

D.C. Tax Revision Commission Policy Options
Policy Option #3: Click-through Nexus

MEMORANDUM

Proposal: Expand the definition of nexus to require online retailers with D.C.-based affiliates to collect the D.C. sales tax

Tax Type: Sales

Origin: William Fox

Commission Goal: Broaden the tax base

Current Law

D.C. does not require out-of-state retailers to collect a sales tax for online purchases made by its residents if these retailers do not have a physical presence in the D.C. (Out-of-state retailers with a physical presence in D.C., such as Target, must collect the sales tax.) Residents are required to pay a use tax on goods purchased online from retailers not collecting a sales tax but often do not.

Proposed Change

Under the proposed change, businesses who do not have physical presence in the District, but have commission-based business relations with entities based in the District, would be required to collect and remit sales taxes on *all sales* made to D.C. residents. To simplify administration, the District could offer a *de minimus* exemption for out-of-state firms with infrequent sales to D.C. residents (e.g. \$10,000 worth of sales in D.C.) to protect small businesses. Such taxes, sometimes referred to as “Amazon taxes,” have been enacted by 12 states including California, New York, Connecticut, North Carolina and Kansas.

Reason for Change

E-commerce continues to expand but D.C. taxes relatively few of these transactions under current law. Establishing click-through nexus allows D.C. to recoup some of these losses without congressional action—the Market Place Fairness Act has been passed by the Senate but has not made progress in the House of Representatives.

Pros

- Allows D.C. to collect the sales tax on some online transactions not currently covered by law.
- Broadens the sales tax base, allowing for increased revenue or a lower sales tax rate.
- Removes a competitive disadvantage for “brick and mortar” retailers and online vendors who establish a business in D.C.

Cons

- Amazon and Overstock have eliminated commission-based relationships in some states with click-through nexus laws and have threatened to do so in jurisdictions that enact such

legislation. Special agreements have been negotiated between Amazon and some states such as New York and California.

- The broader nexus might be challenged under the Commerce Clause. The New York Court of Appeals, agreeing with lower court decisions, recently dismissed a challenge from Amazon and Overstock. The case may be appealed to the Supreme Court. It is also possible that the D.C. law will be litigated.
- The tax imposes an administrative burden on online retailers and may be difficult to audit.

Revenue Impact

The Office of Revenue Analysis estimates that if D.C. passes such a law that, based on the experience of most states, large retailers will terminate commission-based business relationships in D.C. and therefore any revenue increase is likely negligible.

New York is the one state that has seen a sizeable revenue increase since enacting such a law. The state commissioner of taxation reports that since the state asserted click-through nexus in 2008 it has collected \$500 million in state and local sales taxes as a result of the law.