

States Should Not Allow Amazon.com to Bully Them into Forgoing Sales Tax Reform

In just the last few weeks, Arkansas and Illinois joined New York, North Carolina, and Rhode Island in enacting legislation requiring some online retailers, like Amazon.com, to collect sales taxes on purchases made by their state's residents. Vermont's House of Representatives recently passed similar legislation, and Arizona, California, Connecticut, Hawaii, Massachusetts, Minnesota, Mississippi, Missouri, New Mexico, Tennessee, and Texas are considering doing the same. Unfortunately, Amazon.com has been fighting these proposals tooth and nail, doing everything in its power to make this sensible reform as unpalatable as possible. State lawmakers should not allow themselves to be intimidated by Amazon's aggressive tactics.

The Problem

In 1992, the Supreme Court ruled in *Quill Corp. v. North Dakota* that states generally cannot require retailers to collect sales taxes on items purchased from remote sellers. Specifically, companies are only required to collect sales taxes when selling to consumers that live in a state in which that company has a "physical presence" — like a "brick and mortar" store or distribution center. This ruling has resulted in years of constant headaches for state sales tax administrators.

The Supreme Court did not create an actual tax exemption for remote sales in *Quill*. Rather, it ruled that remote sellers, unlike Wal-Mart and other traditional retailers, cannot be required to assist the state in administering its sales tax laws. When a consumer purchases an item from Amazon.com, they owe the same sales tax as if they had bought it at a brick and mortar store like Wal-Mart. The major difference is that Amazon does not have to help the state, or the consumer, in facilitating payment of those taxes. As a result, most purchases made over the Internet escape taxation because consumers are either unaware or unwilling to undertake the effort needed to remit those taxes to the state.

In addition to blowing an enormous hole in state sales tax bases, the *Quill* ruling also created an extremely uneven playing field among different types of retailers. Today, major online retailers are the biggest beneficiaries of the ruling since they're most likely to sell their products to residents located outside of states in which they have a headquarters, distribution center, or other "physical presence." For all practical purposes, big online retailers often sell their wares tax-free, while "mom and pop" stores as well as larger traditional retailers nearly always have to collect sales tax.

In its ruling, the Supreme Court made clear that Congress could remedy this situation by enacting legislation allowing states to collect sales taxes on remote sales. Bills have recently been introduced in Congress that would do just that, but they have failed to advance due to the anti-tax attitudes of many federal lawmakers, as well as a more general apathy toward this uniquely state-level problem.

"Amazon Laws"

In order to address the tax policy problem posed by remote sales, Arkansas, Illinois, New York, North Carolina, and Rhode Island have enacted laws broadening the class of online retailers that must help collect sales taxes. Specifically, under these new laws, any retailer partnering with in-state affiliate businesses is required to pay sales taxes on purchases made by residents of that state. These laws have

often been referred to as “Amazon laws,” since Amazon is the largest company affected by the change, but they affect all remote sellers with in-state affiliates in exactly the same way.

Despite some rhetoric to the contrary, these laws do not create a new tax, or even increase an existing tax. Their sole purpose is to help combat rampant tax evasion on remote sales. This is a goal that Amazon is very clearly uninterested in pursuing, presumably because it believes that making it more difficult for its customers to commit sales tax evasion will reduce its own profits.

Amazon’s Reaction: A Pattern of Bad Behavior

In response to the enactment of these so-called “Amazon laws,” Amazon.com has stopped working with affiliate businesses based out of North Carolina and Rhode Island, and has said it will do the same in Illinois this April 15. Amazon is also challenging the New York law in court, and has threatened to drop its California and Massachusetts affiliates if an “Amazon law” is enacted in those states.

Aggressive actions of this type have unfortunately become Amazon’s standard operating procedure when it comes to state tax changes it dislikes. In Texas, for example, Amazon announced that it will shut down a distribution center in order to avoid having to help the state collect sales taxes. Amazon claimed the distribution center was owned by a subsidiary, and therefore did not establish the “physical presence” needed to subject the company to the state’s sales tax laws. After a lengthy investigation, the Texas Comptroller found this line of argument unpersuasive.

Even more troubling was a decision by Amazon to drop its Colorado-based affiliates after the state enacted a law requiring remote sellers to disclose some information about potentially taxable sales made to in-state residents. In this instance, dropping its in-state affiliates did nothing to shield Amazon from the law’s requirement, and was instead done purely to punish state lawmakers for enacting a law it thought would be detrimental to its bottom line.¹

Other Retailers Step Up

While Amazon’s bullying will no doubt make it more difficult for lawmakers to vote in favor of these “Amazon laws,” other major retailers like Wal-Mart, Sears, Target, Home Depot, and Barnes & Noble are beginning to stand up for reform-minded lawmakers. Fed-up with the unfair tax advantage afforded to remote sellers, each of these companies has either begun lobbying legislators directly in support of these laws, or has offered to partner with Amazon’s recently dropped affiliates. The latter of these two developments is particularly useful in taking the sting out of Amazon’s aggressive tactics. It will be significantly easier for state lawmakers to vote in favor of Amazon laws if they can be assured that their state’s small businesses will continue to have opportunities for partnerships with other major retailers.

Conclusion

With a little courage from lawmakers, and a little help from traditional retailers, it appears that state governments are finally on the verge of narrowing the massive sales tax gap that has been created in part by the intransigence of remote sellers like Amazon. Five states have already passed “Amazon laws,” a dozen more are considering doing the same, and the list of states with a serious interest in this issue seems to be growing by the week. Until the federal government enacts legislation that allows for a more comprehensive approach to this troublesome area of state tax policy, “Amazon laws” will remain an extremely attractive policy option both for improving state tax systems, and for increasing the quality of competition between retailers of all types.

¹ Statement: Michael Mazerov, Senior Fellow, on Amazon’s Cancellation of Its Colorado Affiliate Program. March 9, 2010. <http://www.cbpp.org/cms/index.cfm?fa=view&id=3113>