

March 14, 2018

Chairman Jeffrey Sanchez
House Ways and Means Committee
State House
24 Beacon Street
Room 243
Boston, MA 02133

Re: Opposition to Section 49 of HB 2 – Accelerated Sales Tax Remittance By Payment Processors

Dear Chairman Jeffrey Sanchez:

The Electronic Transactions Association (“ETA”) urges the Ways and Means Committee to **oppose Section 49 of HB 2**. This provision directs the Department of Revenue (“DOR”) to formulate rules and regulations to require third party payment processors to receive and remit sales tax from retail merchants on a daily basis. This is an expensive solution in search of a problem and has been rejected in every state where it has been considered.

ETA is the leading trade association for the payments industry, representing more than 500 companies that offer electronic transaction processing products and services. ETA’s members include all parts of the electronic payments ecosystem including financial institutions, acquiring banks, merchant service providers and processors, and payment card networks. ETA member companies are creating innovative offerings in financial services, revolutionizing the way commerce is conducted with safe, convenient, secure, and rewarding payment solutions.

Executive Summary

- **Accelerated sales tax remittance by payment processors is not a cost-effective proposal. A recent State Tax Research Institute study estimates this proposal will cost \$1.22 billion in up-front costs and \$28 million annually.**
- **This sales tax collection scheme has been rejected by every state where it has been considered and has been dismissed by the National Conference of State Legislatures as “not a solution.”**
- **The payments ecosystem has been developed over the last 50 years to quickly, safely and accurately process and settle transactions. This proposal will require building a duplicative system to run parallel with a well-established complex system of interrelated companies, here in the U.S. as well as globally.**
- **The Commonwealth would have to create, thoroughly test and implement a new remittance channel to receive payments on a daily basis that seamlessly integrates with multiple payment processors servicing Massachusetts merchants. Additionally, it would have to pay royalties in order to collect taxes it can already collect for free.**
- **The proposed change would not affect sales tax on purchases made with cash and checks, so the Commonwealth would have to run two parallel collection systems. In addition, it would require reconciliation of daily reports for each Massachusetts retailer collecting and remitting sales tax, along with the monthly retail reports aggregating the cash and check transactions.**

Background and Recommendation

A related provision was included in the last governor’s budget and the legislature chose to direct DOR to seek public comment as to the feasibility of such a daily remittance scheme. On November 1, 2017, the DOR concluded: “accelerated sales tax remittance cannot be implemented cost-effectively...”

Accelerated Sales Tax Collection Has Been Previously Studied and Rejected

This issue has been studied and rejected by every state in which it has been considered, and it was dismissed by the National Conference of State Legislatures.

Connecticut

In Connecticut, The Department of Revenue Commissioner studied the cost effectiveness of implementing a similar proposal and determined that daily sales tax collection and remittance by payment processors is not cost effective. In fact, Commissioner Kevin Sullivan called it **“a solution in search of a problem or at least it’s the wrong solution.”** In his testimony on March 22, 2016 to the Connecticut Finance Committee, he stated that “Unfortunately, what this proposal will do is add significant cost to credit card processors, retailers, and -ultimately- taxpayers. It will also add significant costs at [the Connecticut Department of Revenue]. Those who will overwhelmingly bear this cost in added fees and expenses are retailers who already meet their state sales tax obligations in full and on time.”

The National Conference of State Legislatures

The bipartisan National Conference of State Legislatures Executive Committee Task Force on State and Local Taxation carefully examined “real-time” remittance of sales taxes by parties other than the taxpayer, such as a payment processor, and concluded that “...’real time’ sales tax process is not a solution.”

Current System

The payments ecosystem has been developed over the last 50 years for quickly, safely and accurately processing and settling transactions. The electronic payments industry includes thousands of companies ranging in size from public Fortune 500 companies to small, local sales organization and tech firms. The current payments ecosystem does not contemplate calculating and remitting sales taxes owed by merchants to the Commonwealth or any other parties. *See Appendix A.*

The Proposal

The proposal is not cost effective and would require thousands of interconnected parties to build a new system to compute and remit sales tax on top of the current system. Those interconnected parties have spent decades building and delivering a secure global payment services network for merchants and consumers.

- The proposal will require redesigning a complex, long-established system of interrelated companies, here in the U.S., as well as globally.
- Every Commonwealth merchant, including the Commonwealth itself, will have to update

and test its point of sale system – costing millions of dollars, just for IT. These costs will be ultimately borne by Massachusetts merchants and their customers.

- Generally, the system is designed to process gross amounts for authorization – inclusive of sale and sales tax amounts. The settlement functions do not contemplate functionality to calculate, collect, retain, remit and reconcile state or local sales tax amounts: in the current payment environment, merchants bear the responsibility to calculate, collect, and remit applicable taxes as required by local jurisdictions.
- The Commonwealth would have to create, thoroughly test and implement a new, duplicative, remittance channel to receive the payments that seamlessly integrates with all payment processors servicing Massachusetts merchants.
- The proposed change would not affect sales tax on purchases made with cash and checks, so the Commonwealth would have to run two collection systems as well as reconcile the new payment card daily reports associated with each retailer with the monthly retail reports aggregating the cash and check transactions.
- The process would significantly decrease the attractiveness of the Commonwealth as a place to do business.

Effect on Massachusetts Merchant Payments Ecosystem

The proposal is not cost effective for merchants. The merchants and merchant Point of Sale (“POS”) ecosystem is not a ‘one-size-fits-all’ proposition – there are multiple variations (e.g. “Brick and Mortar,” Internet, cellphone, peer-to-peer, mobile-food trucks). In larger merchant operations, the POS may also include multiples of legacy systems from previous acquisitions and proprietary software systems like payroll, inventory, and others.

Effect on Processors

The proposal is not cost effective for processors. Processors play an instrumental role in the payments system. They facilitate the ability of merchants to accept card payments from consumers at brick and mortar locations, online or through a mobile device. They facilitate the authorization of the purchase as well as the settlement of funds from the card holder’s bank to the merchant to complete the transaction. The proposed changes would trigger monumental and costly changes to authorization and settlement, as well as fundamentally altering processors’ role in the payments system.

Effect on Networks

This proposal is not cost effective for payment card networks. The effect on payments networks cannot be overstated. Payment networks that contract directly with Massachusetts merchants as processors will be subject to the same challenges outlined above. There will also be additional network-specific impacts for transactions acquired by third-party processors. Ultimately the proposal could force networks to modify existing pricing structures, increasing costs to Massachusetts merchants and consumers.

Effect on the Commonwealth

The Commonwealth will likely receive and have to reconcile sales tax from hundreds of thousands of sales tax settlement files (in varying amounts from thousands of dollars to a few cents) – *each day and then also reconcile them with cash and check sales tax filings each month*. The Commonwealth will need to establish systems that can accommodate a massive daily data upload from every single processor.

Additionally, the Commonwealth would have to pay royalties to companies that claim to have patented the concept of real-time sales tax collection. If that company is successful in claiming its patent, the potential cost is significant and redundant, because the state can and does currently collect taxes without the need to pay royalties to do so.

The Commonwealth is likely to see an increased volume of inbound transactions and remittances that could increase by a factor of 100x, when considering the increased number of parties that are remitting. The Commonwealth will see a large increase in ACH fees from its bank to cover the daily receipt of the sales taxes. Additionally, tax audits would also increase in complexity and cost with multiple parties being added to the tax collection and remittance process.

A new remittance channel would have to be developed between the processor and the Commonwealth, as this does not exist today, so this step would also require development of some kind, for both parties. In effect, Massachusetts would be required to set up an entirely new system that can efficiently communicate connectivity, file data, timing and other specifications to networks and processors and work seamlessly with every single player in the payment system to maintain data links and integration – ultimately establishing a technical dependency between all processors, the Commonwealth and its banking servicer.

In addition to developing this functionality, the Commonwealth will also have to invest heavily in safeguarding transmission channels and stored information from fraud and theft and complying with relevant data security standards.

Minimal Benefits for This Proposal

The proposal would not realize material benefits for the Commonwealth while at the same time raising the costs for the payments ecosystem, merchants, the Department of Revenue, and ultimately Massachusetts consumers. The proposal would not significantly increase revenue or decrease fraud in the Commonwealth in a meaningful way.

Fraud

Large retailers are under a consistent tax audit and are not the types of retailers that collect sales tax and then fail to remit the tax to the state. Given that electronic transactions offer a more visible audit trail, even for small merchants, the most likely companies that could commit tax fraud are small retailers with mostly cash sales. This proposal would not affect those actors. In fact, this proposal would only serve to make electronic payments more expensive and thereby giving merchants an incentive to drive more transactions to cash.

Revenue

The proposal relies on the premise that the proposal would eliminate the time between when sales

tax is collected and remitted to the state, thereby raising revenue. This is called the float. This may provide a one-time revenue increase, but cost many times more than would be raised by the proposal and would saddle, merchants, processors, consumers, and the Commonwealth with significant ongoing costs. The minimal benefits of the proposal of real time sales tax remittance is significantly outweighed by the cost of implementing this system.

If the Commonwealth is interested in eliminating the float with the least disruption to the current system, it could instead consider prepayment of tax by the largest retailers in the state. This is a method which is currently being used in 12 other states and which the largest retailers are already equipped to comply with. While ETA prefers the current system for remittance of sales tax by merchants, because the system works, prepayment of tax represents a more balanced and less disruptive approach to eliminating the float than the current proposal. Additionally, a prepayment of sales tax would be much faster to implement than the current proposal and would provide a way for the Commonwealth to capture this revenue this fiscal year.

Overall Effect on Doing Business in Massachusetts

The fact that this will be a unique process only for Massachusetts could significantly complicate the overall development efforts. Any resources devoted to Massachusetts would decrease resources devoted to the entire country.

For all of the reasons discussed, this proposal would make the business climate much worse for processors and national merchants and many of them would have to strongly consider whether it makes business sense to continue processing for merchants in Massachusetts.

Additionally, the proposal will disrupt the allocation of resources and the drive towards innovation and competition. For example, a software startup would have to decide between investing in making improvements that will work in the other 49 states, or spend those same resources making its software compliant in Massachusetts. At the very least, there will be a lag between what is available nationwide and what is available in Massachusetts. A more realistic scenario would see the consumers in the Commonwealth have less access to electronic payments, higher costs of products, and less retailers available to purchase those products.

Summary

This proposal for real time sales tax collection and remittance by payment processors is a solution in search of a problem. Even if the entire payments ecosystem, merchants, consumers, and the Commonwealth were able to implement this system at a cost of billions of dollars over many years, it would remain unnecessary and ultimately do more harm than good for the businesses and consumers of Massachusetts.

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We appreciate you taking the time to consider these important issues. If you have any questions or wish to discuss any issues, please contact me or ETA Senior Vice President, Scott Talbott at Stalbott@electran.org.

Respectfully submitted,



PJ Hoffman, Director of Regulatory Affairs
Electronic Transactions Association
(202) 677-7417
PJHoffman@electran.org

Appendix A

