterns
      - Example: older people more likely to use services (healthcare) than younger people
    - Shifts to service-based economy: S&U tax is not levied on services, which are a growing portion of our economy
    - Composition of retail and e-commerce sales
      - Increasing reliance on e-commerce sales post-Wayfair decision and due to COVID-19 pandemic

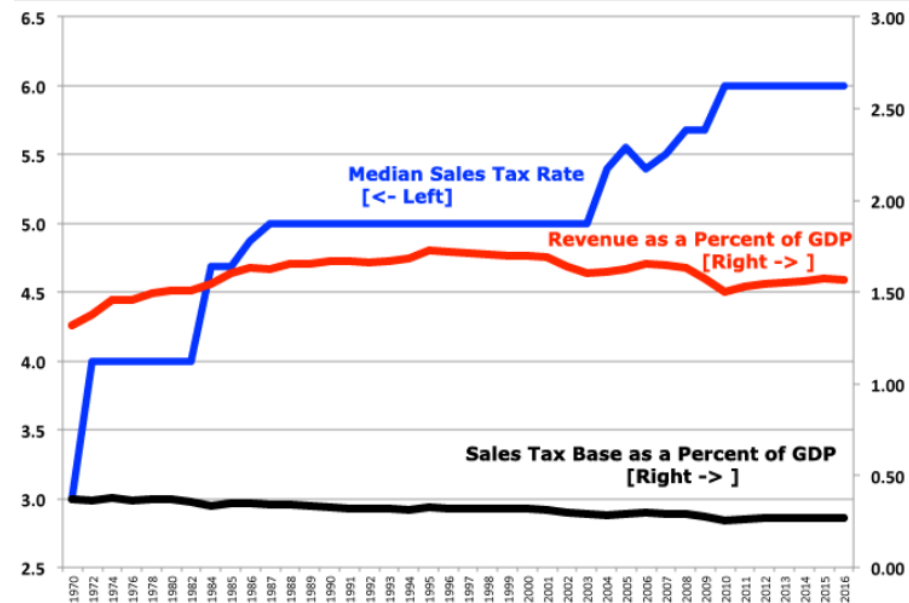
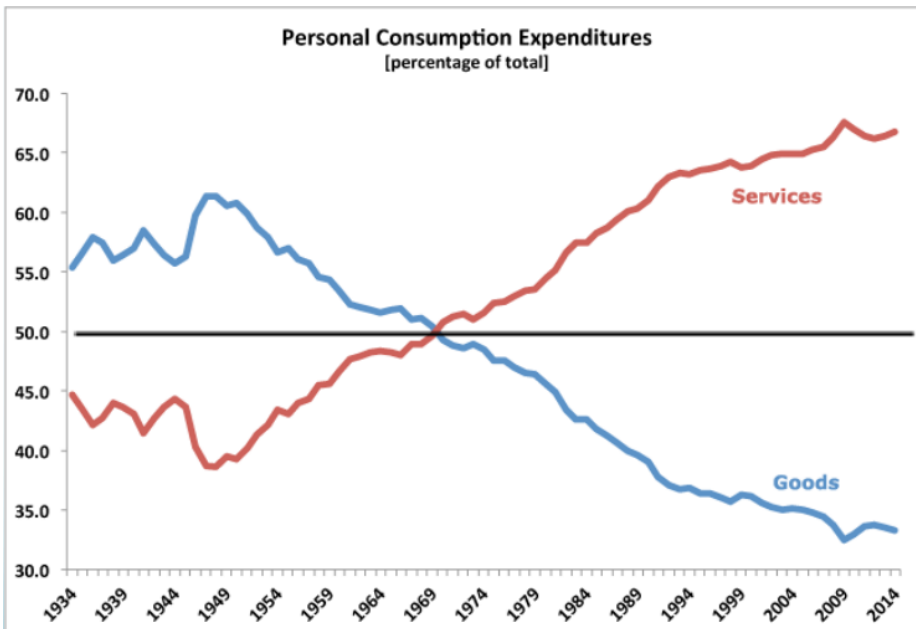
- **Meals and Rooms:**

- Economic forces: tourism is a significant driver (about 55% of all meals revenue, almost all of rooms tax revenue)
      - COVID-19 pandemic has had a significant negative impact on restaurants and hotels
    - “Disruptors:” new sharing economy (AirBnB, VRBO, etc.)



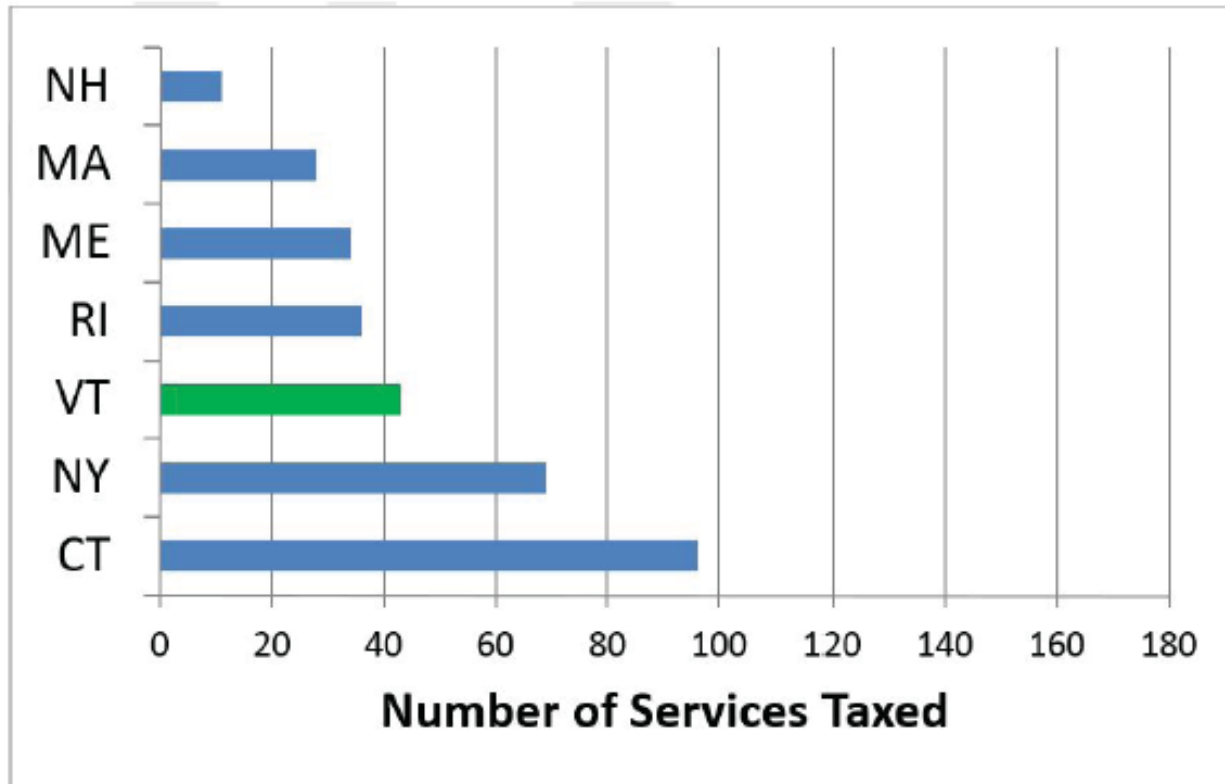
# Sales and Use: Services vs Goods

## Nationwide Trends in the Sales and Use Tax



Source: Federation of Tax Administrators, FTA Services Taxation Survey 2017

# Sales and Use: Services vs Goods



Source: Vermont Department of Taxes: Sales Tax on Services Study, January 2016

Examples of services we tax: Dog grooming, boarding, ski rentals, landscaping

# Fairness

- **Consumption taxes (including S&U and M&R) are generally regressive (vertical equity)**
  - Younger and/or lower-income households spend a greater share on income on goods.
  - However, the tax rate is 6% no matter your ability to pay (horizontal equity)
- **However: Vermont exempts many items to make the S&U tax less regressive**
  - Groceries, clothing, healthcare products exempt because lower-income households spend a higher portion of their income on these items

# Simplicity

- **Exemptions from sales and use tax can make system complex**
  - What is taxable and what is not?
- **Streamlined Sales Tax Agreement**
  - Vermont joined in 2007, 24 states total
  - Standardizes the definitions of products
    - Example: “Tobacco” means cigarettes, cigars, chewing or pipe tobacco, or any other item that contains tobacco.
  - Eases compliance for multi-state sellers

# Simplicity

## Clothing — Exempt

- Aprons, household & shop
- Athletic supporters
- Baby receiving blankets
- Bathing suits & caps
- Beach capes & coats
- Belts & suspenders
- Boots
- Coats & jackets
- Costumes
- Diapers, child & adult, incl. disposable diapers
- Earmuffs
- Footlets
- Formal wear
- Garters & garter belts
- Girdles
- Gloves & mittens for general use
- Hats & caps
- Hosiery
- Insoles for shoes
- Lab coats
- Neckties
- Overshoes
- Pantyhose
- Rainwear
- Rubber pants
- Sandals
- Scarves
- Shoes & shoelaces
- Slippers
- Sneakers
- Socks & stocking
- Steel-toed shoes
- Underwear
- Uniforms, athletic & nonathletic
- Wedding apparel

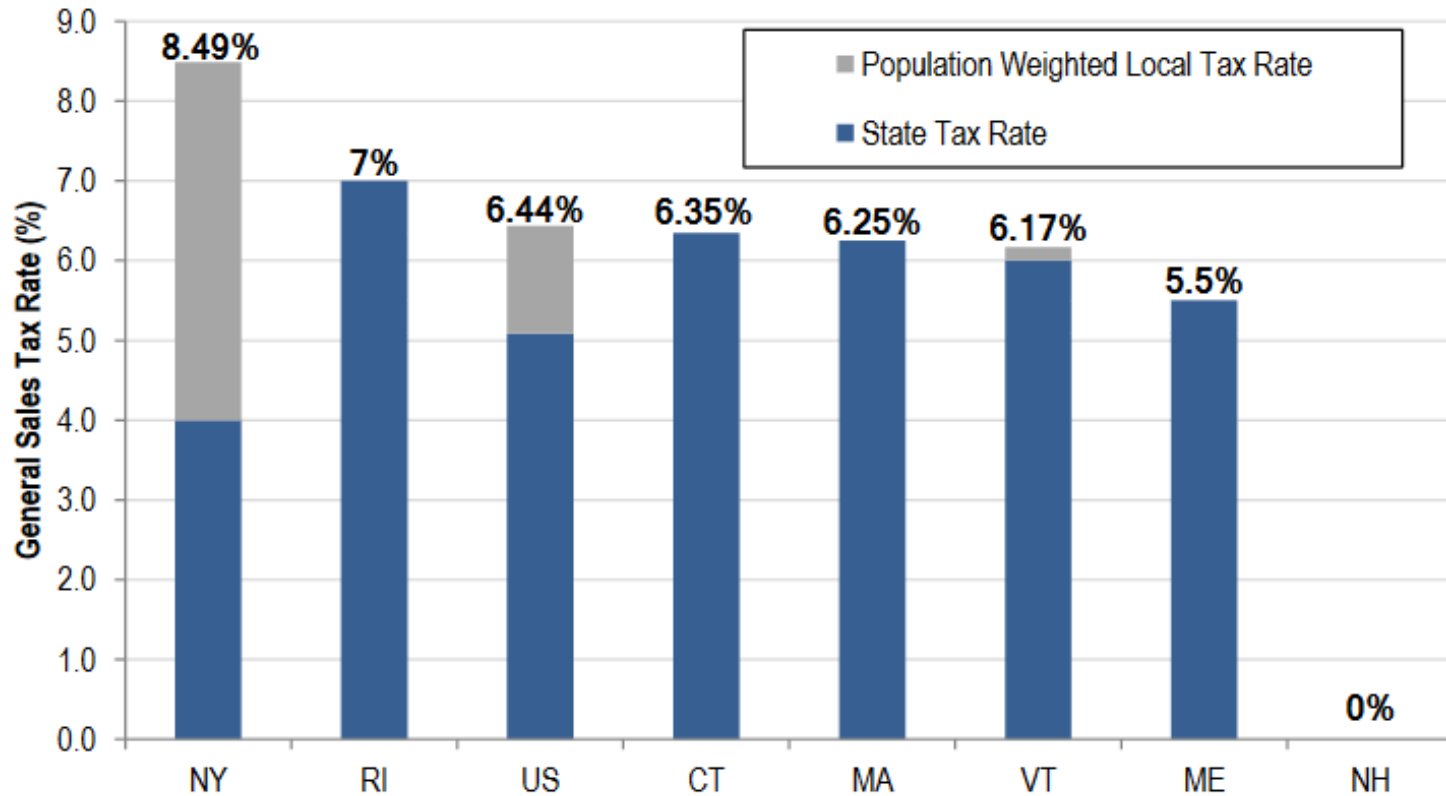
## Clothing Accessories or Equipment — Taxable

- Belt buckles sold separately
- Costume masks sold separately
- Patches & emblems sold separately
- Sewing equipment & supplies including, but not limited to, knitting needles, patterns, pins, scissors, sewing machines, sewing needles, tape measures & thimbles
- Sewing materials that become part of “clothing,” including, but not limited to, buttons, fabric, lace, thread, yarn & zippers
- Briefcases
- Cosmetics
- Hair notions, including, but not limited to, barrettes, hair bows & hair nets
- Handbags
- Handkerchiefs
- Jewelry
- Sunglasses, nonprescription
- Umbrellas
- Wallets
- Watches
- Wigs & hairpieces

# Economic Competitiveness

- **Sales tax: potential cross-border concerns**
  - Below the New England average but NH has no sales tax at all.
  - Comparisons difficult because states exempt different goods
- **Meals and rooms: similar to our neighbors**
  - Maine and NH have meals tax rate of 8% and 9% respectively
  - Other states have varying lodging taxes
    - Connecticut: 15%
    - Massachusetts: 5.7%
    - NH: 9%
  - Many states have cities that charge a local rooms tax rate
    - 14.75% in NYC, 15.75% tax in New Orleans.

# Economic Competitiveness



# Tax Neutrality

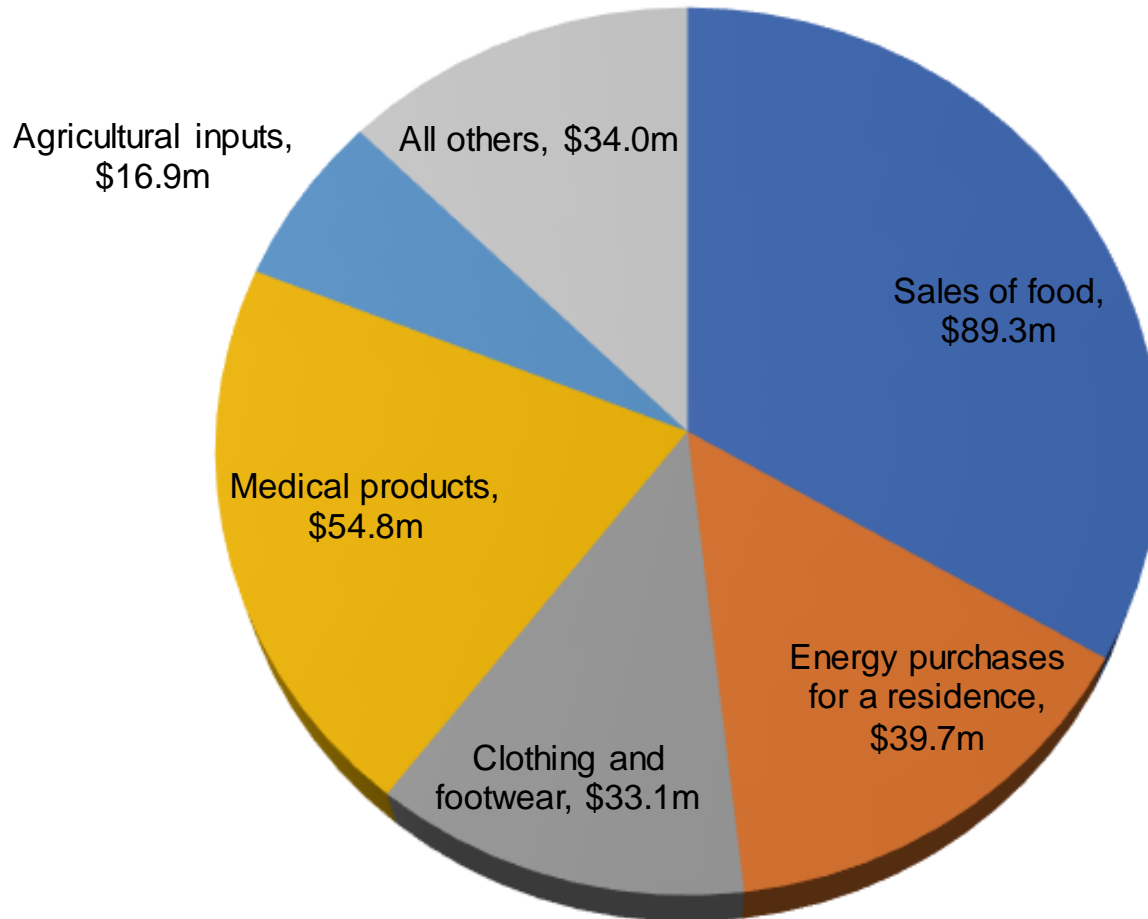
- **Sales and Use: likely to influence behavior to some extent**
  - Individuals may shop in New Hampshire to avoid sales and use tax.
  - In the past, individuals may have shopped online to avoid sales tax
  - Sales taxes may influence behavior (S&U on soda)
- **Meals and Rooms: Moving towards tax neutrality**
  - Any room offered for sleeping that is rented more than 15 days in a calendar year is subject to the tax
  - AirBnB and other online travel agents are fully collecting M&R tax.



# Accountability

- **Sales tax:** Large number of exemptions but are regularly reviewed
  - Tax Expenditure report every 2 years
    - \$267.8 million in exemptions in FY2019
    - Many of these for increasing progressivity
      - Medical products: \$54.8 million
      - Clothing and footwear: \$33.1 million
      - Groceries: \$89.3 million
  - Vermont tries to avoid charging sales tax to intermediate business purchases
    - Avoids “tax pyramiding”
  - Many exemptions are not estimated because data does not exist to accurately do so.
    - Example: sales tax exemption for tracked vehicles
- **Meals and Rooms tax:** fewer exemptions
  - \$9.2 million in FY2017.
    - Exemptions for food served by schools and grocery-type items furnished for take-out (pies, cakes, uncooked pizzas)

## FY2019 Estimated Sales Tax Exemptions: \$267.8 million



# Internet and sales tax

- When a state relies on another person to collect and remit a tax, this is called a “trust tax,” because the person collecting the tax holds the collections in trust for the State.
- A state has to be able to exercise jurisdiction over the person collecting the tax in order to enforce their collection obligation. There are limits placed on a state’s power to tax certain activities.

# U.S. Commerce Clause

- The Commerce Clause of the U.S. Constitution reserves to Congress the power to regulate trade among the states. This is often referred to as “interstate commerce.”
- A state cannot tax goods in interstate commerce in a way that:
  - Discriminates against interstate commerce, or
  - Imposes an undue burden on interstate commerce

# *Quill v. North Dakota* (1992)

- An office supply company called Quill solicited and sold goods in North Dakota via U.S. mail, but had no physical presence in the state. North Dakota sued Quill to collect and remit use tax on goods purchased for use in the state.
- Under the Commerce Clause, the U.S. Supreme Court ruled that a state cannot force a seller to collect and remit sales tax unless the seller has a physical presence in the state.
- In the internet age, this meant that online retailers who lacked a physical presence in a state with a sales tax were not obligated to collect and remit sales tax.

# Two equity problems

- As online sales increased as a proportion of all sales, sales and use tax revenues paid to Vermont went down.
- When online retailers did not collect and remit, they gained a competitive edge over brick and mortar retailers.

# *South Dakota v. Wayfair* (2018)

- South Dakota passed a law that required any vendor, regardless of physical presence in the state, to collect and remit sales tax if the vendor annually delivered goods or services into the state that:
  - exceeded \$100,000 of sales, or
  - made 200 or more individual transactions.
- Several online retailers including Wayfair, Inc., brought suit to invalidate the law.
- U.S. Supreme Court ruled that in light of subsequent developments, the physical presence requirement of *Quill* is “incorrect and unsound”

## *Wayfair* (cont.)

- U.S. Supreme Court concluded that South Dakota's economic presence test did not create an undue burden.
  - The law excluded smaller vendors (\$100,000 or 200 transactions).
  - South Dakota was a member-state of the Streamlined Sales and Use Tax Agreement, reducing the compliance burden on sellers.
- The result is a sense that there is a clear “safe harbor,” provided a state comes with the South Dakota economic presence requirement.



# Vermont anticipated

- Since 2007, Vermont has been a member state of Streamlined Sales and Use Tax Agreement
- Act 134 of 2016:
  - Vermont adopted SD-style requirements for sales tax collection: \$100,000 of sales or 200 transactions in the prior 12-month period
  - Contingent effective date: on the first day of the first quarter after *Quill* was overturned.
  - Following *Wayfair*, these provisions became effective July 1, 2018.

# Post-*Wayfair* Measures

- *Wayfair* allowed Vermont to collect and remit on direct sales into Vermont by a vendor who is not physically located here.
- However, marketplace facilitators, such as Amazon, were not required to collect and remit for indirect or facilitated third party sales. For companies like Amazon, these types of sales can represent the majority of their sales.

# Post-*Wayfair* Measures (cont.)

- While some internet sales and fulfillment are made directly through vendors, many vendors also sell through other businesses that provide a marketplace for online sales. These marketplaces:
  - Promote products
  - Facilitate payments
  - May or may not handle fulfillment
  - Provide other services, such as accounting and inventory tracking

# Marketplace Facilitators v. Marketplace Sellers



- Marketplace facilitator:
  - A business that contracts with third-party sellers to promote their sale of physical property, digital goods, and services through an online marketplace.
  - E.g., Amazon or Ebay
- Marketplace seller:
  - A business that contracts with a marketplace facilitator for services to assist in the sale of their products.
  - E.g., a producer of widgets

# Why is this a problem?

- Compliance issues to collect and remit from every far flung individual vendor
  - Marketplace facilitators encompass a large number of sellers
    - 55% of Amazon's total sales were third party sales in 2017
    - 25% of Amazon's third party sales in 2017 were from non-US global sellers
  - As Amazon has begun collecting sales tax on direct sales, its third party seller services have boomed
- Threshold problems – some small vendors could split sales to avoid the tax

# Vermont's marketplace facilitator law

- Act 46 of 2019: Vermont enacted a marketplace facilitator law.
  - Effective date: June 1, 2019.
- Imposes the same collection requirements on marketplace facilitators that were imposed on remote sellers following *Wayfair*:
  - \$100,000 of sales or 200 transactions in the prior 12-month period

# Vermont's marketplace facilitator law

- Who is a “marketplace facilitator”?
  - A person who contracts with a marketplace seller to facilitate for consideration the sale of products through a physical or electronic marketplace that it operates.
  - A marketplace facilitator must directly or indirectly engage:
    - in one or more of listed affiliate activities; and
    - in providing any of the listed services to sellers.

# Vermont's marketplace facilitator law

- Affiliate activities
  - communicate offer and acceptance between buyer and seller
  - own or operate the infrastructure or technology that connects buyer and seller
  - provide a virtual currency to purchase marketplace items
  - develop software or research related to marketplace activities



# Vermont's marketplace facilitator law

- Services to sellers

- payment processing services;
- fulfillment or storage services;
- listing products for sale;
- setting prices;
- branding sales as those of the marketplace facilitator;
- order taking;
- advertising or promotion; or
- providing customer service or accepting or assisting with returns or exchanges.

# Vermont's marketplace facilitator law

- Marketplace facilitators are required to:
  - collect and remit sales tax on behalf of sellers using its marketplace to conduct retail sales; and
  - certify to each seller that it will collect and remit tax on sales of taxable items made through its marketplace.
  - Once notified, the seller will not need to collect and remit Vermont sales tax for sales made through that marketplace.
- Marketplace sellers will still be required to collect and remit tax on sales not made through the marketplace.

# Meals and Rooms Tax and Alcoholic Beverages Tax

- Vermont law imposes tax on meals, rooms, and alcoholic beverages.
  - 9% rooms tax is collected by an “operator” of a “hotel” on the “rent” received for “occupancy.”
  - 9% meals tax is imposed on a “taxable meal.”
  - 10% tax is imposed on “alcoholic beverages,” which are beer, wine, spirits, or fortified wines served for immediate consumption.

# Rooms tax and the Internet

- An operator may be a traditional lodging establishment such as a hotel or bed and breakfast, or an operator may be a property owner offering a bedroom in their home for short term rent.
  - Hotel includes: inns, motels, tourist homes and cabins, ski dormitories, ski lodges, lodging homes, rooming houses, furnished-room houses, boarding houses, private clubs, and short-term rentals.

# Short-term rentals

- What is taxable?
  - Sleeping accommodations that are:
    - offered to the public
    - for a consideration
    - on premises operated by a private person, entity, institution, or organization; and
    - rented for a total of 15 or more days in any one calendar year.
- Operators of short-term rentals must collect and remit the 9% rooms tax.

# Short-term rental requirements

- Advertising and licenses for tax collection
  - Operators of short-term rentals who advertise on an internet platform must post their own meals and rooms tax account numbers on ads.
  - Operators who use an internet platform such as Airbnb.com may post the meals and rooms tax account number used by the platform. When using the platform's tax account number, there is no need to obtain a Vermont meals and rooms tax account.
- Contact information
  - Operators must post certain contact information within the rental unit.

# Short-term rentals: AirBnB

- AirBnb faced litigation in a number of states regarding whether they had to collect and remit rooms tax.
- In 2016, AirBnB and the State of Vermont entered into an agreement for AirBnB to collect and remit the rooms tax.
- For internet platforms that are not collecting the tax, Vermont authorizes the Department of Taxes to require informational reporting.

# Online Travel Companies

## Hotel Model

- A traveler goes to the website of a hotel in Vermont and books a room.
- The traveler stays in the hotel, and is charged the hotel rate, plus a 9% rooms tax.
- No other parties are involved.
- The hotel keeps the room charge and forwards the \$9 to the State.



# Online Travel Companies

## Merchant Model

- When a traveler uses an online travel company (the “merchant” model), the traveler books a hotel through the OTC 's website.
- The traveler pays one single charge to the OTC, which includes:
  - room rate agreed upon between OTC and hotel
  - taxes owed on that amount, and
  - The remainder, which is kept by the OTC as its fee.

# Merchant model example

- Traveler pays OTC \$109
  - \$100 for room rate
  - \$9 for taxes
- OTC pays hotel \$87.20
  - \$80 for agreed room rate
  - \$7.20 representing 9% tax on \$80
- OTC keeps \$21.80 (\$109 minus \$87.20).
- State receives \$7.20 rather than \$9 paid by traveler

# Litigation ensued

- Numerous states and cities sued OTCs claiming they fit their existing definitions of “hotel” or “operator.”
- Litigation results were mixed, but trend in favor of the OTCs.
- Other states have sought legislative amendments to clarify that the tax is imposed on entire amount paid by the customer to the OTC.

# States with laws taxing full amount collected by OTC

- New York (2010)
- North Carolina (2011)
- South Carolina (2011)
- Georgia (2012)
- Minnesota (2012)
- Oregon (2012)
- Wyoming (2015)
- Rhode Island (2015)
- Maryland (2016)
- Pennsylvania (2018)
- **Vermont (2019)**



# Vermont's update to rooms tax

- In Act 71 of 2019, Vermont amended the rooms tax definitions to require OTCs (as “booking agents”) to collect tax on the entire price paid by the customer.
- Booking agents are subject to the same collection and remittance requirements as other operators.
- Effective date: July 1, 2019.