

Amazon's former Calif. affiliates brace for lost revenue

July 10 2011, By Dale Kasler

For several years now, the military museum in Old Sacramento has quietly earned a nice little income by acting as a sales rep for Amazon.com Inc.

But this small nonprofit, along with thousands of other California organizations and businesses, has been caught in an epic standoff between Amazon and state officials.

The state enacted a law last week requiring Amazon and other [Internet retailers](#) to begin collecting [sales tax](#) from California purchasers. Amazon says the law is unconstitutional and it won't collect the tax.

While [legal experts](#) expect Amazon to sue the state, the online giant already is taking action of a different sort. Hoping to exempt itself from the law, Amazon has fired its 10,000 California affiliates, cutting off their commissions. Scores of other e-commerce companies affected by the law, including Overstock.com and a slew of smaller firms, have done the same.

Their decisions won't prevent [Californians](#) from buying from Amazon and other online [retailers](#).

But they will affect organizations like the California State Military Museum, which earned about \$2,000 a year as an Amazon affiliate.

"That was our book-buying budget," said Dan Sebby, the museum's

director.

A Camarillo, Calif., [trade group](#), the Performance Marketing Association, says 25,000 California businesses, individuals and nonprofits make commissions as affiliates for online retailers. They place links on their websites to the retailers, and earn commissions when visitors "click through" to make a purchase.

For many, it's a sidelight. For others, it's their livelihood. Rebecca Madigan, the trade group's executive director and a critic of the new law, said the California affiliates will lose 25 percent of their Internet income as a result of the controversy.

"Hundreds and hundreds of retailers have terminated their affiliations," she said.

California isn't the first state to feud with Amazon. The Seattle retailer dumped affiliates in several other states, including Connecticut and Arkansas, that imposed an Internet sales tax. It has also rewarded states that remain tax-free.

Citing a business-friendly climate, Amazon announced Wednesday it's building a major distribution facility in Indiana. At the same time, it's continuing a lengthy court fight over a New York law that imposes the tax requirement.

The California controversy could be the most explosive, because of the size of the market and the way the law is written.

"This is going to be going on for some time," said Brian Toman, a San Francisco tax lawyer. "I wouldn't be surprised if this ends up in the (U.S.) Supreme Court."

A 1992 Supreme Court decision says retailers can't be forced to collect sales tax unless they have a "physical presence" in the state. The new California law declares that affiliates, like the Old Sacramento museum, represent a physical presence.

By firing those affiliates, most of the retailers have taken themselves off the hook. The same sequence has played out in a handful of other states, where retailers have escaped the tax by dumping their affiliates.

But the California law, written with Amazon in mind, goes a step further. It says subsidiaries with operations in the state count as a physical presence, too. Amazon operates several subsidiaries in California, including a Silicon Valley company that helped design the Kindle e-reader.

Amazon, however, is refusing to charge the tax.

The impasse likely will come to a head in late October, when merchants are scheduled to turn their sales tax collections from the third quarter over to the state.

"That's the beginning of the confrontation," Toman said.

The law, signed last week by California Gov. Jerry Brown, is designed to generate \$200 million to \$300 million in new revenue for California. It's also supposed to level the playing field between brick-and-mortar retailers, who already charge sales tax, and their online competitors.

But with Amazon and others not charging the tax, critics say the law is likely to generate little revenue. Instead, they say, it will inflict pain in an obscure but crucial corner of cyberspace: the world of affiliated marketers.

"You're going to destroy all of these businesses," said Alan Gray, who owns a small online news site based in Folsom, Calif., called Newsblaze.

Until recently, links with big retailers provided up to 20 percent of Newsblaze's revenue, he said.

Gray said he went to the Capitol to try to persuade lawmakers to kill the tax proposal. He wound up moving back to his native Australia, in part over his disgust with the new law, although Newsblaze still operates.

Affiliates who have been deserted by Amazon and the others have alternatives.

Four big retailers with Internet operations - Wal-Mart, Barnes & Noble, Sears and Best Buy - have been working for weeks to recruit affiliates from Amazon.

Wal-Mart and the other companies already charge tax on Internet sales to Californians. That's because they clearly have a "physical presence" in the state - their brick-and-mortar stores.

Barnes & Noble said it has signed up "a number" of former Amazon affiliates. Wal-Mart said it has received inquiries from affiliates, as well.

"Affiliates can work with us knowing that we'll gladly collect and remit sales tax on their behalf," Wal-Mart spokesman Dan Morales said in an email.

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