DEPARTMENT OF AUDITS AND ACCOUNTS

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December 12, 2016

Honorable Jay Powell
Chairman, House Ways and Means
133 Capitol
Atlanta, Georgia 30334

SUBJECT: Fiscal Note
House Bill (LC 43 0408ER)

Dear Chairman Powell:

The bill expands the definition of a dealer for the purposes of collecting and remitting state sales and use tax. A dealer would include any person who, within the previous or current year, conducts 200 or more separate retail sales or sells at retail more than $250,000 of tangible personal property, for physical or electronic delivery into the state for use, consumption, distribution, or storage. The bill also allows the Department of Revenue to take actions against any person failing to comply with the law and requires that all appeals of Superior Court decisions be made directly to the Supreme Court. The bill would be effective on January 1, 2018.

The bill would likely be subject to legal challenge under the precedent of the U.S. Supreme Court ruling in *Quill Corp. v. North Dakota* (1992) because the bill expands the concept of nexus for purposes of the state sales and use tax from a physical presence standard to one of substantial economic presence or "economic nexus."

Georgia State University's Fiscal Research Center (FRC) estimated that, if the proposed law is upheld, state revenue could increase by up to $274 million in the first full year affected (see Table 1). However, this estimate assumes that the law is upheld and that other challenges are overcome by the state. The revenue increase could be reduced by the difficulty in enforcing payment by out-of-state sellers who now meet the new dealer definition. FRC also noted that there is "significant uncertainty about the amount of currently untaxed online sales into Georgia or the amounts of currently untaxed sales by firms that would reach the proposed thresholds to be taxed." If the expanded definition were successfully challenged, no additional revenue would be collected. Details of FRC's analysis are provided in the attached appendix.

Table 1. Revenue Effects of LC 43 0408ER

($ *millions*)	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
State	$126	$274	$299	$326	$355
Local	$94	$206	$224	$244	$266

The bill could also impact the workload of the Department of Revenue and the state's courts, but we are unable to estimate the number of DOR actions that could be taken or the number of Superior Court decisions that may be appealed to the Supreme Court.

Sincerely,

Greg S. Griffin
State Auditor

Teresa A. MacCartney, Director
Office of Planning and Budget

GSG/TAM/mt

Analysis by the Fiscal Research Center

The potential revenue gains from LC 43 0408ER would arise primarily from extending nexus to online sales by out-of-state sellers who are not required under current law to collect Georgia sales taxes. National estimates of online sales are available and these can be shared down to Georgia, but it is not possible to know what portion of these sales are currently taxed or not taxed in the state. Many online retailers also operate from physical stores and are thus likely to already have nexus in the state. Others that do not operate physical stores may have nexus in the state arising from distribution centers in the state, affiliates with a physical presence, or other nexus triggers. The following summarizes the data and assumptions used in arriving at the upper bound estimates of the bill's revenue impact.

- The US Census Bureau's Annual Retail Trade Survey estimates US e-commerce retail sales for 2014 at approximately $299 billion. Of that amount, approximately $255 billion or 85.3 percent is estimated to be attributable to "nonstore retailers", specifically electronic shopping and mail order houses.

- More recent estimates are not broken out by type of retailer, but the Census estimate of aggregate e-commerce retail sales for the four quarters corresponding to state fiscal year 2016 is approximately $367.4 billion. Assuming the same 85.3 percent share attributable to nonstore retailers, sales for this subset are estimated to have been about $313.4 billion.

- This amount is shared down to Georgia based on Georgia's share of US households with internet access, about 3.15% as of 2012 according to Census data, resulting in an estimated $9.9 billion of nonstore retailers' sales in Georgia.

- The Georgia Department of Revenue (DOR) reports that, for FY 2016, the state collected approximately $190.6 million in state sales tax from NAICS code 4541, electronic shopping and mail order retailers. This revenue represents a 13 percent increase over FY 2015, which itself was 20 percent higher than collections in FY 2014.

- FY 2016 collections correspond to approximately $4.8 billion of taxable sales, leaving $5.1 billion of estimated untaxed sales by nonstore retailers into Georgia. If fully taxed, these sales would have produced $204 million of additional state revenues and $153 million for local governments (assuming an average local tax rate of 3 percent).

- These estimates for FY 2016 represent the upper bound on the potential revenue losses from untaxed online sales, but the actual loss is likely significantly smaller due to several mitigating factors.
  - Many out-of-state online sellers will likely not reach the in-state sales thresholds of the proposed bill and thus will remain untaxed.
  - Some portion of online retail sales are of goods delivered electronically—e.g. digital downloads of music, books, videos, etc., and thus not currently subject to tax regardless of nexus—or are sales that are exempt from sales tax under other provisions of the code.

  Unfortunately, no information is available from which the estimate these mitigating factors.

- The $204 million estimate above for FY 2016 represent about an 18 percent increase over the comparable estimate for FY 2015. However, Census estimates of nonstore e-commerce sales show growth of about 15 percent per year over the two years ending June 2016. Finally, Forrester Research (cited by trade news website internetretailer.com, Jan. 29, 2016) forecasts online sales growth through 2020 to average 9.3 percent annually. Thus the projections assume a growth rate of 12 percent, roughly midway between recent Census-reported growth and Forrester's forecast, for FY 2017, 10 percent for FY 2018, and 9 percent thereafter.