

**California's Tax System – Report #2b**  
**Sales and Use Tax Weakness & Possible Remedies:**  
**Use Tax Collection Challenges**

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*This is one in a series of reports on weaknesses in California's tax system. Report #1 listed several structural weaknesses and policy issues that exist in most of California's taxes and the system overall. Subsequent reports provide further details on each of the weaknesses and issues, along with possible remedies. The purpose of this series of reports is to help promote serious discussion on the need to and the ways to bring California's tax system into the 21<sup>st</sup> century so it may best promote economic growth, be more equitable, efficiently meet state revenue needs, reduce taxpayer frustration, and be understandable and transparent. A blog accompanies these reports to enable online discussion and a website exists to access the reports and the blog:*

*[http://www.cob.sjsu.edu/nellen\\_a/TaxReform/21st\\_century\\_taxation.htm](http://www.cob.sjsu.edu/nellen_a/TaxReform/21st_century_taxation.htm)*

**June 2008 Update**

See end of report.

**Introduction**

Soon after the enactment of a sales tax in 1933, California enacted a *use tax* to ensure that tax was collected on taxable purchases made by California buyers even if the seller was not legally obligated to collect the sales tax. The use tax was intended to put California retailers on “an equal footing with their out of state competitors” who were exempt from the sales tax because they were not located in California.<sup>1</sup> While the sales tax is imposed upon the retailer (although they may pass it on to the buyer), the use tax is legally imposed upon the buyer. The rate and base for each tax is the same.

A seller without a physical presence in the state is not obligated to collect sales tax from buyers located in that state.<sup>2</sup> A non-present (remote) seller may still register with the taxing state and collect sales and use tax, but it is not obligated to do so. Remote sellers have been selling to California customers for decades primarily through catalog sales. E-commerce has brought about another sales approach that does not require the seller to have a physical presence in the state.

Many buyers likely believe that a purchase from a remote vendor is tax free because the buyers are not aware of the use tax. Also, little effort has been made by many states, including California, to educate buyers about the use tax. Just a few years ago, individuals would have to read far into the instruction book for Form 540 (the California individual income tax form) to learn anything about the use tax and how to comply with it. Since there was no line on the Form 540 about a use tax, individuals likely never saw the instruction book information on it. California has since followed the lead of many other states and added a

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<sup>1</sup> *Bank of America National Trust and Savings Association v. State Board of Equalization*, 209 Cal App 2d 780, 26 Cal Rptr 348 (First App Dist 1963).

<sup>2</sup> This standard was confirmed by the U.S. Supreme Court in *Quill Corporation v. North Dakota*, 504 U.S. 298 (1992) and *National Bella Hess .v Department of Revenue of Illinois*, 386 U.S. 753 (1967).

specific line on Form 540 for the use tax.<sup>3</sup> This may cause taxpayers to go to the instruction book to learn about the tax. However, if an individual has not kept records of his taxable purchases during the year for which sales tax was not charged, it is difficult to properly comply with the use tax collection obligation at the time the Form 540 is due.

The e-commerce business model increases the use tax collection issue because that model enables businesses to easily sell to buyers in any state without having a physical presence there. The e-commerce model also enables a vendor to easily avoid all sales tax compliance by following a practice (and noting it on their website) that they ship from State X (where the vendor resides), but do not sell to customers in State X. This approach enables vendors to avoid collecting tax in State X (they have a physical presence there, but no sales) and in any other state because they only have a physical presence in State X. Also, it is easy for online shoppers to search online to find out-of-state online vendors who do not collect sales tax.

This report provides data on the size of the uncollected use tax problem, what some other states have done to address the problem and provides recommendations for improving use tax collection in California.

**Weakness:** Not all use tax owed is collected.

**Remedy:** Educate taxpayers about the use tax and simplify compliance.

## The Extent of the Problem

*Uncollected use tax:* Data on the amount of use tax that goes uncollected varies from study to study. Listed below are results of some key studies conducted in this area.

- A June 1999 study concluded that 63% of business-to-consumer online sales were non-taxable (such as airline tickets, gambling, and interactive games). Of the remaining 37% of business-to-consumer sales, sales tax was paid on 4% (4% of the 100% of business-to-consumer sales), and 20% was a substitute for other remote sales for which no tax was collected, leaving 13% of total business-consumer sales untaxed. The study applied an average state and local sales tax rate of 6.5% to determine that the estimated sales tax loss was \$170 million for 1998, representing one-tenth of 1% of total state and local sales tax collections.<sup>4</sup>
- A June 2000 Government Accountability Office (GAO) study estimated that the state and local sales and use tax losses for all Internet sales for 2000 was between \$0.3 and \$3.8 billion (about 2% of projected sales tax revenue). This included both business-to-business and business-to-consumer Internet sales. The projected loss for 2003 was between \$1.0 and \$12.4 billion (5% of projected sales tax revenue). The differences between the high and low figures was due to varying

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<sup>3</sup> The line was added to the individual and corporate income returns (Forms 540 and 100) to cover purchases of tangible personal property made on or after 1/1/03 through 12/31/09 (SB 1009, Chapter 718, 2003). Sellers registered for sales tax may not use this reporting approach. Use of the income tax reporting approach constitutes an irrevocable election to use that technique rather than the regular reporting method for sales and use tax. Per the Assembly analysis of AB 969 (2007); 5/23/07 (<http://www.leginfo.ca.gov/bilinfo.html>), use tax reported on income tax forms for 2004 was \$2.8 million, \$4.6 million in 2005 and \$5.5 million in 2006. Taxpayers who prepared their own return were 8 times more likely to complete the use tax line than were taxpayers who used paid preparers. The sponsor of AB 969 believes this is due to the elective nature of reporting use tax on the income tax form, which makes it look voluntary. (It is *elective* only because taxpayers could instead file sales/use tax forms in the same year in which they incurred the use tax liability rather than the subsequent year when their income tax form is due. AB 969 proposes to make reporting of use tax on the income tax form mandatory to increase awareness and compliance.)

<sup>4</sup> Ernst & Young, *The Sky is Not Falling: Why State and Local Revenues Were Not Significantly Impacted by The Internet in 1998*, June 18, 1999.

assumptions as to business-to-business compliance rates and the estimated amount of e-commerce sales.<sup>5</sup>

- In March 1999, the California Board of Equalization estimated that California's annual loss of sales and use tax from e-commerce was about \$18.5 million.<sup>6</sup> The June 2000 GAO study projected sales and use tax losses in California from all Internet sales for 2000 as between \$23 and \$533 million. The GAO's projection of lost revenue for 2003 was between \$86 and \$1,720 million.<sup>7</sup>
- For 2004-2005, the BOE reported that failure to pay use tax was the most frequent sales tax error and the second most costly one resulting in audit deficiencies of \$84 million.<sup>8</sup>
- In 2002, the BOE estimated use tax loss from households purchasing from remote vendors as \$309 million from mail order sales and \$146 million from Internet sales for a total of \$456 million in uncollected use tax. They estimated use tax loss from businesses to be \$783 million, for a total of over \$1 billion uncollected use tax each year. Most of the uncollected business use tax was attributable to businesses that do not sell tangible personal property and so are not required to register with the BOE and file sales tax returns.<sup>9</sup>
- The June 2000 report from the GAO indicated a wide range of estimates on what consumer and business compliance rates were with respect to paying use tax. In its estimates, GAO used a consumer compliance rate of between 0% and 5% and 50% to 90% for business purchases with the exception of auto purchases.<sup>10</sup> Because cars must be registered, the use tax can be collected and use tax compliance is about 100%.<sup>11</sup>
- In July 2004, Drs. Bruce and Fox of the University of Tennessee updated earlier estimates of state and local tax revenue losses from e-commerce. The new estimates were reduced due to the reality that "e-commerce has been a less robust channel for transacting goods and services than was anticipated" earlier. The new estimate for 2008 indicates state and local tax revenue loss of between \$21.5 and \$33.7 billion depending on the growth assumption used. The 2003 estimate for losses in California is between \$2.1 and \$2.2 billion, and between \$2.95 and \$4.62 billion for 2008. For the 2008 estimate, between \$637 and \$996 million represents losses for local governments.<sup>12</sup>
- A 2003 report by the Direct Marketing Association questioned the data from the University of Tennessee for 2000 and 2001. The DMA suggested that for 2001, uncollected sales tax on e-commerce was only \$1.9 billion and would likely be \$4.5 billion by 2011 which is 10% of the

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<sup>5</sup> GAO, *Sales Taxes – Electronic Commerce Growth Presents Challenges; Revenue Losses Are Uncertain*, GAO/GGD/OCE-00-165, June 2000.

<sup>6</sup> California Senate, *E-Commerce - Taxing Internet Sales and Access*, Pub. #99-1, September 1999.

<sup>7</sup> GAO, *Sales Taxes – Electronic Commerce Growth Presents Challenges; Revenue Losses Are Uncertain*, GAO/GGD/OCE-00-165, June 2000, Table V.1 and Table V.2.

<sup>8</sup> BOE, 2004-5 Annual Report, Sales and Use Taxes, pp 34 – 35; available at <http://www.boe.ca.gov/annual/pdf/2005/4-sales05.pdf>.

<sup>9</sup> BOE, Staff Legislative Bill Analysis, SB 1009, 6/18/03; available at <http://www.boe.ca.gov/legdiv/sutleg/pdf/sb1009-3bm.pdf>. The BOE also estimated that having a use tax line on the personal income tax form would lead to about 1% of the unpaid use tax being reported with the same 1% result for businesses.

<sup>10</sup> GAO, *Electronic Commerce Growth Presents Challenges; Revenue Losses Are Uncertain*, GAO/GGD/OCE-00-165, June 2000, pages 34 - 35.

<sup>11</sup> Some states, including California, have begun to collect excise and use taxes from consumers on on-line purchases of tobacco products with the help of a 50 year old federal law that requires reporting of purchaser names. David Streitfeld, "Online Tobacco Sales Ignite Fight Over Taxes," *The Washington Post*, August 29, 2000, page A1.

<sup>12</sup> Dr. Donald Bruce and Dr. William F. Fox, "State and Local Sales Tax Revenue Losses from E-Commerce: Estimates as of July 2004," July 2004, available at <http://www.ncsl.org/print/press/Ecommerceupdates.pdf>.

University of Tennessee estimate (the UT estimate was \$54.8 billion<sup>13</sup>). Some of the differences between the UT and DMA estimates are due to the DMA using a higher tax compliance rate for businesses and recognizing the likely growth of multi-channel, clicks and bricks commerce where consumers want to be able to buy online but return at a physical store which will lead retailers to have a physical presence in the state for their online operations and be required to collect sales tax (rather than the consumer having to self-report use tax). Another difference is that DMA suggests that billions of dollars of EDI (Electronic Data Interchange) activity among businesses should have been excluded as not being Internet sales.<sup>14</sup>

- Minnesota has studied its sales tax gap (uncollected sales tax). Results of the study indicated that for 2000, about 28% of the sales tax gap was due to sales by remote vendors where buyers failed to pay the use tax. They projected that this cause of uncollected sales and use tax would grow to be about 50% of the total tax gap by 2007.<sup>15</sup>
- A 2003 report from the Washington Department of Revenue noted that businesses registered in the state failed to report about 28% of the use tax owed on purchases from out of state. The annual use tax loss was over \$100 million. The Department found that use tax noncompliance had increased almost 20% from 1996 to 2003, likely due to the growth of e-commerce use by businesses.<sup>16</sup>

*Growth in e-commerce:* E-commerce continues to grow which will cause the use tax collection problem to also grow. Indications of growth include the following:

- The U.S. Census Bureau reported that e-commerce sales for the first quarter of 2007 were 18.4% higher than for the first quarter of 2006 and represented 3.2% of total retail sales. In 1999, e-commerce represented less than 1% of total retail sales.<sup>17</sup>
- Data from Forrester Research indicates that in 2006 consumers spent more online for clothes (\$18.3 billion) than for computers and software (\$17.2 billion). They also found that over 50% of households in the U.S. shop online on a regular basis. Yet, online sales still represent less than 10% of total retail sales although online shopping represents 21% of total book sales and 41% of total computer and software purchases.<sup>18</sup>

## Why Improve Use Tax Compliance

Reasons for improving use tax compliance include.

1. The use tax has been in existence since 1935; it is not a new tax. Improved collection will provide needed revenue for the state without the need to increase a tax rate or create a new tax.
2. Failure to collect use tax violates the principles of equity and neutrality. Equity and fairness are violated when taxpayers are able to purchase goods online without paying tax while others buying

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<sup>13</sup> Bruce and Fox, "State and Local Sales Tax Revenue Losses from E-Commerce: Updated Estimates," 9/01, available at <http://cber.bus.utk.edu/ecommm/ecom0901.pdf>. Also see additional reports at <http://cber.bus.utk.edu/ecommm.htm>.

<sup>14</sup> Dr. Peter A. Johnson, Direct Marketing Association, "A Current Calculation of Uncollected of Uncollected Sales Tax Arising from Internet Growth," March 2003; available at <http://www.the-dma.org/taxation/CurrentCalculationofUncollectedSalesTax.pdf>.

<sup>15</sup> Minnesota Department of Revenue, "Minnesota Sales Tax Gap study;" available at [http://www.mndor.state.mn.us/legal\\_policy/research\\_reports/content/tax\\_gap\\_study.shtml](http://www.mndor.state.mn.us/legal_policy/research_reports/content/tax_gap_study.shtml).

<sup>16</sup> Washington State Department of Revenue, "Latest Compliance Study Shows Sharp Drop in Use Tax Compliance," 1/24/03; available at [http://www.dor.wa.gov/Docs/Pubs/News/2003/nr\\_03\\_01\\_%20UseTxNonCompliance.pdf](http://www.dor.wa.gov/Docs/Pubs/News/2003/nr_03_01_%20UseTxNonCompliance.pdf).

<sup>17</sup> U.S. Census Bureau News, 5/16/07; available at <http://www.census.gov/mrts/www/data/html/07Q1.html>.

<sup>18</sup> Pia Sarkar, "Fashion purchases outpace tech buys online," *San Francisco Chronicle*, 5/15/07, pg C1.

the same items at their local store pay the tax. Vendors with physical stores can find it difficult to compete with online vendors who can sell without collecting sales tax to consumers who are unaware that they owe a use tax which makes the item comparable in price to that of the other vendor. Also, when buyers perceive that online items are cheaper than the same items purchased at a physical store, they may be inclined to purchase online, thus further exacerbating the use tax collection problem. Additional tax principles are addressed later in the tax policy analysis chart.

## Challenges

Because consumers know so little about the use tax, improved enforcement is likely to be viewed by many as the enactment of a new tax.

Another challenge is that the current sales and use tax rules are not simple. Taxpayers will need guidance as to which of their purchases are taxable and which are not, particularly where handling charges or services are associated with the purchase of tangible personal property.

## Recommendations to Improve Compliance

1. Educate taxpayers about the use tax – what it is, how long it has existed, when it applies, how to calculate it and how to pay it. Information on the amount of uncollected tax should also be provided, perhaps in terms of how it compares to total tax collections or a favored government spending program, such as K-12 education.

Since Internet sales often generate use tax, the Board of Equalization should post informational ads on Internet sites to help educate people about the use tax and how to comply. The Board reports that it did use online advertising in 2005-2006 to educate buyers about the use tax.<sup>19</sup> In early 2007, the Board also mailed letters to tax practitioners in the state encouraging them to discuss use tax compliance with their clients. Greater and more continual effort is needed though.

2. Implement simpler techniques for compliance by individual consumers. In a few states, including Maine, Michigan and New York,<sup>20</sup> individuals may not be required to keep detailed records to calculate the actual use tax owed. Instead, they may use tables prepared by the state tax department that indicate how much use tax is owed based on the taxpayer's income level. In Michigan, if each item purchased for which use tax is owed has a cost under \$1,000, the tax table may be used to compute the use tax which is then reported on the Michigan individual income tax form. For purchases of single items costing \$1,000 or more, the use tax for such items can be added to the table amount.

Alternatively, Minnesota provides an exemption where use tax is not owed unless a person's purchases subject to use tax exceed \$770 for the year.<sup>21</sup> However, this technique will not serve as well as the tax table approach to reduce recordkeeping. In Minnesota, individuals would still need to keep records of purchases to determine if the ones for which sales tax was not collected exceed \$770.

3. Find ways to encourage out-of-state vendors to voluntarily collect the use tax on behalf of their California customers. Remote vendors will be reluctant to voluntarily collect a tax they are not legally required to collect and with good reasons. There are costs associated with compliance including filing and additional credit card fees due to higher charges by customers (because the

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<sup>19</sup> Board of Equalization, 2006-2006 Annual Report, p. 63; available at <http://www.boe.ca.gov/annual/pdf/2006/7-needs06.pdf>.

<sup>20</sup> New York Department of Revenue, *Purchaser's Obligations to Pay Sales and Use Taxes Directly to the Tax Department Questions and Answers*, Publication 774 (3/07), pp 13 – 15; available at [http://www.tax.state.ny.us/pdf/publications/sales/pub774\\_307.pdf](http://www.tax.state.ny.us/pdf/publications/sales/pub774_307.pdf).

<sup>21</sup> Minnesota Revenue, "Use Tax for Individuals," Pub. 156; available at [http://www.taxes.state.mn.us/taxes/sales/publications/fact\\_sheets\\_by\\_name/content/CM1\\_002975.pdf](http://www.taxes.state.mn.us/taxes/sales/publications/fact_sheets_by_name/content/CM1_002975.pdf).

sales tax would be included on the charge). There are also competitive disadvantages of complying when other vendors do not as it will look like the compliant vendor's goods cost more. An advantage to collecting the use tax even when not legally required to do so would probably only exist if the state did a good enough job of educating taxpayers about their use tax obligations. Vendors could then advertise not to worry about use tax compliance because they would handle it for their customers. Incentives might include:

- a. Offering compensation to vendors for collecting the use tax (to help cover compliance costs of the vendors).
- b. Offering simplified compliance techniques, such as annual rather than quarterly reporting and providing technological tools to aid compliance.
- c. Giving a preference to companies registered to collect use tax when the state makes purchases.

While the government would generally prefer to have vendors collect the sales tax rather than having consumers self-report, it is unlikely that the government can always rely on vendors. If a vendor is located outside of the U.S. (with no physical presence in the U.S.) it would be difficult, if not impossible, for the state to get the foreign vendor to collect the state's sales tax. In addition, proposals by Congress to allow states that have simplified their sales tax system (see next item on the Streamlined Sales Tax Project) to require remote vendors to collect the sales tax typically exempt small vendors. Thus, unless a state exempts sales from small vendors from the sales and use tax, consumers would still be required to self-report use tax when they purchase taxable items from such small vendors. Thus, individual consumers will likely always have self-assessment obligations when it comes to the use tax.

4. California could encourage Congress to enact legislation that reverses the U.S. Supreme Court decision of 1992 (the *Quill* decision) that requires a physical presence in order for a state to collect sales tax from a vendor. The Court's rationale for its holding was that imposing tax collection obligations on remote vendors would be contrary to the commerce clause of the U.S. Constitution (it would impede interstate commerce). The Court noted that the commerce clause is within the purview of Congress (that is, Congress can determine what does and does not impede interstate commerce). Thus, Congress could enact a law allowing states to require remote vendors to collect sales and use tax from customers in the state. However, Congress is unlikely to make such a change unless states greatly simplify their sales tax laws, which today, vary from state to state.

Several states are moving towards simplification by enacting a uniform sales and use tax law. This uniform law was created by the Streamlined Sales Tax Project in which many states participate.<sup>22</sup> The hope is that Congress will see that adopting states have simplified sales tax compliance for vendors by having similar laws.<sup>23</sup>

California has not adopted the uniform sales tax law and probably will not do so. However, policymakers should see if perhaps given the size of California and its customer base, a position can be justified that California does not pose compliance challenges for vendors. For example, if almost all states with a sales tax adopt the uniform law, but California and perhaps one or two other large states do not, it might be possible that Congress or the Court could view compliance for multistate vendors as simplified enough such that there are no commerce clause concerns (vendors would have only 2 or 3 systems to deal with assuming the local tax base is equivalent to the state tax base, as it is in California).

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<sup>22</sup> The Streamlined Sales Tax Project began in 2000. The Streamlined Sales and Use Tax Act (SSUTA) and other information on the project can be found at <http://www.streamlinedsalestax.org>.

<sup>23</sup> Various bills have been introduced over the past few years, including S. 34 (110<sup>th</sup> Congress), the Sales Tax Fairness and Simplification Act, which would allow states that have simplified their sales tax, such as by adopting the SSUTA, to collect tax from remote vendors.

## Tax Policy Analysis<sup>24</sup>

The following chart explains how improved use tax collection would satisfy the principles of good tax policy. The rating in the last column indicates whether improved use tax collection would improve the current system.

Principle	Application and Analysis	Rating
<b>Fairness</b>		
<b>Equity and Fairness</b> Similarly situated taxpayers should be taxed similarly.	When consumers do not know about the use tax or fail to keep records to compute it or believe that it is okay to ignore it, they may favor purchasing from remote vendors rather than local ones who will charge them sales tax. Improving use tax compliance will treat online and catalog buyers similarly to those who buy at physical stores and treat all vendors of taxable goods similarly.	+
<b>Transparency and Visibility</b> Taxpayers should know that a tax exists and how and when it is imposed upon them and others.	Educating consumers (as well as some businesses who are not use tax compliant) about the use tax will help them to know the types of transactions for which the tax is owed and the amount owed.	+
<b>Operability</b>		
<b>Certainty</b> The tax rules should clearly specify when the tax is to be paid, how it is to be paid, and how the amount to be paid is to be determined.	Simplification of use tax compliance, particularly for individual consumers, should give taxpayers more confidence that they are paying the proper amount. For example, if consumers had the choice of keeping accurate records of their use tax liability or using an estimate from a table that uses a specified use tax amount based on the consumer's income, certainty would be improved.	+

<sup>24</sup> This analysis uses a document prepared by the American Institute of Certified Public Accountants (AICPA) Tax Division and altered to the above format by Joint Venture: Silicon Valley Network. The AICPA document, *Guiding Principles of Good Tax Policy: A Framework for Evaluating Tax Proposals* (2001) is available at <http://ftp.aicpa.org/public/download/members/div/tax/3-01.pdf>. The Joint Venture workbook is available at <http://www.jointventure.org/PDF/taxworkbook.pdf>. The principles laid out in these documents are frequently used tax policy analyses ones. For more information see Nellen, *Policy Approach to Analyzing Tax Systems*; available at [http://www.cob.sjsu.edu/facstaff/nellen\\_a/Policy%20Approach%20to%20Analyzing%20Tax%20Systems.pdf](http://www.cob.sjsu.edu/facstaff/nellen_a/Policy%20Approach%20to%20Analyzing%20Tax%20Systems.pdf). Note: The author of this report (Annette Nellen) was the lead author for both the AICPA and Joint Venture documents noted here.

<p><b>Convenience of Payment</b> A tax should be due at a time or in a manner that is most likely to be convenient for the taxpayer.</p>	<p>The ideal time to pay sales or use tax is at the time of the purchase when the buyer has the opportunity to not buy the product. Unless a remote vendor voluntarily collects the use tax, paying the tax along with the taxable item won't occur. While co-payment could be achieved with online sales (where the buyer's credit card is charged at the same time by the tax agency for the use tax), it is unlikely to be a solution in the near future.</p>	<p>No effect</p>
<p><b>Economy in Collection</b> The costs to collect a tax should be kept to a minimum for both the government and taxpayers.</p>	<p>Providing consumers with the option of using a table to determine their annual use tax liability would reduce recordkeeping costs for taxpayers and reduce any need for detailed audits by the BOE.</p>	<p>+</p>
<p><b>Simplicity</b> The tax law should be simple so that taxpayers can understand the rules and comply with them correctly and in a cost-efficient manner.</p>	<p>Educating consumers about the use tax including when it applies, how to keep track of the amount owed and how to pay it should provide some simplification relative to consumers wondering at the time they prepare their Form 540 what the use tax line is for. The ability to use a table to compute use tax liability would also simplify use tax calculations and reporting.</p>	<p>+</p>
<p><b>Minimum Tax Gap</b> A tax should be structured to minimize non-compliance."</p>	<p>Improved understanding of the use tax and providing simpler methods for calculating it should result in more of it being paid.</p>	<p>+</p>
<p><b>Appropriate Government Revenues</b> The tax system should enable the government to determine how much tax revenue will likely be collected and when.</p>	<p>Improved use tax compliance would improve the collection of a tax that has been around for decades and for which compliance is low. Better compliance would also improve the tracking of sales and use tax growth to growth in the purchase of taxable goods from remote vendors.</p>	<p>+</p>
<p><b>Appropriate Purpose and Goals</b></p>		
<p><b>Neutrality</b> The effect of the tax law on a taxpayer's decisions as to how to carry out a particular transaction or whether to engage in a transaction should be kept to a minimum.</p>	<p>If more consumers knew about the use tax, they would be less likely to view purchases from a remote vendor as being lower cost than purchases from their local store because they would know that the former is not tax free.</p>	<p>+</p>
<p><b>Economic Growth and Efficiency</b> The tax system should not impede or reduce the productive capacity of the economy.</p>	<p>Better use tax compliance would remove an obstacle that some bricks and mortar vendors have in competing with remote vendors, namely that when remote vendors sell to consumers who do not know that they owe use tax on the transaction, the sales price looks lower than it is when they purchase from the bricks and mortar store.</p>	<p>+</p>

**Additional Reading**

Devin Comiskey, "States Taking Lead in Online Sales Tax Collection," *e-commerce-guide.com*, 12/20/05; available at <http://www.e-commerce-guide.com/news/news/article.php/3572366>.

Kathy M. Kristof, "Bought it out of state? You may owe 'use tax'," *Los Angeles Times*, 3/18/07.



Nina Manzi, Minnesota House of Representatives Research Dept., "Use Tax Collection on Income Tax Returns in Other States," 12/04; available at <http://www.house.leg.state.mn.us/hrd/pubs/usetax.pdf>.

Declan McCullagh, "States push to tax Net shopping," cnetNews.com, 4/12/06; available at [http://news.com.com/2100-1028\\_3-6060450.html](http://news.com.com/2100-1028_3-6060450.html).

### **June 2008 Update**

#### 1. California proposal to allow individuals to use the look-up table approach to determine use tax

AB 1957, introduced February 13, 2008, is primarily a reintroduction of AB 969 which was vetoed by the Governor. These bills aimed to not enable individuals to avoid completing the use tax line on Form 540 (CA Individual Income Tax Return) by allowing them the option to file sales tax forms (see footnote 3 above).

AB 1957 was amended on March 25, 2008 to add the option to allow individuals to use a table to be provided in the Form 540 instructions where they could look up their use tax liability for non-business purchases. For individual non-business items for which use tax is owed that cost \$1,000 or more, the actual use tax must be calculated. In addition to making recordkeeping simpler, the sponsor intends that this simplification address one of the reasons for the Governor's veto – that individuals would not have time to get ready to comply.

Reread in Revenue & Taxation Committee in June 2008.

Find information on AB 1957 (2007-2008) by searching at <http://www.leginfo.ca.gov/bilinfo.html>.

#### 2. Updated report from Minnesota on use tax reporting

For updated information on state use tax reporting, see Policy Brief, Research Department, Minnesota House of Representatives, *Use Tax Collection on Income Tax Returns in Other States*, updated November 2007 (<http://www.house.leg.state.mn.us/hrd/pubs/usetax.pdf>).