

# spotlight

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## THE AMAZON TAX THAT WAS NOT

*North Carolina's Attempt to Expand Sales Taxation Beyond Its Borders*

**KEY FACTS:** • To overcome a Supreme Court ruling that state legislators do not have jurisdiction to tax out-of-state firms, North Carolina and eight other states have an Amazon tax. This categorizes out-of-state firms as in-state and responsible for sales tax collection if they have in-state affiliates.

• Despite the introduction of the Amazon Tax, online trade with out-of-state retailers, including Amazon.com, still enables North Carolinians to avoid sales tax, as retailers are able to circumvent the law. The National Conference of State Legislatures (NCSL) estimates North Carolina's forgone sales tax revenue at \$436.5 million for 2012.

• The North Carolina Department of Revenue has presented no evidence to indicate revenues have increased under the Amazon tax. In fact, the year following its implementation saw a decline of 28 percent in sales tax revenue collected out of state.

• Amazon taxes do not level the taxation playing field. Rather, they create three different levels of sales tax treatment, and they impose a heavy regulatory burden on those affected.

• The Performance Marketing Association estimates that approximately 1,000 online advertisers terminated their North Carolina affiliates when the law passed in 2009, and one third of the harmed affiliates moved out of the state

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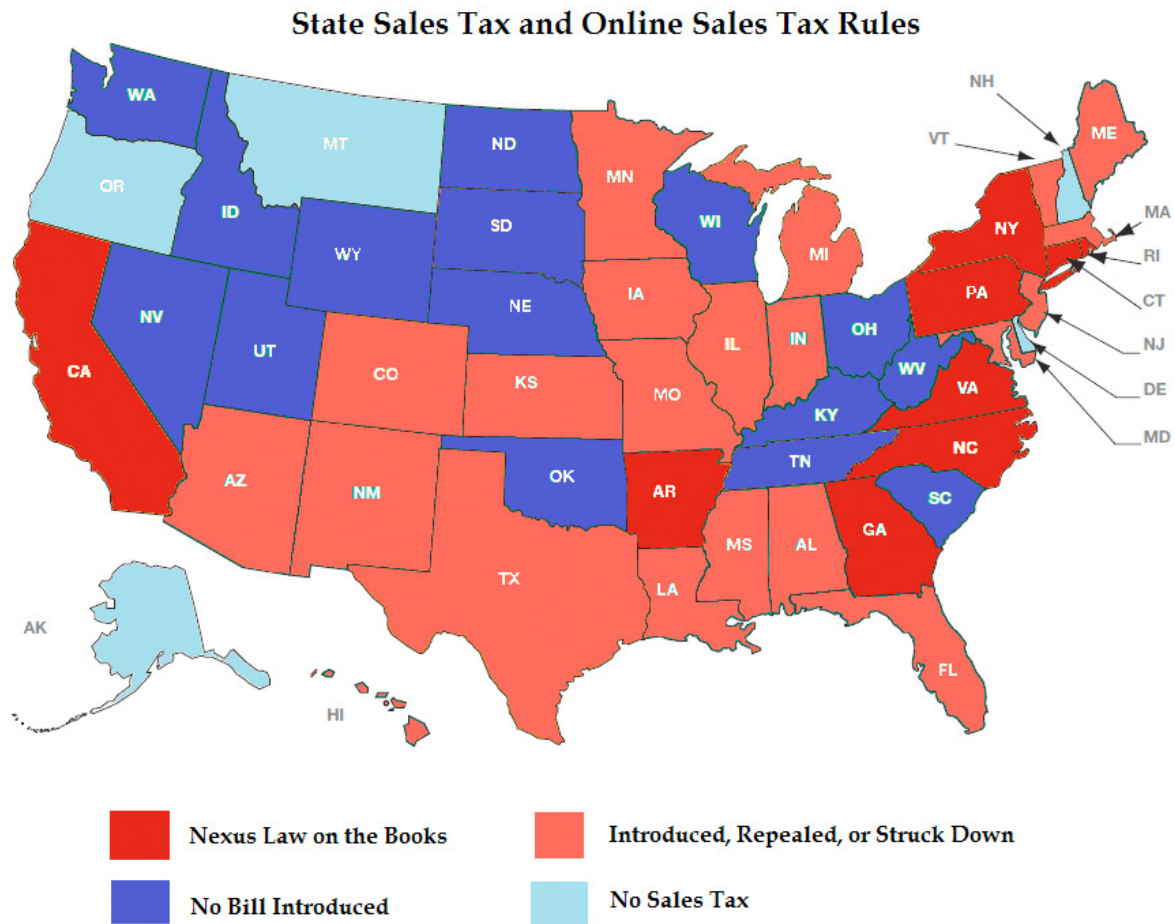
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The trend of individuals toward buying online, and avoiding state sales taxes in the process, has many legislators of both parties concerned.<sup>1</sup> The National Conference of State Legislatures claims the forgone tax revenue from these online purchases to be \$23.3 billion in fiscal year 2012, including \$436.5 million for North Carolina.<sup>2</sup> Conventional, brick-and-mortar retailers have also voiced concern over what they believe to be an uneven playing field.<sup>3</sup>

At present, however, state legislators do not have jurisdiction over firms located in other states, and the “use tax” that residents technically owe on purchases from those firms is almost impossible to enforce.<sup>4</sup> North Carolina’s Department of Revenue has already tried and failed in court to force Amazon.com to reveal customer identities, and thereby enable prosecution, and the company has no plan to do so voluntarily.<sup>5</sup> Members of Congress may intervene and expand states’ taxation powers, but until that happens the imposition of taxation requires a physical presence or “nexus” in the state, as affirmed by the United States Supreme Court in 1992.<sup>6</sup>

That hasn’t stopped state legislators from trying to expand taxation of out-of-state firms, though. As is shown in Figure 1, in 30 states they have introduced various forms of legislation to redefine “nexus” to include online affiliates. These online affiliate, or “Amazon” taxes, as they are better known, mean that any seller with online advertisers, bloggers, or marketers who reside in the state and receive a commission on sales—through coupon promotion, for example—becomes liable for sales tax in that state.<sup>7</sup>

In other words, out-of-state retailers are subject to sales tax collection based on these relationships. While some of these laws have failed in state courts, and others have been repealed, North Carolina’s, which passed in 2009, is one of nine that remain in force.<sup>8</sup>



Source: John Locke Foundation<sup>9</sup>

In terms of achieving their stated goals, however, these Amazon tax laws have failed. Further, they have broken mutually beneficial relationships and reduced economic activity within the states that have imposed them, as subsequent paragraphs explain.

### *The Purportedly Uneven Playing Field*

While out-of-state retailers may compete with in-state retailers for customers, they do not enjoy the benefits of an in-state presence. They do not receive police protection, for example, nor infrastructure or any other government service. Therefore, the application of tax collection on out-of-state retailers does not achieve an even playing field. It also undermines the fair play argument—that one owes taxation in exchange for government services received—and could be considered taxation without representation.<sup>10</sup>

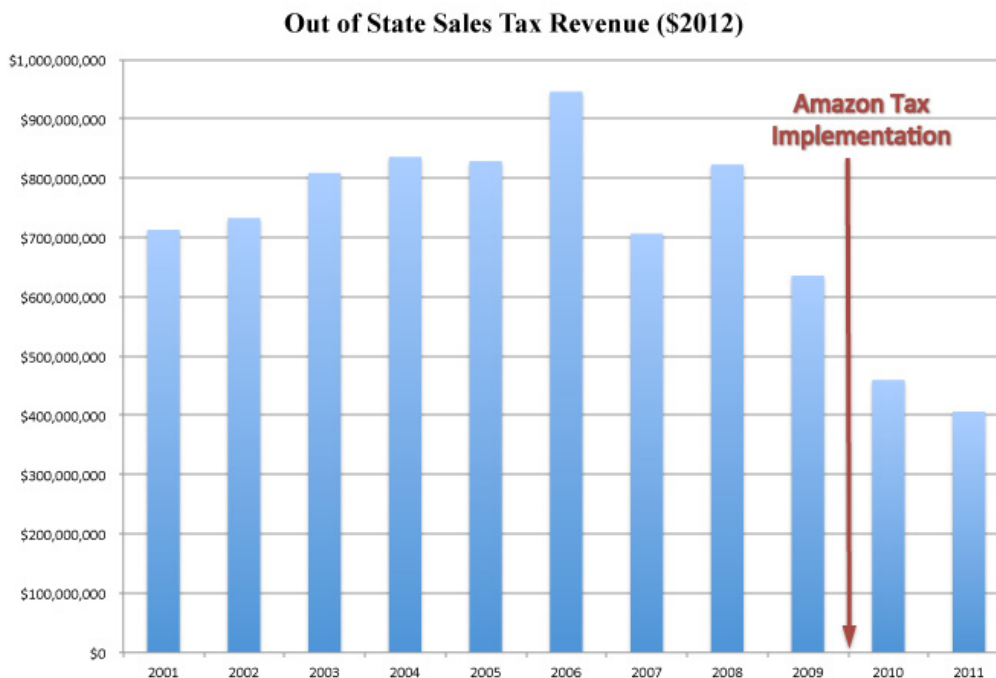
Further, even if one were to make the case that these taxes were legitimate—perhaps on the grounds that they target in-state consumers rather than the suppliers—they only apply to online retailers with marketing affiliates in state. Online retailers with no connection can continue as before, which actually creates three different levels of sales tax treatment: in-state retailers (taxation and government benefits); out-of-state retailers with online affiliates (taxation without government benefits); and independent, out-of-state retailers (no taxation and no government benefits).<sup>11</sup>

To complicate the process further, Amazon taxes change the locational basis for determining sales tax rates.<sup>12</sup> Normally, brick-and-mortar retailers' sales taxes are based on the location of the purchase, the retail outlet (origin-based). Now with online retailers and the presence of Amazon taxes, the rate can be based on the location of the seller or buyer (destination-based).

That distinction may seem trivial, and if individuals were located in the same areas as the stores from which they shopped, it would be. However, there are almost 10,000 different and constantly changing sales tax rates across the United States, not to mention sales tax holidays.<sup>13</sup> Under the Amazon tax, online retailers are stuck with the regulatory burden of charging customers at thousands of different rates, a task so complicated that it poses a challenge even to specialist firms.<sup>14</sup>

### *The Still Forgone Revenues*

The projected sales tax revenues associated with North Carolina's Amazon tax—\$3.8 million in 2010 and \$8.5 million in 2011—have simply failed to arrive; there is no evidence that would indicate increased tax revenues.<sup>15</sup> Unfortunately, the Department of Revenue has not recorded Amazon tax revenues separately. Implementation coincided



with a severe fall in North Carolina's sales tax revenues originating from out of state, from \$635 million in 2009 to \$459 million in 2010.<sup>16</sup> That revenue decline occurred despite an increase in the state sales tax rate from 4.75 to 5.75 percent in October of 2009.<sup>17</sup>

The Amazon tax includes only the minority of online sellers with affiliates in North Carolina, so it simply can not recoup the \$436.5 million of lost revenues that the NCSL has alluded to. Even if the out-of-state revenue had arrived or had been concealed amid normal variability of the taxation

stream, it would only have constituted a meager 0.06% of total state sales tax revenue and 0.02% of General Fund revenue. That negligible but optimistic return comes from the legislature's own Fiscal Research Division.

In addition to the fact that a minority of online retailers fall under the Amazon tax, the ones that do need not move out of state to avoid it; they're already there. They can simply disassociate themselves with in-state affiliates. Amazon.com did this before the law went into effect, so contrary to the moniker, North Carolinians can still buy from that particular website without paying sales taxes.<sup>18</sup>

Beyond Amazon.com, the Performance Marketing Association (PMA) estimates that about 1,000 online advertisers terminated their North Carolina affiliates when the law passed in 2009, which would have negatively impacted income and other state taxes.<sup>19</sup> The PMA has observed "consistent patterns in all the nine states where this has passed" and estimates that one-third of impacted affiliates moved out of state, since South Carolina and Tennessee do not have Amazon taxes.

Of the states that have passed Amazon taxes, only two others, New York and Rhode Island, have had more than a year of enforcement to observe tax revenues. New York, however, has been in a legal battle since 2008 with Amazon.com over the law's constitutionality, and Amazon.com has only agreed to collect the tax while the lawsuit continues.<sup>20</sup>

Rhode Island's legislature did not include a revenue estimate when they passed their version, and they have not published specific Amazon tax revenue figures. However, between 2009 and 2010, when their Amazon tax came into force, the state's sales tax revenues fell by 2 percent and to a lower proportion of the state's total General Fund revenue.<sup>21</sup> The Chief of the Rhode Island Office of Revenue Analysis has even gone on record to say that the Amazon tax is not generating revenue.<sup>22</sup>

### *Concluding Remarks and Recommendations*

North Carolina's Amazon tax creates three tiers of sales tax collection, imposes a new regulatory burden, and dissuades business relationships with the state. There is also no evidence that it is increasing tax revenues. Since it fails on all counts, it merits repeal in the next legislative session (S.L. 2009-451).<sup>23</sup>

Even if one wished to maintain the sales tax rate and base as online activity erodes it, there does not appear to be a mitigating policy that could originate from the North Carolina legislature. Members of Congress may eventually impose a multi-state resolution, but until that happens, online sales from other jurisdictions will continue to generate pressure for North Carolina to lower rates (the disincentive for in-state purchases) and rely less heavily on sales tax revenue.

If Congress does intervene, members ought to do so with an eye on a uniform, origin-based system. Supported by the National Taxpayers Union and online-retailer Overstock.com, this would require all online retailers to begin collecting sales tax, at least those from jurisdictions with sales tax, but it would be without the regulatory burden of different destination-based rates.<sup>24</sup> It would also maintain the incentive for states to remain competitive in their taxation to invite business expansion.

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**Appendix 1: Nexus (Amazon Tax) Laws by State**

| State          | Affiliate Nexus Law?                | Current Status   | Nexus Law on the Books? |
|----------------|-------------------------------------|--|-------------------------|
| Alabama        | HB365 (2011)                        | Failed to pass   | No                      |
| Alaska         | No sales tax                        | N/A  | No                      |
| Arizona        | HB 2551 (2011)                      | Held in Rules Committee  | No                      |
|                | HB1338 (2012)                       | Failed in Senate (March 2012)  |                         |
| Arkansas       | SB 738 (2011)                       | Enacted 4/1/2012 (Act 1001)  | Yes                     |
| California     | ABX1 28 (2011)                      | Repealed until 9/15/12 (AB 155)  | Yes                     |
| Colorado (1)   | HB 10-1193 (2010)                   | Struck down April 2012   | No                      |
| Connecticut    | SB 6652, Sec. 46 (2011)             | Signed by Governor 6/21/11   | Yes                     |
| Delaware       | No sales tax                        | N/A  | No                      |
| Florida        | SB 1514 (2012)                      | Died pending reference review under Rule 4.7(2) 3/9/12                                     | No                      |
|                | SB 2098 (2012)                      | Died in committee 3/9/12   |                         |
|                | HB 861 (2011-12)                    | Died in committee 3/9/12   |                         |
|                | HB 1085 (2011-12)                   | Died in committee 3/9/12   |                         |
| Georgia        | HB 386 (2012)                       | Relevant part takes effect 7/18/12   | Yes                     |
| Hawaii         | HB 1405 (2009)                      | Vetoed by Governor 7/1/09  | No                      |
|                | SB 2226 (2012)                      | In Conference Committee as of 4/17/12; Legislature adjourned sine die 5/3/12               |                         |
|                | HB 1694 (2012)                      | Referred to Economic Development and Technology Committee, Ways and Means Committee 3/8/12 |                         |
| Idaho          | No bill introduced                  | N/A  | No                      |
| Illinois       | HB 3659 (2011)                      | Struck down 4/25/12 (Could be appealed)  | No                      |
| Indiana (2)(5) | SB 100 (2012)                       | Referred to Committee on Tax and Fiscal Policy 1/4/12                                      | No                      |
|                | Deal in which Amazon collects taxes | Effective 1/1/14   |                         |
| Iowa (5)       | HF 2510 (2010)                      | Died in committee  | No                      |
|                | SSB 3178 (2012)                     | Voted – Economic Growth/Rebuild Iowa 2/13/12   |                         |
|                | SSB 3186 (2012)                     | Ways and Means 2/22/12   |                         |
| Kansas (5)     | SB 430 (2012)                       | Senate Committee on Assessment and Taxation on 2/16/2012 – currently pending               | No                      |
|                | SB 371 (2012)                       | Died in House Committee  |                         |

| State          | Affiliate Nexus Law?  | Current Status   | Nexus Law on the Books? |
|----------------|---|--|-------------------------|
| Kentucky (5)   | No bill introduced  | N/A  | No                      |
| Louisiana      | HB 641 (2011)   | Passed House; Failed in Senate   | No                      |
|                | HB 1027 (2012)  | Subject to Call – House Referral; Legislature adjourned without passing              |                         |
|                | HB 1114 (2012)  | Considered by Ways and Means Committee 5/1/12; Legislature adjourned without passing |                         |
| Maine          | LD 469 (2011) – Would have required notification of sales tax obligations | Voted down in committee  | No                      |
| Maryland       | SB 523 (2012)   | Passed by Senate; Sent to House 3/19/12  | No                      |
| Massachusetts  | H. 1731 (2011)  | Died in committee  | No                      |
|                | S. 1450 (2011)  | Died after April 7 hearing   |                         |
|                | S. 1554 (2011)  | Died after April 7 hearing   |                         |
|                | H. 1695 (2011)  | Made through April 7 hearing accompanied by new draft: H. 3673                       |                         |
|                | H. 3673 (2012)  | Committee recommends it passes, referred to House committee on Ways and Means 6/4/12 |                         |
| Michigan (5)   | HB 5004 (2011)  | Referred to Committee on Tax Policy 9/22/11  | No                      |
| Minnesota (5)  | SF 282 (2009)   | Died in committee  | No                      |
|                | SF 458 (2011)   | Added to SF 2391   |                         |
|                | SF 2391; Article 6 (2012)   | Tabled; Legislature adjourned  |                         |
|                | HF 1849 (2012)  | Currently pending in House Committee on Taxes  |                         |
| Mississippi    | SB 2927 (2010)  | Died in committee  | No                      |
| Missouri       | HB 970 (2011)   | Died in committee  | No                      |
|                | HB 1569 (2012)  | Referred to House committee on Rules 3/1/12 – currently pending                      |                         |
| Montana        | No sales tax  | N/A  | No                      |
| Nebraska       | No bill introduced  | N/A  | No                      |
| Nevada (5)     | SB 34 (2012)  | Effective January 2014   | No                      |
| New Hampshire  | No sales tax  | N/A  | No                      |
| New Jersey (5) | SB 905 (2012)   | Referred to Senate Economic Growth Committee – currently pending                     | No                      |

| State               | Affiliate Nexus Law?   | Current Status   | Nexus Law on the Books? |
|---------------------|--|--|-------------------------|
| New Mexico          | HB 50 (2010)   | Died   | No                      |
|                     | SB 95 (2011)   | Died   |                         |
|                     | HB 102 (2011)  | Died   |                         |
| New York            | A09807C (2008)   | Signed by Governor<br>4/23/08 – Chapter 57 of<br>Laws of 2008                    | Yes                     |
| North Carolina (5)  | SB 202 (2009)  | Signed by Governor 8/7/09  | Yes                     |
|                     |  | Repeal attempt – SB 715<br>(2011)  |                         |
| North Dakota (5)    | No bill introduced   | N/A  | No                      |
| Ohio                | No bill introduced   | N/A  | No                      |
| Oklahoma (1)(5)     | HB 2359 (2010)<br>(Notification<br>requirement)  | Signed by Governor 6/9/10  | No                      |
| Oregon              | No sales tax   | N/A  | No                      |
| Pennsylvania (4)    | PA Dept. of Revenue<br>interprets the Tax<br>Reform Code of 1971 as<br>including online sellers<br>for sales tax collection<br>(12/1/11) | Collection delayed until<br>9/1/12   | Yes                     |
| Rhode Island (5)    | Enacted in 2010 Budget   | Signed by Governor<br>6/30/09  | Yes                     |
|                     | Repeal Bill HB 5115<br>(2011)  | Recommended for further<br>study 5/17/12   |                         |
| South Carolina (2)  | SB 36 (2011)   | Became law without<br>Governor's signature<br>6/20/11. Effective January<br>2016 | No                      |
| South Dakota (1)(5) | SB 146 (2011)<br>(Notification<br>requirement)   | Signed by Governor<br>3/11/11  | No                      |
| Tennessee (2)(5)    | HB 1912 (2011)   | Died in committee  | No                      |
|                     | HB 2370 (2012)   | Signed by Governor<br>3/23/12  |                         |
| Texas (2)           | HB 2403 (2011)   | Vetoed by Governor<br>5/31/11  | No                      |
|                     | Deal in which Amazon<br>collects taxes   | Took effect 7/1/12   |                         |
| Utah (3)(5)         | HB 384 (2012)  | Signed by Governor<br>3/22/12  | No                      |
| Vermont (5)         | H. 143 (2011)  | Passed in House; Died in<br>Senate   | No                      |
|                     | H. 639 (2012)  | Pending in committee   |                         |
| Virginia (3)        | SB 597 (2012)  | Enacted 4/4/12   | Yes                     |
| Washington (5)      | No bill introduced   | N/A  | No                      |
| West Virginia (5)   | No bill introduced   | N/A  | No                      |
| Wisconsin           | No bill introduced   | N/A  | No                      |
| Wyoming             | No bill introduced   | N/A  | No                      |

1. Notification requirement
2. Amazon specific
3. Wording #2 (see below)
4. Administrative decision
5. Passed legislation conforming with Streamlined Sales and Use Tax Agreement

Affiliate nexus wording 1 (from North Carolina's SB 202):

A retailer is presumed to be soliciting or transacting business by an independent contractor, agent, or other representative if the retailer enters into an agreement with a resident of this State under which the resident, for a commission or other consideration, directly or indirectly refers potential customers, whether by a link on an Internet Web site or otherwise, to the retailer. This presumption applies only if the cumulative gross receipts from sales by the retailer to purchasers in this State who are referred to the retailer by all residents with this type of agreement with the retailer is in excess of ten thousand dollars (\$10,000) during the preceding four quarterly periods. This presumption may be rebutted by proof that the resident with whom the retailer has an agreement did not engage in any solicitation in the State on behalf of the seller that would satisfy the nexus requirement of the United States Constitution during the four quarterly periods in question.

Affiliate nexus wording 2 (from Utah's HB 384):

- (b) A seller is considered to be engaged in the business of selling tangible personal property, a service, or a product transferred electronically for use in the state, and shall pay or collect and remit the sales and use taxes imposed by this chapter if:
- (i) the seller holds a substantial ownership interest in, or is owned in whole or in substantial part by, a related seller; and
  - (ii) (A) the seller sells the same or a substantially similar line of products as the related seller and does so under the same or a substantially similar business name; or
- (B) the place of business described in Subsection (2)(a)(i) of the related seller or an in state employee of the related seller is used to advertise, promote, or facilitate sales by the seller to a purchaser.



## End Notes

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