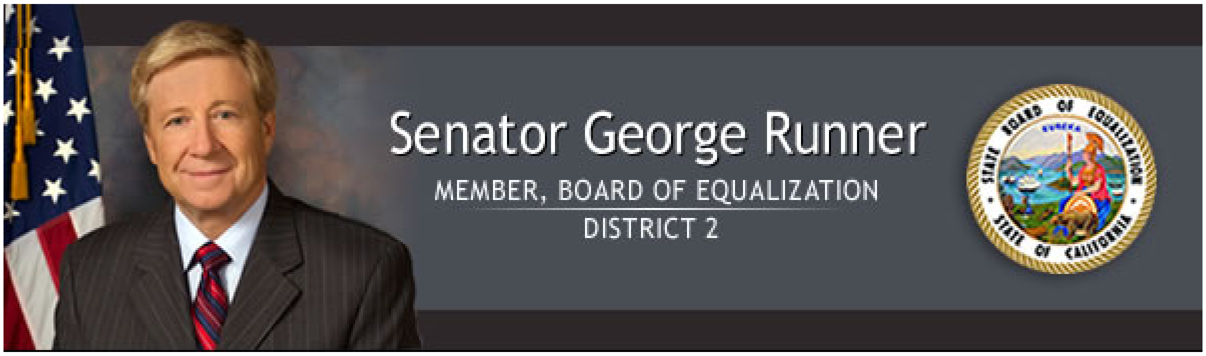

Unintended Consequences

Repeated attempts to boost sales tax collections hurt California's economy, cost jobs.

By George Runner

They're at it again.

Lawmakers in California, in a desperate attempt to generate revenues are again seeking to force out-of-state retailers to collect taxes for online purchases made by California shoppers. If they are successful in passing this legislation, not only will they fail to raise even one more nickel in tax revenue, they will cost the state thousands of jobs.

It's a bit complicated, but allow me to explain: California has a cutting edge industry of internet entrepreneurs called "affiliates." You've seen "affiliates" while surfing the web: blogs and websites that provide "click through" ads to online retailers. If you click through and make a purchase, the affiliate gets a small percentage in payment from the retailer.

According to the Performance Marketing Association, there are nearly 25,000 California-based affiliate businesses that provide information to California consumers and improve the ease and thrift of their shopping experience online or with remote retailers and their catalogs.

One example of a successful California affiliate is Ebates, a company based in San Francisco. Without affiliate relationships, Internet entrepreneurs like Ebates will face a painful choice: cut jobs to keep costs in line with reduced revenue or move out of California to more welcoming states. Either way, California will lose jobs and taxes.

Affiliates like Ebates can conduct business from any state in the country, but they are choosing to make California home. Likewise, online retailers choose to market their products through affiliates like Ebates because they help make the shopping experience for their customers easier.

If the Legislature passes a so-called "nexus" law, which will require out-of-state retailers to collect and remit California's sales tax, those online retailers will terminate their relationship with California's affiliates. They have done it in other states and have said they will do it here.

Paul Misener, Amazon's Vice President for Global Public Policy, recently sent me a letter citing four pending measures aimed at requiring out-of-state online retailers to collect sales tax. He warns: "If any of these new tax collection schemes were adopted, Amazon would be compelled to end its advertising relationships with well over 10,000 California-based participants in the Amazon 'Associates Program.'"

Misener notes that similar statewide terminations have already occurred in North Carolina, Rhode Island and Colorado after those states enacted similar laws.

A Board of Equalization analysis cautions that the proposed legislation's projected revenues would fall by 50% as a result of Amazon's action and be “further diminished” if other online retailers also terminated their affiliate programs. The analysis also warns of an “adverse impact on state employment,” resulting in lower corporate and personal income tax revenues for the state.

Thus, the unintended consequence of this tax policy will be to wipe out one of California's few healthy business industries. That's not what California needs when we have a statewide unemployment rate of more than 12%.

Collectively, affiliate businesses in California last year paid a total of $124 million in state income taxes, plus business, employment and property taxes. If a nexus law is enacted, California can say goodbye to a good portion of those revenues.

With the exodus of affiliates comes a government-sponsored brain drain as those whose mastery of online marketing and entrepreneurial drive have made it easier for California shoppers to find what they’re looking for move their companies elsewhere to find a new home.

How did this whole thing get started? And, why is California even considering a new law that would further damage the economy?

Most people know that they pay a sales tax on typical transactions, but few Californians probably know they have to pay an equivalent tax – the use tax – on their out-of-state purchases. Yet for 75 years, it has been the law. As a member of the Board of Equalization, the publicly-elected tax board charged with collecting this tax, I believe the best course of action is to make it easier for Californians to be aware of their obligations and pay them.

Lawmakers' efforts aside, neither the Board of Equalization nor the Legislature has the authority to force out-of-state retailers to collect sales tax. In 1992 the Supreme Court ruled that the Constitution prohibits states from asserting taxing authority outside their borders unless the retailer maintains a physical presence in the taxing state.

Let's not miss the forest for the trees. California's most pressing problem isn't tax collection, it's jobs. When Californians have jobs in a growing and vibrant economy, the state will have ample revenue to fulfill its responsibilities. But when Californians don't have jobs, we'll always have budget problems. Rather than chase entrepreneurs like Ebates away, lawmakers need to prioritize jobs.

The unintended consequences of a nexus law would be disastrous for thousands of California families. Killing private sector jobs only worsens our state's budget crisis. Lawmakers should reject such ill-conceived measures and instead start helping Californians get back to work.

Elected in November 2010, taxpayer advocate Senator George Runner represents the Second District of the Board of Equalization. Prior to his election to the Board, Runner served twelve years in the State Legislature. As a thoughtful conservative, his legislative priorities included improving the economy, business growth, education excellence, and public safety for all Californians. As a member of the Senate Revenue and Taxation Committee, Runner consistently *led the fight against tax increases and supported tax relief for families and businesses. For more information, visit www.boe.ca.gov/Runner.*