

The Amazon loophole: States seek to collect online sales tax

by [Steve Thorngate](#) in the [February 22, 2012](#) issue



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For several years, the *Century* participated in Amazon.com's affiliate program. By directing readers to the online retailer to buy copies of the books and music we review, we brought in a little extra revenue. But recently we've removed the Amazon links from our website. Some readers—who were glad for the chance to support us when they shopped at Amazon—have written to ask what's going on.

The reason for the change is that Amazon no longer offers the affiliate program in Illinois, where the *Century* offices are located. Why? Because last year the state passed a law requiring Amazon to collect sales tax from its Illinois-based customers—a move that found its rationale in the presence of Amazon affiliates here.

Online retailers have generally enjoyed tax-free sales. The 1992 Supreme Court decision *Quill Corp. v. North Dakota* stipulates that retailers have to charge sales tax only in states where they have a physical presence, such as a store, office or warehouse. But recently cash-starved states have challenged the status quo. Some have simply passed laws requiring online retailers to charge sales tax to state residents. Others have pursued the same end by clarifying that having marketing affiliates—individuals, businesses and nonprofits that make money by promoting Amazon links—is enough to constitute a physical presence in the state.

Illinois took the latter approach, forcing Amazon to choose between its affiliates and its tax-free sales. Amazon sent us a nice note informing us of its choice. It blamed the state government and encouraged us to call our elected officials and complain that they'd shut us down.

I didn't pick up the phone. Amazon's spin aside, the law in Illinois doesn't outlaw affiliate marketing. What it does is require Amazon to collect sales tax from Illinois customers. That's the right call for the state to make.

Amazon sells all sorts of things, but it's made its biggest mark in books. It's a mixed legacy. Amazon's ability to stock an endless list of low-demand titles opened up big-time distribution to publishers of all sizes. But this helped create the "long tail" of the book market: a vast number of books, a vanishing few of which sell many copies.

To remotely located readers, Amazon offers unprecedented selection and prices. Yet the online store is a poor substitute for a good local shop, which can respond to community needs and function as a public commons. (It can also special order titles it doesn't stock.) Along with selling books directly, Amazon functions as a global marketplace for independent booksellers. Of course, one reason many of them need such a thing is that Amazon's own sales have absorbed so much of the local market they used to enjoy.

Amazon has beat local retailers much the way Wal-Mart has: through skillful use of loss leaders and other promotional techniques, an unquestionable convenience advantage, cost control via intense pressure on the supply chain, and staggering economies of scale. As with Wal-Mart, there's an endless debate as to whether all this amounts to a net positive for those of us who don't own stock in the company.

But Amazon has also gotten ahead by not charging sales tax. That has given it an additional price advantage over brick-and-mortar competitors. On this front, the verdict is more straightforward: states badly need revenue to repair crumbling infrastructure, to maintain services for families left vulnerable by the Great Recession, to stanch the bleeding of public-sector jobs. States need to be collecting sales tax on their residents' purchases, and there's no good reason for online-only retailers' customers to be exempt.

Amazon has long fought this view, from coast to coast. But in recent months it's made some compromises. In separate deals with California and Indiana, the company agreed to phase in sales tax charges over time. Most notably, it's

expressed support for the Marketplace Fairness Act, introduced in Congress in November. The bill is the latest in a series of attempts to take a federal approach to ensuring that all states can collect sales tax from online retailers.

Why would Amazon support this bill? For starters, the company likely sees the writing on the wall—the states aren't going to drop this fight—and it would rather comply with a single standard than have to make a separate deal with each state. What's more, the Marketplace Fairness Act exempts small retailers from collecting sales tax, but it sets this threshold lower than the other bills have—that is, more retailers would have to comply. These retailers are Amazon's competitors, and the considerable technical challenge of collecting sales tax in multiple states will hit small retailers harder than it will hit Amazon.

Most important, many of these smaller retailers sell *through* Amazon, as third-party vendors hosted on the Amazon site. And starting in February, Amazon is offering to collect sales tax on these sellers' behalf—for a price.

In short, the Marketplace Fairness Act would level one playing field but not another: online-only retailers would be forced to collect sales taxes just like their brick-and-mortar competitors, but smaller online sellers could be more vulnerable than ever to Amazon and other online behemoths. Amazon appears poised to turn defeat into victory.

Still, the biggest winner coming out of federal action to enforce state sales taxes—whether via the Marketplace Fairness Act or some improvement on it—would be the public. We need states to take in enough revenue to provide the services people rely on. We need this far more than we need tax-free online shopping.

Unless and until a federal bill is passed—or Amazon and Illinois reach a deal—the *Century* will have to do without the steady trickle of revenue the affiliate program used to provide. That's our loss, but this pales in comparison with the potential gain for the common good. If Amazon and other online-only retailers eventually start collecting sales tax from Illinoisans, this will promote the welfare of all state residents.

Meanwhile, we do participate in an affiliate program through IndieBound, a network of independent bookstores. This program helps book buyers support organizations like the *Century* while also supporting independent business. And it does this without evading the sales tax.