

**D.C. Tax Revision Commission Policy Options**

## Policy Option #4: Add Use Tax Line to the Income Tax Return

### **MEMORANDUM**

**Proposal:** Provide D.C. residents a simple way to remit use taxes for online purchases by adding a line to the individual income tax return form

**Tax Type:** Sales (via the income tax)

**Origin:** William Fox

**Commission Goal:** Fairness

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### **Current Law**

When D.C. residents purchase products remotely (such as online), and do not pay the D.C. sales tax on the transaction, they must remit use taxes (equal to the sales tax) to the District. This is because the remote retailer (if it lacks physical presence in D.C.) is not obligated to collect and remit the D.C. sales tax. Very few residents, however, pay the use tax and D.C. cannot effectively enforce the tax.

### **Proposed Change**

- 1) Add a line item to the D.C. individual income tax return to prompt residents to pay any uncollected use taxes for online or other remote purchases.
- 2) Consider a “Use Tax Lookup Table” that allows taxpayers to estimate their liability based on adjusted gross income, as provided in nine states, such as California. This table assists taxpayers who may not track all of their online purchases throughout the year. States with such tables enjoy higher participation rates than those states that do not. Research has also found that states that require taxpayers to clearly indicate no liability—writing in “zero” rather than allowing filers to leave the line blank—generate slightly more voluntary use tax payments.

### **Reason for Change**

The current system is not capturing use tax liabilities effectively—either out of taxpayer ignorance or evasion. In 2012, 25 of the 38 states with both a sales tax and an individual income tax included a line on their income tax returns requiring filers to report a use tax liability (including Virginia but not Maryland). Adding such a line to the D.C. income tax return can help residents fulfill their legal obligation and in a non-intrusive manner.

### **Pros**

- Educates residents on their use tax obligations, and provides them with a simple mechanism to comply with current law.
- Mitigates the sales tax revenue loss from online transactions.
- States that have recently added a use tax line to the income tax return (Louisiana, Massachusetts and Michigan) increased their use tax collections significantly.

## **Cons**

- Adds additional lines/pages to the D.C. income tax form.
- The tax collection is voluntary and auditing online or remote purchases is unlikely.
- While the use tax is a part of current law, adding a new line to the income tax reform could be interpreted as a “new” tax on residents.
- May penalize honest taxpayers.

## **Revenue Impact**

The Office of Revenue Analysis estimates that in the first year of implementation adding a use tax line to the individual income tax form will raise \$1 million in revenue.

New York collected \$34 million in tax revenue via such a use tax line in 2009, the most of any state that year. California (\$10.2 million) was the only other state in 2009 to collect more than \$5 million via the use tax line. Virginia collected \$1.5 million in 2009 and nine states with use tax lines collect less than \$1 million that year.