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Tax VOX

Amazon is losing business in states where it collects online sales tax

Amazon and other online retailers have argued for years that they'll lose business if they have to collect sales taxes on their online transactions. According to a new study of Amazon sales, they're right, which may increase support by some online sellers for federal legislation to standardize sales tax collections.

By [Howard Gleckman](#), *Guest blogger* / April 30, 2014



A United Parcel Service driver delivers packages from Amazon.com in Palo Alto, Calif. A new study looked at five states that required Amazon.com to collect sales taxes. Once Amazon stated collecting, consumers in those states bought 9.5 percent less from the firm.

Paul Sakuma/AP/File

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Online retailers have argued for years that they'll lose business if they have to collect sales taxes on their online transactions. [A new study](#) by three researchers at Ohio State finds they are right. Paradoxically, the study may increase support by some online sellers for federal legislation to standardize collections across states.

The study, by Brian Baugh, Itzhak Ben-David, and Hoonsuk Park, looked at five states that required Amazon.com to collect sales taxes. Once Amazon stated collecting, consumers in those states bought 9.5 percent less from the firm.

Not surprisingly, the authors found that consumers were especially likely to change their shopping behavior to avoid tax on more costly items. For instance, they cut spending by 15.5 percent on purchases larger than \$150, and by nearly 24 percent on goods or services that cost \$300 or more.

The authors also looked at where those consumers did buy. Most just shifted to other online sellers (that, presumably, did not collect sales tax). For instance, many simply bought from Amazon Marketplace merchants that are accessible on Amazon's site but do not have to collect tax. Only a handful—about 2 percent—took their business to local bricks-mortar retailers, the study found. Those Main Street firms do have to collect tax.

The study, published as a working paper by National Bureau of Economic Research, looked at sales data from California, New Jersey, Pennsylvania, Texas, and Virginia before and after they required online sellers with a physical presence in their jurisdictions to collect sales taxes. In practice, the levy applied only to Amazon and a

handful of other e-tailers. Technically, of course, buyers still owe tax whether the seller collects or not but, in reality, almost no-one pays these use taxes.

The Ohio State study is the latest research that appears to confirm that buyers change behavior to avoid paying sales tax. About a year ago, three researchers from Stanford and one from eBay [found similar results](#) after reviewing data from the firm's online marketplace. They found that a 1 percentage point increase in a state's sales tax rate leads to a 3-6 percent decline in online purchases from consumers in that state.

[A third recent paper](#), by Ohio State's Jeffrey Hoopes and the University of Washington's Jacob Thornock and Braden Williams found that when investors expected that online sellers would have to collect sales taxes (following, for instance, published news that lawmakers were considering such a move), stock prices for those firms fell somewhat.

While some older research finds little or no evidence that online sales taxes reduce consumer spending, the Ohio State study and other new work shows strong effects. And they may help explain why the political climate for federal legislation aimed at consistent sales tax rules for all online sellers seems to be changing.

It may seem counterintuitive at first, but Amazon and other large online sellers (though not eBay) now support such a measure. The reason: States are increasingly requiring them to collect. And, rather than lose business to other online sellers, they'd just as soon every retailer face the same burden.

The paper by Baugh and colleagues suggests that these while these online retail powerhouses may have little to fear from Main Street, they need to keep a close eye on their Web-based competitors who don't collect sales taxes.

Online Sales Taxes Reduce Amazon's Sales Then Why Is Amazon In Favour Of Online Sales Taxes?

It's always rather puzzling to see someone, or a corporation, arguing in favour of a public policy which seems to militate against their own direct interests. So it is with Amazon supporting the idea that all online retailers should have to collect sales [taxes](#) for the States that they're delivering to: especially as we now have good research showing us that the collection of such sales taxes actually reduces Amazon's own sales.

When we do find a situation like this we can, of course, simply conclude that people are being altruistic and doing the right thing. OK, once we've left the naive in the dust with that argument, what actually is going on then? Why is Amazon supporting a policy that is quite clearly, as first look, against their own interests?

For we can indeed see that collecting sales tax on sales is detrimental to Amazon at [some level](#):

Our results show that the introduction of the Amazon Tax resulted in a large decline across all states of 9.5% in the value of products (net of sales tax) purchased on Amazon.

Heek! That's a heavy hit. Where are those sales going?

We document that households substitute away from Amazon to competing retailers, whether brick-and-mortar or online. We show a 19.8% increase in purchases at the online operations of competing retailers. We also find a 2.0% increase in local brick-and-mortar expenditures at these retailers.

They're mostly staying online but going to online retailers who are not Amazon. All of which leaves us with a puzzle, for it's very much true that Amazon is supporting the idea that all online retailers must collect sales tax for each and every State where it is applicable. We discussed that [back here](#). So, what gives?

We need to go back a little into the background of sales tax. Some States have it and some don't. That's fine: and it's also true that, normally, if you as a business don't have an outlet in a specific State then you don't have to collect sales tax on deliveries into that State. The proposal is that you will have to in the future, that's what the potential law change is. The definition of an "outlet" is of course subject to all that gloriously confusing minutiae of the law but the presence of a warehouse in a State would normally be regarded as having an outlet, a "permanent establishment" in the jargon, in that State. This is the reverse of international tax law where a warehouse is expressly defined as

not creating a permanent establishment. The consumer is supposed to add the sales tax not yet paid to their State income tax return but a reliably large number of people don't in fact do this.

Amazon has traditionally (and how odd it is to use the root "tradition" for a business less than 20 years old) had very few warehouses in very few States. Thus it gained immensely from being able to ship to the majority of States without having to collect that sales tax. And thus was quite happy with the way the system was set up.

However, Amazon is now expanding its system of warehouses. It wants to be able to do same day deliveries, to move into the groceries trade and so on. This means having permanent establishments in more States: and thus being liable to collect sales tax on sales in those more States. This is now putting Amazon at a competitive disadvantage *vis a vis* the other online retailers who don't have so many warehouses and thus don't need to collect the tax. And as we can see that disadvantage is quite large: as much as 10 % of sales can bleed away to those other online retailers.

The solution for Amazon is therefore obvious: if we're at a competitive disadvantage because we have to collect sales tax and others don't, then why not militate for the law to be changed so that everyone has to collect sales tax? Then our competitive disadvantage on price goes away and our competitive advantage on size, speed of delivery etc becomes more apparent.

You might think this is a rather cynical explanation of the way in which Amazon has changed its mind about whether online firms should be collecting sales taxes or not. And it might even be cynical: the question is whether it is appropriately so and I would insist that it is.

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