

# BRIEFING

## Session Spotlight



### IN THE WAKE OF WAYFAIR, FLORIDA MUST ACT TO REMEDY AN OLD PROBLEM: THE COLLECTION OF TAXES ON REMOTE SALES

APRIL 2019

The non-collection of sales taxes on sales to Florida customers by remote (out-of-state) sellers has been the most significant tax compliance and collection issue facing Florida and other states for many years. Remote vendors sell products by the internet, telephone, and mail. Historically, the courts have held that when a remote seller makes a sale to a person in a state in which the seller does not have a physical presence, that state cannot require the seller to collect the sales tax due and remit it to the state. That changed with the U.S. Supreme Court's *Wayfair* decision last June. But Florida still needs to take steps to address this problem.

When remote sellers do not collect the tax, the tax is still legally owed to the state by the Floridian that made the purchase; however, few Florida residents know that they are required to pay the sales tax (known as the use tax when not collected at purchase) owed on remotely conducted transactions directly to the Florida Department of Revenue (DOR). Even fewer actually make such payments by going to the trouble of downloading DOR's Form DR-15MO, filling it out and sending a check for

the taxes they didn't pay at the time of purchase.

Not collecting sales taxes on remote sales not only costs Florida governments millions in legally owed revenue, it also puts Florida retailers and a competitive disadvantage, distorts purchasing decisions, is unfair to Floridians that do pay the tax, and makes millions of Floridians—often unwittingly—lawbreakers.

Florida TaxWatch has researched this issue for more than 15 years, producing numerous reports and offerings recommendations. But the courts' physical presence requirement has always been a major obstacle. But now that obstacle is gone as a result of the US Supreme Court's *Wayfair* decision, and it is time for the Legislature to fix this. Senate Bill 1112 can achieve this long-elusive goal.

### U.S. SUPREME COURT PROVIDES THE OPPORTUNITY TO FIX THIS LONG-STANDING PROBLEM

Last June, the U.S. Supreme Court handed down a ruling (*South Dakota v. Wayfair, Inc., et al*) that paves the way for a

successful resolution of the remote sales tax problem. The Court ruled that states can apply reasonable requirements for remote vendors to collect sales and use taxes on sales to residents even if the vendor does not have a physical presence in the state. The Court specifically overturned its previous ruling (*Quill Corp. v. North Dakota*) which had prohibited requiring the collection of taxes on these sales unless the vendor has some physical presence in the state.

The physical presence requirement from the *Quill* decision in 1992 limited the state's authority to exercise jurisdiction over vendors that had significant commercial ties to the Florida (i.e., a large volume of sales) but no physical presence. Since the early 2000's and the increasing shift to internet commerce, which is now the most prevalent form of remotely conducted sales, the former legal framework of *Quill* basically meant that the sales and use tax went uncollected on a large and growing percentage of retail sales to Floridians. As the Court's Opinion notes;

*"Each year, the physical presence rule becomes further removed from economic reality and results in significant revenue losses to the States. These critiques underscore that the physical presence rule, both as first formulated and as applied today, is an incorrect interpretation of the Commerce Clause."*<sup>1</sup>

It must be noted that the Court's *Wayfair* ruling does not give blanket approval for all states to begin collecting sales taxes from remote sellers. Despite the elimination of the physical presence requirement of the substantial nexus test regarding the Commerce Clause, there are many other considerations that Florida, or any state looking to enact a law pursuant to this decision, would need to consider.

Other limitations on state activity, and the requirement that substantial nexus be shown, remain. The Opinion reaffirms the standard for substantial nexus as: "Such a nexus is established when the taxpayer or collector 'avails itself of the substantial privilege of carrying on business' in that jurisdiction."<sup>2</sup>

The Opinion in *Wayfair* goes on to note that South Dakota has a simplified sales tax law that does not unduly burden remote sellers, the tax only applies to vendors that do a significant amount of business in the state (more than \$100,000 per year), and there is no attempt to apply the law retroactively.

*For a thorough analysis of the legal evolution of this issue, the legislative options, reasons for acting, other states' responses, and more, see the Florida TaxWatch report Wayfair: Formulating a Florida Response,<sup>3</sup> which was released concurrently with this report.*

## SENATE LEGISLATION IS A SOUND APPROACH TO FINALLY ADDRESSING THIS ISSUE

Senate Bill 1112, sponsored by Sen. Joe Gruters, is so far the only remote sales legislation moving through this legislative session. The approach, informed by the *Wayfair* decision, creates a process that reduces the potential for a successful legal challenge.

The bill amends the definition of "retail sale," as it is used throughout Florida's sales tax law,<sup>4</sup> to include remote sales, and sales facilitated by a marketplace. It further applies the sales and use tax to remote sales. It amends the state's mail order statute<sup>5</sup> to also provide for the taxation of sales made by telephone or the Internet—if the seller is "making substantial number of remote sales."

<sup>1</sup> (South Dakota v. Wayfair, Inc., 585 U.S. \_\_\_\_ (2018) (Opinion of the Court, pp. 12-13)

<sup>2</sup> (Wayfair at 22 citing *Polar Tankers, Inc. v. City of Valdez*, 557 U.S. 1, 11 (2009).

<sup>3</sup> Florida TaxWatch & Robert S. Goldman, *Wayfair: Formulating a Florida Response*, April 2019.

<sup>4</sup> Chapter 212, Florida Statutes

<sup>5</sup> Section 212.0596, Florida Statutes.

Substantial sales mean 200 or more sales to Florida in the previous calendar year or any number of sales totaling more than \$100,000 in the previous calendar year. This provides a threshold, such as is encouraged by *Wayfair*.

The bill also creates a new section to provide for the taxation of marketplace (i.e. Amazon or eBay) sales. A marketplace provider must certify to its marketplace sellers that it will collect and remit the tax imposed on taxable retail sales made through the marketplace. This is important because although Amazon began collecting tax on the sale of its products in Florida after establishing a physical presence in the state, it is not required to collect taxes on sales made by its marketplace sellers.

The bill contains another provision<sup>6</sup> not directly related to remote sales that is not only a long-time Florida TaxWatch recommendation, but can also help assuage concerns of some legislators about the remote sales provisions. Some lawmakers are wary of the perception that collecting taxes on remote is a tax increase (it certainly is not) or that the additional revenue would unnecessarily “grow government.”

The bill would decrease the Business Rent Tax (BRT) from 5.7 percent to 4.2 percent—in effect using additional sales tax collections to reduce the BRT. Florida subjects commercial lease and license payments to the state and local sales tax and it is the only state in the nation that does so. This creates a government mandated increase of up to 8.2 percent in occupancy costs for all business that rent, a cost they would not incur in any other state. This not only costs businesses, but it also costs Florida jobs and drives up prices for all Floridians. Florida TaxWatch has released two reports making the case for the reduction and eventual elimination of this tax.<sup>7</sup>

<sup>6</sup> SB 1112 also contains provisions to create a 14-day sales tax holiday for specified disaster preparedness supplies from June 1, 2019, through June 14, 2019 and to add certain rental heavy equipment to the definition of “inventory”, thereby exempting it from ad valorem taxation.

<sup>7</sup> Now is the Time to Eliminate the Business Rent Tax, April 2017 and

## THE NEGATIVE IMPACTS OF NOT ACTING

### ***Competitive Disadvantage for Florida Retailers***

Not requiring remote sellers to collect legally owed sales taxes puts our state’s “bricks-and-mortar” and “clicks and bricks”<sup>8</sup> retailers at a significant competitive disadvantage. A 6 to 8.5 percent<sup>9</sup> price break is hard to overcome for Florida’s retailers. It is not uncommon for a shopper to go into a store so they can see a product up close, use the store’s employees to answer questions and help compare products, then go home to buy it online; sometimes the only price difference making the online retailer cheaper was the lack of sales tax collection. Many times, Florida TaxWatch has likened this kind of unfair treatment to the Legislature placing a new tax only on retailers that employ a Floridian and specifically exempting any retailer does not. The Supreme Court agrees:

*“Quill puts both local businesses and many interstate businesses with physical presence at a competitive disadvantage relative to remote sellers. Remote sellers can avoid the regulatory burdens of tax collection and an offer de facto lower prices caused by the widespread failure of customers to pay the tax on their own ... In effect, Quill has come to serve as a judicially created tax shelter for businesses that decide to limit their physical presence and still sell their goods and services to a State’s consumers—something that has become easier and more prevalent as technology has advanced.”<sup>10</sup>*

### ***Economic Impacts***

Reduced sales, or worse, stores going out of business because they cannot compete with

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Reducing the Business Rent Tax, September 2015.

<sup>8</sup> Retailers with both online and traditional stores.

<sup>9</sup> Local option sales taxes can add up to 2.5 percent to Florida’s 6 percent state sales tax.

<sup>10</sup> South Dakota v. Wayfair, Inc., 585 U.S. \_\_\_\_ (2018) (Opinion of the Court, pp. 12-13)

remote sellers, costs the state economic activity and costs Floridians jobs. These impacts can ripple through the economy.

Moreover, allowing remote sellers to sell to Floridians tax-free can also keep those businesses from investing in Florida. The *Wayfair* opinion states:

*“Worse still, the rule produces an incentive to avoid physical presence in multiple States. Distortions caused by the desire of businesses to avoid tax collection mean that the market may currently lack storefronts, distribution points, and employment centers that otherwise would be efficient or desirable.”*

### **Unfairness to Floridians Who Pay Their Taxes**

The current system creates several inequities among individual Florida consumers. It is not fair for shoppers that choose to support Florida retailers to pay taxes that others can avoid by sending their money to other states. It is even more unfair for those relatively few conscientious Floridians that voluntarily remit the use tax they owe to the state.

The regressivity of the sales tax is also heightened. Higher-income people shop more online than those with lower-incomes, so the majority of the tax benefits are enjoyed by more affluent shoppers.<sup>11</sup>

Further, not all Floridians get away with not paying taxes on remote sales. DOR has a number of ways to discover use tax liabilities, including reviewing bills of lading of trucks, customs information, insured shipments, and tangible personal property returns.

A woman recently contacted Florida TaxWatch after receiving a letter from DOR saying she had purchased a car part on-line in 2016 and the sales tax was not collected. She was told she was under a self-audit and to complete a worksheet to estimate all her past on-line

purchases and the use tax that she owes. She was also asked to send the auditor her order histories from eBay and Overstock.com. She was confused, scared, and upset, and wanted to make sure she wasn't being scammed, because she couldn't believe that she had to pay the tax herself. She had no idea there was a use tax and thought that if she wasn't charged sales tax when she made a purchase, it was because she didn't need to.

DOR is doing its job, but is it fair to people like her to pay the use tax when most others do not, simply because DOR happens to come across one of their transactions? If the tax would have been collected by the seller, the state would have gotten the money, DOR would not have had to devote the resources to collect it, and this Floridian would have been spared the emotions she felt and the trouble of following through with the audit.

Florida's tax laws should not make millions of Floridians unwitting law breakers.

### **Erosion of the Tax Base**

This issue has also cost Florida's state and local governments hundreds of millions of dollars. Collection of sales and use tax revenue is even more critical for Florida than other states; since we do not have a personal income tax, the sales tax is by far the most important revenue for state government. Estimates of lost revenue have ranged from a few hundred million to over \$1 billion annually.

But collection of these taxes does not have to be a windfall for government. The additional revenue could be used to reduce or eliminate other burdensome taxes, such as the Business Rent Tax. This tax, unique to Florida, puts our businesses at a competitive disadvantage, including retailers already suffering from current the on-line tax scheme.

<sup>11</sup> Business Insider, "The surprising facts about who shops online and on mobile," February 2015.



## CONCLUSION

The U.S. Supreme Court has provided the opportunity to resolve the problem of uncollected sales taxes on remote sales, the negative impacts of which have been plaguing the state for many years. The 2019 Legislature must seize this opportunity. Senate Bill 1112 could bring equity to the state's sales and use tax and provide an economic benefit by providing a boost to the retail sector. Not only would it be fairer to retailers, collecting taxes on online sales also improves equity for consumers/taxpayers.

**Lawmakers and Floridians must understand that this is clearly not a tax increase.** It is a currently legally owed tax that some pay while many others do not. SB 1112 also proposes to use the additional revenue collected to reduce the onerous Business Rent Tax, an approach strongly supported by Florida TaxWatch.

There is also need for clarity and certainty as to the Florida nexus standards so that affected businesses and the DOR know what is expected of them. In addition, virtually all other states that levy a sales tax have adopted responses to *Wayfair*, are considering them, or are attempting to require collection without new legislation.<sup>12</sup> Some Florida retailers making out of state sales will likely find themselves newly required to collect taxes, further increasing the inequity of Florida's *status quo*.

This is about tax system modernization, and the Supreme Court has finally empowered the state to modernize its most important revenue stream while also removing a barrier to competition that had previously been imposed on Florida-based businesses. Florida must take advantage of this opportunity.

<sup>12</sup> Florida TaxWatch & Robert S. Goldman, *Wayfair: Formulating a Florida Response*, April 2019.

## ABOUT FLORIDA TAXWATCH

As an independent, nonpartisan, nonprofit taxpayer research institute and government watchdog, it is the mission of Florida TaxWatch to provide the citizens of Florida and public officials with high quality, independent research and analysis of issues related to state and local government taxation, expenditures, policies, and programs. Florida TaxWatch works to improve the productivity and accountability of Florida government. Its research recommends productivity enhancements and explains the statewide impact of fiscal and economic policies and practices on citizens and businesses.

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