AMERICAN BAR ASSOCIATION

SECTION OF TAXATION

REPORT TO THE HOUSE OF DELEGATES

RESOLUTION

RESOLVED, That the American Bar Association adopts the Model Transactional Tax Overpayment Act, dated February 2011, and recommends its adoption by appropriate legislative bodies.

TRANSACTION TAX OVERPAYMENT MODEL ACT PROJECT

Section 1. Title.

This Act may be cited as the Transaction Tax Overpayment Act.

Section 2. Statement of Purpose and Scope.

This Act applies to state and local taxes that a seller is required to collect from a purchaser on taxable sales. The Act outlines procedures a purchaser may use to seek a refund of an overpayment of those state and local taxes; limits the ability of a purchaser to assert claims against a seller arising from or in any way related to an overpayment; and establishes rights and obligations of purchasers, sellers, and the taxing jurisdiction with respect to such overpayments.

Section 3. Definitions.

As used in this Act:

(a) (1) The term "overpayment" means an amount charged by a seller to a purchaser as tax, paid by the purchaser to the seller, and remitted by the seller to a taxing jurisdiction, if and to the extent that such amount was paid by the purchaser--

(A) in error, including those instances in which the transaction would not have been subject to tax if the purchaser had presented an exemption or resale certificate or other documentation at the time of sale,

(B) when no tax was lawfully due to such taxing jurisdiction at the time of sale, or

(C) in an amount greater than the amount of tax that was lawfully due to such taxing jurisdiction at the time of sale.

(2) The term "overpayment" shall not include a payment of tax to a seller for which an exemption may be available but where entitlement to the exemption is conditioned on the purchaser paying the tax at the time of sale and seeking a refund directly from the taxing jurisdiction.

(b) The term "purchaser" means a person who has been charged an amount by the seller as tax and who has paid, or who is responsible for another person's having paid, such amount to the seller.

(c) (1) The term "refund" means the payment by the seller or the taxing jurisdiction to the purchaser of an overpayment, or by the taxing jurisdiction to the seller of an amount representing an overpayment.

(2) In the case of a refund paid by the seller to the purchaser, or by the taxing jurisdiction to the seller, the term "refund" shall include a credit if and to the extent that—

(A) there is, at the time the credit is issued, a balance on the recipient's account against which to apply the credit, or

(B) the recipient consents to a credit applied to such recipient's account.

(d) The term "purchase" or "sale" means any transaction on which the seller charges the purchaser an amount as tax, collects such amount from or on behalf of the purchaser, and remits such amount to the taxing jurisdiction.

(e) The term "seller" means a person licensed or registered under applicable law to make taxable sales and with respect to such taxable sales is required to collect tax from purchasers and remit such tax to the taxing jurisdiction.

(f) The term "tax" means the tax imposed by *[identify by statutory reference the tax or taxes to which this Act applies]*.[1]

(g) The term "taxing jurisdiction" means the State of _____, or the city, county or other local jurisdiction of such State,[2] that imposes the subject tax; provided, however, that in the event the governmental entity imposing the subject tax is different from the governmental entity responsible for administration of such tax, the term "taxing jurisdiction" shall include, as the context requires, the governmental entity that is responsible for administration of such tax.

Section 4. Purchaser Recourse.

(a) The provisions of this Act apply to any claim by a purchaser against a seller arising from or in any way related to an overpayment, regardless of whether or not such claim is characterized as a tax refund claim.

(b) The relief with respect to any claim by a purchaser against a seller related to an overpayment shall be limited to a refund claim pursuant to Section 5(a)(1).

(c) In any action that arises from or relates to an overpayment, the seller shall not be named as a party to such action by either the purchaser, the taxing jurisdiction or any other party to such action. Nothing in this Act shall preclude a government agency or official from exercising any powers such agency or official possesses to take action to prevent continuing over-collection of tax.

[1] It is intended that this Act would apply to all transaction taxes that the seller is required to add to the sales price of taxable goods, products or services, collect from the purchaser, and remit to the taxing jurisdiction. The Act could also apply to fees and other impositions that have these characteristics.

[2] This Act could be adopted by any U.S. jurisdiction that imposes a transaction tax; and therefore the term "State" is intended to include not only any state of the United States but also other jurisdictions, such as the District of Columbia and Puerto Rico.

(d) Nothing in this Act shall limit any rights or remedies the purchaser may have against the taxing jurisdiction arising from any overpayment under tax refund statutes or other applicable law.

Section 5. Refund Procedures.

(a) (1) A purchaser seeking a refund of an overpayment may, within *[applicable limitations period]* of payment of such amount to the seller, file a refund claim with such seller by providing the seller written notice of the claim, and including with such notice information reasonably necessary for the seller to determine whether all or part of the amount claimed constitutes an overpayment. The seller may, within ninety (90) days following receipt of such notice, refund the amount claimed by the purchaser or such other amount that the seller has determined to be an overpayment. If the seller has not, within ninety (90) days of receiving notice of a refund claim from the purchaser, refunded the amount claimed by the purchaser, the seller shall be deemed to have denied the claim with respect to such amounts not refunded to the purchaser. Notwithstanding any provision of law to the contrary, no interest shall accrue or be paid with respect to amounts refunded by a seller to a purchaser except as provided in Section 5(d)(2).

(2) A purchaser seeking a refund of an overpayment may, within *[limitations period]*, file a refund claim with the taxing jurisdiction pursuant to subsection (b) if—

(A) Such purchaser did not previously file a refund claim with the seller pursuant to this subsection, or

(B) Such purchaser previously filed a refund claim with the seller under this subsection and all or part of such claim was denied or deemed denied; provided, however, that the filing by a purchaser of a refund claim with the seller under this subsection shall extend for one hundred twenty (120) days the limitations period for such purchaser to file a refund claim with the taxing jurisdiction.

(b) A refund claim filed by a purchaser with the taxing jurisdiction shall be in writing and shall include the information reasonably required by the taxing jurisdiction, which may include, but is not limited to, the purchaser's name and address, the name and address of the seller, the amount of the claimed overpayment that has not previously been refunded by the seller (or a reasonable estimate thereof), the approximate date or dates of the claimed overpayment, evidence that the amount claimed was paid to the seller, and a brief explanation of why the purchaser believes that the amount claimed constitutes an overpayment.

(c) (1) The taxing jurisdiction shall, within ninety days following receipt of a refund claim from a purchaser, notify the purchaser in writing of any specific information or records needed for purposes of determining whether and in what amount an overpayment was made.

(2) The taxing jurisdiction may seek information, documents or records in the seller's possession that are needed in processing the purchaser's refund claim; provided,

however, that any such requests must be consistent with the taxing jurisdiction's authority to examine the seller's books and records to determine whether the correct amount of tax has been remitted.

(3) (A) The taxing jurisdiction shall notify the purchaser in writing of its determination with respect to the purchaser's refund claim.

(B) If the purchaser's refund claim is approved in whole or in part, and such approval is based on a new policy or interpretation that would apply to the tax treatment of other transactions, the taxing jurisdiction shall provide guidance concerning such policy or interpretation in the manner generally used for providing informal guidance to taxpayers with respect to the subject tax.

(C) If the purchaser's refund claim is denied in whole or in part, the notification shall include the specific legal and factual reasons for denial. A purchaser's refund claim shall be deemed to have been denied if the taxing jurisdiction does not approve or deny such refund claim within six (6) months of the later of (i) the taxing jurisdiction's receipt of the purchaser's refund claim, or (ii) the taxing jurisdiction's receipt of the purchaser's response to a request for information or records made by the taxing jurisdiction pursuant to this subsection.

(4) If the taxing jurisdiction determines that an overpayment was made, the taxing jurisdiction shall refund such amount to the purchaser and shall allow and pay interest on such amount for the time period and at the rate prescribed by law for overpayments of the subject tax.

(d) Nothing in this Act shall be construed to preclude a seller from acting on its own initiative to refund to a purchaser an overpayment that the seller has determined to have been made or to file a refund claim with the taxing jurisdiction in its own name and have the taxing jurisdiction determine whether an overpayment was made by ruling on such refund claim. Notwithstanding the foregoing, a seller that has received a ruling on a refund claim that an overpayment was made shall only be entitled to receive a refund of such overpayment from the taxing jurisdiction if such seller either—

(1) establishes that the seller has refunded the overpayment to the purchaser or purchasers from whom the amount was collected; or

(2) agrees that, within 30 days or such longer period agreed to by the taxing jurisdiction, the seller will refund the overpayment to the purchaser or purchasers from whom the amount was collected, together with any interest paid by the taxing jurisdiction.

(e) A seller that has previously refunded an overpayment to a purchaser may, within *[the applicable limitations period]*, file a refund claim or take credit for the amount of such overpayment against remittances of the tax; provided, however, that any such credit shall be subject to examination by the taxing jurisdiction, and provided further that the seller shall not be allowed or paid any interest on such amount for the period of time prior to the date the seller

refunded the overpayment to the purchaser, and on or after that date interest shall be paid only in accordance with applicable law.

(f) Nothing in this Act shall be construed to preclude a seller from obtaining a refund of an overpayment from a taxing jurisdiction if such seller establishes that it is obligated to pay or has paid tax in the amount of such overpayment on the same transaction(s) to another taxing jurisdiction pursuant to a valid assessment or claim by such other taxing jurisdiction.

(g) The taxing jurisdiction may establish procedures for assuring that the amount of any overpayment is not refunded by the taxing jurisdiction to both the seller and the purchaser, as well as other procedures necessary to administer this Act.

(h) In the event that a taxing jurisdiction determines, in connection with three or more refund claims from purchasers that it has approved, that there are numerous similar transactions with respect to which tax should not have been collected, the taxing jurisdiction shall send written or electronic notice to all affected registered sellers advising them not to collect tax on such transactions. The taxing jurisdiction shall also post an announcement prominently on its official website notifying affected purchasers of the procedures they must follow in order to request a refund of tax on any such purchase transactions.

REPORT

I. Introduction

A topic of concern to sellers, purchasers and state and local governments alike is seller liability and purchaser remedy procedures for overpaid transaction tax. The conflicting interests of sellers, purchasers and state and local government call for legislation that balances such interests. The attached model, the "Transaction Tax Overpayment Model Act," attempts to resolve these issues in the manner best-suited to addressing the needs of all interested parties. By using the term "transaction tax," we are referring to state and local taxes that a seller is required to collect from a purchaser on taxable sales.

Sellers collecting state and local transaction taxes face two main liability risks: First, if sellers fail to collect sufficient tax, they face liability risks attributable to audit assessments. Second, if sellers over-collect or collect for the wrong jurisdiction, they face potential actions and lawsuits filed on behalf of purchasers or pursuant to consumer protection statutes. These lawsuits can also name state and local governments as codefendants.

Purchaser liability actions relating to collection and administration of state and local transaction taxes generally fall under three main categories: jurisdictional rate assignments, sourcing conventions and product/service taxability.

Sellers often successfully defend against these actions because they used due diligence and remitted the funds to the taxing jurisdictions. Sellers do not benefit from any over-collection because they remitted in full the taxes collected to the taxing jurisdictions. However, even a successful defense is not without costs to the seller. These costs can add up to significant amounts for large sellers. Exposure to lawsuits will increase the cost of collection and will discourage some retailers from voluntarily collecting state and local transaction taxes. It is in the interest of both state and local governments and sellers and purchasers to address liability risks resulting from complying with state and local transaction tax provisions.

Common themes in recent cases and emerging issues in the area of seller liability for transaction tax collection duties include:

1. Most of the recent cases are class actions, with the plaintiffs/purchasers suing the defendant/seller for improperly collecting a state or local transaction tax from the plaintiffs/purchasers.

2. The typical forum is not a tax tribunal, but rather a state trial court of general jurisdiction.

3. Typically, the taxing authority is not a party to the case.

4. In many cases, the court must first decide whether the relevant tax applies to the transaction at hand. In these cases, a non-tax tribunal is deciding the threshold tax issue without the input of the taxing authority.

Even though consideration was given to whether the Streamlined Sales and Use Tax Agreement ("SSUTA") had made seller liability issues moot in the area of sales and use tax collection, SSUTA clearly contemplated a consumer action as a second level/stage remedy, Ultimately, it was concluded that, although SSUTA attempted to balance the rights of purchasers, sellers and state and local governments, it does not resolve all of the problems in this area. The SSUTA is generally silent on refund procedures, but it does require member states whose laws allow consumers to seek refunds from sellers to adopt two seller-protection provisions. That is, SSUTA contemplates that some states will have pre-existing mechanisms for allowing some type of purchaser claims against the seller and does not deprive the purchaser of recourse against an adverse determination of the seller. The 60-day notice language of SSUTA provides additional protection to sellers in those states where it is already clear that state customers have a valid cause of action against the sellers. Unfortunately, in other states where this is not clear, the SSUTA provision appears to enhance the risk of consumer suits. Accordingly, the draft model legislation is consistent with SSUTA while, at the same time, providing an exclusive remedy for a purchaser to obtain a refund of over-collected tax.

Competing public policy concerns regarding the topic of seller exposure to class actions, consumer protection claims, claims for unfair trade practices, etc. have to be taken into account in any model legislation. These concerns include:

1. Difficulties presented when highly technical tax issues are adjudicated in non-tax forums by non-tax lawyers and, perhaps, without involvement of the state revenue departments who are the real parties in interest.

2. Potential chilling effect of the threat of litigation on seller decisions whether to tax a transaction, i.e., incentive to avoid taxing in close cases.

3. Subjecting a seller to material defense costs when it is not the real party in interest with respect to collected taxes may seem unfair and, again, a deterrent to diligent tax collection efforts.

4. The likelihood that consumers who are overcharged taxes in relatively small amounts will not have any effective recourse if they cannot be represented in class actions brought either against retailers or revenue authorities.

5. The impracticality of maintaining refund claims against revenue authorities by groups of small taxpayers other than through the class action approach, i.e., practical problems with lawyers representing large groups of small taxpayers before the revenue departments, difficulty of mobilizing such groups, privacy concerns, decision-making, etc.

"Governing Principles on Transaction Tax Overpayments" which are addressed in the model legislation are set forth below:

Principle 1: The use of licensed sellers to collect transaction taxes on behalf of a taxing jurisdiction is an effective and efficient way to collect transaction taxes.

Principle 2: State legislatures have determined that the collection burden imposed on sellers is justified generally because --

a. the taxing jurisdictions are granting sellers the privilege of doing business in the taxing jurisdiction, and

b. the compliance burden on the purchaser and the administrative burden on the taxing jurisdiction are greatly reduced.

Principle 3: Because sellers are fulfilling a statutory mandate in collecting the tax on behalf of the taxing jurisdiction, the burdens on sellers should be kept as low as possible[3].

Principle 4: In most taxing jurisdictions, the economic burden of the tax is intended to fall on the purchaser – not on the seller. The taxing jurisdiction and the purchaser are the "real" parties in interest in a transaction tax dispute.

Principle 5: Transaction tax laws are complex and their application to various fact situations may be unclear.

Principle 6: Sellers are, in collecting tax from purchasers and paying it over to the taxing jurisdiction, acting merely as agents for the taxing jurisdiction. Accordingly, sellers should not be subject to claims arising from or in any way related to an overpayment by purchasers or liability to such purchasers or anyone else other than a taxing jurisdiction revenue department or other government official, regardless of the nature of the claim or cause of action asserted.

Principle 7: Because sellers may be subject to pay the tax if they fail to collect it from their purchasers, sellers should not have any obligation to construe doubts in favor of the purchaser.

Principle 8: Similarly, sellers should not have any obligation to contest written guidance provided by a revenue department or an audit determination of the revenue department, even if reasonable grounds exist to do so.

Principle 9: Any purchaser who has overpaid a tax should be entitled to a refund if a timely and adequate claim is filed.

[3] For example, some state legislatures have determined that it is appropriate to allow a vendor discount or allowance to compensate the seller, to some degree, for the costs incurred in complying with their collection obligations.

Principle 10: A seller has no right to a refund of any transaction tax that is collected by the seller unless it can demonstrate that the tax has been or will be refunded or credited to the purchaser.

Principle 11: A taxing jurisdiction has a legitimate interest in ensuring that duplicate refunds are not issued. Accordingly, a taxing jurisdiction may establish procedures for that purpose.

Principle 12: Taxing jurisdictions should attempt to minimize costs to the seller of administering any refunds.

Principle 13: A clear and practicable method should be available for a purchaser to obtain a refund of any overpaid tax, which may include expedited procedures or consolidation of claims.

Principle 14: A taxing jurisdiction has a compelling interest in the fair and equitable interpretation of its transaction tax laws and should be an indispensable party in any litigation determining the proper application of those laws.

Principle 15: The taxing jurisdiction has no legitimate interest in administering a lawful tax in an unlawful manner.

Model Transaction Tax Overpayment Act

Findings:

Requiring licensed or registered sellers to collect state and local transaction taxes from purchasers on taxable sales and to remit those taxes to the taxing jurisdiction is an effective and efficient way for the taxing jurisdiction to collect those taxes.

The collection and remittance burdens imposed on sellers are justified because the taxing jurisdiction grants such sellers the privilege of doing business in the taxing jurisdiction and because the compliance burden on the purchaser and the administrative burden on the taxing jurisdiction are greatly reduced.

Because a seller is fulfilling a statutory duty in collecting state and local transaction taxes from a purchaser at the time of sale and remitting those taxes to the taxing jurisdiction, the seller is acting merely as an agent of the taxing jurisdiction; and therefore the burdens on the seller should be kept as low as possible.

Transaction tax laws are complex and their application to various fact situations may be unclear.

Because a seller is fulfilling a statutory duty in collecting taxes from the purchaser at the time of sale, and because the seller can be held liable to the taxing jurisdiction for under remitting tax, the seller has no obligation to resolve doubts as to taxability in favor of purchasers.

The taxing jurisdiction and the purchaser are the real parties in interest in a dispute regarding the application of state and local transaction taxes that a seller is required to collect from the purchaser and remit to the taxing jurisdiction.

A seller should not be subject to claims or liability with respect to an overpayment of state and local transaction taxes that the seller collects from the purchaser and remits to the taxing jurisdiction, regardless of the nature of the claim, provided that tax and other governmental entities should retain any powers they may have to take action to prevent continuing over-collection of tax.

The taxing jurisdiction has a compelling interest in the correct, fair and equitable interpretation of its tax laws and should be an indispensable party in any litigation determining the proper application of those laws.

A clear and practicable method should be available for a purchaser to seek a refund of state and local taxes that a seller has collected from the purchaser if the purchaser believes the taxes were overpaid.

Respectfully submitted,

Charles H. Egerton
Chair, Section of Taxation
February, 2011

GENERAL INFORMATION FORM

Submitting Entity: Section of Taxation

Submitted By: State and Local Tax Committee

1. Summary of Recommendation(s).

That the Association urge all state, territorial and local legislative bodies to adopt the Model Transactional Tax Overpayment Act or an adaptation thereof appropriate to conform with existing state, territorial or local tax procedural requirements. The Act applies to state and local taxes that a seller is required to collect from a purchaser on taxable sales and obligated to remit to state and local tax collectors. The Act provides protections for sellers who merely act as a conduit for such taxes, as required by state and local law, and who have no interest in the amounts collected. The typical state refund procedure requires a purchaser to file any claim for refund after the collected tax is paid over to the taxing authority and, in fairness, the seller should be immune from any liability to the purchaser once the tax is paid over. The Act outlines procedures a purchaser may use to seek a refund of an overpayment of those state and local taxes; limits the ability of a purchaser to assert claims against a seller arising from or in any way related to an overpayment because sellers typically are required by state law to participate in the tax collection system and have no material interest in amounts collected as tax; and establishes rights and obligations of purchasers, sellers, and the taxing jurisdiction with respect to such overpayments. The Act balances the competing interests of tax collectors, purchasers and sellers and promotes compliance with and administration of sound tax policy.

2. Approval by Submitting Entity.

Submitted to House of Delegates contingent on Section Membership approval at the Midyear Meeting Plenary Session on January 22, 2011.

3. Has this or similar recommendation been submitted to the House or Board Previously?

None.

4. What existing Association policies are relevant to this recommendation and how would they be affected by its adoption?

None.

5. What urgency exists which requires action at this meeting of the House?

None.

6. Status of Legislation. (If applicable.)

Not Applicable.

7. Cost to the Association. (Both direct and indirect costs.)

None.

8. Disclosure of Interest. (If applicable.)

None.

9. Referrals.

To all Sections and Divisions. NCCUSL has been given an opportunity to review this recommendation and did not have any substantive issues with the Act and, as they have previously looked at, and decided against, working in the area of state sales tax, they anticipate that there would not be any conflict with their ongoing work. They did ask, however, that the report to the House of Delegates reflect the fact that that the Section consulted with NCCUSL in accordance with Bylaw 24.6 of the American Bar Association. The Section of Litigation has also been given the opportunity to review this recommendation.

10. Contact Person. (Prior to the meeting.)

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11. Contact Person. (Who will present the report to the House.)

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EXECUTIVE SUMMARY

1. Summary of the Resolution

That the Association urge all state, territorial and local legislative bodies to adopt the Model Transactional Tax Overpayment Act or an adaptation thereof appropriate to conform with existing state, territorial or local tax procedural requirements. The Act applies to state and local taxes that a seller is required to collect from a purchaser on taxable sales and obligated to remit to state and local tax collectors. The Act provides protections for sellers who merely act as a conduit for such taxes, as required by state and local law, and who have no interest in the amounts collected.

2. Summary of the Issue that the Resolution Addresses

The typical state refund procedure requires a purchaser to file any claim for refund after the collected tax is paid over to the taxing authority and, in fairness, the seller should be immune from any liability to the purchaser once the tax is paid over.

3. Please Explain How the Proposed Policy Position will address the Issue

The Act outlines procedures a purchaser may use to seek a refund of an overpayment of those state and local taxes; limits the ability of a purchaser to assert claims against a seller arising from or in any way related to an overpayment because sellers typically are required by state law to participate in the tax collection system and have no material interest in amounts collected as tax; and establishes rights and obligations of purchasers, sellers, and the taxing jurisdiction with respect to such overpayments. The Act balances the competing interests of tax collectors, purchasers and sellers and promotes compliance with and administration of sound tax policy.

4. Summary of Minority Views

No minority views have been identified at this time.