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# **Experience of Applying Retail Sales Taxes in the Digital World**

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**Workshop on the Application of Non-  
Discriminatory Internal Taxes to Electronic  
Transmissions**  
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# Experience of Applying Retail Sales Taxes in the Digital World

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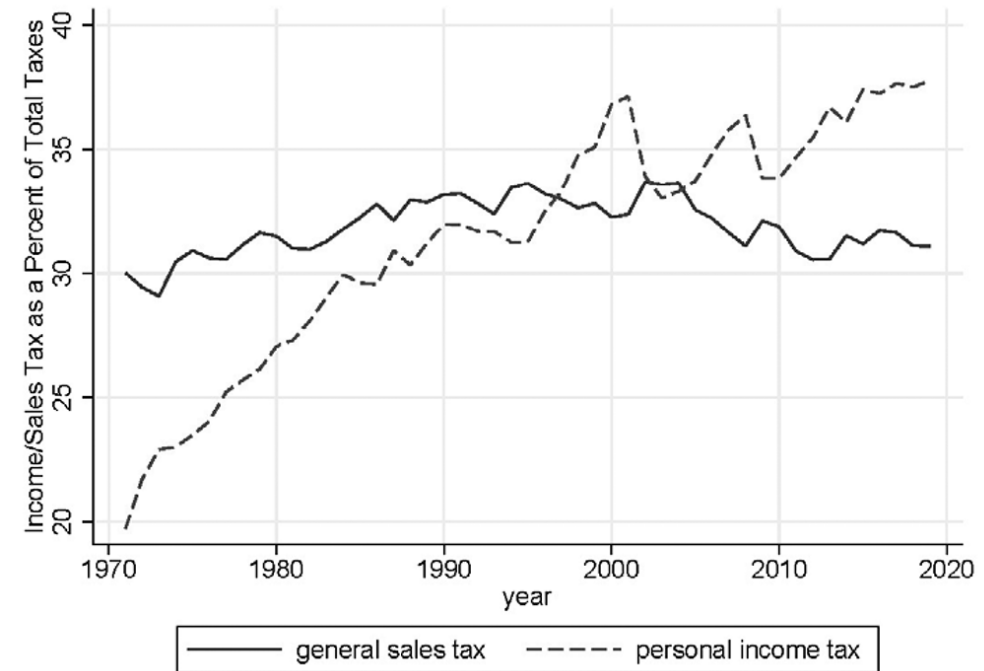
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\*The views do not necessarily reflect those of the U.S. Treasury  
Department.

# Background

- The Federal government does not tell US States what taxes to use to raise revenue
- Not all States have a retail sales tax (RST) and reliance on RST has been declining over time
- If a State has an RST, then local governments may have one too

Panel A: Income and Sales Tax Revenue as a Percent of Total Tax Revenue



# Limited Tax Base of RSTs

State RST bases reflect the Depression

1. tax purchases of tangible/goods (3)
  2. tax purchases of tangible/goods and a list of services (38)
  3. tax purchases of tangible/goods and services equivalently (4)
- Tax base has been subject to erosion over time with exemptions
    - Food at home, clothing, prescription medicines...
  - States often tax business purchases resulting in cascading (40%)

| Personal Consumption Expenditures by Category |          |          |
|---|----------|----------|
|   | 1979 (%) | 2019 (%) |
| Durable goods                                 | 14.3     | 10.5     |
| Autos   | 5.7      | 3.6      |
| Furniture and household                       | 4.1      | 2.5      |
| Other durables                                | 4.5      | 4.5      |
| Nondurable goods                              | 32.3     | 20.5     |
| Food and beverage                             | 13.8     | 7.1      |
| Other nondurables                             | 18.5     | 13.4     |
| Services                                      | 53.5     | 69       |
| Total expenditures                            | 100      | 100      |
| Agrawal and Fox (2021), Table 1               |          |          |

# Taxation of Digital Service

- Limited and varied
- But tend to tax digitized service if similar service in non-digitized form is taxed

| Services  | Number of States Taxing the Services | Services   | Number of States Taxing the Services |
|---|--------------------------------------|--|--------------------------------------|
| Intrastate telephone — industrial   | 41                                   | Online data processing                               | 10                                   |
| Interstate telephone — industrial   | 25                                   | Software — downloaded                                | 33                                   |
| Cellular — industrial   | 42                                   | Books — downloaded                                   | 28                                   |
| Electricity — industrial  | 36                                   | Music — downloaded                                   | 28                                   |
| Intrastate telephone — residential  | 41                                   | Rental of video for home                             | 45                                   |
| Interstate telephone — residential  | 27                                   | Movies/video — downloaded                            | 27                                   |
| Cellular — residential  | 43                                   | Other electronic downloaded                          | 23                                   |
| Electricity — residential   | 22                                   | Streaming music/audio                                | 16                                   |
| Newspaper   | 4                                    | Streaming video                                      | 18                                   |
| Magazine  | 4                                    | Cable TV   | 28                                   |
| Telemarketing services  | 18                                   | Direct satellite                                     | 25                                   |
| Canned software   | 46                                   | Software as a service — generally                    | 14                                   |
| Modifications to canned software  | 27                                   | Remote access to hosted software — individual        | 13                                   |
| Custom software — material  | 19                                   | Remote access to hosted software — business          | 15                                   |
| Custom software — professional services                                     | 13                                   | Remote access to hosted software — business customer | 7                                    |
| ISP — dial-up   | 8                                    | Infrastructure as a service — generally              | 7                                    |
| ISP — broadband   | 9                                    | Personal cloud storage — backup                      | 7                                    |
| Information services  | 14                                   | Business cloud storage — backup                      | 8                                    |
| Data processing   | 10                                   | Business data warehouse                              | 9                                    |
| Mainframe computer access   | 19                                   | Provision of virtual computing capacity              | 8                                    |
|   |                                      |  |                                      |
| Note: This table shows the number of states taxing each service as of 2017. |                                      |  |                                      |
| Agrawal and Fox (2021) Table 3  |                                      |  |                                      |

# Remote Vendor Taxation

- Originally US Supreme Court required sellers to have a physical presence in the State in order to be subject to a State's RST
  - Requiring remote seller to collect RST was an undue burden on interstate commerce
  - Estimates varied with the revenue loss being roughly 5% up to 10% of RST prior to ...
- US Supreme Court - South Dakota v. Wayfair (June 2018)

In 2016 South Dakota require remit RST if

- Gross Sales into SD > \$100,000/year OR
- Seller more than 200 transactions/year into SD
- Physical presence replaced with economic nexus standard



| Require Remote Firms to Remit Sales Tax |                    |                      |                 |                       |                  |    |                     |                      |                 |                       |                  |
|---|--------------------|----------------------|-----------------|-----------------------|------------------|----|---------------------|----------------------|-----------------|-----------------------|------------------|
|   | State              | Effective Date       | Sales Threshold | Transaction Threshold | SSTP Participant |    | State               | Effective Date       | Sales Threshold | Transaction Threshold | SSTP Participant |
| 1                                       | Alabama            | 1-Oct-18             | \$250,000       |                       |                  | 25 | Missouri (proposed) | 1-Jan-21             | \$100,000       |                       |                  |
| 2                                       | Alaska             | Local rules apply    |                 |                       |                  | 26 | Montana             | No general sales tax |                 |                       |                  |
| 3                                       | Arizona            | 1-Oct-19             | \$200,000       |                       |                  | 27 | Nebraska            | 1-Apr-19             | \$100,000       | 200                   | Yes              |
|   |                    | 2020                 | \$150,000       |                       |                  | 28 | Nevada              | 1-Nov-18             | \$100,000       | 200                   | Yes              |
|   |                    | 2021                 | \$100,000       |                       |                  | 29 | New Hampshire       | No general sales tax |                 |                       |                  |
| 4                                       | Arkansas           | 1-Jul-19             | \$100,000       | 200                   | Yes              | 30 | New Jersey          | 1-Nov-18             | \$100,000       | 200                   | Yes              |
| 5                                       | California         | 1-Apr-19             | \$500,000       |                       |                  | 31 | New Mexico          | 1-Jul-19             | \$100,000       |                       |                  |
| 6                                       | Colorado           | 1-Dec-18             | \$100,000       | 200                   |                  | 32 | New York            | 21-Jun-18            | \$300,000       | 100                   |                  |
|   |                    | 14-Apr-19            | \$100,000       |                       |                  |    |                     | 24-Jun-19            | \$500,000       | 100                   |                  |
| 7                                       | Connecticut        | 1-Dec-18             | \$250,000       | 200                   |                  | 33 | North Carolina      | 1-Nov-18             | \$100,000       | 200                   | Yes              |
|   |                    | 1-Jul-19             | \$100,000       | 200                   |                  | 34 | North Dakota        | 1-Oct-18             | \$100,000       | 200                   | Yes              |
| 8                                       | Delaware           | No general sales tax |                 |                       |                  |    |                     | 31-Dec-18            | \$100,000       |                       |                  |
| 9                                       | Florida (proposed) | 1-Jul-20             | \$100,000       | 200                   |                  | 35 | Ohio                | 1-Jan-18             | \$500,000       |                       | Yes              |
| 10                                      | Georgia            | 1-Jan-19             | \$250,000       | 200                   | Yes              |    |                     | 1-Aug-19             | \$100,000       | 200                   |                  |
|   |                    | 1-Jan-20             | \$100,000       | 200                   |                  | 36 | Oklahoma            | 1-Nov-19             | \$100,000       |                       | Yes              |
| 11                                      | Hawaii             | 1-Jul-18             | \$100,000       | 200                   |                  | 37 | Oregon              | No general sales tax |                 |                       |                  |
| 12                                      | Idaho              | 1-Jun-19             | \$100,000       |                       |                  | 38 | Pennsylvania        | 1-Jul-19             | \$100,000       |                       |                  |
| 13                                      | Illinois           | 1-Oct-18             | \$100,000       | 200                   |                  | 39 | Rhode Island        | 1-Jul-19             | \$100,000       | 200                   | Yes              |
| 14                                      | Indiana            | 1-Oct-18             | \$100,000       | 200                   | Yes              | 40 | South Carolina      | 1-Nov-18             | \$100,000       |                       |                  |
| 15                                      | Iowa               | 1-Jan-19             | \$100,000       | 200                   | Yes              | 41 | South Dakota        | 1-Nov-18             | \$100,000       | 200                   | Yes              |
|   |                    | 1-Jul-19             | \$100,000       |                       |                  | 42 | Tennessee           | 1-Oct-19             | \$500,000       |                       | Yes              |
| 16                                      | Kansas (proposed)  | 1-Oct-19             | \$100,000       |                       | Yes              |    |                     | 1-Oct-20             | \$100,000       |                       |                  |
| 17                                      | Kentucky           | 1-Oct-18             | \$100,000       | 200                   | Yes              | 43 | Texas               | 1-Oct-19             | \$500,000       |                       |                  |
| 18                                      | Louisiana          | 1-Jul-20             | \$100,000       | 200                   |                  | 44 | Utah                | 1-Jan-19             | \$100,000       | 200                   | Yes              |
| 19                                      | Maine              | 1-Jul-18             | \$100,000       | 200                   |                  | 45 | Vermont             | 1-Jul-18             | \$100,000       | 200                   | Yes              |
| 20                                      | Maryland           | 1-Oct-18             | \$100,000       | 200                   |                  | 46 | Virginia            | 1-Jul-19             | \$100,000       | 200                   |                  |
| 21                                      | Massachusetts      | 1-Oct-17             | \$500,000       | 100                   |                  | 47 | Washington          | 1-Oct-18             |                 | 200                   | Yes              |
|   |                    | 1-Oct-19             | \$100,000       |                       |                  |    |                     | 14-Mar-19            | \$100,000       |                       |                  |
| 22                                      | Michigan           | 1-Oct-18             | \$100,000       | 200                   | Yes              | 48 | Washington, D.C.    | 1-Jan-19             | \$100,000       | 200                   |                  |
| 23                                      | Minnesota          | 1-Oct-18             | \$100,000       | 100                   | Yes              | 49 | West Virginia       | 1-Jan-19             | \$100,000       | 200                   | Yes              |
|   |                    | 1-Oct-19             | \$100,000       | 200                   |                  | 50 | Wisconsin           | 1-Oct-18             | \$100,000       | 200                   | Yes              |
| 24                                      | Mississippi        | 1-Sep-18             | \$250,000       |                       |                  | 51 | Wyoming             | 1-Feb-19             | \$100,000       | 200                   | Yes              |

# State Reactions to Wayfair

- Rapid
- Most States have sales and transactions thresholds similar to SD
  - Recognition of administrative and compliance costs weighed against revenue collected
- Reform of remittance rules expanding to online marketplace facilitators (marketplace contracts with 3<sup>rd</sup> party sellers)
  - Shift from option to collect to require
  - 42 States require marketplace to collect tax

# Why did Wayfair decision take the form it did?

- Compliance challenges and related costs can have a significant impact on interstate commerce
- US studies estimate average compliance costs of 3% of sales tax collected
  - Regressive compliance costs – 13% of tax collected for small remote sellers and 2% for large remote sellers
- Streamlined Sales and Use Tax Agreement – uniform rules, tax bases, rates
  - 24 States – including SD

# Streamlined Sales and Use Tax Agreement

- SSUTA membership provides sellers with reduced tax compliance costs and access to sales tax software paid for by the State as well as audit liability immunity
- Certified Service Providers (CSPs) – example of Avalara
  - Business register to collect and remit sales tax through SSTP
  - Contract with CSP
  - During 12 months before register, no fixed business in State, less than \$50,000 payroll, less than \$50,000 property, and less than 25% of total property in State
- Similar program non-SSUTA – PA, IL, NM if work with CSP
- Note uniform rate for local government RST

# Experience of Tennessee (TN) – Agrawal and Fox (2021)

- Wayfair decision enabled State to get remote sellers of goods to collect RST
  - But many were already collecting RST – Walmart’s online sales – as early as 2012
- Historically, remote sellers could remit a combined State and county tax rate as opposed to trace to the specific county
  - Uniform 2.25% with local option
  - October 1, 2019 to begin to collect local sales tax based on destination
- Prior Wayfair, sales tax revenue from out-of-state sellers represented approximately 14% of local tax revenue

# Continued

- Post Wayfair, local sales tax revenue from out-of-state sellers increased by \$40 million of which only \$5 million was from newly registered vendor
- Estimates of State sales tax revenues rose 2.5% from economic nexus and 6.1% from marketplace facilitator legislation
- In TN new vendor about 10% of revenue from remote vendors
  - However, switch in distribution of local sales tax collections across counties
  - Remote sellers switch to destination based tax rate
- Combination of remote sellers no longer using uniform rate and Covid's increase in remote sales and rural shoppers not able to go to stores resulted in redistribution of local sales tax from large to small counties

Thank you