

Cash-hungry states eye online retail for tax revenue

July 22 2010, By Mike Zapler

Web-savvy shoppers can often save big buying online instead of at the local mall. But a chunk of the savings comes at the expense of state and local governments, in the form of sales taxes that are never paid on many Web purchases.

The losses add up for cash-starved state and local governments across the country: California alone loses out on more than \$1 billion a year.

Now states are starting to get serious about collecting that money. Options under consideration include rewriting the rules on which dot-coms have to charge sales tax -- or even requiring online retailers to send their customer lists to the government.

And in an ironic twist, states are getting support from tax-wary business groups, which complain that online retailers such as Amazon and Overstock are exploiting a legal loophole to undercut the competition on pricing.

"It's no longer a thing of us wanting to do it for budgetary purposes," California Assemblywoman Nancy Skinner, a Democrat, said at a recent budget hearing, referring to her proposal to step up the state's collection efforts. "It's our own businesses and largest employers asking for it, because they're being put at a competitive disadvantage."

In California, almost \$1.1 billion in [sales taxes](#) from online and catalog purchases is owed but not paid each year, according to state tax officials.

Technically, shoppers are supposed to keep track of their out-of-state purchases and pay sales taxes on them come tax time (perhaps you noticed that line on the state income tax form). But that rarely happens -- in 2009, California collected only \$10 million from such scrupulous souls.

The tax disparity stems from a 1992 U.S. Supreme Court decision that allowed mail order and, later, Internet retailers to avoid charging and collecting sales taxes if they lacked a physical presence -- namely, stores or headquarters -- in the state where the buyer lives. Amazon, for example, is based in Washington state, so it does not tack on the sales tax to purchases made by Californians.

That translates into a sizable advantage for out-of-state retailers over their in-state, brick-and-mortar competitors. A Nintendo Wii has the same base price at Amazon or Best Buy, \$199.99. But buying it at a Target in San Jose, Calif., (or on the company's Web site, which Amazon happens to run) means paying Santa Clara County's 9.25 percent sales tax -- an extra \$18.50.

States have begun to fight back, devising creative ways around the [Supreme Court](#) ruling to make Amazon and other online retailers pay up. In 2008, New York enacted a measure, dubbed the "Amazon law," redefining what it means for a business to have a "physical presence" in the state. Any company that has an affiliate relationship with another business in the state would have to collect and remit the sales tax. Amazon has an affiliate program with Web sites, including some in New York, that post Amazon ads.

Amazon sued but lost in lower court, and a ruling on appeal is expected soon.

Colorado, meanwhile, passed a law requiring out-of-state retailers that

don't collect sales taxes to provide a list to the state of the names of customers who bought items and how much they spent, so tax collectors could seek payment. That legislation also is being challenged in court, with opponents charging that it violates privacy rights.

Democratic legislators in Sacramento, Calif., said at a recent budget hearing that they're considering both approaches. They received a boost last month when two prominent business groups, the California Retailers Association and the California Business Properties Association, wrote letters in favor of legislation mimicking the New York law.

Small online retailers argue that collecting and paying sales taxes to states would be difficult or impossible to manage, given the thousands of tax jurisdictions across the country, each with its own rates and rules for what items are taxable. Others counter that simple computer software can handle the task easily.

In Congress, meanwhile, Rep. William Delahunt, D-Mass., introduced a bill this month calling for a national solution to ease states' online sales tax collections. Dubbed the "Main Street Fairness Act," it would allow states that agree to streamline their sales tax systems to collect taxes from out-of-state retailers, whether or not they have a physical presence in the state. EBay has come out against the bill unless an exemption is carved out for most small businesses.

But the big kahuna in the debate is Amazon, which in the mid-1990s reportedly considered opening its headquarters on an Indian reservation to minimize its tax obligations, and which currently collects sales taxes in only five states. The Amazon subsidiary that developed the Kindle e-reader is based in Cupertino, Calif., but the online retailer still does not collect sales taxes in California.

"Amazon has been particularly aggressive in exploiting a hole in the

law," said Michael Mazerov, a senior fellow at the Washington-based Center on Budget and Policy Priorities.

An Amazon spokeswoman did not respond directly to that charge, saying in an e-mail that the retailer opposes state-level efforts to collect more sales taxes from remote sellers but "will continue to work with all interested parties on a truly simple and equitable national resolution."

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