



MEMORANDUM

TO: HIGH PERFORMANCE TRANSPORTATION ENTERPRISE BOARD
FROM: NICHOLAS FARBER, ACTING DIRECTOR, HPTE
ANDREW GOMEZ, ASSISTANT ATTORNEY GENERAL
DATE: APRIL 17, 2019
SUBJECT: EFFECTS OF DEPARTMENT OF REVENUE "DESTINATION SOURCING RULE"

Purpose

The purpose of this memorandum is to describe the effects of the Department of Revenue's ("DOR") new sales tax regulations that compels retailers to collect and remit sales tax based on where a taxable good is *delivered*, instead of where it is *sold*. Because HPTE sells taxable goods to the public (in the form of switchable transponders), HPTE is subject to the regulations.

Requested Action

Because of the effects of the new sales tax regulations, the HPTE Board is asked to provide policy direction based on the options below.

Background

Effective June 1, 2019, DOR's new sales tax regulations become law (see generally 1 CCR 201-4). The new regulation compels online retailers that selling over \$100,000 annually to collect and remit sales tax based on the jurisdiction's tax rate at the taxable good's place of delivery (the "Destination Sourcing Rule"). Previously, online retailers needed to collect and remit sales tax based on the location of the business's address only, and not the location of the customer's address who purchased the taxable good.

For example, HPTE (as the online retailer selling over \$100,000 annually) collects and remits sales tax on the purchase of its switchable transponders using CDOT Headquarters' address in determining the tax rates. Because CDOT Headquarters is housed within the boundaries of the City and County of Denver ("CCD"), HPTE complies with all applicable sales tax rates specific to CCD. Once that sales tax is collected, it is then remitted to CCD on a monthly basis. This process is similarly followed as it relates to the State of Colorado's state sales tax collection and remittance procedures for two branches (Denver and Arapahoe County), as well as four Use Tax/Rural Taxing Authorities. Thus, in sum, HPTE collects and remits sales tax for seven taxing jurisdictions. Currently, these tax rates are determined manually through Excel spreadsheets that are received from E-470.

Now, with the Destination Sourcing Rule, HPTE must charge the appropriate sales tax rate that applies to the location to which the transponder is delivered, including any overlapping special district taxes and County taxes. Additionally, HPTE must remit the collected tax with that specific taxing jurisdiction, which includes purchasing a tax and/or business license with that taxing jurisdiction. This means that HPTE could, conceivably, be compelled to collect and remit sales tax with the 700+ taxing jurisdictions in Colorado, not including states outside of Colorado that have their own tax law compliance procedures. Based on past transponder purchases, HPTE estimates an average of 75 taxing jurisdictions and a total of 500 returns filed annually.

Overview of Transponder Purchases

HPTE purchases transponders from Neology for \$10.30 per transponder, which is then sold online to the public for \$15.00. The \$15 per transponder was calculated in 2014 to cover HPTE's sales tax liability and overhead (envelopes and postage). Each month, HPTE averages 4,400 transponders sold to the public, with over \$60,000.00 in sales. The average amount of sales tax remitted per month is \$900.00. E-470 provides an Excel spreadsheet documenting the addresses.

Because of the Destination Sourcing Rule, HPTE has contacted several vendors who specialize in sales tax compliance. Any tax vendor would file and remit on behalf of HPTE. Pricing varies amongst the vendors. Additionally, any changes to the way transponder sales are sold will likely incur added fees from E-470.

Policy Considerations / Options

Given that the Destination Sourcing Rule will likely increase HPTE's cost of doing business, the Board must consider several options:

1. *Do not charge a fee for the transponders*, thereby avoiding any sales tax payments. E-470 has indicated that updating their software to reflect free transponders would cost \$122,150.
2. *Raise the price of the transponders to cover the added cost of calculating and remitting sales tax*. E-470 is still researching if there's a cost associated with this, but has indicated there might be little to no cost for HPTE to implement an increase in the transponder price.
3. *Sell transponders at the CDOT region offices*, thereby making sales tax calculations static. E-470 has indicated that updating their software to reflect sales at region offices would cost \$82,928.
4. *Create a deposit system* whereby customers do not own the transponders and instead place a deposit of \$15 that is to be remitted back to the customer once the transponder is returned to HPTE. Sales tax would still be due once the deposit period has expired. E-470 has indicated that updating their software to reflect a deposit scheme would cost \$291,720.
5. *Keep the cost of transponders at \$15 and take no action*.

Decision Matrix

1. **Staff Recommendation:**
 - a. Approve an outside sales tax vendor until a permanent solution is determined. Staff will also research emerging transponder technologies, and will have options to present to the Board in the Fall of this year.
 - b. Implement Option 2: Raise the price of transponders to cover the added costs of calculating and remitting sales tax. The attached Break-Even Cost Analysis shows a range between low sales, where the cost of the transponder would have to be \$18.59 to breakeven, and average sales would be \$17.54 to breakeven. To cover any fluctuations in sales, HPTE staff recommends a transponder sale price of \$18.00.

Attachment

Break-Even Cost Analysis

3.502608089							8.31%	
Transponder cost (per Unit)	Fulfillement and management cost (per unit)	Tax filing cost (per month) ¹	Tax filing cost (per unit) ¹	CDOT staff cost (per month)	Average tax rates	Breakeven sale price per unit		
\$ 10.30	\$ 3.50	\$ 9,000	\$ 3.14	\$ 650.00	\$ 0.23			
			total	\$ 17.17	8.31%	\$ 18.59		

Low sales

Note	
1	Sales tax owed by HPTE for transponders purchased by customer Sales and Business Licenses Sales tax preparation and filing

	2017	2018
Sales	44,943	\$ 674,145
Refunds	(862)	\$ (12,930)
Net	44,081	\$ 661,215
		51,763
		(1,225)
		50,538
		\$ 758,070

average sale per month							4029	
Transponder cost (per Unit)	Fulfillement and management cost (per unit)	Tax filing cost (per month) ¹	Tax filing cost (per unit) ¹	CDOT staff cost (per month)	CDOT staff cost (per unit)	Average tax rates	Breakeven sale price per unit	
10.3	3.5	9000	2.23	650	0.161313672	8.31%		
			total	16.19			\$ 17.54	

With average sale