

Collecting Sales Tax on Internet Purchases Makes Sense As Part of Tax Modernization

But New Revenues Should Not be Offset by Reductions

Florida's antiquated, inadequate, unfair tax structure is ripe for modernization after escaping serious examination by the Florida Legislature for many years. Several bills pending in this legislative session, known collectively as the Fair Economy Act,¹ would begin a comprehensive overhaul. They would close corporate income tax loopholes and increase disclosure of results of subsidies given to companies for job creation.² Another bill would mandate a study of the hundreds of sales tax loopholes in current law.³ None of those bills, however, is advancing in the legislative session.

Among the bills that are being considered are measures with the potential to increase state revenue by hundreds of millions of dollars each year – by applying an existing tax – while making the state's tax system fairer. However, some of those bills, which would enforce collection of sales taxes on Internet purchases, would squander the additional revenue and actually make Florida's tax system even more unfair.⁴

Overcoming the obstacles to collecting unpaid sales tax and raising additional revenue makes sense, particularly as part of a comprehensive plan to modernize the state's tax system to make it fairer to average Floridians and small business owners.

More promising are bills that would add Florida to the states pushing for a national solution to the issue. But they, like other progressive tax modernization bills, are languishing in both the House of Representatives and the Senate.⁵

At issue is enforcement of current law, which says that purchasers of taxable goods owe sales tax whether they made the purchase in a Florida store, by mail order, or over the Internet. In reality, however, sales tax is not collected on remote purchases made from out-of-state retailers, due to legal and practical obstacles.

As a consequence, the state loses hundreds of millions of dollars a year that could be used to fund essential functions of government like education, and health care, and social services.

Overcoming the obstacles to collecting unpaid sales tax and raising additional revenue makes sense, particularly as part of a comprehensive plan to modernize the state’s tax system to make it fairer to average Floridians and local small business owners.

Internet Tax Issue Shows How Florida’s Tax Structure Is Outmoded

Throughout the U.S., some retailers have been able to escape collecting state sales taxes on remote purchases due to a 1967 decision of the U.S. Supreme Court. The court denied states the authority to require collection of sales taxes by mail-order companies that had no physical presence in the state. It said that varying sales tax rates imposed in different states and localities created an undue compliance burden on out-of-state retailers. However, the court opened the way to a solution, ruling that Congress had the authority to resolve the collection issue.

The state of Florida and local governments lose at least \$250 million annually from untaxed online sales, according to the lowest estimate, and perhaps as much as \$800 million.

Since the 1967 case, out-of-state commerce has moved far beyond mail-order sales into the much larger, rapidly growing Internet sales realm. The shift from purchasing goods at bricks-and-mortar stores to ordering online has placed retailers located in Florida at a competitive disadvantage, while also eroding the state’s tax revenue. In effect, online sellers using the loophole enjoy more than a six percent price advantage over stores operating in Florida – the six percent state sales tax plus applicable local sales taxes. By law, purchasers of goods from remote sellers are supposed to pay

the tax themselves. But few do, either because they are unaware of the requirement or believe the state is unlikely to enforce it.

The loss to the Florida treasury is substantial. Although many retailers that sell online have a physical presence in Florida and therefore collect sales taxes, others, such as Amazon and eBay, do not. The state of Florida and local governments lose at least \$250 million annually from untaxed online sales, according to the lowest estimate, and perhaps as much as \$800 million.⁶

The revenue loss will grow because the share of U.S. retail sales made on the Internet continues to increase.⁷

The Internet tax problem illustrates the outmoded nature of Florida’s tax structure. When the state sales tax was first imposed in 1949, the Internet didn’t even exist, of course, nor could it have been foreseen. Today seven percent of all sales nationally are placed online. The economy has changed in other ways, as well – increasingly involving purchases of services instead of goods, for example – but the state tax system has not changed with it.

States Pursue Varied Efforts to Collect Taxes on Internet Purchases

Forty-five states levy a sales tax and an accompanying *use tax*,⁸ which is designed to prevent residents from avoiding the sales tax by buying goods in another state. Use taxes establish the principle that purchases are taxable where they are *used*, not where they are bought.⁹

In attempting to collect the sales and use tax on remote purchases, states have pursued several strategies.

One is enacting so-called “Amazon laws,” named after the largest online retailer, forcing Amazon and similar companies to collect sales tax by expanding the definition of what constitutes “physical presence” in a state. By considering distribution centers and local marketing “affiliate” programs through which companies get sales as constituting physical presence, states are trying to force out-of-state retailers to collect the use tax and remit it to the state.

(Affiliates are online sites used by companies like Amazon and eBay to advertise products in exchange for a commission on sales or pay-for-click.) Connecticut, Arkansas, New York, and Illinois are among the states to pass such laws.

Amazon has responded to states’ actions in several ways: legally challenging some of the new laws; ending affiliate programs in some states so Amazon is not subject to the new requirements; and negotiating to delay collection of the sales tax in exchange for building facilities and hiring workers in the state.

A Senate committee has advanced a Florida version of an Amazon law, which would force the company to collect taxes by redefining physical presence in Florida. But the bill would give back any additional revenue gained.

Bill Would Give Back New Revenue Under “No New Taxes” Philosophy

In Florida, several approaches to the problem have been offered. Amazon has floated a proposal to legislators that would exempt the company from collecting the sales tax for two years in exchange for an investment of up to \$200 million in building distribution centers in the state.¹⁰ Florida business interests oppose the exemption; they maintain that Amazon would likely build distribution facilities in the state anyway, without the tax break. No official action regarding Amazon’s offer has occurred in the legislature.

Meanwhile, two Senate committees have passed Florida versions of an Amazon law that would redefine physical presence in the state to force out-of-state retailers to collect sales taxes at the time of purchase.¹¹ There is no guarantee that such a law would survive a legal challenge, however, legislative staff analyses conclude.¹²

Furthermore, one bill (PSB 7206) would give back any additional revenue gained. It would require state economists to determine each year how much new revenue the Internet tax produced and the

legislature in the following year would cut taxes by that amount.¹³

That approach is the result of the opposition of Governor Scott and legislative leaders to any measures that would raise taxes or fees (although legislative leaders propose another tuition increase).¹⁴ Because enforcing collection of the sales tax on Internet purchases would add revenue, they maintain that such action constitutes imposing a new tax – even though state law already makes such purchases subject to taxation.¹⁵

They insist that if action were taken to collect the tax already owed, other taxes should be lowered to make the net effect “revenue-neutral”. The Senate committee bill would require the legislature to offset new collections with sales tax holidays, lowering the sales tax rate, or implementing “other tax relief as it deems appropriate.”¹⁶

Other bills introduced in this legislative session suggest some options for “other tax relief.” One bill would reduce local property taxes devoted to public schools to offset increased sales tax collections.¹⁷ An idea pushed by business organizations would reduce the state corporate income tax to offset revenue gained from collecting Internet sales tax.¹⁸

National Solution Is Possible, But Florida Has Not Joined the Effort

A better approach to Internet taxation would be implemented under bills (Senate Bill 430 and House Bill 321) that would make Florida part of a broad national effort to resolve the Internet taxation issue. The

Collecting taxes owed on Internet purchases makes sense, especially if done in concert with a review of exemptions, exclusions, deductions, and credits. But proposals that would offset additional revenues would worsen existing flaws in Florida’s tax structure.

national solution would build upon action begun in 2000, when representatives of many states began devising a simple, uniform sales tax system designed to eliminate the collection burdens on businesses. Their work led to a Streamlined Sales and Use Tax Agreement ratified in 35 states in 2001-02. The agreement became operational in 2005 when 13 states revised their laws to fully comply with the agreement.¹⁹ That number has increased to 24 through May 1, 2011; those states have begun receiving some tax revenue from retailers who voluntarily participate in the simplified system.²⁰

Florida, however, is not among the states that have passed laws implementing the agreement. In 2001, the legislature did authorize state officials to participate in discussions about a simplified sales and use tax.²¹ But the legislature has not yet followed up by enacting legislation that would change the state’s sales tax law in conformity with the Streamlined Sales and Use Tax Agreement.²²

Doing so would allow Florida to benefit if Internet sales tax legislation passes Congress, where supporters are growing more confident of eventual success. The most recent bill, the Marketplace Fairness Act filed in the U.S. Senate by 10 senators of both parties, would authorize states that have

adopted the streamlined sales tax to require all sellers doing more than \$500,000 in business annually to collect and remit sales tax on remote sales.²³ Because it establishes uniform standards on taxable items across the nation, Amazon supports the bill.²⁴

Conclusion

Collecting taxes owed on Internet purchases makes sense, especially if done in concert with a review of exemptions, exclusions, deductions, and credits and other tax loopholes. Requiring out-of-state retailers to collect the tax would level the playing field for Florida-based companies and strengthen the state's tax structure. The national solution using the streamlined sales tax agreement would provide the most comprehensive and legally defensible approach to the Internet tax issue.

But proposals that would offset additional revenues with reductions elsewhere would worsen existing flaws in Florida's tax system. First, a "revenue-neutral" Internet tax policy would miss a large opportunity to make the state's tax system more adequate to meet needs. The state particularly needs additional sources of revenue to regain ground lost to deep budget cuts for education, health care, and social services over the last five years.

Even worse than offsetting new revenues through other sales tax cuts would be cutting the corporate income tax.

Secondly, increasing sales tax collections while reducing other taxes would make Florida's tax structure even more unfair than it is now. It's already ranked as the second-worst in terms of fairness in the nation,²⁵ in part because it relies more heavily than any other state on the sales tax. Without a state income tax or a state property tax, Florida already receives 83 percent of its general revenues from the general sales tax and selective sales taxes on consumption of items such as alcohol, tobacco, and gasoline.²⁶

Sales taxes are considered the most regressive because they impose a greater burden on lower-income individuals than on those with high incomes: The lower a family's income, a larger share of it will be spent on taxable items the family must buy. (An income tax, in contrast, is progressive: the higher a person's income, the higher burden the tax rate.)

Even worse than offsetting new revenues through other sales tax cuts would be cutting the corporate income tax, which would also make Florida's tax system even more unfair. When the corporate tax is reduced, budget cuts follow, and average Floridians would fund a greater share of the budget while profitable multistate and multinational corporations escape paying their share for the benefits they receive when doing business in the state. Florida needs to close corporate tax loopholes, not reduce or eliminate the tax.

This report was researched and written by Alan Stonecipher. The report and its findings do not necessarily reflect the views of the FCFEP Board of Directors.

Endnotes

¹ <http://floridafaireconomy.org/>

² Senate Bills 1590 and 1592; House Bill 1335.

³ Senate Bill 1832 and House Bill 907.

³ “Application of Florida’s Sales Tax to Sales by Out-of-State Retailers,” Budget Subcommittee on Finance and Tax, Florida Senate, August 2011.

⁴ House Bill 1181 and Senate Bill 7206.

⁵ House Bill 321 and Senate Bill 126.

⁶ “Application of Florida’s Sales Tax to Sales by Out-of-State Retailers,” Budget Subcommittee on Finance and Tax, Florida Senate, August 2011.

<http://www.flsenate.gov/PublishedContent/Session/2012/InterimReports/BFT1072012-107ft.pdf>

⁷ “Forrester Forecast: Online Retail Sales Will Grow To \$250 Billion By 2014,” March 8, 2010, techcrunch.com.

<http://techcrunch.com/2010/03/08/forrester-forecast-online-retail-sales-will-grow-to-250-billion-by-2014/>

⁸ 2010 State Tax Collection by Source, Federation of Tax Administrators.

<http://www.taxadmin.org/Fta/rate/10taxdis.html>

⁹ “Streamlined Sales Tax Project – Implementing Language,” Interim Project Report 2003-126, January 2003, Florida Senate.

¹⁰ “State Weighs Whether to Tax Amazon’s Online Sales or Cut Jobs Deal,” Tampa Bay Times, January 26, 2012.

<http://www.tampabay.com/news/business/economicdevelopment/state-weighs-whether-to-tax-amazon-or-cut-a-deal/1212338>

¹¹ SPB 7206, Florida Senate. <http://www.flsenate.gov/PublishedContent/Committees/2010-2012/BFT/MeetingRecords/2-2-12epacket.pdf>; Senate Bill 1514.

<http://www.flsenate.gov/Session/Bill/2012/1514/Analyses/P5GTiYXPy1r5xRQ5valldF7RK6g=|11/Public/Bills/1500-1599/1514/Analysis/2012s1514.pre.cm.PDF>

¹² Ibid.

¹³ SPB 7206. <http://www.flsenate.gov/Session/Bill/2012/7206>

¹⁴ “Arduin: Florida’s Sales Tax Base Is Eroding,” Orlando Sentinel, November 6, 2011.

http://blogs.orlandosentinel.com/news_politics/2011/11/arduin-floridas-sales-tax-base-is-eroding.html?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+news%2Fpolitics%2Fpolitic+alpulse+%28Central+Florida+Political+Pulse%29

¹⁵ “Application of Florida’s Sales Tax to Sales by Out-of-State Retailers,” Budget Subcommittee on Finance and Tax, Florida Senate, August 2011.

<http://www.flsenate.gov/PublishedContent/Session/2012/InterimReports/BFT1072012-107ft.pdf>

¹⁶ SPB 7206. <http://www.flsenate.gov/Session/Bill/2012/7206>

¹⁷ HB 1181 – Revenue-Neutral Tax Reform, Florida House of Representatives.

<http://www.myfloridahouse.gov/Sections/Bills/billsdetail.aspx?BillId=48418>

¹⁸ “Pro-Growth Tax Reforms & Internet Based Sales,” Arduin, Laffer & Moore Econometrics, September 2011.

<http://mymainstreetflorida.com/files/2011/11/2011-ALME-Internet-Sales-Tax.pdf>

¹⁹ “Closing the Online Tax Loophole,” National Conference of State Legislators, April 2008.

<http://www.ncsl.org/?tabid=12585>

²⁰ Streamlined Sales Tax Governing Board, Inc. <http://www.streamlinedsalestax.org/index.php?page=faqs>

²¹ “Streamlined Sales Tax Project – Implementing Language,” Interim Project Report 2003-126, January 2003, Florida Senate.

²² SB 430: Streamlined Sales and Use Tax Agreement, Florida Senate.

<http://www.flsenate.gov/Session/Bill/2012/430>

²³ S. 1832, U.S. Senate. <http://www.gpo.gov/fdsys/pkg/BILLS-112s1832is/pdf/BILLS-112s1832is.pdf>

²⁴ “The Last Tax Free Cyber Monday?” Forbes, November 23, 2011.

<http://www.forbes.com/sites/janetnovack/2011/11/23/the-last-tax-free-cyber-monday/>

²⁵ “Who Pays? A Distributional Analysis of the Tax Systems in All 50 States,” Third Edition, Institute on Taxation and Economic Policy, November 2009. <http://www.itepnet.org/whopays3.pdf>

²⁶ 2010 State Tax Collection by Source, Federation of Tax Administrators.

<http://www.taxadmin.org/Fta/rate/10taxdis.html>