This proposal was prepared by Annette Nellen, member of the Executive Committee and the Tax Policy Committee of the State Bar of California’s Taxation Section. The author wishes to thank reviewers Sanford Millar and Charles Taylor, for their helpful comments.

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1 The comments contained in this paper are the individual views of the author who prepared them, and do not represent the position of the State Bar of California or the Taxation Section of the State Bar.

2 Although the participants on this project might have clients affected by the rules applicable to the subject matter of this paper and have advised such clients on applicable law, no such participant has been specifically engaged by a client to participate on this project.
EXECUTIVE SUMMARY

California, like other states, has a decades-old problem of a use tax gap, that is expected to grow with the continued growth of e-commerce. Should Congress enact legislation to allow states to impose sales tax collection obligations on more vendors, there will still be a need for California buyers to know of the use tax and pay it.

This paper provides some background on California's use tax and collection activities. Several suggestions to improve collection are offered including the following:

- Establish a public awareness campaign and educational activities
- Mandate use of Form 540 or Form 100 to pay use tax
- Specify a penalty for noncompliance
- Clarify and improve the use tax line on Form 540
- Clarify instructions for amended returns
- Improve the "Qualified Purchaser" Program
- Make the use tax law consistent among consumer purchases
- Ensure compliance among employees
- Pursue technological solutions
- Support efforts to find non-compliant vendors
- Encourage out-of-state vendors to voluntarily collect use tax or assist in its collection
- Work with Congress and other states
DISCUSSION

I. INTRODUCTION

A. The Problem

For decades, states have struggled to collect all of the sales and use tax owed, particularly from in-state buyers who make purchases from outside of the state. While for decades, catalog sales were the focal point of the use tax gap, for the past decade and ongoing, e-commerce sales are the focal point. While states have tried a variety of approaches and Congress has offered proposals and even held hearings on the use tax collection problem and solutions, state collection problems remain and are expected to grow with the continued growth of e-commerce.

While California has made changes to improve use tax collection, a significant use tax gap remains. Additional legislative and administrative actions can be taken to further reduce this tax gap.

This paper offers both administrative and legislative suggestions on how California might improve its use tax collection from both businesses and individual consumers.

B. Approach of this Paper

The paper provides a brief overview to the use tax gap and California's current use tax collection strategies. Suggestions are provided for how to further improve use tax collection. Some examples of approaches used in other states are also noted.

II. Use Tax Basics

Soon after the enactment of a sales tax in 1933, California enacted a use tax to ensure that tax was collected on taxable purchases made by California buyers even if the seller was not legally obligated to collect the sales tax. The use tax was intended to put California retailers on “an equal footing with their out of state competitors” who were exempt from the sales tax because they were not located in
While the sales tax is imposed upon the retailer (although they may pass it on to the buyer), the use tax is legally imposed upon the buyer. The rate and base for each tax is the same.

A seller without a physical presence in the state is not obligated to collect sales tax from buyers located in that state. A non-present (remote) seller may still register with the taxing state and collect sales and use tax, but it is not obligated to do so. Instead, the state must rely on buyers knowing of their use tax obligation and voluntarily following through after the purchase to pay the tax. States must therefore have procedures for informing taxpayers of the use tax and providing appropriate procedures for compliance.

A. Compliance and Avoidance Challenges

A problem for California and other states is that many buyers are not aware of the use tax or their use tax obligation. For example, when they shop online for tangible goods and are not charged sales tax at checkout, they likely believe that the purchase is not taxable because it was an online purchase.

In April 2012 the Board of Equalization (BOE) hired Harris Interactive to conduct a survey of the attitudes and perceptions of roughly one thousand California residents about the use tax. The survey results included the following (survey results page noted):

- 25% of respondents indicated they were extremely or very familiar with the use tax while 19% said they had not heard of it and 27% had heard of it but were not familiar with it. In contrast, 79% were extremely or very familiar with the sales tax and only 2% had never heard of the sales tax. (7 and 21)

- Only 16% of respondents indicated they had paid use tax in the past year although 79% had purchased from out of state. (7 and 22)

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4 This standard was confirmed by the U.S. Supreme Court in Quill Corporation v. North Dakota, 504 U.S. 298 (1992) and National Bella Hess v Department of Revenue of Illinois, 386 U.S. 753 (1967).
5 Information from BOE Member George Runner at http://www.boe.ca.gov/members/runner/info/surveys.htm.
6 Supra.
When asked why they did not pay tax when they purchased goods from out-of-state, 28% of respondents indicated they did not know tax was due. (26)

Some shoppers might intentionally search for websites that do not charge sales tax on purchases. Bricks and mortar stores may find shoppers who visit in order to see and touch the merchandise, but then go online (perhaps using their iPhone while still in the store) to see if they can get a better price, perhaps also without sales tax being charged.⁷

Some buyers who are aware of the use tax might not follow through on paying it due to the small amount involved, a perception that they won't get caught, or because they do not think they have the information necessary to comply.

E-commerce offers some vendors an opportunity to legally avoid collecting sales and use tax altogether. A vendor can easily avoid all sales tax compliance by following a practice (and noting it on their website) that they ship from State X (where the vendor resides), but do not sell to customers in State X. This approach enables vendors to avoid collecting tax in State X (they have a physical presence there, but no sales) and in any other state because they only have a physical presence in State X.

B. Use Tax Collection

Per the BOE, use tax collections were as follows per various taxpayer types and methods of remittance.\(^8\)

<table>
<thead>
<tr>
<th>Source</th>
<th>Period</th>
<th>Use Tax Reported (in millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Registered with BOE</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Use Tax Reported by Registered California Consumers (excluding</td>
<td>CYE 12/31/10</td>
<td>113</td>
</tr>
<tr>
<td>Qualified Purchasers (service businesses)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Use Tax Reported by Registered Out-of-State Retailers</td>
<td>CYE 12/31/10</td>
<td>1,697</td>
</tr>
<tr>
<td>Use Tax Reported by Seller's Permit Holders</td>
<td>CYE 12/31/10</td>
<td>1,356</td>
</tr>
<tr>
<td>Use Tax Assessed in Audits</td>
<td>FYE 06/30/11</td>
<td>161</td>
</tr>
<tr>
<td>Not Registered with BOE</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Use Tax Reported on One-Time, Individual Use Tax Returns</td>
<td>CYE 12/31/10</td>
<td>7</td>
</tr>
<tr>
<td>Use Tax Reported on California Income Tax Returns</td>
<td>CYE 12/31/10</td>
<td>11</td>
</tr>
<tr>
<td>Use Tax Reported on Out-of-State Purchases of Vehicles, Vessels, and</td>
<td>FYE 06/30/11</td>
<td>42</td>
</tr>
<tr>
<td>Aircraft</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Use Tax Collected by DMV on Private Party Transactions</td>
<td>FYE 06/30/11</td>
<td>500</td>
</tr>
<tr>
<td>Use Tax Reported for Mobile Homes</td>
<td>FYE 06/30/11</td>
<td>4</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>$3,917</td>
</tr>
</tbody>
</table>

\(^*\)CYE = Calendar Year Ending, FYE = Fiscal Year Ending
Updated 03/2012

C. California Actions to Improve Use Tax Compliance

California has taken actions to help buyers know of their use tax liability. Instructions to income tax forms have included information on the use tax. The BOE website also has information on the use tax.

\(^8\) BOE, Use Tax Basics; viewed 1/8/13; [http://www.boe.ca.gov/taxprograms/usetax/index.html](http://www.boe.ca.gov/taxprograms/usetax/index.html)
In 2003, California followed the lead of many other states and added a specific line on Form 540 and Form 100 for the use tax. This may cause some taxpayers to go to the instruction book to learn about the tax. However, if a person does not know what a "use tax" is, they may instead just skip that line on the Form 540 altogether, assuming it does not pertain to them.

Starting in 2011, California alleviated the recordkeeping challenge many individuals face in that they do not have records showing all of their purchases for which sales tax was not charged. Now, individuals may use an optional "look-up" table that estimates use tax owed based on income. This eliminates the need to keep records of each purchase for which use tax is owed, although the use tax for any purchase of an item of $1,000 or more must be added to the table amount. The BOE estimates that the table will increase collections by $10.6 million annually.

Another effort in California to improve use tax collection from businesses was created via legislation enacted in 2009 (Chapter 16; AB x4-18). This legislation requires "qualified purchasers" to register with the BOE and pay use tax directly to the BOE. A qualified purchaser has $100,000 or more of annual gross receipts from their business and is not required to hold a seller's permit (such as because they are a service provider and do not sell items subject to California sales tax).

A report from the BOE in 2011 noted the following results for the "Qualified Purchaser" Program as of June 30, 2011. Per this report, 51 BOE staff work on this program including 30 who had previously worked on the BOE's Tax Gap Program.

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9 The line was added to the individual and corporate income returns (Forms 540 and 100) to cover purchases of tangible personal property made on or after 1/1/03 through 12/31/09 (SB 1009, Chapter 718, 2003). Sellers registered for sales tax may not use this reporting approach. SB 858 (Chapter 721; October 2010) made permanent the requirement to have the use tax line on Forms 540 and 100. Such reporting constitutes an irrevocable election to report qualified use tax in that manner (on the income tax form).

10 SB 86 (Chapter 14, 2011). It is estimated that the look-up table will generate $10.6 million annually.


12 See R&T §6225 and http://www.boe.ca.gov/sutax/useTaxRegFAQ.htm.

13 BOE-1489, Informal Issue Paper - Discussion of proposed changes to the Qualified Purchaser Program (June 2009); http://www.boe.ca.gov/meetings/pdf/P3_2_072611_Informal_Issue_Paper.pdf.
Per the BOE, the majority of returns filed (85%) reported no use tax liability.\textsuperscript{14}

In 2011, California enacted a so-called "Amazon law" to require vendors with a specified connection or relationship with specified entities or affiliates in the state to collect sales tax.\textsuperscript{15}

### III. The Use Tax Gap

California, along with all states that impose a sales tax, has a use tax gap. That is, not all of the use tax that is owed to the state is collected by the state.

The BOE estimates that the annual use tax gap is about $1.1 billion.\textsuperscript{16}

In contrast, the National Conference of State Legislatures (NCSL) estimates that for 2012, California's use tax gap was $4.1 billion stemming from the following types of transactions:\textsuperscript{17}

<table>
<thead>
<tr>
<th>Transaction Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-electronic business to consumer (B-C)</td>
<td>$1,136,801,607</td>
</tr>
<tr>
<td>Non-electronic business to business (B-B)</td>
<td>$1,118,366,340</td>
</tr>
<tr>
<td>Electronic B-B and B-C</td>
<td>$1,904,500,000</td>
</tr>
<tr>
<td>Total</td>
<td>$4,159,667,947</td>
</tr>
</tbody>
</table>

\textsuperscript{14} BOE, Staff Legislative Bill Analysis, AB 2059, April 18, 2012; \url{http://www.boe.ca.gov/legdiv/pdf/2059ab041812lrb.pdf}.

\textsuperscript{15} AB 155 (Chapter 313; 9/23/11), effective 9/15/12, changing R&T §6203. Reg. 1684 as modified. Also see BOE Special Notice (Aug 2012; L-324; \url{http://www.boe.ca.gov/news/pdf/l324.pdf}), and BOE, FAQ at \url{http://www.boe.ca.gov/sutax/abx1-28faq.htm}. For more on affiliate nexus or so-called "Amazon" laws enacted in California and other states, see \url{http://www.cob.sjsu.edu/nellen_a/affiliate_nexus.html}.

\textsuperscript{16} BOE News Release, 4/4/12; \url{http://www.boe.ca.gov/news/2012/35-12-G.pdf}.

\textsuperscript{17} NCSL, Estimated Uncollected Use tax from all Remote Sales in 2012; \url{http://www.ncsl.org/issues-research/telecom/2012-uncollected-use-tax.aspx} (viewed 10/25/12).
The primary reason for the use tax gap is the failure of buyers to self-assess and pay use tax when they purchase taxable goods for which sales tax was not charged because the seller was not obligated to collect the tax.

The gap can also stem from otherwise compliant taxpayers who do not pay all of their use tax. Complexity of the sales and use tax might cause compliant taxpayers to not pay all of the use tax that is owed. For example, many individuals do not know that if they purchase goods out-of-state and paid that state's sales tax, they still owe use tax in California when they bring the goods home. The amount owed is the excess of the amount of California sales that would have been owed if purchased in-state over the amount that was paid out-of-state. Also, taxpayers may not know when use tax should also be paid for shipping and handling charges for goods purchased online or via catalogs.

IV. Why Improve Use Tax Compliance

Reasons for improving use tax compliance include:

1. The use tax has been in existence since 1935; it is not a new tax. Improved collection will provide needed revenue for the state without the need to increase a tax rate or create a new tax.

2. Failure to collect use tax violates the principles of equity and neutrality. Equity and fairness are violated when taxpayers are able to purchase goods online without paying tax while others buying the same items at their local store pay the tax. Vendors with physical stores in California can find it difficult to compete with online vendors who can sell without collecting sales tax. Because so many consumers are unaware of their use tax obligation they do not factor it in when comparing in-store and online prices. Also, when buyers perceive that online items are cheaper than the same items purchased at a physical store, they may be inclined to purchase online, thus further exacerbating the use tax collection problem.

V. Challenges to Use Tax Collection

There are several reasons why states face challenges in collecting use tax and reducing the use tax gap. Some of the key reasons are described next.
A. Confusion and Low Understanding of the Use Tax

Because consumers know so little about the use tax, improved enforcement is often viewed by many as the enactment of a new tax. This misunderstanding is perpetuated when reporters and even sometimes elected officials, refer to the use tax as a new tax.

B. Tax Base Complexity

Another collection challenge is that sales and use tax rules are not simple. Taxpayers need clear guidance as to which of their purchases are taxable and which are not, particularly where handling charges or services are associated with the purchase of tangible personal property.

C. U.S. Constitutional Constraints and Waiting for Congress

Challenges also exist in finding remedies that allow the state to have the preferred system of thousands of vendors collecting the use tax rather than relying on millions of consumers to self-report the tax. In 1992, the U.S. Supreme Court ruled in Quill Corp. v. North Dakota, 504 U.S. 309, that the commerce clause of the U.S. Constitution requires that a vendor have a physical presence in a state before the state can impose sales/use tax collection obligations upon it. While Congress has authority under the commerce clause to overturn or modify this ruling, it has not done so. Possible reasons for inaction by Congress include the complexity of varying state sales tax rules and the high costs of compliance if all vendors were required to collect and report sales/use tax in all state and local jurisdictions in which they have customers.

While Congress has considered legislative proposals to modify the Quill physical presence requirement since at least 1994, nothing has been enacted. In the 112th Congress, there were three proposals to broaden the definition of sales tax nexus for businesses with sales beyond specified de minimus levels.\(^{18}\)

VI. Suggested Solutions

This section describes suggestions for how California can improve use tax collection.

\(^{18}\) S. 1832, H.R. 3179 and H.R. 2701 (112th Congress).
A. Establish a Public Awareness Campaign and Educational Activities

While the BOE has undertaken some public awareness efforts, there are still too many people who have not heard of a use tax or do not know what it is. Thus, when they see the "use tax" line on Form 540, they are likely to skip it.

The April 2012 Harris Interactive survey indicated interest in public education about the use tax. Messages noted as helpful were that the use tax:

- Helps provide for necessary government services.
- Is the law and residents are obligated to pay it.
- Helps in-state businesses be competitive.

While a state would prefer to have vendors collect the sales tax rather than having consumers self-report, it is unlikely that a state can always rely on vendors. If a vendor is located outside of the U.S. (with no physical presence in the U.S.) it would be difficult, if not impossible, for the state to get the foreign vendor to collect the state’s sales tax. In addition, proposals by Congress to allow states that have simplified their sales tax system to require remote vendors to collect the sales tax exempt small vendors and won't apply to foreign vendors. Thus, unless a state exempts sales from small vendors from the sales and use tax, consumers would still be required to self-report use tax when they purchase taxable items from such small vendors. Thus, individual consumers will likely always have a self-assessment obligation when it comes to the use tax. Thus, efforts are needed to make all individuals as aware of the use tax as they are of income taxes.

Possible activities include:

a. **Advertising.** Website ads (including ones that can be posted at no charge on state agency websites) as well as television and radio ads are needed that explain what the use tax is, how long it has existed, when it applies, how to calculate it and how to pay it. Information on the amount of uncollected tax should also be provided, perhaps in terms of how it compares to total tax collections or a favored government spending program, such as some part of K-12 education spending. In addition, ads could note that if everyone

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paid their use tax, the state's budget problems would be lessened. An example of a descriptive ad from Michigan is included in this paper at Exhibit C.

b. *Continued outreach to tax advisers.* In early 2007 and later years, the BOE mailed letters to tax practitioners in the state encouraging them to discuss use tax compliance with their clients. Greater and more frequent efforts are needed. For example, ads could be posted to websites of organizations that represent or attract return preparers. The BOE can offer free continuing education that provides appropriate credit and includes instruction on how individuals meet their use tax obligations.

c. *State agency outreach.* State agencies should be required to place use tax reminders on pay stubs throughout the year, addressing both recordkeeping and reporting requirements, with a URL provided for obtaining additional information. State mailing envelopes can include a reminder stamped on the outside about paying use tax.

d. *Simplicity and clarity.* Be sure use tax information on the BOE website is simple and up-to-date. As of January 2013, there were a few pages that covered use tax and at least one had outdated information or broken links. For example, the following page ([http://www.boe.ca.gov/ads/news06.htm](http://www.boe.ca.gov/ads/news06.htm)) states that a use tax form in Publication 79-B can be used. The link though, takes the reader to an e-Reg page because the form is no longer used. The link for use tax FAQs takes the reader to this page:

Consideration should be given to how the BOE website can direct non-business individuals to one location to learn what a use tax is, the importance of paying it, and how to pay. While there is a lot of helpful information on the BOE website on use tax, it seems to be
mostly directed to businesses, which is obviously necessary, but will likely be confusing to non-business consumers.\textsuperscript{21}

One BOE website directed at 2012 filings was found, but it is unclear if this is something consumers will easily find. (The author found it in looking for data on how much use tax is collected due to the Form 540 use tax line.) The website below also includes the 2012 look-up table.

\begin{center}
\textbf{MAKE ONLINE PURCHASES?}
\textbf{YOU MAY OWE USE TAX.}
\end{center}

\begin{itemize}
\item You may owe "use tax" if you made a purchase from an out-of-state retailer and were not charged California tax on the purchase.
\item If you have not saved your receipts, you may calculate and pay estimated use tax on your 2012 California Income Tax return, based upon your income.
\item The Lookup Table below may be used to pay estimated use tax for personal items purchased for less than $1,000 each.
\item For more information about Use Tax, please visit: \url{http://www.boe.ca.gov/info/use_tax_table.html}
\end{itemize}

\begin{center}
\textbf{Example}
\end{center}

\begin{itemize}
\item \textbf{SUBTOTAL (3 ITEMS)} $69.95
\item \textbf{SHIPPING} FREE
\item \textbf{If you didn't pay California tax here then you likely owe use tax} $0
\item \textbf{GRAND TOTAL} $69.95
\end{itemize}

\begin{center}
\url{http://www.boe.ca.gov/info/use_tax_table.html}
\end{center}

e. \textit{Tax prop software}. Work with tax preparation software companies to provide explanation of the use tax line and help in designing questions to ensure that customers do not overlook their use tax obligation.

f. \textit{VITA}. Be sure that VITA training on California returns includes the use tax line. Provide use tax publications at VITA sites to help inform taxpayers of this tax.

g. \textit{High school curriculum}. High school civics curriculum and standards should include knowing the basics of California's tax system and individual tax obligations.

h. \textit{Role for elected officials}. Elected officials should be encouraged to note in public statements, particularly during the filing season, that

\begin{itemize}
\item See, for example, the use tax basics website at \url{http://www.boe.ca.gov/taxprograms/usetax/index.html}. At January 2013, this website did not cover use tax obligations of consumers at the "basics" tab.
\end{itemize}
they paid their use tax and encourage their constituents to do so as well. The public needs to hear: "I paid my use tax. Did you?"

B. Mandate Use of Form 540 or Form 100 to Pay Use Tax

Today, taxpayers who are not qualified purchasers or required to have a seller's permit, have a choice of methods for paying their use tax. As explained in FTB 988 (April 2012): 22

"In an effort to assist you with your use tax reporting requirements, the Franchise Tax Board (FTB) included a use tax line on FTB Forms 540A, 540 2EZ, and 540, California Resident Income Tax Returns. This gives you the option to report your use tax liability on your individual income tax return for out-of-state purchases. In addition, the form instructions include a Use Tax Worksheet and use tax rates to help you compute the proper use tax liability. New for 2011, you may use the Estimated Use Tax Table to estimate and report the use tax due on individual, nonbusiness items you purchased for less than $1,000 each. Your other available option is to file BOE-401-DS, Use Tax Return with BOE."

Despite the FTB reference to BOE-401-DS (see above), the BOE website tells individuals who do not report use tax on their income tax form, to pay directly to the BOE via "eReg." 23

Some taxpayers, such as those with a seller's permit, are not allowed to report use tax on their Form 540. Also as noted above and in the Form 540 instructions (see Exhibit A of this paper), an individual need not report use tax on Form 540, but can instead report and pay use tax directly to the BOE. These requirements and options enable paid tax return preparers to not pursue client reporting of use tax on Form 540 under the assumption that the client is reporting the tax on their own to the BOE.

Prior to enactment of AB 2270 (Chapter 200, 8/27/12), a use tax form filed separately with the BOE by a taxpayer eligible to report use tax on their income tax form was due by January 31 of the following year (for example, January 31, 2012 for 2011 use tax). AB 2270 changed the date to April 15 to

22 The full text of FTB 988 (2 pages) can be found at https://www.ftb.ca.gov/forms/misc/988.pdf.
coincide with the due date of the Form 540. While this is helpful for compliant taxpayers, it is unlikely to increase the number of compliant taxpayers.

The choice issue was noted in the Assembly analysis of AB 969 (5/23/07). That analysis noted that use tax reported on income tax forms for 2004 was $2.8 million, $4.6 million in 2005 and $5.5 million in 2006. Taxpayers who prepared their own return were eight times more likely to complete the use tax line than were taxpayers who used paid preparers. The sponsor of AB 969 believed this was due to the elective nature of reporting use tax on the income tax form. AB 969 proposed to make reporting of use tax on the income tax form mandatory to increase awareness and compliance.

Possible remedies to reduce the confusion as to how taxpayers who are not qualified purchasers or holders of seller's permits pay use tax and to better ensure that use tax is reported and paid by these taxpayers include the following.

1. Eliminate the option for these taxpayers to report use tax on a form other than Form 540 (or 100). A benefit of this is that it would require paid tax return preparers to explain the tax to clients and require reporting of some amount (including zero if appropriate) on the line. A similar effect would result with tax preparation software. A requirement would be needed that the use tax line be completed, even by noting $0 (rather than leaving it blank).

The New York individual income tax form notes that filers are to enter "zero" rather than leave the line blank. For example, the 2012 Form IT-201 includes:

59 Sales or use tax (see page 29; do not leave line 59 blank) .............

A downside of this option is that some taxpayers who owe use tax might not have an income tax liability so are not filing an income tax return. Such taxpayers could still be required to file an income tax form though, such as Form 540 2EZ.

Another downside is that preparers may have conflicts with some clients who insist on reporting zero despite the preparer's knowledge that they made online purchases for which use tax is owed. A public awareness

24 The analysis is available at http://www.leginfo.ca.gov/pub/07-08/bill/asm/ab_0951-1000/ab_969_cfa_20070523_170127_asm_floor.html.
campaign about the use tax, the ease of reporting and the obligation to report should proceed elimination of the option to report use tax on a separate BOE form.

2. Keep the current options (income tax form or BOE use tax form), but add a line to the income tax form following the current use tax line:

"If line 95 (use tax) is blank, did you file a separate use tax form with the BOE or will you file one by the required April 15 due date?"

Taxpayers would then check a box to indicate "yes" or "no." If yes, FTB can share that information with BOE who can follow up if no form is filed.

Again, this would require paid return preparers to ask about the client’s use tax compliance.

C. Specify a Penalty for Noncompliance

The importance of reporting and remitting use tax could be enhanced by imposing a penalty for non-compliance including leaving the Form 540 and Form 100 use tax line blank (including not entering $0). The penalty could be noted as part of these income tax return lines.

The April 2012 Harris Interactive survey indicated that 73% of respondents would be more likely to pay the use tax if they knew a penalty could be assessed for non-compliance.25

D. Clarify and Improve the Use Tax Line on Form 540

The California Form 540 for 2012 (and prior years) includes the following use tax reporting line:

Similarly, the 2012 Form 100 includes this line:

In contrast, the use tax line on the Michigan personal income tax form explains what the use tax is attributable to. Line 23 of the 2012 Michigan Form MI-1040 follows:

23. **USE TAX. Use tax due on Internet, mail order or other out-of-state purchases from Worksheet 1, line 3, p. 9.**

The instructions to line 23 of the Michigan personal income tax form state that if no use tax is owed, enter zero on line 23. Further improvement could be made by noting that instruction on line 23, as New York does. Such an instruction seems to make it more likely that filers will make an effort to learn about the tax.

If the Form 540 line explained the use tax on the use tax line (as is done on the Michigan tax form) and noted that a number must be entered unless the filer notes they filed a separate use tax form, compliance should improve. Should there continue to be an option of separately filing a use tax form with the BOE, as noted earlier, a check box should be added following line 95 (or line 40 on Form 100) asking filers to check if they have filed a separate use tax report. The type of form filed should also be noted and the date.

In addition to providing more details of the "use tax" on the reporting line, the instructions for Form 540 should be clarified and highlighted on a single page rather than spread over 3 pages. The Michigan instruction book has a single page devoted solely to the use tax (see Exhibit B to this paper).

In addition, the 2012 California instructions state: "See page 20 for a general explanation of California use tax." Unfortunately, the instruction book ends at page 18 (there is no page 20).

Exhibits A and B at the end of this report contain the individual income tax instructions for the use tax for California and Michigan, respectively.

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26 The page confusion seems to be that the FTB website includes a shortened version of the 540 instructions for 2012 that ends at page 18 ([https://www.ftb.ca.gov/forms/2012/12_540a_540ins.pdf](https://www.ftb.ca.gov/forms/2012/12_540a_540ins.pdf)). This was also the situation in 2010 and 2011. Apparently, the page reference is to the longer instruction booklet (unable to verify for 2012 as that booklet was not available at January 14, 2013). Individuals who only find the shortened version with the reference to the non-existent page 18 are likely to conclude that the information is not important since it was omitted.
E. Clarify Instructions for Amended Returns

The Form 540 instructions (see Exhibit A to this paper) state that an amended 540 should not be used to amend the use tax line. Per page 19 instructions: "Changes in use tax reported. Do not file an Amended Income Tax Return (Form 540X) to revise the use tax previously reported. If you have changes to the amount of use tax previously reported on the original return contact the State Board of Equalization."

This instruction buried in the 540 instruction booklet is unlikely to be known by taxpayers or preparers. In addition, it is vague (e.g., how do you contact the BOE?) and likely inhibits efforts to correct use tax errors including errors of prior omission.

F. Improve the "Qualified Purchaser" Program

Improvements should be made to the "Qualified Purchaser" Program including those recommended by a 2012 legislative proposal and a 2009 BOE informal issue report.

A June 2009 "Informal Issue Report" of the BOE explained the administration of the Qualified Purchaser Program and offered the following administrative changes to improve the program:

1. Stop the practice of BOE personnel registering businesses they believe meet program criteria.
2. Let taxpayers close their permit if their receipts drop below $100,000 for two years.
3. Have BOE cancel the registration of businesses that filed returns with zero use tax owed for three consecutive years.

AB 2059 (2012) proposed to make changes to the Qualified Purchaser Program including increasing the participation threshold to over $500,000 of receipts (from $100,000) and to allow for a filing extension.

Suggestions for improving this program:

a. Implement the administrative improvements noted in the 2009 report.

b. Conduct a survey of qualified purchasers to gather comprehensive data beyond some of the informal data gathered already.²⁹

c. If the gross receipts threshold is increased, find a simple way for businesses no longer required to participate in the program to pay their use tax. For example, they could be allowed to pay their personal use tax obligations on the Form 540 use tax line and use the look-up table, and report any use tax from their business on their Schedule C, Form 100 or Form 565 (rather than have to file a separate use tax form).

G. Make the Use Tax Law Consistent Among Consumer Purchases

The California sales tax law includes a variety of exemptions. One of these exemptions relevant to use tax is for foreign purchases of tangible personal property hand carried into California (such as being carried on the airplane). This exemption applies to up to $800 of otherwise taxable goods provided it is all reported on a single U.S. Customs duty declaration. The exemption can be used once within a 30-day period. The exemption does not apply if the California resident ships the goods to California.³⁰

This exemption raises a question of fairness which can lead to disrespect for the tax system and lowered use tax compliance. For example, someone purchasing $100 of goods from an Internet retailer and not charged sales tax might question why they are obligated to pay use tax when someone who buys

²⁹ The 2009 Informal Issue Report includes an attachment of comments from some small business owners noting problems with the program, such as the compliance costs. BOE Member George Runner has a website noting his concerns with the program and inviting people to take a survey about the program (http://www.flashreport.org/blog/2011/07/07/qualified-purchasers-survey/ posted 7/7/11). The comments note a need for action, as well as assurance that a random set of purchasers are questioned. A formal survey would provide more balanced and complete data (such as was done with the April 2012 Harris Interactive survey noted earlier).

³⁰ This exemption is provided in R&T §6405 which reads as follows: "Notwithstanding Section 6246, the storage, use, or other consumption in this state of the first eight hundred dollars ($800) of tangible personal property purchased in a foreign country by an individual from a retailer and personally hand-carried into this state from the foreign country within any 30-day period is exempt from the use tax. This section shall not apply to property sent or shipped to this state."

Annette Nellen
the same $100 of goods while vacationing abroad is not obligated to pay use tax when they bring the goods back with them on the airplane.

This exemption is also questionable from a tax policy perspective in that there is an administrative structure already in place via the U.S. Customs Office to make tax compliance simple. The declaration includes the dollar amount of the goods. As noted on the BOE website, BOE staff have authority under Rev. & Tax. §7054 to audit the duty declarations.  

This exemption for foreign goods hand carried into the country from a foreign trip should be repealed. Repeal would make the sales and use tax more equitable. It would also reduce the administrative burden for the BOE in that they would not have to monitor the dollar value of goods hand carried into California by residents during any 30-day period.

All sales and use tax exemptions should be reviewed against principles of good tax policy and to determine if their original purpose is still relevant today.

H. Ensure Compliance Among Employees

If not already in place, a requirement should be added that a person cannot be hired or appointed to work at a California state tax agency if they have not fulfilled their use tax obligation for the past three years. That is, if the use tax line on Form 540 is blank, no separate use tax form was filed and they cannot verify that no use tax was owed, they cannot be hired. Alternatively, the applicant could be given the option to become compliant.

Individuals running for an elected position involving tax administration, should be required to disclose or have verified that they have fulfilled their use tax obligation for the past three years. Such a requirement might be considered for all elected positions.

31 The information on the foreign purchase use tax exemption is on the same BOE website as other information on use tax compliance. See http://www.boe.ca.gov/taxprograms/usetax/foreign_purchase.html.
32 For examples of formulations of principles of good tax policy, see Nellen, Comparison of Sets of Principles Commonly Used in Analyzing Tax Proposals; available at www.cob.sjsu.edu/nellen_a/TaxReform/PolicyApproachToAnalyzingTaxSystems.pdf.
I. Pursue Technological Solutions

Despite being in the information age today, states tend to rely on 1930's techniques for reporting and collecting use tax. Technological solutions include having the use tax charged to buyers at time of purchase. The buyer's credit card or Paypal account could be charged for the use tax by the state tax agency (rather than by the vendor). That is, the vendor charges for the cost of the goods/services and the state charges for the tax. This approach shifts the credit card fee for the use tax from the vendor to the state, eliminates reporting obligations for most, if not all, consumer purchases, speeds up collection time for the tax, and simplifies state audits of the use tax.

Approaches could also be implemented to use such a collection system for catalog orders (those not over the Internet). Obstacles include consumer reluctance, but that might be removed if more consumers understand that the alternative is to self-report and remit use tax. Use of a third party collector for the state could eliminate consumer concerns over the state having access to their credit card or purchase information. Vendor concerns might also be reduced as this system would be simpler and less costly than requirements to collect sales/use tax from all customers and file sales tax forms in all jurisdictions. States should work together, and with vendors, to pursue such a tax collection system.

J. Support Efforts to Find Non-Compliant Vendors

State auditors should continue efforts to find vendors with an in-state presence – either directly or through a sales representative, who are not collecting sales tax. Additional funding should be given to the BOE to enable it to locate non-registered vendors that may indeed have a physical presence in the state through property, related entities, agents or representatives.

The BOE should be given authority and appropriate funding to increase intra-agency information sharing as well as interstate information sharing.33

33 For example, the Southeastern Association of Tax Administrators (SEATA), is a group of twelve states that share sales tax information and encourage businesses to register in states in which they do not have a physical presence. This type of information sharing among states might be a useful way to find businesses that are not reporting use tax. For more information, see http://www.seatastates.org/.
K. Encourage Out-of-State Vendors to Voluntarily Collect Use Tax or Assist in Its Collection

Remote vendors will be reluctant to voluntarily collect a tax they are not legally required to collect and with good reasons. There are costs associated with compliance including filing and additional credit card fees due to higher charges by customers (because the sales tax would be included on the charge). There are also competitive disadvantages of complying when other vendors do not as it will look like the compliant vendor’s goods are more expensive. An advantage to collecting the use tax even when not legally required to do so would probably only exist if the state did a good enough job of educating taxpayers about their use tax obligations. Vendors could then advertise not to worry about use tax compliance because they would handle it for their customers.

Incentives for voluntary collection by vendors or assistance with use tax compliance might include any of the following:

a. Offer compensation to vendors for collecting the use tax (to help cover their compliance costs).

b. Offer simplified compliance techniques, such as annual rather than quarterly reporting and providing technological tools to aid compliance.

c. Offer an amnesty period to entice vendors who may owe or possibly owe sales/use tax to register with past liabilities forgiven.

d. Give a preference to companies registered to collect use tax when the state makes purchases.

e. Require all vendors who sell to any California government agency or office to register for sales tax collection.

f. Provide a "safe harbor" to remote vendors if they include a notice on invoices of California customers reminding them of their use tax obligation and the vendor completes a nexus checklist and it indicates they do not have sales tax nexus. Should the BOE later determine that the vendor has nexus, but acted in good faith in completing the questionnaire, past obligations would be forgiven.
L. **Work with Congress and Other States**

California could encourage Congress to enact legislation that reverses or minimizes the effect of the U.S. Supreme Court decision of 1992 (the *Quill* decision) that requires a physical presence in order for a state to collect sales tax from a vendor. The Court’s rationale for its holding was that imposing tax collection obligations on remote vendors would violate the commerce clause of the U.S. Constitution (it would impede interstate commerce). The Court noted that the commerce clause is within the purview of Congress (that is, Congress can determine what does and does not impede interstate commerce). Thus, Congress could enact a law allowing states to require remote vendors to collect sales and use tax from customers in the state, or require them to provide use tax notice and report information to states. However, Congress is unlikely to make such a change unless states greatly simplify their sales tax laws, which today, vary from state to state. States need to join efforts and approach Congress for assistance in reducing their use tax gaps.

Several states have simplified their sales/use tax laws by adopting uniform rules established by the Streamlined Sales and Use Tax Project.\(^\text{34}\) The hope of adopting states is that Congress will reverse the *Quill* decision for them.\(^\text{35}\)

Several years ago, California evaluated whether the SSUTA would be appropriate for the state. The SSUTA should be re-evaluated today in light of the current status of the SSUTA with over 20 states participating and the possibility that Congress might only reverse the *Quill* decision for adopting states.

\(^{34}\) The Streamlined Sales and Use Tax Project began in 2000. The Streamlined Sales and Use Tax Act (SSUTA) and other information on the project can be found at [http://www.streamlinedsalestax.org](http://www.streamlinedsalestax.org). The Board of Equalization has a background paper on the SSUTA at [http://www.boe.ca.gov/legdiv/pdf/Streamlined_Sales_and_Use_Tax_Agreement.pdf](http://www.boe.ca.gov/legdiv/pdf/Streamlined_Sales_and_Use_Tax_Agreement.pdf) (7/6/09).

\(^{35}\) Various bills have been introduced over the past few years, including H.R. 5660 (111\(^{\text{th}}\) Congress), the Main Street Fairness Act, which would allow states that are members of the Streamlined Sales and Use Tax Agreement (SSUTA) to collect tax from remote vendors. An exception would be provided for small vendors (not defined in the legislation). See [http://thomas.loc.gov/cgi-bin/bdquery/z?d111:hr.05660:](http://thomas.loc.gov/cgi-bin/bdquery/z?d111:hr.05660:). Legislative proposals of the 112th Congress included H.R. 3179, H.R. 2701 and S. 1832. Variations among these bills included the size of the de minimis seller rule and the nature of a state's sales tax simplification to be eligible to collect sales tax from remote sellers. In addition, not all of the bills required states to be part of the SSUTA to be eligible for broader sales tax collection. For more information on these bills and links to hearings held on them, see [http://www.cob.sjsu.edu/nellen_a/affiliate_nexus.html#Federal](http://www.cob.sjsu.edu/nellen_a/affiliate_nexus.html#Federal).
Exhibit A
Use Tax Instructions for 2011 California Individual Income Tax Return

Note: 2011 instructions are shown below because the longer Form 540 instruction booklet was not available at January 14, 2013.

From page 14 of the instructions:

Use Tax

Line 95 – Use Tax. This is not a total line.
California use tax applies to purchases of “tangible personal property” from out-of-state sellers (for example, purchases made by telephone, over the Internet, by mail, or in person). If you have questions about whether a purchase is taxable, go to the State Board of Equalization’s website at boe.ca.gov, or call their Taxpayer Information Section at 800.400.7115 or California Relay Service (CRS) 711 (for hearing and speech disabilities.)
The following taxpayers are required to report purchases subject to use tax directly to the State Board of Equalization and may not report use tax on their income tax return:
• Individuals or businesses that have a California seller's permit.
• Businesses that are not required to hold a California seller's permit, but receive at least $100,000 in gross receipts.
• Individuals or businesses that have a California consumer use tax account.

If you are not required to report purchases subject to use tax directly to the State Board of Equalization, you may report use tax on your income tax return. The Use Tax Worksheet and Use Tax Table below will help you determine how much use tax to report. If you owe use tax but you do not report it on your income tax return, you must report and pay the tax to the State Board of Equalization. For information on how to report use tax directly to the State Board of Equalization, go to their website at boe.ca.gov and type “use tax” into the Search box.
Failure to report and timely pay may result in the assessment of interest, penalties and fees.
See page 20 for a general explanation of California use tax.

Use Tax Worksheet
You must use the Use Tax Worksheet below to calculate your use tax liability if any of the following apply:
• You prefer to calculate the amount of use tax due based upon your actual purchases subject to use tax.
• You owe use tax on non-business purchases of individual items of property with a sales price of $1,000 or more.
• You owe use tax on any item purchased for use in a trade or business not registered with the Board of Equalization.

If you have a combination of individual items purchased for $1,000 or more and individual, non-business items purchased for less than $1,000, you may either:
• Use the Use Tax Worksheet to compute use tax due on all purchases, or
• Use the Estimated Use Tax Table to estimate the use tax due on individual, non-business items purchased for less than $1,000.
Use Tax Worksheet
Use whole dollars only.
1. Enter purchases from out-of-state sellers made
   without payment of California sales/use tax.
   See worksheet instructions below. .................. $ _______00
2. Enter the applicable sales and use tax rate. ...........
3. Multiply line 1 by the tax rate on line 2.
   Enter result here. .................................. $ _______00
4. Enter any sales or use tax you paid to another state for
   purchases included on line 1. See worksheet
   instructions below. .................................. $ _______00
5. Subtract line 4 from line 3. This is the total use tax due.
   Enter the amount due on line 95. If the amount is
   less than zero, enter -0-. ........................... $ _______00

Worksheet, Line 1, Purchases Subject to Use Tax
- Report purchases of items that would have been taxable if purchased in
  a California store. For example, you would include purchases of clothing,
  but not purchases of prescription medicine.
- Include handling charges.
- Do not include any other state's sales or use tax paid on the purchases.
- Enter only purchases made during the year that correspond with the tax
  return you are filing.
- If you traveled to a foreign country and carried items back to California,
  generally the use tax is due on the purchase price of the goods you listed

From page 15 (continued from page 14):
on your U.S. Customs Declaration less the $800 per-person exemption. This $800 exemption does not apply to goods sent or shipped to California by mail or other common carrier.

- If your filing status is “married/RDP filing separately,” you may elect to report one-half of the use tax due or the entire amount on your income tax return. If you elect to report one-half, your spouse/RDP may report the remaining half on his or her income tax return or on the individual use tax return available from the State Board of Equalization.

**Note:** Report and pay any use tax you owe on the following purchases directly to the State Board of Equalization, **not** on your income tax return:

- Vehicles, vessels, and trailers that must be registered with the Department of Motor Vehicles.
- Mobile homes or commercial coaches that must be registered annually as required by the Health and Safety Code.
- Vessels documented with the U.S. Coast Guard.
- Aircraft.
- Leases of machinery, equipment, vehicles, and other tangible personal property.
- Cigarettes and tobacco products when the purchaser is registered with the State Board of Equalization as a cigarette and/or tobacco products consumer.

**Worksheet, Line 2, Sales and Use Tax Rate**

- Enter the sales and use tax rate applicable to the place in California where the property is used, stored, or otherwise consumed. If you do not know the applicable city or county sales and use tax rate, using your computer or mobile device please go to the State Board of Equalization’s website at [boe.ca.gov](http://boe.ca.gov) and click on City and County Tax Rates or call their Taxpayer Information Section at 800.400.7115 or California Relay Service (CRS) 711 (for hearing and speech disabilities.)
- The statewide sales and use tax rate decreased by 1% effective July 1, 2011. If you made purchases prior to July 1, 2011, please use the rates in effect at that time.

**Worksheet, Line 4, Credit for Tax Paid to Another State**

- This is a credit for tax paid to other states on purchases reported on Line 1. You can claim a credit up to the amount of tax that would have been due if the purchase had been made in California. For example, if you paid $8.00 sales tax to another state for a purchase, and would have paid $6.00 in California, you can claim a credit of only $6.00 for that purchase.
Estimated Use Tax Table

You may use the Estimated Use Tax Table to estimate and report the use tax due on individual non-business items you purchased for less than $1,000 each, instead of reporting your use tax liability determined using the Use Tax Worksheet. This option is only available if you are permitted to report use tax on your income tax return and you are not required to use the Use Tax Worksheet to calculate the use tax owed on the purchases of such items. Simply include the use tax liability, that corresponds to your California Adjusted Gross Income, on line 95 and you will not be assessed additional use tax on the individual non-business items you purchased for less than $1,000 each.

You may not use the Estimated Use Tax Table to estimate and report the use tax due on purchases of items for use in your business or on purchases of individual non-business items you purchased for $1000 or more each. See the instructions for the Use Tax Worksheet if you have a combination of purchases of individual non-business items for less than $1,000 each and purchases of individual non-business items for more than $1,000.

<table>
<thead>
<tr>
<th>California Adjusted Gross Income (AGI) Range</th>
<th>Use Tax Liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less Than $20,000</td>
<td>$ 7</td>
</tr>
<tr>
<td>$20,000 to $39,999</td>
<td>$21</td>
</tr>
<tr>
<td>$40,000 to $59,999</td>
<td>$35</td>
</tr>
<tr>
<td>$60,000 to $79,999</td>
<td>$49</td>
</tr>
<tr>
<td>$80,000 to $99,999</td>
<td>$63</td>
</tr>
<tr>
<td>$100,000 to $149,999</td>
<td>$88</td>
</tr>
<tr>
<td>$150,000 to $199,999</td>
<td>$123</td>
</tr>
<tr>
<td>More than $199,999 – Multiply AGI by 0.070% (.0007)</td>
<td></td>
</tr>
</tbody>
</table>

From page 16 (not a continuation of the above text):

**Penalties.** To avoid late payment penalties for use tax, you must report and pay the use tax with a timely filed income tax return, or California Individual Use Tax return.
Additional Information

California Use Tax General Information

The use tax has been in effect in California since July 1, 1935. It applies to purchases from out-of-state sellers and is similar to the sales tax paid on purchases you make in California. If you have not already paid all use tax due to the State Board of Equalization, you must report and pay the use tax due on your state income tax return. See the information below and the instructions for line 95 of your income tax return.

In general, you should pay California use tax on purchases made from out-of-state (for example, by telephone, over the Internet, by mail, or in person) if:
- The seller does not collect California sales or use tax.
- You use, give away, store, or consume the item in this state.

Example: You live in California and purchase a dining table from a company in North Carolina. The company ships the table from North Carolina to your home for your use and does not charge California sales or use tax. You owe use tax on the purchase.

Complete the Use Tax Worksheet on page 14 to calculate the amount due.

Extensions to file. If you request an extension to file your income tax return, wait until you file your tax return to report your purchases subject to use tax and make your use tax payment.

Penalty. Failure to timely report and pay the use tax due may result in the assessment of penalties.

Changes in use tax reported. Do not file an Amended Income Tax Return (Form 540X) to revise the use tax previously reported. If you have changes to the amount of use tax previously reported on the original return contact the State Board of Equalization.

For assistance with your use tax questions, go to the State Board of Equalization’s website at boe.ca.gov or call their Taxpayer Information Section at 800.400.7115 or California Relay Service (CRS) 711 (for hearing and speech disabilities). Income tax information is not available at these numbers.
Exhibit B
Use Tax Instructions for 2011 Michigan Individual Income Tax Return

Use Tax

Every state that has a sales tax has a companion tax for purchases made outside that state by catalog, telephone, or Internet. In Michigan, that companion tax is called “use tax,” but might be described more accurately as a remote sales tax because it is a 6 percent tax owed on purchases made outside of Michigan.

Use tax is due on catalog, telephone, or Internet purchases made from out-of-state sellers as well as purchases while traveling in foreign countries when the items are to be brought into Michigan. Use tax must be paid on the total price (including shipping and handling charges).

How to Report Use Tax

Use Worksheet 1 below to calculate your tax and enter the amount of tax due on MI-1040, line 22.

Worksheet Calculation

Line 1: For purchases of $0-$1,000, multiply your total purchases times 6 percent (0.06) and enter the amount on Line 1, or

If you have incomplete or inaccurate receipts to calculate your purchases, you may use Table 1 - Use Tax to estimate your taxes. (See the following example.)

Line 1 should contain a number unless you made no purchases under $1,000 subject to the use tax. If we later determine that you owe use tax, you may be subject to penalty and interest.

Line 2: In all cases, if a single purchase is $1,000 or more, you must pay 6 percent use tax on those purchases.

Example: Kurt ordered a computer from a catalog retailer in New York for $1,437.50. Kurt also purchased items over the Internet for less than $1,000 during the year, but lost his receipts. He is sure he did not pay Michigan sales tax. Kurt’s AGI is $46,500. Kurt would complete Worksheet 1 as follows:

Line 1: Kurt selects $36 from the table based on his AGI $36
Line 2: Kurt enters $1,437.50 x 6 percent $86.25
Line 3: Total use tax due $122.25

Kurt would enter $122 (no cents) on his 2011 MI-1040, line 22.

Estimating your taxes does not preclude Treasury from auditing your account. If additional tax is due, you may receive an assessment for the amount of the tax owed, plus applicable penalty and interest.

<table>
<thead>
<tr>
<th>TABLE 1 - USE TAX</th>
</tr>
</thead>
<tbody>
<tr>
<td>AGI*</td>
</tr>
<tr>
<td>Tax</td>
</tr>
<tr>
<td>$0 - $10,000</td>
</tr>
<tr>
<td>$10,001 - $20,000</td>
</tr>
<tr>
<td>$20,001 - $30,000</td>
</tr>
<tr>
<td>$30,001 - $40,000</td>
</tr>
<tr>
<td>$40,001 - $50,000</td>
</tr>
<tr>
<td>$50,001 - $75,000</td>
</tr>
<tr>
<td>$75,001 - $100,000</td>
</tr>
</tbody>
</table>

Above $100,000... Multiply AGI by 0.08% (0.0008)

* AGI from Mi-1040, line 10.

Use Tax on the Difference

If you paid at least 5 percent to another state on your purchase, you do not owe use tax to Michigan. If you paid less than 5 percent, you owe the difference.

Note: The full 6 percent use tax is owed on purchases made in a foreign country.

For more information, visit www.michigan.gov/taxes.

**Exhibit C**

**Michigan Use Tax Ad**

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**INTERNET, MAIL ORDER AND OUT-OF-STATE PURCHASES**

**What is Michigan’s Use Tax?**

Every state with a sales tax has a companion tax for purchases made outside the state. In Michigan, that tax is called the “use tax” but might be more aptly described as a remote sales tax. As a general rule, you owe this tax if you purchased merchandise and did not pay sales tax. Typically this happens when you purchase an item (for example, clothing, books, furniture, computers) by telephone, catalog, Internet, or in person from out-of-state businesses that do not add the Michigan sales tax to your bill. While many Michigan residents are not aware of the use (remote sales) tax, it has been on the books since the 1930s.

**Who Benefits from Michigan’s Use Tax?**

- **Stronger Schools:** The direct beneficiary of nearly three-quarters of all sales tax and a third of all use tax is the state’s K-12 school system.
- **Local and State Services:** Local and state government services such as libraries, fire departments, road improvements, higher education, and public protection services are supported by sales and use taxes.
- **Michigan’s Retailers:** Collection of this tax will ensure a level playing field for Michigan businesses. Without collection of this tax, out-of-state retailers enjoy a 6 percent competitive price advantage.

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<table>
<thead>
<tr>
<th><strong>These companies collect Michigan tax.</strong></th>
<th><strong>These companies do not collect Michigan tax.</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>If you order from these companies your responsibility is met.</td>
<td>If you order from these companies you need to file and pay tax.</td>
</tr>
<tr>
<td>Amway Corporation</td>
<td>Save your receipts!</td>
</tr>
<tr>
<td>Borders Online, Inc.</td>
<td>Amazon.com, Inc.</td>
</tr>
<tr>
<td>Gateway Companies, Inc.</td>
<td>Coldwater Creek Inc.</td>
</tr>
<tr>
<td>Crate and Barrel</td>
<td>DAMARK International, Inc.</td>
</tr>
<tr>
<td>Eddie Bauer, Inc.</td>
<td>Dell Catalog Sales, L.P.</td>
</tr>
<tr>
<td>Herman Miller, Inc.</td>
<td>Fingerhut Companies, Inc.</td>
</tr>
<tr>
<td>JC Penney Company, Inc.</td>
<td>L.L. Bean, Inc.</td>
</tr>
<tr>
<td>K Mart Corporation</td>
<td>Lands’ End, Inc.</td>
</tr>
<tr>
<td>QVC Network Inc.</td>
<td>Spiegel Catalog, Inc.</td>
</tr>
<tr>
<td>Talbots, Inc.</td>
<td>The Orvis Company, Inc.</td>
</tr>
<tr>
<td>Wal-Mart Stores, Inc.</td>
<td>...and many more</td>
</tr>
<tr>
<td>Walt Disney Catalog Inc.</td>
<td>If you are unsure of the amount of purchases on which you owe the use tax, contact the company from which you made the purchase.</td>
</tr>
<tr>
<td>Williams-Sonoma, Inc.</td>
<td>...and many more</td>
</tr>
<tr>
<td>...and many more</td>
<td></td>
</tr>
</tbody>
</table>

The above lists are intended as helpful guidelines and are not all inclusive. They are examples of companies that collect the tax for you and companies that leave the burden of compliance with you.

For more information on the Use (Remote Sales) or visit our web site at: [www.michigan.gov/treasury](http://www.michigan.gov/treasury).

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