

NEW YORK: DOUBLE-DEALING ON RETAIL TAXES

by George A. Pieler

With economic uncertainty everywhere, government dragnets are tracking down every penny of “lost” revenue they can get their hands on. After all, it’s much easier to crack down on tax compliance than to actually rein in frivolous, wasteful spending commitments that most states made during boom times. Not for the first time, New York State is leading the way.

What politicians too often forget is the average American’s sense that there is something basically unfair about changing the tax rules mid-stream. Yet that’s exactly the trap New York walked into (with others ready to follow) by going after out-of-state sales tax revenues, hoping to fly under the taxpayer’s radar by invoking the image of “fairness” to New York-based, brick-and-mortar retail establishments.

On June 1, New York began forcing online retailers to collect sales tax from vendors of any goods shipped to New York. From Jamestown to Poughkeepsie, New Yorkers who purchase online from, say, Sunnyland Farms (Georgia Pecans) or wildpacificsalmon.com (Alaska), are liable for New York sales tax if they have some kind of web-link or marketing presence with even a tenuous New York connection. Oh, and these small vendors in Georgia, Alaska, and everywhere else are legally liable for collecting that tax. That’s right, folks, this is not just about Amazon.com and Overstock.com, the two online biggies that are challenging New York in court.

What’s wrong with this picture? If sales tax is due anyway, what’s wrong with asking the online vendor to collect and remit that tax to New York (or to any other state that wants to use this collection system)? It’s really a simple Ponzi scheme being played on tax-

payers. New Yorkers pay taxes of all kinds (the fourth-highest in the nation, according to the Tax Foundation), including sales tax to vendors of all kinds, in New York and (depending on local convenience), New Jersey, Connecticut, Pennsylvania, and any state they may be vacationing in and passing through. As a practical matter, sales taxes are naturally associated with the physical location of the actual sales transaction. Folks who pay up at the sales counter, no matter where in the country that counter is located, understandably feel they have done their duty to the tax-person, and should not *also* have to pony up when they buy in cyberspace, a location not obviously controlled by any one state.

In short, the rules of the game are being changed mid-stream. The stakes seem manageable because no one taxpayer is tapped too heavily, but the principle—rather the lack thereof—is pretty disturbing.

Unless you are the *New York Times*, that is. Saul Hansell, writing the *Times*’ Technology Blog on June 2, 2008, nonchalantly asserted that New York’s so-called “Amazon Tax” “isn’t actually a change in the law—New York residents always owed tax on their purchases—it is an expansion of the law that is meant to force online retailers to collect the tax and send it to New York.” No sir, it *is* a change, and no sir, New Yorkers do *not* necessarily owe tax on all online purchases.

The reasons are both legal and prudential. The issue is hardly new, since sales-tax collection has been a major point of dispute between local retailers and mail-order sellers for decades. The Supreme Court has spoken to the question, and in the *Quill* decision said

that for a state to order sales tax collections from out-of-state retailers, those retailers must have some physical connection (nexus) with the state. That could be just one retail outlet, even a major warehousing facility, but never just a purchaser located in the taxing state. Yet the right to force merchants to collect tax based on those purchasers being in New York is what New York now asserts.

Understand this is not just the Supreme Court splitting the difference between opposing positions, but of applying the constitutional genius of the Founding Fathers to modern commercial practice. The Constitution gives power over cross-border (interstate) commerce to the national government, not to New York State. When goods arrive at (or services are provided at) a point of sale in New York, New York has plenary power to tax. Everything else is a grey area. The Court tried to take away some of that grey by propounding its nexus standard, a somewhat complex formula based on location of physical facilities and activity in a state. New York now overrides that legal standard with an act of legislative imagination: Its new on-line sales tax law is widely interpreted to mean having an advertising or marketing presence in New York is enough to trigger tax collection. But of course, *every* on-line retailer has that, and it has never been deemed to create a “nexus” with New York before now. That’s why Overstock.com promptly terminated its affiliate relations with any and all New York-based companies.

Immediate result? New York companies lost valuable business, and New York lost valuable revenues generated by that business. The tax collector, ever trying to outfox the market, never learns his (or her) lesson. Chasing after every last dollar of theoretically collectible tax always costs more revenue than it gains. This is particularly true of Internet sales, the biggest growth area of the consumer economy in the past decade. Has it ever occurred to the geniuses in Albany that New York-based sellers of online goods and services have a lot at stake here too? If and when other states pick up the cause of on-line sales taxes, the resulting tax burden will put a big damper on sales of New York bagels, wines, cheeses, paper goods and so much more that can be purchased in cyberspace.

The Internet can’t be looked at as a new way to define a point for assessing sales tax. Internet sales in general are

a catalyst for economic activity, and that activity generates robust revenues from the companies doing business on the Internet. Many of those companies are mom-and-pop, or mother-and-daughter, operations that could quickly become nonviable if they have to be out-of-state tax collectors. Small startups—remember Ebay, the early years?—are the very genius of Internet commerce. New York would kill them in their cradles, and all to generate, on paper, a few extra tax dollars. In fact, if this kind of tax-raising competition gains steam, there won’t be any extra tax dollars, just less economic growth. Is 2008 really the year to pursue that particular policy line?

The New York State Senate, having second thoughts, thinks not: It’s already voted to repeal the “Amazon tax,” but that may just be a politically convenient way to have it both ways in facing the voters. Either way, prudentially, or constitutionally, New York is not offering us the change we need. As for the *New York Times*, well, its revenues haven’t been that great this year, either. Why expect them to understand the miracle of Internet commerce?

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