



MEMORANDUM

To: Mayor and City Council

From: Mike Land, City Manager

Date: January 14, 2020

Reference: Report on Texas Administrative Code Rule 3.334, concerning proposed changes to local sales and use tax sourcing

General Information:

A 2018 U.S. Supreme Court decision, *South Dakota v. Wayfair, Inc.*, allows local taxing jurisdictions to require out-of-state remote sellers to collect local sales or use taxes on items that are delivered into their city. The Texas legislature passed two bills, HB 1525 and HB 2153 bill, in the 2019 session to address this issue, and the Texas Comptroller of Public Accounts has already put rules into place to allow the State and local entities to collect interstate generated sales and use taxes.

Recently, the Texas Comptroller recommended additional policies that would substantially negatively impact Coppell and many other communities by changing 70 years of traditional sales and use tax collections.

Currently, Coppell receives the sales and use tax generated by a sale if an individual or another business orders items from one of the warehouses, distribution or fulfillment centers located within Coppell, no matter where that person or business resides or is located within the state. Under the Comptroller's proposed rules, the sales and use tax would instead be designated for the city where the product is delivered even though the sale is consummated and fulfilled in Coppell.

The sales and use tax revenue that is currently collected in Coppell is used by the City to provide all the public services required to not only support the warehouses, distribution and fulfillment centers that are receiving the sales order and delivering the product, but to also maintain a high quality of life for Coppell residents. These sales and use tax revenues allow Coppell to provide

residents and businesses with vitally important municipal services such as police, fire protection and paramedic services, along with well-maintained streets and medians, parks, utilities and other crucial infrastructure. If this revenue stream, which is estimated to be approximately 60% of Coppell's total sales and use tax revenue, is eliminated under the Comptroller's proposed rules, city services will be negatively impacted, which will ultimately impact the Coppell community.

This is a radical change, not envisioned by the Texas Legislature when they passed HB 1525 and HB 2153 during the last legislative session. This change would have a devastating impact on Coppell and many other Texas cities. The approach proposed by the Texas Comptroller would disrupt decades of established local sales tax sourcing rules. Coppell and other cities are asking the Comptroller of Public Accounts to reconsider the current proposed rules and to keep the current origin sourced sales and use tax collection process in place. The City of Coppell is prepared to take additional steps if necessary, should the State Comptroller's office not amend the language as currently published and as requested.

Q&A

How much money would this change cost Coppell?

If the proposed rules went into effect this April, Coppell would lose approximately \$6 million in sales tax revenue, or \$12 million annually from the General Fund alone. The total Fiscal Year 2019-2020 budget approved by the Coppell City Council amounts to \$73 million. In total, the annual sales tax revenue reduction for all funds, including the General Fund, the Coppell Recreation and Development Corporation, the Street Maintenance Fund and the Crime Control District would be approximately \$24 million.

What would this mean for city services?

Twelve million dollars is approximately 16% percent of the City's General Fund budget. The City of Coppell management team is currently working on strategies to address this reduction in revenue, should the proposed rule changes be adopted. With such a significant reduction, it is possible that some services could be eliminated or scaled back, and some projects could be delayed.

Can't the city just raise property taxes to make up the difference?

The decision to raise property rests with the Coppell City Council, and, if necessary, Coppell voters. However, raising property taxes is certainly not the first option being considered to address this issue.

Ironically, the state legislature, just this past session, made it more difficult for cities to raise property taxes. Additionally, the annual loss of nearly \$12 million in sales and use tax revenue to the General Fund far exceeds any additional property tax revenue that could be realized as a result of growth or increased property tax collections on existing property.

What other cities would be impacted?

Unfortunately, it is unclear how many cities would be impacted because neither the State of Texas nor the State Comptroller have performed any analysis on the impact of this proposed change. The Speaker of the Texas House of Representatives recently charged the House Ways and Means Committee to specifically study the impact of changing from the State's historic method of sales and use tax collections, from origin based sourcing to destination based sourcing, as proposed by the State Comptroller with this new rule.

Several cities throughout the State whose economic development make up is similar to Coppell's have joined together for the purposes of working with the Comptroller's office to resolve this issue.

Does South Dakota v. Wayfair, Inc. require the comptroller to make these rules?

The U.S Supreme Court's decision in the S.D. v. Wayfair case was specific to interstate sales, allowing states like Texas and their local jurisdictions to collect sales and use tax on purchases that are consummated with out-of-state remote sellers. During the 2019 legislative session, the State of Texas Legislature approved two pieces of legislation, HB 1525 and HB 2153 that addressed these types of interstate transactions. The State of Texas Comptroller of Public Accounts has already put into place the necessary rules authorizing the collection sales and use taxes from these interstate sales. The proposed rules, as currently published, go beyond the Supreme Court's decision and the intent of the State Legislature. Changing how sales tax is sourced within the State of Texas is a legislative issue, not a bureaucratic process.