

POLICY POSITION

2. REGARDING SALES TAX COLLECTIONS AND E-COMMERCE TRANSACTIONS IN SOUTHERN STATES

BACKGROUND

In the past decade, the reach of the Internet into the lives of Americans, particularly in the area of commerce, has grown unrelentingly. It will expand even further in the future. At the end of the first quarter of 2012, the U.S. Department of Commerce estimated that e-commerce sales amounted to \$53.2 billion, an increase of 3.1 percent from the fourth quarter of 2011. Even as a percent of total sales (\$1.1 trillion for the first quarter of 2012), e-commerce sales stood at 4.9 percent. In contrast, at the end of the first quarter of 2002, a decade earlier, e-commerce sales as a percent of total sales was 1.3 percent, a clear indication of growing dominance of the e-commerce sector. In addition, while e-commerce sales jumped by 15 percent over the first quarter of 2011, total retail sales only grew 6 percent over the same period. Unfortunately, this stratospheric growth in e-commerce transactions in the past few years has exposed a major structural flaw in state and local government tax systems: the erosion of sales tax revenues of state and local governments given the prohibition on these governments recouping sales taxes on e-commerce purchases.

The genesis for the prohibition on state and local governments universally collecting sales taxes on e-commerce transactions may be traced to a 1992 U.S. Supreme Court ruling, *Quill Corporation v. North Dakota*, which held that an online retailer is only required to collect sales tax on a transaction if the retailer has a physical presence in the state of the purchasing customer. Even when the revenue flows in state and local governments improve to more robust levels from the depths of the Great Recession, the inability for all states to uniformly levy sales taxes on e-commerce transactions will result in state and local governments hemorrhaging billions of dollars in revenue every year. In fact, the latest study from the University of Tennessee's Center for Business and Economic Research estimates that, in 2012, states will lose between \$11.4 billion and \$12.65 billion from untaxed online sales.

From the perspective of the 'brick-and-mortar' retailers, the fact that online retailers do not have to collect sales taxes for online purchases from consumers represented a serious price disadvantage. Requiring the collection of sales taxes on e-commerce transactions by online retailers represents an effort to even the playing field between 'brick-and-mortar' retailers and online retailers.

The most expeditious and efficient way to bridge the gaping structural chasm in state tax and revenue systems – one that will only continue to widen – triggered by the *Quill* ruling requires remedial action primarily at the federal level. In that context, there is new found optimism in many circles regarding *The Marketplace Fairness Act*, legislation introduced in November 2011 in the U.S. Senate by a bipartisan group of 10 U.S. senators. The bill, which was immediately referred to the U.S. Senate Finance Committee (in addition, the U.S. House Judiciary Committee held hearings on the topic in late July 2012), establishes a system for states and localities to collect sales taxes generated by online purchases, the kind of federal initiative that states have sought for some time. In fact, *The Marketplace Fairness Act* explicitly recognizes that “[S]tates should have the ability to enforce their existing sales and use tax laws and to treat similar sales transactions equally, without regard to the manner in which the sale is transacted, and the right to collect - or decide not to collect - taxes that are already owed under state law.” While similar legislation had been previously introduced, these efforts did not have the force of bipartisan

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support and, equally importantly, did not have the support of the nation's largest online retailer, Amazon. Amazon expressing "strong support" for the federal legislation remains a transformational move, and the bipartisan nature of the proposed bill enhances the likelihood of its passage, twin developments that previously never were achieved. Along with Amazon, traditional retailers with an online presence, such as Barnes & Noble, Wal-Mart and Target, also support the federal legislation alongside groups such as the National Retail Federation and the Retail Industry Leaders Association. In an effort to mitigate the potential negative impact on small businesses, the federal legislation exempts online businesses making less than \$500,000 a year from collecting sales taxes.

RECOMMENDATIONS

The Southern Legislative Conference of The Council of State Governments supports the ongoing efforts in the U.S. Congress to level the playing field and establish greater equity in the area of sales tax collections between transactions at 'bricks-and-mortar' establishments and online retailers.

In addition, the Southern Legislative Conference of The Council of State Governments urges the passage of *The Marketplace Fairness Act*, or one with a similar purpose, which establishes a system for states and localities to collect sales taxes generated by online purchases.

Further, the Southern Legislative Conference of The Council of State Governments requests that a copy of this policy position be forwarded to the Southern Congressional delegation and the president of the United States.