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Texas Tax Update:
Bill Proposal Regarding Local Sales Tax Sourcing
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This article provides an update on House Bill 134 regarding local sales tax sourcing in Texas.

After a multi-year court-battle to shift certain local tax sourcing from origin sourcing to destination, the Legislature is now considering a bill that would achieve the Comptroller's proposed destination sourcing by amending the Texas local tax sourcing laws.

On March 12, 2025, Representative Morgan Meyer introduced House Bill 134. This proposal would amend the municipal and county sales tax statutes to essentially codify destination sourcing for many sales made through shopping websites or apps and fulfilled through fulfillment centers. Instead of being sourced to the location where the orders are received, they would be sourced to the area where the item is delivered to the customer.

This proposed shift to destination sourcing mirrors the Comptroller's position in multiple rounds of rulemaking over the last few years and the position he took in litigation against Round Rock, Coppell, and other Texas cities.

Similar bills have been introduced in previous legislative sessions, but those bills faced resistance and ultimately weren't passed. Opponents pointed to the high compliance costs for small businesses and the State stripping away the benefits of economic development agreements that were negotiated long ago. Perhaps to avoid resistance from those same constituents, this bill provides exceptions for small businesses and those benefiting from economic development agreements under which the local government made payments on or before January 1, 2025.

The sourcing of local sales tax is vital to taxpayers and local government entities who have entered into economic development agreements. Under the "origin" sourcing that has been prevalent in Texas for decades, many cities entered economic development agreements to attract out-of-state businesses, encouraging them to establish facilities in their cities by sharing a portion of the sales local tax revenue the cities collected. Dell Computer Corporation, for example, entered into an agreement with the City of Round

Rock back in 1993 that allows Dell to receive a monthly payment of a percentage of the sales tax revenue it generates for Round Rock. Neither the taxpayer nor the city that entered into such an economic development agreement would benefit, however, if the taxes for online sales were sourced to the delivery locations.

Comptroller Hegar argued that the origin-based sourcing that these agreements relied upon is unfair to counties, cities, and other local tax jurisdictions that do not benefit from local tax revenue when the goods are delivered to their residents in other parts of Texas. After many cities realized they faced losing substantial tax revenue from the Comptroller's recent rule amendments, they sued the Comptroller to block enforcement. The preceding litigation resulted in an injunction against the Comptroller which the Comptroller has advised he plans to appeal.

House Bill 134 attempts to enact changes to Texas Tax Code Section 321.002(a) by explicitly stating that a place of business does not include computer servers, protocol addresses, domain names, websites, or software applications. It replaces the "catchall" default sourcing from the seller's place of business to "the location in this state to which the item is shipped or delivered or at which possession is taken by the customer."

It proposes guidance on what it means for an order to be "received." According to the bill, an order is "received" at the location where the seller receives enough information to determine whether it can be accepted, and not to a location where the order is subsequently accepted, completed, or fulfilled.

The bill would allow retailers with economic development agreements to elect to source their sales to their place of business in those locations, but that carve-out would automatically expire on December 31, 2030. It also provides that sales by small businesses are generally consummated at their principal place of business, effectively exempting them from the shift to destination sourcing.

The introduced bill would make each of the changes above to the municipal sales tax laws. Instead of making parallel changes to the county sales tax laws, it would simply repeal the county sourcing laws and instead provide that the same sourcing provisions apply to both city and county taxes.

The House Ways & Means Committee heard extensive testimony from interested parties on March 18, 2025. Ray Langenberg, Special Counsel for the Comptroller, testified that the Comptroller's revenue estimating department was unsure what the ultimate financial impact would be. However, the Comptroller estimated in its fiscal note that the bill would result in a net loss to local taxing jurisdiction from instances where taxes would be sourced to destinations that have lower or no local tax. The Comptroller estimated that this would result in a net loss to cities, counties, transit authorities, and special districts totaling approximately $150 million per year. Because the Comptroller receives a 2% fee of all local taxes to compensate the agency for collecting and administering local taxes, the state would lose approximately $3 million per year. Mr. Langenberg emphasized the uncertainty in the Comptroller's estimate.

The text of this bill can be located by following this link:
https://capitol.texas.gov/tlodocs/89R/billtext/html/HB00134I.htm

The bill was heard on Monday, March 17, 2025 and has been left pending in committee.