The Daily Dish

States and the Taxation of Online Sales

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On Monday Senate Majority Leader Mitch McConnell (R-KY) said that he is willing to use a special budgetary procedure that will allow him, and his fellow Republicans, to overhaul the U.S. tax code. Senator McConnell said this move, called reconciliation, would allow the GOP to pass tax reform without a single Democratic vote. The same process was used in 2010 by the Democrats to make changes to the Affordable Care Act (ACA).

Yesterday the American Action Forum (@AAF) released a new analysis examining the flaws of the Renewable Fuels Standard (RFS). AAF notes in the analysis that the EPA's RFS targets, released last month, continue a pattern of falling under those mandated by Congress. The targets recently released by the EPA fall short by almost 5 billion gallons of biofuel, ethanol, and other renewable sources.

Eakinomics: States and the Taxation of Online Sales

The typical state taxation of retail sales has two components: (a) a "sales" tax that is collected by stores and remitted to the state treasury, and (b) a "use" tax on purchases from out-of-state that is the responsibility of households to pay. Use taxes are notoriously hard to collect, a problem that has ballooned with the growth of internet-based sales. Online sales have gone from 5.7 percent of the total $3.613 trillion of retail sales in 2003 to 8.9 percent of the total sales figure of $5.068 in 2013, and continue to grow.

These trends have produced two pressures. First, brick and mortar retailers find themselves at a competitive disadvantage when taxes are not collected on internet sales, and voice their displeasure to state legislatures. Second, state treasuries lose out when in-state sales are transformed into out-of-state purchases with a use tax liability.

One might think that the the easy solution is to simply make all sellers — in-state or out-of-state — collect and remit the state sales tax. The problem is that the status quo was established by a 1992 Supreme Court decision, Quill Corp. v. North Dakota, which said that retailers without a physical presence in a state can't be forced to collect sales taxes on purchases.

The alternative strategy is to beef up collections of the use tax, a strategy followed by Colorado. It passed a law requiring out-of-state sellers to report to the state the names and purchase amounts of Colorado customers. The law was challenged in court on the grounds that it violated Congress' constitutional right to regulate interstate commerce. An appeals court has upheld the law, but the Wall Street Journal reports that the Supreme Court has declined to take up an appeal, noting "The National Governors Association, the National Conference of State Legislatures and other groups urged the court to decline the case and wait for the South Dakota litigation [a related case working its way through the courts] or another chance to squarely address the Quill precedent."

The equal treatment of equals is an old rule for good tax policy, which will continue to be violated unless Quill gets overturned or the Congress legislates.