

2015

Taxing Honesty

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TAXING HONESTY

*Adam B. Thimmesch**

	ABSTRACT	148
I.	INTRODUCTION.....	148
II.	THE USE-TAX SYSTEM.....	151
	A. <i>The Emergence of the Use-Tax Gap</i>	151
	B. <i>A Deeper Look at the Use Tax</i>	155
	C. <i>Existing Efforts to Close the Use-Tax Gap at the State Level</i>	157
III.	THE CASE FOR USE-TAX ENFORCEMENT.....	160
	A. <i>Why Enforce Use Taxes at All?</i>	161
	B. <i>The Economic Imperative for a Consumer-Centric Approach</i>	162
	C. <i>The Moral Case for a Consumer-Centric Approach</i>	167
	1. <i>The Morality of Nonenforcement</i>	167
	2. <i>The Moral Implications of the Difficulty of Use-Tax Compliance</i>	173
	D. <i>The Psychological Case for a Consumer-Centric Approach</i>	176
	E. <i>Other Benefits from Adopting a Consumer-Centric Approach</i>	180
IV.	THE CASE FOR NONENFORCEMENT.....	182
	A. <i>The Economic Costs of Enforcement</i>	183
	B. <i>The Politics of Enforcement</i>	184
	C. <i>The Economics of Nonenforcement</i>	186
V.	SALVAGING THE VALIDITY OF THE USE TAX	189
	A. <i>Enforcement Action</i>	189
	B. <i>Substantive Reform to the Use Tax</i>	190
	1. <i>Necessary Use-Tax Exemptions</i>	190
	2. <i>Limitations on Use-Tax Exemptions</i>	192
	3. <i>Tax Tables</i>	193
	4. <i>Other Options</i>	194
	C. <i>Decriminalizing Use-Tax Noncompliance</i>	195
VI.	CONCLUSION	195

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ABSTRACT

It is commonly accepted that state use taxes, most notably those that are due on Internet purchases, are largely unenforceable against individual consumers. Consistent with that view, states have focused their enforcement efforts on forcing retailers to collect those taxes at the point of sale, and taxpayers have maintained nearly complete indifference toward remitting the tax of their own accord. This combination of factors has transformed the state use tax into a de facto tax on honesty—a tax with which only our most principled, risk-averse, or perhaps foolish even attempt to comply. The current structure of these taxes is further troubling because compliance is a practical impossibility. Unfortunately, however, academic attention to the state use tax has focused almost exclusively on whether and under what conditions states should be allowed to compel vendors to collect that tax. This Article takes a different approach and evaluates the current structure and enforcement of state use taxes from economic, moral, and psychological perspectives. That analysis establishes that states' current vendor-centric approaches are problematic and that states must instead adopt consumer-centric approaches that focus on the design of the tax and on its enforcement against individual taxpayers. The Article concludes by addressing potential arguments against that approach and by outlining the precise changes that are required to salvage the validity of the use tax.

*“Don't tax you, Don't tax me, Tax that fellow behind the tree.”*¹

I. INTRODUCTION

Senator Long's quip reflects an attitude that seems all too common in the United States. Many appear comfortable with the notion that government should not tax them or their current confidant, but that it should tax someone else, perhaps anyone else. Shifting the tax burden onto “them” often seems to be the right, or politically expedient, course of action. What happens, though, when “they” are our most honest citizens? Like George Washington in the fable of the cherry tree, these people simply cannot tell a lie.

An explicit tax on honesty, on our “Washingtons,” would be clearly problematic, but many taxes currently operate in that manner. The demands of those taxes coupled with limited tax-enforcement budgets mean that many tax laws are not only unenforced, but may also be nearly unenforceable. The result is that only the honest comply. One particular tax of this kind has recently been the subject of intense debate, including before Congress and the U.S. Supreme

¹ William B. Mead, *Congress Tackles the Income Tax*, MONEY, July 1973, at 55 (quoting Senator Russell B. Long).

Court—the state use tax.² That tax is a relatively unknown or misunderstood tax that applies when a consumer makes a purchase of a taxable good or service, but does not pay the vendor an amount of tax that is equivalent to her local sales tax.³ A common situation where that occurs is when a consumer makes a purchase over the Internet from a vendor that does not collect sales tax. Consumers are technically required to self-remit use tax in that situation, but few actually do.⁴ Only our most honest, or perhaps foolish, comply.⁵

Use tax non-compliance has a significant economic consequence, with some estimating states' aggregate revenue losses to be over \$20 billion each year.⁶ To put this in perspective, that loss is roughly equivalent to the estimates

² See Marketplace Fairness Act of 2015, S. 698, 114th Cong. (2015); Marketplace Fairness Act of 2013, S. 743, 113th Cong. (2013); Transcript of Oral Argument, *Direct Mktg. Ass'n v. Brohl*, 135 S. Ct. 1124 (2015) (No. 13-1032), http://www.supremecourt.gov/oral_arguments/argument_transcripts/13-1032_3d94.pdf.

³ This formulation is for when use tax is due (i.e., when there is a purchase “for use in the state” is imprecise, but serves to illustrate when use taxes may apply). See *infra* Part II.B (discussing the different state use-tax formulations).

⁴ See Scott W. Gaylord & Andrew J. Haile, *Constitutional Threats in the E-Commerce Jungle: First Amendment and Dormant Commerce Clause Limits on Amazon Laws and Use Tax Reporting Statutes*, 89 N.C. L. REV. 2011, 2025 (2011) (noting that “use tax compliance has been extremely low historically”); Nina Manzi, *Use Tax Collection on Income Tax Returns in Other States*, HOUSE RES. DEP’T 10 (April 2015), <http://www.house.leg.state.mn.us/hrd/pubs/usetax.pdf> (noting that the percentage of taxpayers who report use tax in states where that tax can be reported on income-tax returns is approximately 1.9%).

⁵ Construing the use tax as a tax on honesty may seem a bit dramatic, but it is not a new characterization. See Walter Hellerstein & Jon Sedon, *State Taxation of Cloud Computing: A Framework for Analysis*, 117 J. TAX’N 11, 23 (2012) (referring to the use tax as a tax on honesty). Thanks to Eric Johnson for bringing this particular characterization to my attention.

⁶ See DONALD BRUCE ET AL., STATE AND LOCAL GOVERNMENT SALES TAX REVENUE LOSSES FROM ELECTRONIC COMMERCE (2009), <http://cber.utk.edu/ecom/ecom0409.pdf>. This number is not without debate. See, e.g., Noah Aldonas, *DOR Disputes E-Commerce Sales Tax Loss Estimates*, 65 ST. TAX NOTES 576 (2012) [hereinafter Aldonas] (noting statements by Nebraska’s then Tax Commissioner that the Bruce and Fox estimates of lost use-tax revenue from e-commerce sales was significantly overstated); Joseph Henchman, *Internet Sales Tax Collections Falling Far Short of Experts’ Estimates*, TAX FOUND. (Mar. 18, 2013), <http://taxfoundation.org/blog/internet-sales-tax-collections-falling-far-short-experts-estimates> (noting that the \$11 billion estimate related to e-commerce is “far off” and “probably overstated by four- or five-fold”); Laura Mahoney et al., *States See Little Revenue from Online Sales Tax Laws, Keep Pressure on Congress*, BLOOMBERG BNA (Jan. 8, 2014), <http://www.bna.com/states-little-revenue-n17179881226/> (noting that other studies have estimated the annual losses at \$3.9 billion and \$3.55 billion per year). These critiques often rely on recent experiences in states where vendors have started to collect use taxes shows that scholars’ estimates are overstated. It is thus fair to question the exact magnitude of the uncollected use tax, but it is too early to tell whether current estimates are incorrect. It may be that revenue collections are less than expected because vendor-centric approaches fail to take into account consumers’ behavioral responses to those taxes. See *infra* Part III.B (discussing the reasons why vendor-centric approaches will fail to completely close the use-tax gap); see also Billy Hamilton, *Fox and Friends: The Rest of the Story on E-Commerce Tax Loss Estimates*, 68 ST. TAX NOTES 535 (2013) (discussing the reasons that state collections may not match estimates).

of the *ten-year* federal revenue losses from corporate inversions—an issue that has received significant attention in the last year.⁷ Given their losses, states have been keenly interested in taking action to ensure that use taxes are paid. Remarkably, however, they have directed little of their energy towards collecting that tax from the individual consumers who owe it. States have instead focused their energy on getting retailers to collect the required use taxes at the point of sale.⁸ One vehicle for those efforts has been federal legislation like the Marketplace Fairness Act, which would grant states the authority to reach across state lines and require remote vendors (typically Internet vendors) to collect and remit their taxes. That legislation would represent an expansion of state authority and is garnering more support from politicians on both sides of the aisle.

States' focus on vendors is sensible from an economic standpoint. Individual consumers' liabilities are generally very small. For example, a consumer in a state with an 8% sales-tax rate who makes \$2000 of Internet purchases would owe a maximum of \$160 of use tax.⁹ That amount, while something, is not enough to support enforcement action, especially given the fact-intensive nature of the liability and the potential difficulty of sifting through a year's worth of credit card and bank statements to establish that liability. Not surprisingly, then, use-tax enforcement and voluntary compliance are virtually non-existent. Only our Washingtons pay the tax.

Most analyses of the state use tax accept this situation and evaluate only whether and under what conditions vendors should be required to assist states in their collection efforts. This Article is the first to challenge that “vendor-centric” approach and the general apathy regarding consumer compliance. Use-tax nonenforcement at the consumer level creates significant problems that states' current approaches will not alleviate.¹⁰ This Article identifies and addresses those issues by undertaking a comprehensive review of the state use tax, specifically addressing the economic, moral, and

⁷ See DONALD J. MARPLES & JANE G. GRAVELLE, CONG. RESEARCH SERV., R43568, CORPORATE EXPATRIATION, INVERSIONS, AND MERGERS: TAX ISSUES 12 (2014), <http://digital.library.unt.edu/ark:/67531/metadc462056/>. See generally *id.* (for a robust discussion of corporate inversions).

⁸ This may lead some observers to believe that the sales tax is a tax on retailers. Although this might be the case with regard to the legal incidence of the tax in some states, all state sales taxes are designed to be borne by consumers. See JEROME R. HELLERSTEIN & WALTER HELLERSTEIN, STATE TAXATION ¶ 12.01 (3d ed. 2000) (introducing the different types of taxes commonly classified as “sales taxes”).

⁹ This presumes that all of the taxpayer's purchases are subject to the state sales tax and that the merchants collected none of the tax at the point of sale. As these assumptions relax, the consumer's tax liability would only be reduced.

¹⁰ States, of course, do enforce use taxes in particular situations. See *infra* Part II.C. References to use-tax nonenforcement herein refer to the lack of meaningful efforts towards use-tax enforcement at the consumer level, in the aggregate. It does not mean that states do not enforce use taxes in any way.

psychological impacts of the current structure and nonenforcement of that tax. That analysis shows that states' current use-tax structures and vendor-centric approaches will fail to close the current use-tax "gap,"¹¹ infringe upon basic principles of morality and the Rule of Law, and ignore the negative psychological effects of an unenforced tax. The Article thus establishes that states must adopt a "consumer-centric model" of use-tax compliance that focuses on *consumer* compliance. That approach is admittedly at odds with those being considered today, but must be taken to salvage the validity of the use tax.

The Article proceeds as follows. Part II introduces the current use-tax landscape and the basic structure of those taxes across the country. Part III then evaluates the current economic, moral, and psychological shortcomings of states' vendor-centric approaches. It thus builds the case for the consumer-centric model noted above. Part IV introduces and evaluates several potential arguments against this approach. Part V then proposes the actions that are necessary to salvage the validity of the state use tax and to mitigate its impact on the public's perception of the legitimacy of state revenue authorities—and perhaps government more broadly. The impacts of that discussion thus go far beyond the issue of use taxes. To the extent that state revenue authorities act in ways that are perceived to be immoral or illegitimate, respect and trust in government will wane. The situation presented by the current nonenforcement of use taxes thus has much broader implications than whether we can shop online without paying tax. Part VI concludes.

II. THE USE-TAX SYSTEM

A. *The Emergence of the Use-Tax Gap*

States have imposed sales taxes since the 1930s.¹² Those taxes are imposed on consumers who purchase taxable property or services¹³ and are generally collected by merchants at the point of sale. Using merchants to collect the tax, however, means that purchasers can avoid sales tax by purchasing goods from a merchant that does not collect that tax—perhaps a

¹¹ The term "tax gap" is used widely, but has many different technical definitions. For purposes of this Article, it is sufficient to note that the tax gap generally is the difference between the amount of tax owed under the substantive law and the amount that is voluntarily paid by taxpayers. We can further refine this to mean only the amounts paid timely or we can include amounts paid after the taxing authorities pursue enforcement action. *See, e.g.,* Nina E. Olson, *Minding the Gap: A Ten-Step Program for Better Tax Compliance*, 20 STAN. L. & POL'Y REV. 7, 8 n.3 (2009) (providing definitions for the "gross tax gap" and the "net tax gap"). Because state taxing authorities generally do not pursue enforcement action with respect to use taxes, the difference between the gross and net use-tax gaps is not significant for purposes of this Article.

¹² *See* HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 12.02.

¹³ Sales and use taxes apply to both goods and certain services. For purposes of simplicity, however, the remainder of this Article will refer only to transactions involving goods.

vendor in a neighboring state. Every state with a sales tax consequently also has a compensating use tax that is owed when a purchaser *uses* property in the state but did not pay sales tax at the point of sale.¹⁴ Consumers are obligated to voluntarily remit the required use tax directly to the state.

Of course, states have always understood that relying on consumers to voluntarily remit use taxes would be less effective than simply requiring out-of-state vendors to collect that tax on their behalf, and states thus experimented with statutes requiring remote vendors to do just that. Those vendors were understandably resistant to those obligations and challenged them as violating the U.S. Constitution. The Supreme Court ultimately responded in favor of remote vendors by determining that states could only exercise their taxing power over vendors that had a physical presence within their boundaries.¹⁵ The Court thus prohibited states from reaching vendors who did business with their residents only from afar.

The Court last directly addressed this issue in 1992 in *Quill Corp. v. North Dakota*.¹⁶ In that case, the Court granted certiorari to review a decision by the North Dakota Supreme Court in which that state court held that vendors who merely economically exploited the state's market could be fairly called upon to collect and remit its tax.¹⁷ The lower court reasoned that the physical-presence rule had become an anachronism because of the changing nature of the interstate marketplace and the technological advances of the day.¹⁸ The Supreme Court disagreed and upheld the physical-presence rule as a Dormant Commerce Clause limitation on state taxing power, specifically noting that Congress was better equipped to deal with the issue.¹⁹

Regardless of whether the Court's reasoning was sound in 1992 or still holds true today,²⁰ it is clear that the physical-presence rule has taken more

¹⁴ The use tax also applies in other situations, which are described more fully below. *See infra* Part II.B (providing an in-depth look at additional situations in which the use tax applies).

¹⁵ *Nat'l Bellas Hess, Inc. v. Dep't of Revenue*, 386 U.S. 753, 758 (1967) ("But the Court has never held that a State may impose the duty of use-tax collection and payment upon a seller whose only connection with customers in the State is by common carrier or the United States mail.").

¹⁶ 504 U.S. 298 (1992). Justice Kennedy recently addressed the physical-presence rule in his concurring opinion in a case addressing a state use-tax reporting statute. *Direct Mktg. Ass'n v. Brohl*, 135 S. Ct. 1124 (2015). In his opinion, Justice Kennedy called that rule "a serious, continuing injustice" that was "now inflicting extreme harm and unfairness on the States." *Id.* at 1134 (Kennedy, J., concurring). He invited a case to review the validity of that rule, but his comments were simply *obiter dictum*. *Id.* at 1135. The Court has thus not taken an official position on the physical-presence rule since *Quill* in 1992.

¹⁷ *Quill Corp.*, 504 U.S. at 298.

¹⁸ *Id.* at 303–04.

¹⁹ *Id.* at 318.

²⁰ Academic critique of the physical-presence rule as a normative matter has been extensive. *See* Adam B. Thimmesh, *The Tax Hangover: Trailing Nexus*, 33 VA. TAX REV. 497, 510 n.56

prominence with the emergence of Internet commerce.²¹ Many online vendors do not have physical presences in the states where their customers are located, and they are thus freed from the burden of collecting taxes in those states. Compliance falls to consumers.

Consumer compliance with the use tax is generally accepted as very low, but there is a lack of formal data on use-tax compliance across the United States. Fortunately, a study recently performed by the Research Department of the Minnesota House of Representatives does provide some significant insight. That study reports data obtained for the tax year 2012 from 27 states that collect use tax on their income-tax returns.²² In that year, less than 2% of returns reported any use tax due in 18 of those states.²³ The participation was above 5% in only 2 states—Maine and Vermont.²⁴ The average reporting rate in the sampled states was approximately 1.9%.²⁵ Nine states in the study also provided taxpayers with lookup tables to estimate their tax liabilities, and the participation rate in those states was 2.8% versus a participation rate of 1.12% in states without such tables.²⁶ Interestingly, however, the average *amount* of tax reported was lower in states with lookup tables.²⁷

(2014); *see also* Direct Mktg. Ass’n, 135 S. Ct. at 1127–29 (Kennedy, J., concurring) (rejecting the normative basis for the physical-presence rule).

²¹ Overall “e-commerce” in the United States exceeded \$80 billion in the first quarter of 2015 and represented 7% of total retail commerce in the United States. *Quarterly Retail E-Commerce Sales*, U.S. CENSUS BUREAU (Aug. 17, 2015, 10:00 AM), http://www.census.gov/retail/mrts/www/data/pdf/ec_current.pdf.

²² Manzi, *supra* note 4, at 7.

²³ *Id.* at 7 tbl.1.

²⁴ Maine’s participation rate of 10.2% was significantly higher than the overall rates reported, but researchers noted that the state had undergone a compliance campaign in 2006 and had an earlier practice of assessing liabilities for taxpayers who left the use-tax line on their tax returns blank. *Id.* at 7–8.

²⁵ *Id.* at 13. The average amount of tax reported ranged from \$39 in Pennsylvania to \$876 in Connecticut. *Id.* at 7 tbl.1. Connecticut is a clear outlier. The next highest average amount reported is \$154 in California. *Id.*

²⁶ *Id.* at 7. State lookup tables allow taxpayers to consult with a table published by the state to provide them with an estimated amount of use tax owed based upon their income levels. Taxpayers are not necessarily shielded from liability, however, if they rely on those tables. *See* KAN. DEP’T OF REV., KANSAS 2014 INDIVIDUAL INCOME TAX 8 (2014), <http://www.ksrevenue.org/pdf/ip14.pdf> (noting that “[e]stimated amounts from [the lookup table] do not supersede actual amount of use tax owed”); MICH. DEP’T OF TREASURY, 2014 MICHIGAN MI-1040 INDIVIDUAL INCOME TAX FORM AND INSTRUCTIONS 7 (2014), http://www.michigan.gov/documents/taxes/MI-1040_book_Instructions_477624_7.pdf (“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.”); N.J. DIV. OF TAX’N, NEW JERSEY RESIDENT RETURN NJ-1040 36 (2014), <http://www.state.nj.us/treasury/taxation/pdf/current/1040i.pdf> (“Using the Estimated Use Tax Chart when calculating the amount of use tax to report . . . does not preclude the Division of Taxation from auditing your account.”).

²⁷ *See* Manzi, *supra* note 4, at 11.

These data show that compliance rates are indeed small. The numbers reported in the study represent data from states where the tax issue is directly presented to taxpayers on their income-tax returns. Presumably, compliance is even lower in states where taxpayers must take the affirmative step of seeking out an unfamiliar use-tax return to report and pay their tax. We could thus presume a participation rate of effectively zero in the remaining states.

This low level of compliance is costly. The sales-tax revenue lost due to e-commerce alone is estimated to be approximately \$12 billion annually.²⁸ Adding in the lost revenue from catalogue sales takes this number to nearly \$20 billion annually.²⁹ States have thus hoped for a reversal of the physical-presence rule from either the Court or Congress.

To date, the Court has shown little interest in reviewing the physical-presence rule,³⁰ but Congress is currently considering legislation that would allow states to require Internet vendors of a certain size to collect and remit their taxes. The Senate actually passed such legislation, the Marketplace Fairness Act,³¹ in early 2013, but the House failed to take action on the bill.³² In 2014, commentators were more optimistic that the House would revise the bill to appeal to more conservatives, but it took no action beyond holding a hearing by the House Judiciary Committee.³³ In early 2015, a new version of the Marketplace Fairness Act (the “Act”) was introduced.³⁴ That version is fundamentally the same as the 2013 version, but has a delayed effective date.³⁵ Neither house of Congress has passed that bill.

²⁸ BRUCE ET AL., *supra* note 6, at ii. The study gave two estimates—one based on a “baseline” growth estimate and one based on an “optimistic” growth estimate. *Id.* The estimated losses were \$11.4 billion and \$12.65 billion, respectively. The magnitude of these estimated revenue losses is not without debate. *See, e.g.*, Aldonas, *supra* note 6, at 576; Henschman, *supra* note 6; Mahoney et al., *supra* note 6. These critiques often rely on recent experiences in states where vendors have started to collect use taxes but the resulting revenue gains have been lower than scholars’ estimates. It is thus fair to question the exact magnitude of the uncollected use tax, but it is too early to tell whether current estimates are incorrect. *See* Hamilton, *supra* note 6.

²⁹ BRUCE ET AL., *supra* note 6, at ii–iii.

³⁰ *But see* note 16 (discussing recent comments by Justice Kennedy on this matter).

³¹ S. 743, 113th Cong. (2013); H.R. 684, 113th Cong. (2013).

³² Press Release, U.S. House of Representatives Judiciary Comm., House Judiciary Committee to Hold Hearing on the Internet Sales Tax Issue (Mar. 10, 2014), <http://judiciary.house.gov/index.cfm/2014/3/house-judiciary-committee-to-hold-hearing-on-the-internet-sales-tax-issue>; H.R. 684 (showing that the House version of the Marketplace Fairness Act was referred to committee on February 14, 2013, and has not emerged).

³³ *Id.*

³⁴ S. 698, 114th Cong. (2015).

³⁵ *Id.* § 3(h). A similar bill was introduced in June of 2015: the Remote Transactions Parity Act of 2015 (the “RTPA”). *See* H.R. 2775, 114th Cong. (2015). The RTPA operates like the Act, but is different in how the small-seller exception operates, how audits are conducted, and how certain terms are defined. Billy Hamilton, *Why Does Chaffetz Hate the Internet So Much?*, 77 ST. TAX NOTES 43, 45 (2015); Stephen P. Kranz, Mark Yopp & Eric Carstens, *Remote Transactions Parity Act Introduced in the U.S. House*, INSIDE SALT (June 15, 2015),

A full discussion of the Act is beyond the scope of this Article, but a couple of key points should be discussed. First, the Act would not give states blanket authority to require remote vendors to collect their taxes. It would only give that authority to states whose laws conformed to a number of simplifying provisions.³⁶ States that were unwilling or unable to do so would not gain any power. Second, the Act contains a “small seller” exception that would significantly limit its grant of authority.³⁷ That exception protects vendors who make no more than \$1 million in remote sales in a year.³⁸ Both of those aspects of the Act would limit its effectiveness in closing the use-tax gap, and are discussed in further detail below.³⁹

B. A Deeper Look at the Use Tax

Internet purchases currently represent the paradigmatic example of when use taxes are due, but they do not tell the whole story.⁴⁰ One additional situation in which they apply is when a consumer physically travels across state lines and purchases a good at low or no tax. Take, for example, a resident of Massachusetts who travels to New Hampshire to purchase some item for use back home. That person would avoid tax at the point of sale because New Hampshire does not impose a sales tax and because the sale occurred in that

<http://www.insidesalt.com/2015/06/remote-transactions-parity-act-introduced-in-the-u-s-house/>. Those differences are largely irrelevant for purposes of this Article, and this Article will thus focus its discussion on the Act rather than comparing the two. *But see infra* note 79 (discussing the impact of the difference between the two bills’ small-seller exceptions). This Article will also not discuss a draft bill introduced by House Judiciary Committee Chair Bob Goodlatte: The Online Sales Simplification Act. *See* Hamilton, *supra*, at 44. That draft relies on an origin-sourcing concept that is heavily critiqued by those in the tax community. *See* John A. Swain, *Reconciling the Marketplace Fairness Act and Origin Sourcing*, 75 ST. TAX NOTES 809 (2015); Maria Koklanaris, *NCSL Blasts Goodlatte for Hybrid Origin-Sourcing Proposal*, 75 ST. TAX NOTES 251 (2015).

³⁶ S. 698, § 2.

³⁷ *Id.* § 2(c).

³⁸ *Id.*

³⁹ *See infra* Part III.B.

⁴⁰ State enforcement of use taxes is generally limited to consumers with very high value purchases like airplanes, motor vehicles, or artwork. *See* Paul Merrion, *Illinois Sales Tax Collectors Crack Down on Out-of-State Boat Purchasers*, CRAIN’S CHI. BUS. (Dec. 4, 2010), <http://www.chicagobusiness.com/article/20101204/ISSUE01/312049980/illinois-sales-tax-collectors-crack-down-on-out-of-state-boat-purchasers> (noting that Illinois was enforcing use tax against “owners of boats, airplanes, expensive vehicles and other big-ticket items”); Paul Walsh, *Minnesota Says It’s After Owners of RVs Who’ve Dodged Sales Tax*, STARTRIBUNE (Nov. 17, 2011), <http://www.highbeam.com/doc/1G1-272675835.html> (discussing state enforcement of use taxes on purchases of recreational vehicles); Jenifer Warren, *Art—and Tax Bills—Are in the Eye of Beholder*, L.A. TIMES (May 14, 1995), http://articles.latimes.com/1995-05-14/news/mn-574_1_ted-field (noting that “[i]n reality, authorities only go after big-ticket items, such as planes, vehicles, boats and art. The effort to track down sweater buyers would cost the state more than the payoff in taxes, officials say”).

state.⁴¹ Technically, however, the Massachusetts use tax would apply when the consumer used the item back home.⁴²

The situation just noted is similar to that presented by many Internet purchases because the vendor collected no tax at the point of sale. We can create a more complex example, however, by assuming a situation in which the vendor did collect *some* amount of local sales tax, but at a rate less than the purchaser's local rate. Imagine, for example, a resident of Fort Worth, Texas, who travelled to the 2015 College World Series in Omaha, Nebraska, and purchased a souvenir Texas Christian University Horned Frogs baseball cap for his child at home. That person would pay sales tax on the purchase at a rate of 7% (the local rate in Omaha).⁴³ His local sales tax rate in Fort Worth, however, is 8.25%.⁴⁴ Technically, then, he would owe an additional 1.25% to his home jurisdiction to make up this difference. For a \$20 hat, that would represent an additional liability of \$0.25. This result stems from the technical way that use taxes apply, which is that the use tax is always owed on the use of taxable items in the state. Taxpayers receive a credit, however, for any sales taxes paid on the purchase of the product.⁴⁵ Under Texas law, then, the purchaser would owe tax at a rate of 8.25% but receive a credit for the 7% tax that he paid.⁴⁶ As a consequence, he would be legally required to remit his final 1.25%, or \$0.25, to the state.

The applicability of the use tax in this situation raises significant difficulties for the administration and enforcement of the tax. Consumers may make a multitude of those types of purchases throughout the year with little record keeping. The individual liabilities may also be very small, like for our loyal Horned Frogs fan. A taxpayer wanting to comply with the use tax may thus find it nearly impossible to comply unless she keeps a use-tax journal on her at all times.

As implausible as compliance sounds under the facts just discussed, consumer compliance may actually be more difficult in other situations. It is possible, for example, for use taxes to be owed when an individual uses her possessions in a new state after moving her residence across state lines. The application of use tax in that situation depends on the wording of the state's

⁴¹ *Frequently Asked Questions—General*, N.H. DEP'T OF REVENUE ADMIN., <http://www.revenue.nh.gov/faq/general-information.htm> (last visited Oct. 8, 2015) (noting that New Hampshire does not have a sales tax).

⁴² MASS. GEN. LAWS ch. 64I, §§ 2, 7(c) (2015).

⁴³ *Current Local Sales and Use Tax Rates*, N.H. DEP'T OF REVENUE, <http://www.revenue.nebraska.gov/question/sales.html#o> (last visited Oct. 8, 2015).

⁴⁴ *Local Sales and Use Tax*, TEX. COMPTROLLER OF PUB. ACCT., <http://www.window.state.tx.us/taxinfo/local/city.html> (last visited Oct. 8, 2015).

⁴⁵ HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 16.01[2]; *see, e.g.*, MASS. GEN. LAWS ch. 64I, § 7(c) (providing an exemption from use tax for sales tax that "was legally due without any right to a refund or credit thereof"); TEX. TAX CODE ANN. § 151.303(c) (West 2015).

⁴⁶ TEX. TAX CODE ANN. § 151.303(c).

use-tax statute. Some statutes apply only when items are purchased specifically “for use” in the taxing state.⁴⁷ A number of other states, however, have statutes that are not as lenient. In those states, the use tax applies both to goods that are purchased “for use” in the state and also to goods that simply are so used.⁴⁸ In those states, bringing your household items with you on a move can prove costly—theoretically.⁴⁹ Some states with that type of statute provide relief by reducing the tax owed based on the value of the property at the time it is moved into the state, rather than its original purchase price,⁵⁰ but the tax is still technically owed.

As this discussion establishes, use taxes are an issue with respect to Internet commerce but apply much more broadly. The tax is structured as a complete complement to the state sales tax and creates significant burdens as such. Compliance with the use tax under these situations can be incredibly complex, even for consumers who dutifully track their activities. The combination of these difficulties and consumers’ low levels of knowledge of the tax means that use-tax compliance is virtually nonexistent.

C. Existing Efforts to Close the Use-Tax Gap at the State Level

Despite the high levels of noncompliance discussed above, states largely fail to enforce their use taxes against individual consumers.⁵¹ That

⁴⁷ HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 16.03[1] (“Roughly half of the states confine their use taxes to tangible personal property purchases for use within the state.”). Those types of statutes are often coupled with presumptions that apply in determining whether an item falls within this construct. *Id.* Massachusetts’s law, for example, provides a presumption that an item is purchased for use in the state if it is “shipped or brought into the commonwealth within six months after its purchase.” MASS. GEN. LAWS ch. 64I, § 8(f).

⁴⁸ HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 16.03[3].

⁴⁹ The “theoretically” qualifier is necessary because use taxes are rarely, if ever, enforced in this situation.

⁵⁰ HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 16.03[3]. This may be required both as a matter of constitutional law and to align the tax with the consumption that is actually occurring in the state. *Id.* at n.78. A reduced value for the item means that the taxpayer has “consumed” some of the asset’s value before moving into the new state. That amount of consumption thus occurred outside of that state and it should not be taxable there.

⁵¹ Manzi, *supra* note 4, at 3–4; see Phillip W. Gillet, Jr., *Privacy Issues May Add to the Debate over State Taxation of e-Commerce*, J. MULTISTATE TAX’N, Sept. 2001, at 16 (noting that use-tax enforcement is “a logistical nightmare” and that “states rarely actively enforce their use tax provisions”). There are exceptions worthy of note. For example, use taxes are generally enforced against business taxpayers. This is because businesses often have sales-tax filing obligations with respect to their normal business activities and report use tax as a part of that filing process. A state audit may thus effectively capture that activity. Specifically, a business may owe use tax when it pulls an item out of inventory and uses it for another purpose. HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 16.09. A business may also owe use tax when it utilizes a produced good for a purpose other than sale. *Id.* ¶ 16.07. States also enforce use taxes on titled vehicles and significant asset purchases like recreational vehicles, airplanes, boats, or artwork. See Merrion, *supra* note 40; Walsh, *supra* note 40; Warren, *supra* note 40. Perhaps most

inaction may seem permissible or practically compelled because use taxes seem unenforceable. Each individual consumer owes relatively little in tax, so enforcing the tax through individual audits seems unadvisable from a return-on-investment perspective. This is especially true when enforcement dollars are scarce. States have, however, recently taken two different notable approaches.

First, states have begun to incorporate use-tax payments into their income-tax filing processes instead of using a separate use-tax return. Twenty-seven states currently do so by including a use-tax line item on their individual income-tax returns.⁵² Implementation of this method has taken different forms. Some states provide a line-item on their return and nothing more, some provide tables for taxpayers to find an average amount of tax due, and some require taxpayers to specifically write “zero” in the use-tax line if they are reporting no use-tax liability.⁵³ The State of Michigan has gone one step further, and provides a warning to taxpayers when they access the state’s income-tax return online.⁵⁴ The state’s webpage displays a warning that, if the taxpayer reports “zero” on the use-tax line, she is “certifying that no USE TAX is owed.” The warning then notes that “[i]f it is determined that Use Tax is owed, the taxpayer will be liable for the deficiency as well as interest and may be subject to penalty.”⁵⁵

Despite the ragged nature of these approaches, they have been somewhat successful, in that they have generated *some* revenue.⁵⁶ Compliance

significant among these is the use tax on personal automobiles. If a vendor does not collect sales tax at the dealership, states generally require remittance of the use tax as a condition to registering the vehicle. *See, e.g.*, LA. STAT. ANN. § 47:303 (2015); ME. STAT. tit. 29-A, § 409 (2015); NEV. REV. STAT. § 482.225 (2015). Use-tax enforcement and compliance on vehicles should thus approach 100%. Use tax is also collected anytime that a consumer purchases an item from an out-of-state vendor with an in-state physical presence. Where such a purchase technically occurs out of state, there is no in-state sale on which the sales tax can apply. The vendor, however, is compelled to collect the sales or use tax by virtue of its physical presence in the state. Technically, the tax collected is a use tax because the only taxable event in the state is the customer’s use of the product therein. Most would consider this tax payment a sales tax nonetheless because it is collected at the point of sale.

⁵² Manzi, *supra* note 4, at 2.

⁵³ *Id.* at 5–7; *see supra* note 26 and accompanying text (discussing state lookup tables).

⁵⁴ MICH. DEP’T OF TREASURY, *supra* note 26.

⁵⁵ The pop-up box containing these statements is initiated when the website is accessed. *Id.* This approach is obviously remarkable.

⁵⁶ Manzi, *supra* note 4, at 7 tbl.1. A recent study of use-tax payments in Illinois reported that the number of taxpayers reporting use taxes increased from a mere 8,000 to more than 240,000 after the state included a use-tax line item on the state’s income tax return and provided taxpayers with a use-tax lookup table. Of those reporting use tax, 60% reported the precise amount provided on the look-up tables. *See* JOANNA KOH, DAVID MERRIMAN & HECTOR M. VIELMA, FACTORS INFLUENCING USE TAX PAYMENT IN ILLINOIS 159 (2014), <http://www.irs.gov/pub/irs-soi/13rescontaxpayment.pdf> (noting that states make “almost no effort to audit personal income tax filers’ use tax payments”).

rates in those states, however, are still shockingly low.⁵⁷ The data discussed above show that the percentage of returns reporting use tax in states where there is a line item on the income-tax return ranges from 0.2% to 10.2%.⁵⁸ Those data are skewed by states with reporting percentages significantly above the average. As noted above, average compliance in states without a lookup table is 1.3% and is 2.2% in states with a lookup table.⁵⁹

The other major state effort to collect use taxes from individual taxpayers has been certain states' efforts to implement information-reporting systems with respect to catalogue and online purchases. Those efforts started with Colorado in 2010. In that year, the state adopted a unique statute that imposes three different obligations on retailers who sell to consumers in the state but who do not collect and remit the state's sales or use taxes. The first is a transaction-based notice that vendors are required to provide to Colorado purchasers during the course of their purchase transaction.⁶⁰ That notice informs consumers of the existence of the state use tax and their responsibility for paying that tax.⁶¹ The law also requires vendors to send consumers an annual report that summarizes their annual purchase activity from that vendor.⁶² Finally, the law requires that the vendors mail an annual summary statement to the Colorado Department of Revenue.⁶³ That statement informs the state of taxpayers' total annual purchases from the vendor.⁶⁴

A number of states have adopted similar, but less extensive, reporting laws in the style of the original Colorado law.⁶⁵ Those laws are different because they only require a point-of-sale notification and not annual summaries that must be sent to consumers or to the state. Thus, although they are similar in that they seek to increase the salience of the use tax, they do not take complete advantage of the information-reporting aspects of the Colorado law.

⁵⁷ Manzi, *supra* note 4, at 7 tbl.1.

⁵⁸ *Id.* at 13 tbl.3.

⁵⁹ *Id.* at 10.

⁶⁰ COLO. REV. STAT. § 39-21-112(3.5)(c)(I) (2015).

⁶¹ *Id.*

⁶² *Id.* § 39-21-112(3.5)(d)(I)(A).

⁶³ COLO. REV. STAT. § 39-21-112(3.5)(d)(II)(A).

⁶⁴ *Id.* This information-reporting scheme has been the subject of constitutional challenge since shortly after its enactment and that litigation is currently ongoing. *See* Direct Mktg. Ass'n v. Brohl, 135 S. Ct. 1124 (2015) (holding that a challenge to the Colorado legislation in federal court was not barred by the Tax Injunction Act and remanding the case to the Tenth Circuit for further consideration). The ultimate resolution of the case may involve an affirmation or rejection of the ongoing validity of the physical-presence rule.

⁶⁵ KY. REV. STAT. ANN. § 139.450 (LexisNexis 2015); OKLA. STAT. tit. 68, § 1406.1 (2015); S.C. CODE ANN. § 12-36-2691(E) (2015); S.D. CODIFIED LAWS § 10-63-2 (2015); VT. STAT. ANN. tit. 32, § 9783 (2015).

Beyond these limited activities, states have done very little to systematically encourage knowledge of, or compliance with, their use taxes.⁶⁶ States have undertaken some efforts that were limited in scope and duration, but those programs have failed to have long-standing effect.⁶⁷ That lack of success may cause further indifference towards compliance efforts aimed at individuals. For reasons discussed below, however, that indifference is problematic.

III. THE CASE FOR USE-TAX ENFORCEMENT

The preceding materials introduced the current structure of state use-tax systems, the lack of state enforcement of those taxes, and the difficulties that consumers would face when attempting to comply with those taxes. States' responses to these problems have largely focused on getting vendors to collect that tax at the point of sale, which has many advantages. It centralizes the collection and remittance procedure so that states obtain greater benefits from audit activity, vendors likely have existing systems for handling those duties, and consumers, who are largely unaware of the technical tax rules, are protected from worrying about the tax. This vendor-centric approach is not without consequence though, and the following sections build the case for an approach to use-tax enforcement that focuses specifically on consumers and their obligations—a consumer-centric approach.

At the outset, it is important to understand why the use tax should be enforced at all, and the first section that follows explains why use taxes matter within the context of states' tax systems.⁶⁸ The second section addresses the economic necessity for states to adopt consumer-centric approaches to use-tax compliance. The third then addresses the moral case for use-tax enforcement. The fourth discusses the negative psychological impacts that nonenforcement is likely to have on taxpayers. Finally, the fifth analyzes how a consumer-centric approach would specifically respond to concerns that are currently being voiced regarding states' vendor-centric approaches. Together, these sections establish that states' current approaches are insufficient to address the issues that currently exist with the state use tax and that states must instead adopt a consumer-centric approach to that tax.

⁶⁶ The State of North Carolina has taken the discussed approaches and also unsuccessfully attempted to gather its residents' purchasing information directly from Amazon.com. See Gaylord & Haile, *supra* note 4, at 2025–39 (discussing the state's attempts to collect use tax and its litigation with Amazon.com over consumer information).

⁶⁷ See Adam B. Thimmesch, *Testing the Models of Tax Compliance: The Use-Tax Experiment*, 2015 UTAH L. REV. (forthcoming 2015) (manuscript at 27–30) (on file with author) (discussing other state efforts to generate use-tax compliance).

⁶⁸ This is important both for states and for consumers. States must be concerned with the role that use taxes play in their overall tax system. Individuals, on the other hand, may need to understand why use taxes matter if they are to be compelled to care about voluntary compliance.

A. *Why Enforce Use Taxes at All?*

It is safe to assert that use-tax enforcement is not something that concerns many taxpayers. Increased enforcement is more likely to be met with significant opposition than welcomed. It is thus fair to ask why use-tax enforcement efforts would be worth the hassle for states. The response to this is multifaceted. As an initial matter, the economics suggest that states have an immense interest in enforcing the tax. As noted above, one estimate suggests that the use-tax gap is approximately \$20 billion annually.⁶⁹ The lack of that revenue has necessarily impacted states. They must have compensated for those losses either by raising their sales-tax rates, by relying more heavily on other taxes, by limiting the services that they offer, or by going into debt. States could thus use that revenue to increase spending on matters of public need or to simply restructure their tax systems to lower the forms of tax that are currently above their desired levels.⁷⁰

Use-tax compliance also matters because the use tax plays an integral role in the design of a rational, neutral consumption tax. As discussed above, the use tax functions as a backstop to the sales tax,⁷¹ and their tax bases should therefore be the same. Any mismatch simply creates a tax distortion. Exempting Internet purchases from the use tax, for example, creates a system where the imposition of a state's consumption tax depends on taxpayers' methods of completing an exchange. If a consumer completes a purchase at a physical store, he will pay sales tax. If the consumer purchases the item online, he will not pay any tax. No normative theory of taxation supports this result. It is simply a subsidy to one form of commerce.⁷²

⁶⁹ *But see supra* note 6 (providing citations to sources discussing the accuracy of those estimates).

⁷⁰ Some states have seen laws enacted or introduced that would apply any revenues from the Marketplace Fairness Act to reduce their income taxes. *See infra* notes 179–82. Of course, theoretically, a state could desire none of these things. It could support no additional spending and could feel as though its tax burden is distributed equitably among citizens and tax types based on how consumers currently allocate their consumption between vendors. For those states, then, use-tax enforcement may not have an economic impact. That is not to say, however, that there are not non-economic benefits that would be derived from use-tax enforcement in this unlikely scenario.

⁷¹ *See supra* Part II.A.

⁷² *See infra* Part IV.C (discussing whether use-tax nonenforcement is justifiable as an effort to promote electronic commerce). Of course, the real-world subsidy that stems from use-tax nonenforcement is more nuanced than introduced. In contrast to the example in the text, sales tax *would not* be collected on a purchase made in a physical store if the state in which the store is located does not impose a sales tax. Similarly, use tax *would be* collected on an Internet purchase if the vendor has a taxable nexus with the purchaser's home state. The first refinement means that use-tax nonenforcement provides an additional distortion—one in favor of purchasing in states without sales taxes. The latter means that the distortion in favor of Internet commerce does not extend to *all* Internet commerce.

The likely distributional aspect of use-tax nonenforcement is also important. Consumption taxes are generally accepted as regressive in nature.⁷³ That is, they consume a larger percentage of the income of low-income taxpayers than they do of high-income taxpayers. The very nature of the transactions that lead to use tax likely shifts that burden even further onto our lowest-income citizens. The main types of transactions that lead to use tax (Internet purchases, catalogue purchases, and out-of-state purchases) are generally more available to those of means. Shopping online requires not only available credit or funded debit cards, but also requires a stable address at which to receive packages. These may not be available to our poorest of citizens. With respect to out-of-state purchases, one can only travel out of state to make purchases if one has reliable transportation and income available for such trips.⁷⁴ Those trips also often represent pleasure trips or trips associated with business requirements, and those situations may not present themselves as frequently for our less-affluent citizens. The likely distributional impact of the failure to enforce use taxes thus provides further reason that action is warranted.⁷⁵

There are at least two other important reasons to enforce the use tax—the moral imperative to do so and the negative impacts that nonenforcement will have on tax compliance generally. Those two issues are discussed in detail below with respect to why use taxes should be enforced *specifically against consumers*. A discussion of those rationales here would thus be largely duplicative and is omitted. Those rationales apply broadly, however, to suggest that use-tax enforcement is an important issue without regard to whom states direct the enforcement activity.

B. *The Economic Imperative for a Consumer-Centric Approach*

States prefer vendor-centric approaches to the use tax for logical reasons—vendors are more likely to comply with a tax-collection obligation than consumers are to pay the tax of their own accord, and auditing vendors is much easier than auditing all of their customers. Vendor-centric approaches therefore appear to have the best chance of actually raising revenue with little effort on the part of states, and it is easy to understand why state efforts to close the use-tax gap have recently focused on the Marketplace Fairness Act and similar legislation. Unfortunately for states, however, analysis of the Act shows that it is unlikely to provide the relief that they seek. Even if they were

⁷³ See HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 12.03.

⁷⁴ Of course, this depends on the proximity of a taxpayer to the state's border, but among similarly situated taxpayers, geographically, means still matter.

⁷⁵ Even if a state feels that the overall distribution of its tax burden is equitable, it makes sense to impose that burden as transparently as possible. Obtaining an equitable level of tax distribution through uncontrollable consumer behavior (i.e., shopping online or in remote states) and enforcement mechanisms, is simply too opaque to be favored—even if it is possible.

somehow able to get the Act through Congress, many factors would stand in the way of full, or near full, use-tax collection. These include the impact of the small-seller exception, states that do not conform to the requirements of the Act, the difficulty of enforcement against international sellers, and distorted consumer purchasing decisions.

Most significant among these is likely the small-seller exception discussed above. That exception would insulate retailers from use-tax collection obligations under the Act unless they generate more than \$1 million of annual remote sales.⁷⁶ That exemption is intended to protect smaller vendors from onerous reporting obligations and the potential for costly audits. Unfortunately for states, however, those “small” vendors do a significant amount of commerce. The percentage of online commerce done by such retailers represents just over 40% of the total annual online sales.⁷⁷ The large vendors that make the remaining sales also already collect tax in many states. Experts thus estimate that passage of the Act with a \$1 million small-seller exception would reduce the use-tax gap by *less than 50%*.⁷⁸ On these numbers, even if the Act were passed, a significant amount of revenue would still go uncollected. Further, if congressional negotiation were to drive the small-seller exception upwards, the benefits of the Act would naturally go down.⁷⁹

Another factor reducing the effect of the Act is that it does not grant blanket authority to states. To take advantage of the Act, states must either become a member of the Streamlined Sales and Use Tax Agreement (the “SSUTA”) or their laws must be consistent with certain “simplification requirements” provided by the Act.⁸⁰ Becoming a member of the SSUTA requires adherence to requirements related to the administration of sales and use taxes, the tax base, certain procedural requirements related to changes to their laws, rate harmonization requirements, adherence to defined sourcing rules, uniform definitions for terms, exemption procedures, rules related to

⁷⁶ S. 698, 114th Cong. § 2(c) (2015).

⁷⁷ Donald Bruce & William F. Fox, *An Analysis of Internet Sales Taxation and the Small Seller Exemption*, SBA (Nov. 2013), <http://www.sba.gov/sites/default/files/rs416tot.pdf>.

⁷⁸ *Id.* at 40.

⁷⁹ One major alternative to the Act, the Remote Transactions Parity Act (the “RTPA”), includes a small-seller exception that differs significantly from the one in the Act. First, the dollar threshold in the RTPA refers to *all* taxable sales made by the retailer, rather than to the amount of *remote* sales made by the retailer. Remote Transactions Parity Act of 2015, H.R. 2775, 114th Cong. § 2(c)(1)(A)(i), (B)(i), (C)(i) (2015). Second, the exception protects retailers making sales of \$10 million or less in the first year after its enactment, with that amount falling to \$5 million and \$1 million in the second and third years after its enactment. *Id.* After the third year, no small-seller exception would apply. This construct would obviously reduce the benefits of the RTPA in the first two years (as compared to the Act), would be equal in the third year, but would provide a greater benefit in all subsequent years. Given the current discussions regarding congressional intervention in this area, it seems unlikely that a bill with no small-seller protection will be politically viable.

⁸⁰ S. 698, § 2(a)–(b) (2015).

sales tax holidays, and refund procedures, among others.⁸¹ Currently, 24 states comply with the SSUTA requirements.⁸² Those states are generally less-populated states⁸³ and represent only 31% of the entire U.S. population.⁸⁴

The alternative way to “qualify” under the Act requires states to similarly simplify and harmonize the administration of their taxes, their tax bases, and their sourcing rules.⁸⁵ It also requires that states provide vendors with certain information about their taxes and free software for calculating sales-tax liabilities.⁸⁶ States must further relieve sellers and the software providers from certain liabilities related to sales and use-tax errors.⁸⁷

Regardless of which route is analyzed, states that are not currently SSUTA members or whose systems do not meet the required simplification measures could have significant work to do in order to take advantage of the Act. That may involve political battles with local governments that currently have functionally independent sales-tax systems. States that are unable or unwilling to modify their systems in the ways required under the Act would thus not obtain any additional revenue from the Act.

The Act also fails to address the difficulties inherent in attempting to impose collection obligations on international merchants. Technically, the Act could subject any vendor worldwide to state authority,⁸⁸ and state use taxes generally apply to international purchases.⁸⁹ Enforcing the tax against international vendors, however, obviously involves much more difficult and costly questions for states. Use-tax collection on purchases made from

⁸¹ STREAMLINED SALES AND USE TAX AGREEMENT OF 2002 (2013), http://www.streamlinedsalestax.org/uploads/downloads/Archive/SSUTA/SSUTA_As_Amended_10-30-13.pdf.

⁸² *About Us*, STREAMLINED SALES TAX GOVERNING BOARD, INC., <http://www.streamlinedsalestax.org/index.php?page=About-Us> (last visited Oct. 8, 2015).

⁸³ *Streamlined State Status 01-01-14*, STREAMLINED SALES TAX GOVERNING BOARD, INC., http://www.streamlinedsalestax.org/uploads/images/state%20map%202014_1_1.jpg (last visited Oct. 8, 2015).

⁸⁴ *About Us*, *supra* note 82.

⁸⁵ S. 698, § 2(b)(2)(A)–(C) (2015).

⁸⁶ *Id.* § 2(b)(2)(D).

⁸⁷ *Id.* § 2(E)–(H).

⁸⁸ Foreign sellers in many countries are protected from U.S. taxation by tax treaties that limit U.S. taxation to those sellers with permanent establishments in the country. *See* BORIS I. BITTKER & LAWRENCE LOKKEN, *FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS* ¶¶ 67.1.3, 67.6.9 (3d ed. 2005). Notably, though, those treaties generally do not impact state authority. HELLERSTEIN & HELLERSTEIN, *supra* note 8, ¶ 8.17[1][c] (noting that “the tax treaties into which the United States has entered do not generally cover the taxing activities of subnational governmental units such as States”).

⁸⁹ California is a notable exception and allows an exemption for up to \$800 of taxable goods purchased in a foreign country. *See* Annette Nellen, *California Use Tax Exemption for Foreign Purchases Should Be Repealed*, 72 ST. TAX NOTES 601 (2014) (discussing and advocating for the removal of California’s exemption).

international vendors would thus be more likely to continue to rely on self-reporting by taxpayers.

The ease with which consumers modify their behavior to the addition of use-tax collection on online sales would also amplify the impact of each of the previously discussed revenue-reducing factors. To the extent that consumers can shift their consumption to vendors that fall within the small-seller exception or that are located internationally, state revenue gains from the Act will be reduced. Unfortunately for states, recent research shows that consumers do respond quickly to the collection of tax by online retailers. Recent research on consumers who use eBay, for example, showed that buyers were less likely to purchase goods from a seller that would collect sales tax on the transaction.⁹⁰ Research on consumer response to the collection of sales taxes by Amazon.com also supports those results and shows that consumers quickly change their online shopping behavior by purchasing from vendors that do not collect tax, even those vendors who sell on Amazon's platform.⁹¹

In the Amazon study, researchers looked at purchases on Amazon.com in five states for which that retailer started collecting use taxes between 2012 and 2013.⁹² The researchers found that consumers in those states reduced their shopping on Amazon during that period by 9.5% based on the value of products purchased.⁹³ Consumers reduced their purchases most dramatically with respect to high-value items.⁹⁴ The researchers also looked into whether consumers were substituting away from Amazon by purchasing from local brick-and-mortar stores or by purchasing from other online vendors. They found that consumers in the study did increase their purchases from local retailers, but that the sales of competing online retailers increased much more significantly.⁹⁵ The substitution effects were more significant when looking at purchases over \$300. For those purchases, the researchers found a 6.5% increase in purchases at local stores but a 23.7% increase in purchases from other online retailers.⁹⁶ Perhaps most strikingly, merchants who sold their goods using the Amazon Marketplace saw an increase in those "large sales" by 60.5%.⁹⁷ This last result is striking. Consumers responded to the collection of tax by Amazon, in many cases, not by leaving that website, but by simply purchasing from third-party

⁹⁰ Liran Einav et al., *Sales Taxes and Internet Commerce*, 104 AM. ECON. REV. 1, 24 (2014).

⁹¹ Brian Baugh et al., *The "Amazon Tax": Empirical Evidence from Amazon and Main Street Retailers* (Nat'l Bureau of Econ. Research, Working Paper No. 20052, 2014), <http://www.nber.org/papers/w20052.pdf>.

⁹² *Id.* at 1.

⁹³ *Id.* at 2.

⁹⁴ *Id.* at 2–3.

⁹⁵ *Id.* at 3.

⁹⁶ *Id.*

⁹⁷ *Id.* The Amazon Marketplace allows retailers to sell their products using the Amazon platform by paying the retailer a fee. See *Getting Started with Selling on Amazon*, AMAZON, <http://services.amazon.com/content/sell-on-amazon.htm> (last visited Oct. 8, 2015).

merchants that sell on the website. The way that the Amazon Marketplace is operated, consumers can purchase from such a merchant without even realizing it.⁹⁸ Amazon may handle the merchant's inventory and shipping, and the consumer receives the item in an Amazon.com branded box.⁹⁹ Consumers are thus able to avoid paying tax without any real change to their behavior, and they do so in large numbers. These data indicate that we would see further diversion of sales to smaller vendors if and when the Act were enacted.¹⁰⁰

As noted above, one collateral issue to also consider is how voluntary compliance might suffer *because of* the Act. Use taxes are fundamentally taxes on consumers, not on retailers. One reason that use-tax payments are low may be that consumers simply do not understand that the obligation is theirs. In one 2011 study, nearly two-thirds of respondents did not know or did not believe that they were required to pay use tax on Internet purchases if the tax was not collected by the vendor.¹⁰¹ In another study, over 45% of the respondents reported that they did not pay use tax because either the retailer did not charge the tax or because they were unaware of their liability.¹⁰² In another study, over 65% of Florida participants and over 37% of Illinois participants reported having no knowledge of use taxes.¹⁰³ Although these data do not speak to the reasons for that lack of knowledge, it is plausible that states' vendor-centric approaches and the narrative surrounding "taxing Amazon" may have caused consumers to fail to internalize the obligation as their own—even if they are aware of the tax.¹⁰⁴ If that is the case, the collection of use taxes by vendors under the Act will only exacerbate the problem because states will continue to signal to consumers that vendors will handle their obligations. That, in turn, may make it more difficult for states to convince consumers that they have the responsibility to remit tax on the purchases for which the tax is not collected by the vendor. Similarly, states will have even less reason to enforce use taxes against individual consumers because individuals' liabilities will be even lower.

⁹⁸ Baugh et al., *supra* note 91, at 16.

⁹⁹ *Id.*

¹⁰⁰ A recent online article noted this strategy as one of the "20 Secret Tips Everyone Who Shops on Amazon Needs To Know." Richard Padilla, *20 Secret Tips Everyone Who Shops on Amazon Needs to Know*, BUZZFEED (Jan. 18, 2015, 9:11 AM), <http://www.buzzfeed.com/betonnorthshore/secret-amazon-shopping-tips-that-will-save-you-168v4>.

¹⁰¹ *Two-Thirds of Consumers Are Confused by On-Line Sales-Tax Compliance*, THE CTR. OF SHOPPING (July 28, 2011), <http://www.thecenterofshopping.com/blog/two-thirds-of-consumers-are-confused-by-online-sales-tax-compliance>.

¹⁰² Geoffrey Propher, *Use Tax Awareness and Compliance: A Survey Analysis*, 65 ST. TAX NOTES 257, 258 tbl.1 (2012).

¹⁰³ Christopher Jones & Yuyun Sejati, *Improving Use-Tax Compliance by Decreasing Effort and Increasing Knowledge*, 11 ATA J. OF LEGAL TAX RES. 1, 10 (2013). The authors note that the difference in knowledge levels may be due to the inclusion of a line-item on the Illinois income tax return specifically for use taxes. *Id.* at 9. Florida has no income tax, so it cannot rely on that method.

¹⁰⁴ Thanks to Brian Leopard for this observation.

The sum of this discussion is that states should not be optimistic that the Marketplace Fairness Act, or similar legislation, would significantly close the current use-tax gap. The Act simply does not extend far enough and consumer demand flows to areas where the taxing authority cannot reach. Thus, even if Congress were to pass the Act, states would still have an economic need to take consumer-centric enforcement activity.

C. *The Moral Case for a Consumer-Centric Approach*

The economic case against relying on vendor-centric approaches to use-tax compliance is strong, and states should be reasonably concerned about relying on those approaches for that reason alone. Notwithstanding that pragmatic issue, though, states should also note that the failure to think about individual compliance has resulted in a tax that raises significant moral questions. This moral claim regarding use taxes rests both on their overall design and on their current nonenforcement.

The concept of morality is incredibly broad and implicates a significant amount of work by legal scholars and philosophers. It is thus important to note at the outset that this Article does not address the morality of the *substance* of the use-tax laws,¹⁰⁵ but addresses morality from a procedural perspective. That is, are governments legitimately exercising their power in adopting and administering the tax? The use tax raises moral concerns under that formulation for two primary reasons: (1) because states continue to urge taxpayers to pay the tax, but they do not take enforcement action against those who fail to comply;¹⁰⁶ and (2) because compliance with the tax is virtually impossible. Those aspects of the tax are discussed below.

1. The Morality of Nonenforcement

Incongruity between the law as written and as applied by the government has long been recognized as raising moral questions.¹⁰⁷ A

¹⁰⁵ One could, for example, raise a moral argument regarding the regressive nature of consumption taxes in general, or about specific aspects of those taxes that make them more regressive (e.g., the inclusion of clothing or food in the tax base).

¹⁰⁶ This is not to say that there is *no* use-tax enforcement, but that enforcement is generally reserved for individuals who make very large purchases without paying use tax. See *McIntyre v. Farr*, No. 09-2145-III (Tenn. Ch. Ct. Jan. 26, 2012) (imposition of use tax on an airplane); *Simon v. Director, Div. of Tax'n*, 24 N.J. T.C. 509 (2009) (addressing application of use tax to the purchase of a sailboat); Suzanne Beaudelaire, *California Art Collectors Be Warned!*, 31 ST. TAX NOTES 1098 (2004) (discussing enforcement action against those with purchases of significant artwork); Mike Maciag, *Use Tax Revenues: How Much Are States Not Collecting?*, GOVERNING (May 1, 2012), <http://www.governing.com/blogs/by-the-numbers/state-use-tax-collection-revenues.html> (noting that “[s]tates rarely pursue those who skirt use tax obligations” and that “[t]argeting use tax cheats is largely impractical”).

¹⁰⁷ LON L. FULLER, *THE MORALITY OF LAW* 39, 81–91 (Yale Univ. Press 2d ed. 1969); JOHN RAWLS, *A THEORY OF JUSTICE* 210 (President & Fellows of Harvard Coll. 1999) (1971)

government that lays out one set of rules, but that enforces another, raises significant questions regarding the legitimacy of its authority.¹⁰⁸ Complete congruity is not essential for these purposes. Resource constraints often prevent agencies from perfectly enforcing the laws as written. This particular issue was prominent in the public, press, and legal community in 2014 as President Obama took administrative action with respect to our nation's immigration laws.¹⁰⁹ That administrative action took the form of executive actions that, in part, expanded programs that deferred removal actions, allowed work authorization for certain individuals, and expanded the use of waivers for unlawful presences.¹¹⁰ The administration noted in the implementation of those actions that they were being made out of administrative necessity due to limited resources and pursuant to the executive branch's prosecutorial discretion.¹¹¹

(discussing the need for governments to take “a conscientious effort . . . to determine whether an infraction has taken place and to impose the correct penalty”); JOSEPH RAZ, *The Rule of Law and Its Virtue*, in *THE AUTHORITY OF LAW* 210, 218 (1979) (noting that “[t]he police should not be allowed to allocate its resources so as to avoid all effort to prevent and detect certain crimes or prosecute certain classes of criminals”). Fuller recognized that enforcement resources are limited, but suggested that incongruent enforcement be carefully evaluated. Lon L. Fuller, *A Reply to Professors Cohen and Dworkin*, 10 *VILL. L. REV.* 655, 663 (1965). The “conscientious prosecutor” should ask at least whether there is a pattern of discrepancy between the law as enforced and as written and whether any resulting revision to the laws is defensible. *Id.*

¹⁰⁸ The problems with the congruence requirement are not only moral, but constitutional. In recent years, a number of questions have arisen out of the Obama administration's decision to not enforce controversial laws regarding immigration and same-sex marriage. Scholars have thus recently evaluated the permissibility of the executive branch's discretionary power. *See, e.g.*, Kate Andrias, *The President's Enforcement Power*, 88 *N.Y.U. L. REV.* 1031 (2013); Robert J. Delahunty & John C. Yoo, *Dream on: The Obama Administration's Nonenforcement of Immigration Laws, the DREAM Act, and the Take Care Clause*, 91 *TEX. L. REV.* 781 (2013); Joseph Landau, *DOMA and Presidential Discretion: Interpreting and Enforcing Federal Law*, 81 *FORDHAM L. REV.* 619 (2012); Zachary S. Price, *Enforcement Discretion and Executive Duty*, 67 *VAND. L. REV.* 671, 688 (2014); Michael Sant' Ambrogio, *The Extra-Legislative Veto*, 102 *GEO. L.J.* 351 (2014). Use-tax nonenforcement clearly does not garner the same level of political interest as the federal policies discussed above. It is also fueled not as much by politics, but by economic compulsion. (Some governors may feel politically precluded from enforcing the tax, but that is likely more on general anti-tax grounds than on a specific substantive rejection of consumption taxes on Internet commerce with remote vendors *qua* Internet commerce with remote vendors). Many of the same considerations arise, though, when talking about use-tax nonenforcement. Notwithstanding those questions, this Article will focus only on the moral dimension of nonenforcement and leave the legal questions for another day.

¹⁰⁹ Michael D. Shear, *Obama, Daring Congress, Acts to Overhaul Immigration*, *N.Y. TIMES*, Nov. 20, 2014, at A1; *Executive Actions on Immigration*, USCIS [hereinafter USCIS, *Executive Actions*], <http://www.uscis.gov/immigrationaction> (last visited Oct. 8, 2015); *Fixing the System: President Obama Is Taking Action on Immigration*, *THE WHITE HOUSE*, <http://www.whitehouse.gov/issues/immigration/immigration-action> (last visited Oct. 8, 2015).

¹¹⁰ USCIS, *Executive Actions*, *supra* note 109.

¹¹¹ *See* Memorandum from Jeh Charles Johnson, Sec'y, Dep't of Homeland Sec., to Thomas S. Winkowski, Acting Direct, U.S. Immigration & Customs Enf't (Nov. 20, 2014), http://www.dhs.gov/sites/default/files/publications/14_1120_memo_prosecutorial_discretion.pdf; *Consideration of Deferred Action for Childhood Arrivals (DACA)*, USCIS,

The rationale given for these actions is consistent with what can be termed a “worst-first” enforcement methodology where an agency pursues only the most brazen offenders or those causing the highest social harm.¹¹² For example, it is more reasonable to dedicate police efforts to stopping individuals going 20 miles over the speed limit than two miles over the speed limit. It is similarly more reasonable to direct significant enforcement effort to stopping concentrated sources of file sharing rather than to stopping one individual who downloads a pirated movie.

Use-tax nonenforcement certainly shares similarities with these situations. Most use-tax violations would appear to be “minor” since individuals generally owe non-substantial amounts of that tax. Auditing these individuals would thus appear to be a misuse of enforcement resources.¹¹³ There is also *some* enforcement effort aimed at “bigger” offenders.¹¹⁴ Notwithstanding those factors, though, use-tax nonenforcement also differs from the nonenforcement of other laws because, in part, states continue to affirmatively compel individuals to pay use taxes, through their tax returns, instructions, websites, and other interactions with taxpayers.¹¹⁵ Those

<http://www.uscis.gov/humanitarian/consideration-deferred-action-childhood-arrivals-daca> (last visited Oct. 8, 2015) (noting that “[d]eferred action is a use of prosecutorial discretion to defer removal action against an individual for a certain period of time”).

¹¹² The use of these enforcement strategies in the tax law has been extensively analyzed recently. See Leigh Osofsky, *Concentrated Enforcement*, 16 FLA. TAX REV. 325, 333–38 (2014) (discussing the use of worst-first enforcement strategies).

¹¹³ Individual use-tax audits may not make economic sense in isolation, but that does not mean that states have no options to compel compliance. As an initial matter, they could audit use-tax compliance with any income tax audit. They could also easily respond to returns reporting absolutely zero use tax with a letter. The simple act of noticing taxpayer error and informing taxpayers of that fact is a form of sanction that could have a positive impact on reporting rates. See Thimmesh, *supra* note 67 (manuscript at 38–39). States can also direct attention directly to tax-return preparers who consistently file returns showing no use tax due. A full list of ideas for use-tax enforcement is beyond the scope of this paper, but suffice it to say that states must look beyond the simple expected value of a single audit. If nothing else, research shows that individual audits have a multiplier effect in that people who hear about audits are more likely to comply themselves. See Susan C. Morse, *Tax Compliance and Norm Formation Under High-Penalty Regimes*, 44 CONN. L. REV. 675, 711 n.145 (2012) (listing studies establishing this “indirect audit effect”). See generally Thimmesh, *supra* note 67 (providing a comprehensive discussion of the ways in which states could leverage research on tax compliance to help build a compliance norm with respect to state use taxes).

¹¹⁴ See sources cited *supra* note 106.

¹¹⁵ See, e.g., *Consumer Use Tax Return and Instructions*, COLORADO, <https://www.colorado.gov/pacific/sites/default/files/DR0252.pdf> (last visited Oct. 8, 2015) (requiring the payment of use taxes); *Do You Owe Use Tax?*, DEP’T OF REVENUE WASH. ST., <http://dor.wa.gov/Content/GetAFormOrPublication/PublicationBySubject/TaxTopics/UseTax.aspx> (last visited Oct. 8, 2015) (discussing the variety of ways in which states have included use tax line items on their tax returns); *Holiday Shoppers May Owe Use Tax on Internet Purchases*, IDAHO ST. TAX COMMISSION (Nov. 25, 2014), <http://tax.idaho.gov/n-feed.cfm?idd=523> (informing consumers of their use tax responsibilities); Manzi, *supra* note 4 (discussing the variety of ways in which states have included use-tax line items on their tax returns); *Questions*

communications all continue to articulate that taxpayers must comply and even reference the very situations where use-tax compliance is the most difficult—situations where taxpayers purchase items at lower tax rates in other states.¹¹⁶ Some states also have voluntary disclosure programs that specifically reference enforcement action and individuals' potential liabilities for taxes due in past years.¹¹⁷ These communications are problematic because they are in stark contrast to the reality of how use taxes are currently being administered. They serve only to prey upon our “Washingtons,” and they thus make fools of those who we should hold out as models. Those who listen to the appeals of the state bear the entire burden of the tax while their less impressionable peers escape sanction. A state cannot morally place citizens in this position. If states are not going to enforce the tax, they cannot continue to threaten sanction.

Notwithstanding this analysis, it may seem too bold to claim that a state's failure to enforce this tax necessarily means that it has a moral obligation to abandon the tax altogether. States continue to urge compliance with speeding limits, for example, even though violations at the margin appear to be rarely enforced. Are state speeding limits thus immoral as well? There are two immediate responses to this line of inquiry. First, morality is not necessarily binary. Something is not either moral or immoral. Rather, the morality of the law lies on a spectrum, and each individual factor must be evaluated and measured with other aspects of that law.¹¹⁸ The lack of

and Answers Regarding Use Tax, ST. OF NEV. DEP'T OF TAX'N, http://tax.nv.gov/uploadedFiles/taxnv.gov/Content/TaxLibrary/TPI-01_02_Use_Tax_Questions_and_Answers_04-09-09%5B1%5D.pdf (last visited Oct. 8, 2015) (discussing the variety of ways in which states have included use-tax line items on their tax returns); *Sales & Use Tax*, KY.GOV, <http://revenue.ky.gov/Business/salesanduse.htm> (last visited Oct. 8, 2015) (informing consumers of their use-tax responsibilities); *Paying Individual Use Tax for Online, Out-of-State or Catalogue Purchases*, MASS.GOV [hereinafter *Paying Individual Use Tax*], <http://www.mass.gov/dor/all-taxes/sales-and-use/individual-use-tax/> (last visited Oct. 9, 2015) (discussing the variety of ways in which states have included use tax line items on their tax returns).

¹¹⁶ See, e.g., PA. DEP'T OF REVENUE, *USE TAX FOR INDIVIDUALS* 2 (2015), <http://www.revenue.pa.gov/FormsandPublications/FormsforBusinesses/Documents/Sales-Use%20Tax/rev-1748.pdf>; MINN. DEP'T OF REVENUE, *MINNESOTA SALES AND USE TAX INSTRUCTION BOOKLET 3* (2014), http://www.revenue.state.mn.us/Forms_and_Instructions/sales_tax_booklet.pdf; S.D. EFORM- 1350 V10, at 1 (2011), <https://www.state.sd.us/eforms/secure/eforms/E1350V10-UseTaxForm.pdf>; *Paying Individual Use Tax*, *supra* note 115; *Use Tax on Art Acquisitions by Individuals*, DEP'T OF REVENUE WASH. ST. [hereinafter *Use Tax on Art Acquisitions*], http://dor.wa.gov/Docs/Pubs/ExciseTax/RetailSales_UseTax/UseTaxOnArtQAs.pdf (last visited Sept. 16, 2015).

¹¹⁷ See, e.g., *Disclosure of Use Tax for In-State Consumers*, CA.GOV, <http://www.boe.ca.gov/sutax/isvdprog.htm> (last visited Oct. 8, 2015); *Illinois Use Tax*, ILL. REVENUE, <http://www.revenue.state.il.us/Individuals/Illinois-Use-tax.htm> (last visited Oct. 8, 2015); *Use Tax on Art Acquisitions*, *supra* note 116, at 2.

¹¹⁸ See SURI RATNAPALA, *JURISPRUDENCE* 170–71 (Cambridge Univ. Press 2009); Bruce P. Frohnen, *The Irreducible, Minimal Morality of Law: Reconsidering the Positivist/Natural Law*

enforcement of use taxes, then, simply adds to the complete picture of the morality of the law.

In addition, one must realize that tax-law nonenforcement has a particularly uneasy tone as compared to the nonenforcement of other laws because of the presence of a tax return. As noted above, individuals in many states are required to declare their use-tax liabilities on their annual income-tax returns.¹¹⁹ That return-filing requirement means that individuals are required to affirmatively certify, at least annually, that they have complied with their tax obligations. A taxpayer must therefore either truthfully report her use taxes or knowingly file an incorrect return. The latter is generally tax fraud, which can be a felony.¹²⁰

Tax returns also generally include a jurat, which requires the taxpayer to attest to the accuracy of the return, often under penalties of perjury.¹²¹

Divide in Light of Legal Purpose and the Rule of Law, 58 ST. LOUIS U. L.J. 467, 475–78 (2014) (providing a summary of Thomas Aquinas’s natural-law philosophy and concluding that “at least for Aquinas, law exists on a continuum from just to unjust, true to perverse or crooked, pure to corrupt”).

¹¹⁹ See Manzi, *supra* note 4, at 2 (noting that 27 states include a use-tax line item on their income-tax returns).

¹²⁰ See, e.g., ARK. CODE ANN. § 26-18-202 (2015) (providing that the willful failure to pay a tax or file a return is a felony); CONN. GEN. STAT. § 12-428 (2015) (classifying the willful delivery of a return that is known to be fraudulent or false in any material matter as a felony); KY. REV. STAT. ANN. § 131.445(2) (LexisNexis 2015) (classifying the willful submission of a false return with the intent to evade payment of tax as a felony); 68 OKLA. STAT. tit. 68, § 241 (2015) (classifying the filing of a false or fraudulent return as a felony); WASH. REV. CODE § 82.32.290(2)(a)(iii), (b) (2015) (same).

¹²¹ See, e.g., STATE OF CAL. FRANCHISE TAX BD., 2014 CALIFORNIA RESIDENT INCOME TAX RETURN FORM 540 (2014), https://www.ftb.ca.gov/forms/2014/14_540.pdf?WT.mc_id=Individuals_Popular_540form; IDAHO STATE TAX COMM’N, FORM 40 IDAHO INDIVIDUAL INCOME TAX RETURN (2014), http://tax.idaho.gov/forms/EFO00089_10-14-2014.pdf; KAN. DEP’T OF REVENUE, FORM K-40 (2014), <http://www.ksrevenue.org/pdf/k-4014.pdf>; ME. DEP’T OF ADMIN. & FIN. SERVS., MAINE INDIVIDUAL INCOME TAX FORM 1040ME (2014), http://www.maine.gov/revenue/forms/1040/2014/14_1040me_downloadable.pdf; MICH. DEP’T OF TREASURY, *supra* note 26; NEB. DEP’T OF REVENUE, NEBRASKA INDIVIDUAL INCOME TAX RETURN FORM 1040N (2014), http://www.revenue.nebraska.gov/tax/14forms/f_1040n.pdf; OHIO DEP’T OF TAXATION, FORM IT 1040 (2014), http://www.tax.ohio.gov/Portals/0/forms/ohio_individual/individual/2014/PIT_IT1040.pdf; UTAH STATE TAX COMM’N, UTAH INDIVIDUAL INCOME TAX RETURN FORM TC-40 (2014), <http://tax.utah.gov/forms/current/tc-40.pdf>; VT. DEP’T OF TAXES, VERMONT INCOME TAX RETURN FORM IN-111 (2014), <http://www.state.vt.us/tax/pdf.word.excel/forms/income/2014/2014-IN-111-web.pdf>. In the area of taxation, the penalties for perjury and for perjurious statements can be complicated. Under federal law, there is a substantive difference between a charge of perjury and the related charge under the tax code. Perjury is punishable under 18 U.S.C. § 1621 and requires the filing of a return, specifically under penalty of perjury, that “willfully subscribes as true any material matter which [the taxpayer] does not believe to be true.” 18 U.S.C. § 1621(2) (2012). Under the tax law, a felony is also imposed for making “a false declaration under penalties of perjury.” 26 U.S.C. § 7206(1). That charge is not *technically* a perjury charge. See *Escobar v. United States*, 388 F.2d 661, 664–65 (1967), *cert denied*, 390 U.S. 1024 (1968). It is a separate crime *based on* a perjurious

Perjury, like fraud, is a serious crime. Use-tax noncompliance thus requires a taxpayer to commit legal violations in addition to simply failing to pay the amounts technically owed. This factor serves to differentiate use-tax nonenforcement from other types of nonenforcement. If a taxpayer were required to annually certify, under penalties of perjury, that she had not sped during the year, we might view that legal requirement differently. The annual certification process simply makes use-tax compliance and use-tax nonenforcement much different than similar positions with respect to other laws.¹²²

Of course, one may feel disinclined to give these considerations any weight given this Article's explicit admission that use taxes are unenforced. Of what consequence is a potential charge for fraud or perjury if we know that the charges will never occur? Indeed, without consequence, it is debatable whether a law can be immoral at all.¹²³ To many, then, the moral appeals made herein may be made impotent. The lack of consequence may indicate that there is no use-tax obligation at all, and that as a result, any references to fraud and perjury are of no consequence. This analysis, however, falls short. There are at least two ways in which use-tax noncompliance *does have* consequence regardless of states' current nonenforcement postures.

First, requiring taxpayers to either pay a tax that their neighbors do not pay or to become a fraudster and perjurer is a consequence in and of itself. Many appropriately feel aversion to committing those offenses, or felonies in general. Even if the tax is not enforced, the internal psychological sanction of

statement. The charge is often a lesser-included offense of tax fraud or tax evasion because the perjury charge does not require that any tax was avoided. *See* ROBERT S. FINK, *TAX FRAUD—AUDITS, INVESTIGATIONS, PROSECUTIONS* § 16.02 (2001); MICHAEL I. SALTZMAN & LESLIE BOOK, *IRS PRACTICE AND PROCEDURE* ¶ 7A.04[1] (2d ed. 2014). *See generally* *United States v. Bishop*, 412 U.S. 346 (1973) (evaluating the difference between the two penalty provisions). The crime does, however, require that a false statement on a return be “material.” *See* 26 U.S.C. § 7206(1). Under the federal law, this does not mean that the amount is substantial, just that the item being reported is material. Thus, false statements as to gross income have been held to be material without regard to the amount of income omitted. *United States v. Clavey*, 578 F.2d 1219 (7th Cir. 1978) (en banc); *United States v. DiVarco*, 484 F.2d 670, 673 (7th Cir. 1973), *cert. denied*, 415 U.S. 916 (1974). In addition, an incorrect claim for a deduction was held to be material even though no tax was owed when the error was corrected. *United States v. Farnan*, 948 F.2d 1283 (4th Cir. 1991), *cert. denied*, 504 U.S. 913 (1992). For purposes of this discussion, the semantic difference between a perjury charge and a charge based on a perjurious statement is without effect. Outside of a few highly specialized lawyers, the difference is likely unknown and, even if known, of no effect. The material factors are that knowingly making a false statement on a tax return can be a crime and that it can be a felony.

¹²² These problems are even more troubling once one realizes that even our Washingtons likely know that they cannot fully recount their transactions for the year. Under current law, even they can hardly claim that their returns are accurate or that they did not knowingly fail to report any liability.

¹²³ *See* Ronald Dworkin, *Philosophy, Morality, and Law: Observations Prompted by Professor Fuller's Novel Claim*, 113 U. PA. L. REV. 668, 674–75 (1965) (noting that violations of Fuller's canons have “no moral flavor at all” if they have no consequences).

having to commit those offenses should not be ignored.¹²⁴ It is no small relief to one burdened by these internal consequences to say that the law was no law from a philosophical standpoint or that the law is not, or likely will not be, enforced. Second, we must remain mindful that states can change their nonenforcement postures and seek back use taxes from consumers and impose significant penalties for their noncompliance, each to the extent that the applicable statutes of limitation allow. Taxpayers thus bear the risk of sanctions even though the tax is *currently* unenforced. This cannot be accepted. If the state is to hold that power over individuals, it should be responsible for making a meaningful effort to punish those who ignore the mandate. If it is unwilling to do so, the moral approach would be to relieve taxpayers of the burden through a change in law or a binding nonenforcement position.

2. The Moral Implications of the Difficulty of Use-Tax Compliance

States' nonenforcement postures are also troubling because they have allowed states to ignore significant problems with how those taxes are structured. It seems obvious to say that a law that requires one to perform an impossible task is immoral and fails to rise to the level of something that can be respected as "law" under a rule-of-law framework.¹²⁵ A statute requiring that a person be in two places at once, for example, would be a mere penalty on existence. It would represent nothing more than a naked use of force against the governed. Of course, the line between something that is extremely difficult and something that is impossible is not clear.¹²⁶ The former might be "harsh and

¹²⁴ See James Alm, Gary H. McClelland & William D. Schulze, *Changing the Social Norm of Tax Compliance by Voting*, 52 KYKLOS 141, 149 (1999) (recognizing that taxpayers may suffer a psychological loss by evading taxes); Ronald G. Cummings, Jorge Martinez-Vazquez, Michael McKee & Benno Torgler, *Tax Morale Affects Tax Compliance: Evidence from Surveys and an Artefactual Field Experiment*, 70 J. ECON. BEHAV. & ORG. 447, 449 (2009) (noting the "psychic cost associated with evading one's own tax liability"); Kathleen DeLaney Thomas, *The Psychic Cost of Tax Evasion*, 56 B.C. L. REV. 617, 619 (2015) (discussing the psychological discomfort taxpayers feel when evading tax).

¹²⁵ See FULLER, *supra* note 107, at 39 (noting that a law that commands the impossible is not a valid rule of law); RAWLS, *supra* note 107, at 208 ("First of all, the actions which the rules of law require and forbid should be of a kind which men can reasonably be expected to do and to avoid. . . . It must not impose a duty to do what cannot be done."); RAZ, *supra* note 107, at 213 (noting that "the law must be capable of being obeyed"); Frohnen, *supra* note 118, at 484 (stating that "[a] purported law, the sanctions of which are unavoidable (for example, a law imposing the death penalty for walking on one's feet rather than one's hands), is not a law, according to Neumann; it is simply an imposition of punishment" (citing MICHAEL NEUMANN, *THE RULE OF LAW: POLITICIZING ETHICS* 60 (2002))). Fuller specifically noted that there "[c]ertainly . . . can be no rational ground for asserting that a man can have a moral obligation to obey a legal rule that . . . was unintelligible . . . or commanded the impossible." FULLER, *supra* note 107, at 39. Similarly, Rawls noted that "[l]aws and commands are accepted as laws and commands only if it is generally believed that they can be obeyed and executed." RAWLS, *supra* note 107, at 208.

¹²⁶ FULLER, *supra* note 107, at 79. Fuller's conception of the morality of law is not without debate, but has, however, seen resurgence as of late. See generally KRISTEN RUNDLE, *FORMS*

unfair” but in accordance with the purpose of the legal order. Demands that are “patently impossible,” in contrast, conflict with that purpose.¹²⁷ Such demands show an “indifference” to one’s powers of self-determination.¹²⁸ Laws must therefore be designed such that we can reasonably expect compliance.

As they are currently structured, use taxes are highly problematic under this principle because full compliance with those taxes is virtually impossible. As discussed above, use taxes apply in many situations. The most well-understood situation in which they apply is when a taxpayer purchases an item online or via catalogue without paying any sales tax.¹²⁹ Use taxes also apply, however, when consumers purchase goods in a state without paying sales tax and then use the goods in another state.¹³⁰ They also apply when consumers pay sales tax at a lower rate than the rate of taxation in their jurisdiction of use.¹³¹ Finally, use taxes may apply where an individual purchases and uses property in their current home state and then subsequently uses the property in another state, perhaps after a change of residence.¹³²

The use tax likely violates the principle of possibility in all but the first situation. That situation (i.e., Internet and catalogue purchases) likely survives scrutiny for two principal reasons. First, those transactions are almost certainly completed using a form of exchange that creates a paper trail, at least digitally. Purchases on the Internet and through catalogues would generally involve a credit or debit card, and perhaps a check. As a result, taxpayers can effectively track their purchasing activities. Second, with respect to Internet purchases, even where a taxpayer does not track those purchases through their bank or

LIBERATE: RECLAIMING THE JURISPRUDENCE OF LON L FULLER (2012) (providing a detailed look and reconceptualization of Fuller’s legal theory); Mark Bennett, *Leaving the Hart-Fuller Debate and Reclaiming Fuller: Form, Agency, and Morality in Kristen Rundle’s Forms Liberate*, 44 VICTORIA U. WELLINGTON L. REV. 461 (2013) (reviewing Kristen Rundle’s analysis and offering a complimentary view of Fuller’s work); Frohnen, *supra* note 118 (arguing that law’s intrinsic purpose—to provide order—is a moral good in line with Fuller’s concept of internal morality); Colleen Murphy, *Lon Fuller and the Moral Value of the Rule of Law*, 24 L. & PHIL. 239 (2005) (defending “Lon Fuller’s view that the rule of law has conditional non-instrumental as well as instrumental moral value”). It is not important, for purposes of this piece, whether one agrees with Fuller’s criterial account or in the non-instrumental value of that account. If use taxes fail to be *law* (in that states have not enacted or administered them in a way that gives them legitimacy), a state is on morally questionable grounds if it imposes sanctions on those who fail to pay those taxes regardless of which rule of law framework is applied.

¹²⁷ FULLER, *supra* note 107, at 79.

¹²⁸ *Id.* at 162.

¹²⁹ See *supra* notes 60–65 and accompanying text.

¹³⁰ Of course, some states impose their use tax in that situation only if the goods were purchased for use within their boundaries and other states impose their use tax simply if the goods are so used. See *supra* Part II.B. Under the latter type of statute, there is a difference between a meal purchased and eaten while on vacation and a souvenir shirt purchased under the same conditions.

¹³¹ See *supra* notes 43–46 and accompanying text.

¹³² See *supra* notes 48–50 and accompanying text.

credit-card company, their online retailer likely tracks those purchases, or *can* track those purchases if a consumer creates an online account. For example, Amazon.com allows users to view their purchases by year under the “Your Account” tab at the top of its webpage. The e-tailing platform simply allows for information collection and maintenance that is not as readily available in the traditional retailing format.

These compliance-assisting factors do not necessarily apply to the three additional categories of purchases noted above. Those three categories all generally involve purchases made at a physical store. Unlike purchases made online, in-store purchases need not be completed using a credit card and they are not likely to be tracked through an accessible customer account. This is not to say that these simplification measures *could not* apply to these categories of purchases, but even if a consumer used a credit card for those purchases, for example, she would still need to track all of her annual purchases, where she used the purchased items, whether tax was collected at the point of sale for those items, and, if so, what rate was applied. A credit-card receipt or bank statement would provide only one of the necessary items of information.

This discussion evidences that use-tax compliance is virtually impossible in many situations. Taxpayers who travel around the country during the course of a year and make purchases using a combination of cash, credit, and perhaps check would be able to comply with their state use-tax obligations only if they were to keep contemporaneous logs of every remote purchase and the state and local sales taxes collected. This is simply impractical. Compliance for anyone, then, is an educated guess at best.

This discussion has not yet even touched on the obligation of an individual who changes residences after acquiring property for many years. What rate of sales tax did he pay on his purchase of the lawn mower or the silverware? All of the issues discussed above are thus magnified when a state imposes its use tax without a first-use exception.

This analysis suggests that the use tax does indeed raise moral questions, but the claims regarding the impossibility of compliance should not be overstated. Compliance *is technically possible* if one assumes a taxpayer who structures her affairs so carefully as to track, examine, and recall every transaction. One could thus argue that compliance with these taxes is simply extremely difficult and that no moral issue is presented.¹³³ I argue that this pushes that conception too far. To command an individual to be nothing more than an accountant carrying a notebook cataloguing the year’s purchases is to command something that cannot be respected. It commands a task that is unreasonably difficult in light of the regulatory objective. The use tax is not intended to guide behavior by requiring taxpayers to direct such a significant level of energy towards compliance. Although such burdens may be

¹³³ See FULLER, *supra* note 107, at 79.

appropriate when the end goal is furthered by those actions,¹³⁴ cataloging one's daily affairs with the zeal of the most dutiful bookkeeper does not further the goal of raising revenue in and of itself. The use tax, in its current form, simply imposes an obligation with so many costs (social, opportunity, etc.) that it is fair to categorize as a tax with which compliance is practically impossible.¹³⁵

D. *The Psychological Case for a Consumer-Centric Approach*

This Section critiques use-tax nonenforcement based on its likely impact on taxpayers' motivations to comply with the tax laws more generally. To understand that impact, one must first recognize that a number of factors go into a person's decision of whether to comply with a particular government mandate.¹³⁶ One of those factors is a person's view of the legitimacy of that government's authority.¹³⁷ Indeed, people who view an authority as legitimate are generally more likely to comply with the commands of that authority regardless of their personal feelings regarding the desirability of the commanded act.¹³⁸ Undermining that legitimacy can thus have a negative impact on compliance and should be avoided.

Research suggests that the legitimacy of government is determined in part by citizens' perceptions of the trustworthiness of government and by their perceptions of the fairness of the processes used by government.¹³⁹ Though

¹³⁴ Take for example, onerous safety regulations. The very acts required to come into compliance may likely serve the end goal of safety in and of themselves.

¹³⁵ Of course, the moral concerns stemming from the impossibility of compliance may be lessened or eliminated by the nonenforcement of the use tax. As discussed above, however, states' nonenforcement positions do not mitigate the moral problems inherent in the use tax. States continue to compel individuals to comply and to require them to attest to the veracity of their tax-return positions. For the same reasons that we cannot excuse states' nonenforcement generally, we cannot excuse a system with which compliance is not possible.

¹³⁶ See generally Thimmesch, *supra* note 67 (manuscript at 7–22) (discussing the theories regarding why people comply with the tax laws and how they apply to use taxes).

¹³⁷ TOM R. TYLER, *WHY PEOPLE OBEY THE LAW* 25–27 (Princeton Univ. Press 2006) (1990); Margaret Levi, Audrey Sacks & Tom Tyler, *Conceptualizing Legitimacy, Measuring Legitimizing Beliefs*, 53 *AM. BEHAV. SCIENTIST* 354, 354–56 (2009) [hereinafter Levi, *Conceptualizing Legitimacy*]. See generally Margaret Levi, Tom R. Tyler & Audrey Sacks, *The Reasons for Compliance with Law*, in *UNDERSTANDING SOCIAL ACTION, PROMOTING HUMAN RIGHTS* 70 (Ryan Goodman, Derek Jinks & Andrew K. Woods eds., 2012) [hereinafter Levi, *Reasons for Compliance*] (describing research results that support the claim that individuals' views regarding the legitimacy of government authority impact voluntary compliance rates).

¹³⁸ See TYLER, *supra* note 137, at 57–62; see also Levi, *Conceptualizing Legitimacy*, *supra* note 137, at 354–55.

¹³⁹ See Levi, *Conceptualizing Legitimacy*, *supra* note 137, at 356. This research differentiates between “value-based legitimacy” and “behavioral legitimacy.” *Id.* The former refers to individuals' internal sense that they *should* obey a government mandate. *Id.* The latter refers to whether they actually do so. *Id.* The research of Levi, Tyler, and Sacks suggests that value-based

these two concepts are related, they are distinct.¹⁴⁰ Citizens' perceptions regarding the trustworthiness of government depend on their judgments regarding the motivations of government officials and of those officials' competency and performance.¹⁴¹ Citizens' perceptions regarding procedural justice, on the other hand, more specifically depend on the fairness of the processes used by government in its interaction with citizens.¹⁴²

The positive relationship between trust in government and voluntary compliance¹⁴³ is impacted by a number of factors, including citizens' perceptions regarding *the way* in which government exercises its power¹⁴⁴ and citizens' perceptions of the government's administrative competency.¹⁴⁵ Importantly, citizens' competency judgments are partially based on their evaluations of whether the government will enforce the laws against those who do not comply.¹⁴⁶ That is because "coercion is important for reassuring citizens that others will be punished. It signals government competence and protects citizens from being a sucker while others free ride."¹⁴⁷ In one study, citizen perception that the government was competent and honest translated into a 15 percentage point increase in the probability that a taxpayer would accept a tax

legitimacy enhances behavioral legitimacy. Levi, *Reasons for Compliance*, *supra* note 137, at 82–84. That is, when people feel an obligation to comply with the law, they generally do so.

¹⁴⁰ Levi, *Reasons for Compliance*, *supra* note 137, at 72.

¹⁴¹ *Id.*

¹⁴² TYLER, *supra* note 137, at 174–76.

¹⁴³ TOM BEERS, ERIC LOPRESTI & ERIC SAN JUAN, FACTORS INFLUENCING VOLUNTARY COMPLIANCE BY SMALL BUSINESSES: PRELIMINARY SURVEY RESULTS 13–14 (2012), <http://www.taxpayeradvocate.irs.gov/2012-Annual-Report/downloads/Research-Studies-Factors-Influencing-Voluntary-Compliance-by-Small-Businesses-Preliminary-Survey-Results.pdf> (reporting that taxpayers in a high-compliance group were more likely to trust the government); ERIC KIRCHLER, THE ECONOMIC PSYCHOLOGY OF TAX BEHAVIOUR 202–06 (2007); Katharina Gangl et al., "How Can I Help You?" *Perceived Service Orientation of Tax Authorities and Tax Compliance*, 69 PUB. FIN. ANALYSIS 487, 500–04 (2013).

¹⁴⁴ Lars P. Feld & Bruno S. Frey, *Deterrence and Tax Morale: How Tax Administrations and Taxpayers Interact*, 3 OECD PAPERS 1 (2003), <http://www.oecd.org/tax/administration/2789923.pdf>; Gangl et al., *supra* note 143, at 501–04; Erich Kirchler, Erik Hoelzl & Ingrid Wahl, *Enforced Versus Voluntary Tax Compliance: The "Slippery Slope" Framework*, 29 J. ECON. PSYCHOL. 210, 213 (2008).

¹⁴⁵ Levi, *Reasons for Compliance*, *supra* note 137, at 73; Margaret Levi & Audrey Sacks, *Legitimizing Beliefs: Sources and Indicators* 12, 15–16 (Afrobarometer, Working Paper No. 74, 2007) [hereinafter Levi, *Legitimizing Beliefs*], <http://afrobarometer.org/sites/default/files/publications/Working%20paper/AfropaperNo74.pdf>.

¹⁴⁶ Levi, *Reasons for Compliance*, *supra* note 137, at 73; Levi, *Legitimizing Beliefs*, *supra* note 145, at 12, 15–16. In this way, enforcement impacts both taxpayers' views of retributive and procedural justice. This is very important in our discussion of use-tax compliance because enforcement of those taxes is virtually nonexistent.

¹⁴⁷ Levi, *Reasons for Compliance*, *supra* note 137, at 73.

administrator's authority.¹⁴⁸ That result is consistent with the results of research on the role and importance of retributive justice in society.¹⁴⁹ Although the reasons for why individuals care about retributive justice are uncertain, individuals do generally care that those who do not comply with social norms are sanctioned.¹⁵⁰ Those sanctions can be monetary or social, but justice requires some signal that the noncompliant behavior was deviant.

Significant research also establishes that citizens' beliefs regarding the legitimacy of government are tied to concepts of procedural justice.¹⁵¹ At a base level, citizens care about the decision-making process and think about "representation, neutrality, bias, honesty, quality of decision, and consistency."¹⁵² They "value being treated politely and having respect shown for their rights."¹⁵³ As a result, individuals may be motivated to comply based more on the fairness of their prior interactions with an authority than on the actual outcomes of those interactions.¹⁵⁴

In the tax context, a procedural-justice framework would suggest that the tone and method of the taxing authority's communications with taxpayers¹⁵⁵

¹⁴⁸ *Id.* at 79–80, 80 n.7. Those results were based on survey data from a number of sub-Saharan African countries. *Id.* at 77.

¹⁴⁹ See generally KIRCHLER, *supra* note 143, at 87–90 (discussing retributive justice as it relates to fairness); TOM R. TYLER ET AL., SOCIAL JUSTICE IN A DIVERSE SOCIETY 103–32 (1997) (discussing research on retributive justice).

¹⁵⁰ See, e.g., TYLER ET AL., *supra* note 149, at 106–11.

¹⁵¹ See Levi, *Conceptualizing Legitimacy*, *supra* note 137, at 359–60; see also TYLER, *supra* note 137, at 170–73.

¹⁵² TYLER ET AL., *supra* note 137, at 175.

¹⁵³ *Id.*

¹⁵⁴ This work has been extended specifically to tax compliance with generally positive results. In one study, a citizens' belief that the government operated in a procedurally just manner corresponded to a 19 percentage-point increase in the probability that the taxpayer would defer to the authority of the tax administrator. Levi, *Reasons for Compliance*, *supra* note 137, at 80 & n.9. A study performed in Australia also showed a positive impact on compliance when fairness concepts were incorporated into "reminder" letters that were sent to taxpayers. Michael Wenzel, *Principles of Procedural Fairness in Reminder Letters: A Field-Experiment* 29 (Austl. Nat'l Univ. Ctr. for Tax Sys. Integrity, Working Paper No. 42, 2002), <http://hdl.handle.net/1885/42671> ("The present study yielded some, but largely patchy, evidence for the assumption that procedural justice principles in reminder letters improve levels of compliance with the reminders."). Other studies on the interplay between procedural justice and tax compliance show similar results. See, e.g., BEERS, LOPRESTI & SAN JUAN, *supra* note 143, at 15 (reporting that principles of procedural justice appear to impact taxpayer behavior); Martina Hartner et al., *Procedural Fairness and Tax Compliance*, 38 ECON. ANALYSIS & POL. 137, 149 (2008) (reporting a "clear direct effect of procedural justice on motivational postures" in all sampled groups); Kristina Murphy, *Procedural Justice and Tax Compliance*, 38 AUSTL. J. OF SOC. ISSUES 379, 389–97 (2003) (evaluating the negative impacts of enforcement actions on tax compliance).

¹⁵⁵ See generally Feld & Frey, *supra* note 144 (establishing "a systematic relationship between external intervention (in this case, how the tax officials deal with taxpayers) and intrinsic motivation (in this case, individuals' tax morale)"); Michael Hallsworth et al., *The Behavioralist as Tax Collector: Using Natural Field Experiments to Enhance Tax Compliance*

and their respect for taxpayers¹⁵⁶ matter. Additionally, it would suggest that a taxpayer undergoing an audit will base her opinion of the revenue authority on how well she is treated in the audit, rather than on the results of the audit.¹⁵⁷ A commitment to procedural justice would seem to require that taxpayers not be penalized harshly for violations that were not purposeful, involved *de minimis* amounts, involved unclear law, or that were previously unenforced. The essence of procedural justice is “the commitment of government to uphold the laws fairly and to apply them equally to all.”¹⁵⁸ Any violation of those fundamental concepts of fairness threatens to undermine citizens’ views of the legitimacy of the government’s authority.

States’ nonenforcement of the use tax is likely to have an impact on taxpayers’ views of the legitimacy of their states’ revenue authorities under both the competency—and thus trust—and procedural-justice frameworks.¹⁵⁹ States currently implore citizens to pay those taxes and threaten them with penalties for noncompliance.¹⁶⁰ When they fail to follow through on those threats even against the most brazen offenders, their credibility takes a significant hit. It also results in a procedurally unjust administration of the tax laws. As noted above, the impact of those postures is that the use tax is an implicit tax on honesty. It treats the honest as “suckers”¹⁶¹ while letting the remainder go without rebuke. That result would surely not be adopted as a legislative matter, and to administer the tax to bring about the same result is highly problematic. It reflects an inequitable administrative choice that fails to

(Nat’l Bureau of Econ. Research, Working Paper No. 20007, 2014), <http://www.nber.org/papers/w20007> (focusing on the “timely payment of taxes” rather than “the honest declaration of income”); Michael Wenzel, *A Letter from the Tax Office: Compliance Effects of Informational and Interpersonal Justice*, 19 SOC. JUST. RES. 345 (2006) (testing the “effects of an authority’s fairness . . . on perceptions of fairness and actual compliance”).

¹⁵⁶ KIRCHLER, *supra* note 143, at 84–85; Murphy, *supra* note 154, at 381.

¹⁵⁷ KIRCHLER, *supra* note 143, at 84–85.

¹⁵⁸ Levi, *Reasons for Compliance*, *supra* note 137, at 74.

¹⁵⁹ Levi, Tyler, and Sacks found that incompetency does not directly influence individuals’ perceptions of government legitimacy, but it did so through the mediating variable of trust. Levi, *Reasons for Compliance*, *supra* note 137, at 76.

¹⁶⁰ See *supra* notes 115–17 and accompanying text. It might be a different matter if states simply ignored their use-tax laws, like the many outdated state and local laws that often make Internet lists. See, e.g., BIG GOV’T. SMALL BRAINS. DUMB LAWS., <http://www.dumblaws.com/> (last visited Sept. 7, 2015) (listing so called “dumb laws” in the United States and around the globe). These websites often include fake laws, but many are purported to have been verified.

¹⁶¹ Levi, *Reasons for Compliance*, *supra* note 137, at 73; see Ari Armstrong, *Confession of a Colorado Use Tax Chump: I Am the 0.08 Percent*, COMPLETE COLO.–PAGE TWO (Apr. 9, 2014, 2:13 PM), <http://completecolorado.com/pagetwo/2014/04/09/confession-of-a-colorado-use-tax-chump-i-am-the-0-08-percent/> (evidencing taxpayer response to the lack of enforcement of use taxes); see also Bruce Smith, Letter to the Editor, *Apparently Only the Stupid Pay the State Use Tax*, CASPER STAR TRIB. (July 19, 2014, 9:45 AM), http://trib.com/opinion/letters/smith-apparently-only-the-stupid-pay-the-state-use-tax/article_122d41a3-2785-57c7-a8be-05d490f34ee1.html (suggesting that only “the stupid” would pay use tax).

respect taxpayers' rights. Given this enforcement posture, then, our Washingtons will likely respond, or have already responded, by losing respect for the legitimacy of government and by joining the crowd of those who do not comply.¹⁶²

One might reasonably ask why this analysis matters given that virtually no one currently pays the use tax. Citizens who lack trust in the government or who feel as though states have acted in a procedurally unjust way cannot pay *less* use tax than what they currently pay. Additionally, these issues cannot impact taxpayers who are not even aware of the existence of the tax. These observations are apt, but there are at least two reasons that they do not negate the importance of this issue. First, as states continue to increase the salience of the use tax and the sanctions for non-compliance, they must be concerned that they are taken seriously. Taxpayers will ultimately judge the legitimacy of their tax administrator when they are confronted with the tax. Second, states must think beyond how those judgments impact use-tax collections specifically. Taxpayers who do not trust the state revenue authority or who feel that it operates in a procedurally unjust manner may feel less inclined to properly report their other taxes as well. States should thus recognize that their perceived ineptness with regard to the use tax may affect their other efforts.

In sum, states' current nonenforcement postures with respect to use taxes have the potential to significantly undermine citizens' views regarding the legitimacy of government and their willingness to obey the law. That nonenforcement likely impacts citizens' views regarding the competency of government and their views regarding the fairness of government procedures. Neither of those impacts is positive. States must take those impacts into account when determining how to enforce their taxes. In the context of state use taxes, this likely requires a consumer-centric approach.

E. Other Benefits from Adopting a Consumer-Centric Approach

The preceding sections have addressed the economic, moral, and psychological factors that compel a consumer-centric approach to the state use tax. Notably, those factors would compel that approach *even if* the Marketplace Fairness Act were enacted. This Section, however, explores a different set of factors that would support adopting a consumer-centric approach *instead of* relying on the Marketplace Fairness Act. Those factors include the avoidance of commercial concerns, concerns under the Due Process Clause, and political opposition to that Act.

With respect to the commercial concerns, it is worth noting that the Court adopted its physical-presence rule under the Dormant Commerce Clause

¹⁶² See Bryan T. Camp, *The Play's the Thing: A Theory of Taxing Virtual Worlds*, 59 HASTINGS L.J. 1, 22–23 (2007) (noting that the American tax system's reliance on voluntary compliance "will break down when it . . . makes suckers out of compliant taxpayers by imposing requirements that are practically unenforceable against noncompliant taxpayers").

because of the impacts that expansive state authority could have on interstate commerce.¹⁶³ The Court's *National Bellas Hess, Inc. v. Department of Revenue*¹⁶⁴ and *Quill* decisions also specifically indicated concern for vendors whose operations would not support the burdens of complying with multi-state tax obligations.¹⁶⁵ Passage of the Act would raise those same commercial concerns. Smaller vendors operating on the Internet would necessarily incur costs if they were required to collect and remit sales tax for states across the nation. Compliance with those requirements would necessitate the purchase (or at least incorporation) of software to determine which items are subject to remote states' taxes and the appropriate levels of tax to charge.¹⁶⁶ Vendors would also have to remit the taxes owed and deal with the costs of any audits performed by those states. The extent of those costs is subject to debate, but could be significant compared to the profits of smaller vendors. As a result, much of the opposition of the Act comes from Internet vendors concerned about those compliance costs. The Act's simplification requirements and small-seller exception are intended to address those concerns, but many disagree that they go far enough.¹⁶⁷

This Article does not seek to settle this debate. Rather, it will suffice to note that there are commercial concerns that have demanded attention by, and concession from, states and other proponents of the Act. Those concerns may not tip the scales towards rejecting that Act, but they are still a thumb on that scale and should not be forgotten in the overall analysis.

There are also potential Due Process Clause concerns with the Act. Under that clause, states lack jurisdiction over nonresidents unless those nonresidents have purposefully availed themselves of the benefits of the

¹⁶³ *Quill Corp. v. North Dakota*, 504 U.S. 298, 313–18 (1992).

¹⁶⁴ 386 U.S. 753 (1967).

¹⁶⁵ See John A. Swain, *State Sales and Use Tax Jurisdiction: An Economic Nexus Standard for the Twenty-First Century*, 38 GA. L. REV. 343, 356–63 (2003) (noting that “the Court’s burdens concern seems to be that businesses with low volume contacts with multiple states may have costs of compliance that are excessive in comparison to the amount of business done in those states”).

¹⁶⁶ The Act would require states to provide software to vendors that would calculate the appropriate levels of sales tax owed on purchases. See Marketplace Fairness Act of 2015, S. 698, 114th Cong. § 2(b)(2)(D)(ii) (2015). Despite that requirement, there is no requirement that states’ software is complementary or that it can be easily incorporated with the software that the vendor uses to run its online sales platform.

¹⁶⁷ See, e.g., Drexden Davis, *Marketplace Fairness Act Is Not Fair to the Marketplace*, THE HILL: CONGRESS BLOG (Dec. 8, 2014, 1:00 PM), <http://thehill.com/blogs/congress-blog/economy-budget/226157-marketplace-fairness-act-is-not-fair-to-the-marketplace>; Mckane Davis, *The Marketplace Fairness Act Will Be as Hard to Implement as Obamacare*, THE DAILY CALLER (Dec. 4, 2013, 11:24 AM), <http://dailycaller.com/2013/12/04/the-marketplace-fairness-act-will-be-as-hard-to-implement-as-obamacare/>; *Debunking the Myths Around the Marketplace Fairness Act*, EBAY MAIN STREET (May 3, 2013), <http://www.ebaymainstreet.com/news-events/debunking-myths-around-marketplace-fairness-act> (noting that “[s]oftware is not a panacea”).

state.¹⁶⁸ The structure of the small-seller exception raises concerns under that constitutional provision because the exception would allow vendors to be subject to tax requirements in *any* conforming state as long as the vendor's *aggregate* remote sales exceeded \$1 million.¹⁶⁹ This means that a Georgia vendor could make \$1 million of remote sales into New York and \$2 of remote sales into Nebraska but be subject to Nebraska's taxing authority. Whether that would be permissible under the Due Process Clause is questionable, and Congress has no right to authorize that action if barred. Ultimately, the Act, at its boundary, raises this Due Process issue, which is similar to those that have been debated with respect to the Internet for years.¹⁷⁰

Finally, irrespective of these issues, some are simply opposed in principle to the cross-border power that the Act would grant. For them, the Act authorizes offensive extraterritorial exercises of power regardless of the costs imposed on vendors. It allows Nebraska, in our example, to impose burdens beyond its boundaries. They thus urge defeat of the Act on those grounds.¹⁷¹

This discussion is not intended to suggest that these factors are sufficient to counsel against passage of the Act. Rather, it is intended to point out that a consumer-centric approach would simply avoid these concerns altogether. Consumers would report their use-tax liabilities directly to their states without requiring anything of vendors. Remote vendors would not be subjected to audits by remote states and would avoid increased compliance costs. There are, then, some benefits to taking a consumer-centric approach in lieu of passage of the Act.

IV. THE CASE FOR NONENFORCEMENT

The case for a consumer-centric approach to use-tax enforcement is compelling, but not without potential critique. First, the costs of increased enforcement are certain, but the benefits are speculative. Second, the defects of the current system do not manifest themselves concretely or in a way that can be directly attributed to the tax's nonenforcement. Third, citizens may perceive use-tax enforcement to be the imposition of a "new" tax, and politicians may not be willing to face the scorn that accompanies that suggestion in today's political environment. Finally, some might argue that use-tax nonenforcement is justified as a form of assistance to the development and use of the Internet. These potential arguments against use-tax enforcement are addressed below.

¹⁶⁸ See *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 291–98 (1980).

¹⁶⁹ H.R. 684, 113th Cong. § 2(c) (2013).

¹⁷⁰ See generally Richard E. Kaye, *Internet Web Site Activities of Nonresident Person or Corporation as Conferring Personal Jurisdiction Under Long-Arm Statutes and Due Process Clause*, 81 A.L.R. 5th 41 (2000).

¹⁷¹ See Cassandra Carroll, *Marketplace Fairness Act Would Cripple Small Businesses*, AM. FOR TAX REFORM (Oct. 22, 2014, 9:30 AM), <http://www.atr.org/marketplace-fairness-act-would-cripple-small-businesses>.

A. *The Economic Costs of Enforcement*

It is easy to put oneself in the shoes of the tax administrator or state politician contemplating these issues. The conclusions of the foregoing analysis are that the current nonenforcement of use taxes results in significant revenue loss, is morally questionable, and has negative psychological impacts on taxpayers. Revenue authorities may feel, however, that the economic costs can be recouped through federal intervention and that the costs from an immoral and procedurally unfair system of taxation are too speculative, indirect, or controversial to necessitate action. In contrast, the costs for states to take enforcement action are clear. Any funds that are directed towards use-tax enforcement must be diverted from elsewhere. Why would a state redirect funds based on these speculative harms? This is an especially apt question since states are focusing their attention on the Act and since individual audits would appear to provide little, if any, positive net revenue.

One answer to this critique is that states must look beyond the economics of individual audits. Each audit may not independently produce gains to the fisc, but enforcement action can have an impact on taxpayers other than those being audited. Taxpayers who are aware of enforcement action against others may increase their own compliance.¹⁷² Taxpayer compliance also may increase for reasons other than the deterrent or competency effects of enforcement action. That action may work to increase compliance simply by increasing the salience of the tax. Further, a comprehensive approach to promoting compliance could make use of a variety of modern tax-compliance theories that could help to promote compliance without relying solely on costly audits.¹⁷³

The problem with these arguments is, of course, that they try to counter concerns about the speculative costs of nonenforcement by offering speculative gains from enforcement. For the skeptical state policy maker, then, the only concrete reason to focus on individual compliance may be that the Act simply will not close the use-tax gap. As shown above, even if that legislation were passed, less than half of that gap would be closed.¹⁷⁴ States may win the battle, but the war will not be won.

Finally, it should be noted that cost-benefit analyses have their role, but that the indeterminacy of the costs and benefits in this situation does not mean that we should not take action. It just means that a more qualitative approach should be taken. On that metric, enforcement action is not only warranted, but also compelled.

¹⁷² See Morse, *supra* note 113, at 711 n.145.

¹⁷³ See generally Thimmesch, *supra* note 67 (manuscript at 34–49).

¹⁷⁴ See *supra* note 78 and accompanying text.

B. *The Politics of Enforcement*

Anyone who follows politics even remotely is aware of the immense aversion to any action that can be classified as a “new” tax.¹⁷⁵ Unfortunately, given the existing norm of use-tax noncompliance, many may consider use-tax enforcement to be the imposition of such a tax. This impediment to enforcement action is very real and perhaps signals the death knell for use-tax reform. To convince states to take consumer-centric enforcement action, then, we must convince the politicians that enforcement of the tax does not result in a new tax and we must convince their constituents of the same.¹⁷⁶ The former should not be controversial. The use tax is a long-standing tax that has gone unenforced for largely economic reasons. Enforcement of the tax would represent a “new” tax no more than when the IRS moved to increase enforcement on taxpayers who used undisclosed, offshore bank accounts to avoid taxation.¹⁷⁷ Taking effort to reduce tax evasion is not the imposition of a new tax.

There also appears to be a solution for those politicians who simply do not want to do anything to increase revenues. A key component of many Republican governors’ tax policies has been to advocate for the reduction of income taxes and for the further utilization of consumption taxes.¹⁷⁸ Use-tax enforcement would be directly in line with those efforts. States could earmark the revenue for precisely that purpose. Indeed, many states have already introduced or adopted legislation to that effect. Wisconsin, for example, passed legislation that would require the additional revenue collected because of the Act to be used to eliminate the state’s alternative minimum tax or to provide an

¹⁷⁵ Individuals’ general aversion to taxes is demonstrated in intriguing behavioral research. See generally Kay Blaufus & Axel Mohlmann, *Security Returns and Tax Aversion Bias: Behavioral Responses to Tax Labels*, 15 J. BEHAV. FIN. 56 (2014); Abigail B. Sussman & Christopher Y. Olivola, *Axe the Tax: Taxes Are Disliked More than Equivalent Costs*, 48 J. MARKETING RES. 91 (2011); see also Edward J. McCaffery & Jonathan Baron, *Thinking About Tax*, 12 PSYCHOL. PUB. POL’Y & L. 106, 117–19 (2006).

¹⁷⁶ Though venturing into the political aspects of tax reform often moves the tax scholar outside his or her area of comfort, the realities of the modern day counsel attention to these issues. See generally Joseph Bankman & Paul L. Caron, *California Dreamin’: Tax Scholarship in a Time of Fiscal Crisis*, 48 U.C. DAVIS L. REV. 405 (2014) (critiquing the “dominant conception of legal tax scholarship,” which is “apolitical and confined to subjects about which the writer can demonstrate mastery,” as “limit[ing] our voice on a subject about which [tax scholars] have much to say”).

¹⁷⁷ See Susan C. Morse, *Tax Compliance and Norm Formation Under High-Penalty Regimes*, 44 CONN. L. REV. 675, 711–18 (2012) (describing the IRS’s recent enforcement efforts related to the reporting of foreign bank accounts).

¹⁷⁸ See Richard W. Stevenson, *Governors Push Bigger Reliance on Sales Taxes*, N.Y. TIMES (Jan. 24, 2013), <http://www.nytimes.com/2013/01/25/us/politics/republican-governors-push-taxes-on-sales-not-income.html> (discussing proposals by Republican governors in Louisiana, Nebraska, and Kansas).

income-tax reduction.¹⁷⁹ Ohio enacted legislation that would use the additional tax collections to create an “Income Tax Reduction Fund.”¹⁸⁰ Utah and Rhode Island, in contrast, would use the revenue to reduce their sales-tax rates.¹⁸¹ Other states have proposed legislation adopting a number of methods for using that revenue.¹⁸²

This discussion regarding the use of funds may create tension for those who are discontent with the general regressivity of state tax systems. Any increased reliance on consumption taxes will generally lead to a more regressive state-tax structure, especially if that increased revenue is offset with cuts to the most (and perhaps only) progressive state tax—the state income tax.¹⁸³ This concern is limited somewhat when discussing use-tax enforcement because we would expect that the current use-tax noncompliance has had a regressive impact on our tax system. Our poorest are not likely incurring large use-tax liabilities as compared to our most wealthy. This is an issue that should be considered very carefully, however, and those interested in making their state tax systems more progressive should be especially aware of the impacts of the Act if it means offsetting the additional revenue with income-tax cuts. Ultimately, however, it seems most likely that the arguments for use-tax enforcement are strong enough to counsel action. A morally questionable and procedurally unjust system should not stand in order to make incremental gains with respect to the distribution of the tax burden. That issue should be addressed in a more direct, comprehensive fashion.

The discussion thus far has addressed the concerns that politicians or policy makers might have about enforcing use taxes, but what about our taxpayers? If taxpayers resist the enforcement of the tax, politicians would seem to risk their careers if they supported that action. This concern may be legitimate, but it appears to be overstated given the fact that many Republican governors have already publicly supported the Act.¹⁸⁴ It seems as though those

¹⁷⁹ 2013 Wisconsin Act 20, Assemb. B. 40, 2013 Leg., Reg. Sess. § 1460d (Wis. 2013).

¹⁸⁰ See OHIO REV. CODE § 5741.03 (2014).

¹⁸¹ See UTAH CODE §§ 59-12-103.1 to .2 (2013); R.I. GEN. LAWS § 44-18-18 (2014).

¹⁸² See, e.g., H.B. 593, 62d Leg., 2d Reg. Sess. (Idaho 2014); H.B. 2730, 2014 Leg., Reg. Sess. (Kan. 2014); H.B.4973, 97th Leg., Reg. Sess. (Mich. 2013); H.B. 1424, 108th Gen. Assemb., Reg. Sess. (Tenn. 2014); S.B. 6571, 63d Leg., Reg. Sess. (Wash. 2014).

¹⁸³ See INST. ON TAXATION & ECON. POLICY, WHO PAYS? A DISTRIBUTIONAL ANALYSIS OF THE TAX SYSTEMS IN ALL 50 STATES 6 (2015), <http://www.itep.org/pdf/whopaysreport.pdf>. The ITEP report is not without its critics. See Liz Malm et al., *Comments on Who Pays? A Distributional Analysis of the Tax Systems in All 50 States (Second Edition)*, TAX FOUND. (Jan. 16, 2015), <http://taxfoundation.org/article/comments-who-pays-distributional-analysis-tax-systems-all-50-states-second-edition> (critiquing several elements of the ITEP study, but not contesting basic conclusions regarding the regressivity and progressivity of particular state taxes).

¹⁸⁴ Bernie Becker & Kevin Bogardus, *GOP Governors Bolster Online Sales Tax Push*, THE HILL (June 6, 2012, 10:00 AM), <http://thehill.com/policy/finance/231899-gop-governors-bolster-sales-tax-push>. Of course, one should not ignore the differences between governors supporting Congress taking action that would lead to taxpayers paying the use tax and *their own*

politicians have obtained an adequate comfort level with use-tax collection given its broad impact on their state government's finances.

A final benefit of use-tax enforcement is that it might actually increase taxpayer support for a federal solution like the Act. If taxpayers were faced with the administrative hassles of determining and paying their own tax, they might soon favor collection of the tax at the point of sale. Consumer sentiment regarding the Act might change, and Internet vendors may find that tax collection is a valuable customer service.¹⁸⁵ Enforcement may thus provide the path to where states would prefer to be in any event.

Ultimately, obtaining taxpayer support or at least relative indifference to use-tax enforcement likely rests in taking the very actions that will be required to obtain voluntary compliance as well. Taxpayers must be educated about the tax, the purpose for the tax, and the benefits that the state will see from enforcement.¹⁸⁶ Governors that wish to use the revenue to offset other taxes can also use the tax cut as the "lead" with taxpayers. Some may also wish to specifically direct the funds collected to projects with broad taxpayer support.¹⁸⁷ In the end, given the relatively small impact of use-tax enforcement on each individual consumer and the potential benefits from collecting that tax, fear of political backlash should not prevent state action on this issue.¹⁸⁸

C. *The Economics of Nonenforcement*

Having addressed the concerns about the economic and political costs of enforcement, it is worth considering the other side of the picture. Could there be benefits, separate from administrative cost savings, from not enforcing the use tax? Professors Leandra Lederman and Ted Sichelman have recently theorized that selective, measured nonenforcement could be utilized as a method of effectively changing the substance of tax law to increase social welfare.¹⁸⁹ This could occur either when taxation prevents transactions with a positive social welfare¹⁹⁰ or when the elasticity of demand for a product or

administration taking that action. Governors get political cover with the former, but may be unwilling to risk the latter.

¹⁸⁵ The Author's own experience supports this view. Shopping on websites that collect the tax makes use-tax filing much simpler, and commerce with such vendors is preferred in his household for that reason.

¹⁸⁶ See Thimmesch, *supra* note 67 (manuscript at 35–38) (discussing the information-provision aspect of state enforcement efforts).

¹⁸⁷ Of course, money is fungible, so this is largely a matter of marketing.

¹⁸⁸ This statement is made as a normative matter, not as a prediction of what political action will be taken.

¹⁸⁹ Leandra Lederman & Ted Sichelman, *Enforcement as Substance in Tax Compliance*, 70 WASH. & LEE L. REV. 1679 (2013).

¹⁹⁰ Social welfare for purposes of this model includes consumer surplus and producer surplus. The authors adopted simplifying assumptions that the tax system imposes no costs and that tax

activity subject to the tax is high, but the purchase of the product or engagement in the activity has positive externalities.¹⁹¹ For example, it might be that joining (and using) a gym has positive externalities, but that the demand for gyms is highly elastic. In contrast, it might be that joining a cigar club has negative externalities, but that demand for that product is highly inelastic. A broad sales tax that applies to both would have the result of reducing demand for gyms, and thus reducing the positive externalities associated with exercise activities, while impacting cigar club membership purchases very little. In that situation, enforcement of the sales tax against the gyms may produce a suboptimal result compared to dedicating enforcement of the tax to the cigar clubs.

Could this type of analysis be used to suggest that the current nonenforcement of use taxes is actually an optimal policy decision from the standpoint of increasing social welfare or maximizing positive externalities? To begin with, the former is highly unlikely. The construct built by Lederman and Sichelman applies to situations with very particular sets of facts and is centered on the taxation of particular products. As they recognize, the taxing agency that applies this type of analysis would need to evaluate “the relevant demand curves, supply curves, and the seller’s production and opportunity costs.”¹⁹² This strategy also relies on taxpayers that are informed of the taxing agency’s audit and penalty rates.¹⁹³ It thus requires taxpayers to read, understand, and apply “detailed information.”¹⁹⁴ Lederman and Sichelman note that their model “may only be suitable for only the most sophisticated taxpayers.”¹⁹⁵

These conditions are not met when evaluating the large-scale nonenforcement of use taxes. As a primary matter, the transactions covered by the use tax are incredibly varied and likely include every product that can be sold. Complete nonenforcement ignores the individual supply and demand curves for products and sellers’ production and opportunity costs for those products. Nonenforcement of use taxes is not measured nonenforcement, but blunt nonenforcement.¹⁹⁶

revenues provide no greater utility than if those funds remained with producers. *Id.* at 1712, 1717 n.171.

¹⁹¹ *Id.* at 1706–24.

¹⁹² *Id.* at 1726.

¹⁹³ *Id.* at 1728.

¹⁹⁴ *Id.*

¹⁹⁵ *Id.*

¹⁹⁶ To be sure, states could perhaps use targeted use-tax nonenforcement to increase social welfare with respect to certain *types* of transactions. This, however, would be based on the types of products being purchased and not their method of purchase. Further, even assuming that states could establish that use taxes generally result in inefficiencies that exceed the social benefits from taxation, it is unclear that measured nonenforcement (rather than complete nonenforcement) would be advisable. As noted, that approach requires that the targeted taxpayers are sophisticated persons who make cost-benefit analyses with respect to their tax decisions. They must incorporate the likelihood of audit and their penalty potential when making tax-reporting

The measured enforcement model might have more applicability when looking at the externality rationale. Recall that Lederman and Sichelman posited that selective enforcement might be justified in order to promote the consumption of goods with positive externalities and to discourage the consumption of goods with negative externalities.¹⁹⁷ Although use-tax nonenforcement applies too broadly to affect the consumption of particular goods, one could conceivably argue that it might encourage the positive externalities that come from promoting Internet commerce and the use of the Internet, more broadly. Certainly, there have been immense positive social impacts from the emergence of the Internet and its development as a significant forum for commercial transactions. In that way, one could argue that providing an enforcement “safe harbor” for Internet transactions is economically justified and that states should not seek to enforce their use taxes for that reason. This protectionist philosophy is reflected in Congress’s passage of the Internet Tax Freedom Act, which has prohibited states from imposing taxes directly on Internet access, and from imposing discriminatory or multiple taxes on electronic commerce, since 1998.¹⁹⁸ Congress has felt that protecting the Internet from that type of taxation would serve the goal of supporting a valuable tool for public good.

The biggest problem with justifying use-tax nonenforcement as a way of tapping into the positive externalities of the Internet is again one of fit. If we wanted to increase those externalities, we would expect states to simply exempt *all* Internet sales from consumption taxes. In reality, though, states “exempt” only a portion of Internet commerce from taxation, and that is only because the Supreme Court’s physical-presence rule requires them to do so. Having rejected that rationale, then, it seems like an untenable position to argue against use-tax enforcement simply to maintain those externalities in more limited form.¹⁹⁹

Finally, use-tax nonenforcement extends well beyond Internet purchases. As noted throughout this Article, use taxes may also be owed on catalogue purchases and purchases made while physically present in a remote

decisions. Best success would therefore be with our “most sophisticated taxpayers.” *Id.* at 1728. This construct does not hold when talking about broad-based consumption taxes. Consumers, as a whole, are unlikely to digest and incorporate detailed information about audit rates and penalties with respect to the great number of products that they purchase during the year. *See id.* (noting the difficulties presented when a single tax return reports “many classes of transactions”). Measured enforcement policies with respect to use taxes are thus likely to be difficult to construct to achieve their purposes.

¹⁹⁷ *See id.* at 1719–23.

¹⁹⁸ Internet Tax Freedom Act, Pub. L. No. 105-277, 112 Stat. 2681 (1998).

¹⁹⁹ We can further question whether a subsidy in the form of use-tax nonenforcement is really of significant benefit. The Internet is firmly entrenched in modern American life, and its use is certainly not limited to those situations in which a consumer makes a purchase from a remote vendor.

state. If we were to accept use-tax nonenforcement as a subsidy for the Internet, we would expect to see enforcement of the tax in other situations.

This analysis ultimately shows that the model of measured enforcement is unlikely to provide a justifiable reason for failing to enforce use taxes as a matter of economic, rather than political, theory. Even if Internet sales would optimally escape state consumption taxes, the method in which states are currently failing to enforce those taxes does not comport with that goal. To be sure, the use of second-best solutions is often warranted, but this situation does not appear to be a compelling one in which to apply that construct.

V. SALVAGING THE VALIDITY OF THE USE TAX

This Article has thus far outlined the problems with states' current vendor-centric approaches to the state use tax and has advocated for the adoption of a consumer-centric approach instead. That approach involves more than simply attempting enforcement actions against taxpayers, and this Part thus outlines the many facets involved and provides specific policy proposals for states to consider. These include enforcement strategies, but also include substantive reforms to the tax and modifications to how use-tax noncompliance is penalized.

A. *Enforcement Action*

The consumer-centric model for use-tax enforcement starts first and foremost with states taking meaningful efforts to enforce the tax.²⁰⁰ Those enforcement efforts should include both coercive enforcement action in the form of audits and litigation, but also educational efforts to ensure that use-tax laws, and punishments for their violation, are known. As discussed above, this is not only a matter of economic imperative but of moral imperative. If the government does not seek to punish those who do not comply with the tax, it has no right to require our Washingtons to pay the tax or to label them as fraudsters or perjurers for failing to do so.

Of course, enforcement action need not necessarily mean a widespread use-tax audit program. States could adopt many small measures to induce compliance. This could include auditing taxpayers' use-tax payments as a part of any income-tax audit or sending taxpayers inquiry letters if they report a suspiciously low, or no, amount of use tax due. States could also use targeted compliance efforts. Professor Leigh Osofsky, for example, has written on the potential benefits of micro-deterrence strategies, and states could experiment

²⁰⁰ This Article's discussion of state enforcement efforts is necessarily brief. The methods in which states can enforce their use taxes implicate concerns in a number of areas discussed in the tax-compliance literature. I have set out a full strategy for use-tax enforcement in a contemporaneous Article. *See generally* Thimmesch, *supra* note 67 (manuscript at 34–49).

with those approaches in lieu of broad campaigns.²⁰¹ Regardless of the approach, states must take meaningful action to enforce their use taxes.

B. Substantive Reform to the Use Tax

State efforts to enforce use taxes will only increase the need for states to reform those taxes to make compliance possible. Without those reforms, enforcement action may serve only to further undermine the morality and unfairness of the tax. Luckily, reform is possible.

The difficulties that taxpayers have complying with use taxes stem from the fact that the use tax is structured as a full complement to the state sales tax. That leads to practical difficulties that prevent taxpayer compliance.²⁰² Consumers simply cannot reasonably track the required data across an entire year, or many years, without unwarranted cost. Full compliance with the tax is thus virtually impossible. There are only two options for salvaging the validity of the tax in this respect—the tax must be scrapped altogether or it must be reformed so that compliance is possible. The former is neither feasible nor advisable. The tax plays an important role in state public finance and is necessary to maintain the efficacy of the state sales tax.²⁰³ To save the legitimacy and morality of the tax, then, states must modify the tax to allow consumers to comply. This likely means exempting certain purchases from the tax or allowing consumers to rely completely on tables issued by the state. Either will require states to accept a tax that does not fully complement the state sales tax.

1. Necessary Use-Tax Exemptions

As discussed above, complying with the use tax is most difficult with respect to purchases made while the taxpayer is physically present in jurisdictions with no or low sales tax rates.²⁰⁴ One way to “fix” the use tax

²⁰¹ See Osofsky, *supra* note 112. The micro-deterrence approach recognizes that enforcement resources are limited and challenges the idea that those resources should be dedicated to the “worst” offenders first. *Id.* at 368–77 (making the case for concentrated enforcement specifically within the cash business tax sector). Instead, targeted, rotating enforcement can increase compliance by making subpopulations compliant and generating norms of compliance from a micro-level. *Id.* at 354–57. States considering such an approach would, of course, need to be concerned with ensuring that its efforts do not violate taxpayers’ notions of procedural justice.

²⁰² See *supra* Part III.C.2 (discussing the difficulties with complying with state use taxes).

²⁰³ This is true despite consumers’ massive noncompliance. First, the tax is collected in a number of situations other than those causing the estimated \$20 billion use-tax gap. See *supra* notes 51–67 and accompanying text (discussing a variety of ways in which the use tax is currently collected). Additionally, the very existence of the tax prevents further shifts to out-of-state purchasing in those areas.

²⁰⁴ See *supra* Part II.B. (showing that “low” sales tax rates, for this purpose, means rates that are lower than the rate of tax that will apply in the jurisdiction of the purchaser’s use).

would thus be for states to provide exemptions from the use tax in one or both of those situations. The more limited approach would be for states to provide a use-tax exemption as long as *some* amount of local sales tax was paid on the purchase of the item. (This would address the plight of our poor Horned Frogs fan discussed above.)²⁰⁵ That exemption would eliminate the need for consumers to track the amount of tax that they pay on all out-of-state purchases and to calculate and pay tax on any differential between that amount and the amount of sales tax that would have been owed if the purchase were made in the state of use. This approach would thus assist greatly in ensuring that consumers stood a reasonable chance of complying with state use taxes.

Only exempting purchases made in low-tax states would, however, still leave taxpayers responsible for tracking their purchases made while physically in *no-tax* states. That different result may be conceptually justifiable—it is certainly easier for a taxpayer to know the use tax that she owes when she paid no sales tax on a purchase than when she paid some amount of tax and must recall that amount. This does not mean that compliance in that situation is simple though, especially when a state does not have a first-use doctrine.²⁰⁶ Consumers would still be required to track their annual activity and to determine the taxability of many transactions over the course of a year or longer. Taxpayers who live near no-tax states would face an especially high burden. Those individuals may frequently travel to those states, and may consequently be required to track a significant amount of out-of-state purchases. Compliance would thus remain virtually impossible even if states exempted purchases on which some amount of sales tax was paid. To fully ensure that individuals are able to comply with use taxes, then, an exemption for *all* purchases made by a consumer while physically out of their home state appears to be proper.

One immediate concern that states may have with a full exemption of the sort just proposed is that it could certainly *cause* consumers to go to their neighboring low-tax states to make purchases. The exemption would thus distort consumer behavior by explicitly giving a preference to that consumption. This would certainly not be favored by local merchants and would raise equity concerns for taxpayers not fortunate enough to live near the border with such a state. These concerns are legitimate, but that situation would bear little difference from the current state of affairs. Purchasers wishing to avoid state sales tax can already travel to neighboring states to make their purchases, and they are not currently paying the required use tax.²⁰⁷ Providing an explicit exemption for those purchases would thus have no real effect on their behavior and would result in only paper losses. The only individuals

²⁰⁵ See *supra* text accompanying notes 43–46.

²⁰⁶ See *supra* notes 48–50 and accompanying text.

²⁰⁷ Research supports the conclusion that current policies do indeed have an impact on consumer shopping behavior. See THE OXFORD HANDBOOK OF STATE AND LOCAL GOVERNMENT FINANCE 416 (Robert D. Ebel & John E. Petersen eds., 2012).

impacted by this exemption would appear to be our Washingtons. Given the opportunity to avoid tax legally, they may do so. What we know for certain, though, is that all of our Washingtons would benefit from not having to worry that their inability to track their liabilities might lead to significant legal offenses. That would be a favorable result.

2. Limitations on Use-Tax Exemptions

Notwithstanding the desirability of the broad-based exemptions proposed above, some limits would be advisable. First, there should be a dollar limit on the applicability of the exemption, on a per-transaction basis. The exemption should not apply to any purchase above \$100 or \$500, for example.²⁰⁸ Recall that the reason for the proposed use-tax exemption is that tracking small purchases is too difficult from an administrative perspective. A consumer who travels across state lines and makes a significant purchase is not in that position. Those types of transactions are much easier to track and recall for tax-reporting purposes. They are also of a type where traveling out of state solely to avoid tax is more likely. For example, a purchaser is much more likely to travel across state lines to save sales tax on furniture or an airplane than on coffee pods. Consumer education on the issue would also be relatively easy. Setting a bright-line threshold creates a clear rule that is easily understood.²⁰⁹

States that would be uncomfortable allowing taxpayers to purposefully avoid tax by making a purchase out of state may be tempted to consider adopting a catch-all provision that denies the exemption to any purchase made with the specific intent of avoiding the use tax. That type of provision would match the purpose of providing the use-tax exemption (i.e., protecting taxpayers from unknown or unknowable liabilities) while not protecting those who purposefully structure their affairs to avoid taxation. The latter group can hardly be said to fall within our group for whom compliance is impossible. A purchase made with the intent to evade tax is a known purchase that can be tracked and on which tax can be paid. For this reason, such a limitation may make imminent sense.

Unfortunately, there are three practical difficulties with such an approach. First, states would have to determine what role a taxpayer's intent to avoid tax would have to play in the purchase. Need it be the sole reason for a purchase or merely a contributing factor? Clearly, taxpayers who purposefully travel to another state to purchase an item without paying sales tax are not

²⁰⁸ The precise amount would be an administrative decision taking into account the state's revenue needs, administrative costs, and impressions regarding consumer responsiveness to tax "breaks."

²⁰⁹ Of course, the bright-line rule would cause price distortion at the margins. With a \$500 threshold amount, one could assume that retailers selling goods in a low-tax state with a high-tax neighbor would gravitate toward \$499 prices for goods in that value range. This type of gamesmanship would be expected at any price point, but should be considered by states when setting their threshold amounts.

unfairly subject to state use tax. However, what about a taxpayer who decides to purchase a coat partially because her location of travel is a bit cold and partially because she can pay a relatively low sales tax? Would that purchase be subject to use tax under an intent-based standard?

The second difficulty with this approach is how it would be administered. How could a state determine the particular intent associated with a purchase? Outside of the most egregious of cases, or those where there is a paper trail for some reason, states will be unable to determine why a purchaser made a particular purchase. Again, the tax would only fall on the most honest.

Finally, an intent-based approach would also raise concerns about the possibility of compliance with the law under the view of morality introduced above.²¹⁰ If a taxpayer cannot know when her intent was “enough,” she cannot be sure that she can comply with the law, and the legitimacy of that law can be called into question. This approach should not be taken unless necessary.

These concerns are worthy and call into question the advisability of an intent-based system. Fortunately, though, states’ concerns leading to such a system would likely be reduced in importance by the use of a dollar limitation on the exemption. It is much more likely that a taxpayer will purposefully structure a purchase to occur out-of-state when an asset of significant value is involved. States should thus focus on adopting specific exemptions with *de maximus* limitations.

3. Tax Tables

Another way for states to make use-tax compliance possible would be for them to stop requiring taxpayers to track their purchases altogether. A number of states currently allow taxpayers to report use tax by relying on tables published by the state.²¹¹ Those tables provide taxpayers with an amount of tax that they are able to report in lieu of determining the actual amount of tax that they owe based on their purchase history. This approach is perhaps the most favorable from an administrative standpoint. It provides taxpayers with clear relief from determining their liabilities and assures the taxing authority that taxpayers reporting that amount have met their obligations. Of course, to provide those benefits, a taxpayer’s use of the table must firmly establish her use-tax liability, but many states that provide tables currently do not follow that approach. They instead retain the ability to audit and adjust the taxpayer’s reported liability.²¹² This practice undermines the benefits of the table approach from the moral perspective introduced above and is not ideal. A taxpayer’s use of a table should be conclusive as to her liability.

²¹⁰ See *supra* Part III.C.2.

²¹¹ See *supra* note 26 and accompanying text.

²¹² See *supra* note 26.

This approach provides administrative benefits for states and taxpayers, but some taxpayers might object to this approach as simply rewriting the substantive law to require a set amount of tax to be paid. A taxpayer who reports any amount less than the amount shown on the table would be inviting an audit, and it would be difficult for such a taxpayer to prove that her liabilities were indeed so low. This could have negative consequences for those with below-average liabilities under current law. Without other reforms to the use-tax system, those taxpayers would effectively have the choice of relying on the table and paying more tax than is owed or attempting to comply by keeping and assembling an incredible amount of information about their annual purchase activity. Reliance on tables, alone, may therefore be a disfavored choice for the psychological reasons discussed above—it may not appear to be a fair option.

The benefits of this approach, however, likely make it worth considering. The clarity of that approach along with its reduction of the costs imposed on taxpayers (in terms of compliance costs) makes this very attractive. Further, data show that more taxpayers report use tax in states with lookup tables than in states without lookup tables.²¹³ Finally, any unfairness to those with below-average liabilities under current law is offset (at least partially) by the additional fairness achieved by implementing a system with which compliance is possible.

4. Other Options

Before concluding this Section, it is important to discuss two other potential reforms that may seem to address the problems addressed herein. First, states could simply provide a *de minimis* exemption to their use taxes. Such an exception would eliminate the requirement that consumers track every single transaction with accountant-like precision and would seemingly allow taxpayers to report their liabilities without worrying that they have missed some trivial transaction. This would be similar to the approach taken by Minnesota, which provides an exception from the use tax for the first \$770 of purchases in a year.²¹⁴

While a *de minimis* exception may seem to provide relief at first blush, it fails upon further inspection. At a very basic level, the only way for a taxpayer to know whether such an exception applies is to track her purchases. Blind reliance on a *de minimis* threshold is no more comforting for our Washingtons than the current system. A *de minimis* exception merely moves the ball; it does not eliminate it.

²¹³ Manzi, *supra* note 4, at 8–10. Although the participation rate is higher in those states, the average amounts of use tax reported on returns in those states was actually lower. *Id.* at 10–11. This suggests that the provision of a table could bring more taxpayers into a reporting posture, but that other efforts should be used to increase their individual compliance rate.

²¹⁴ MINN. STAT. § 297A.67, subd. 21(2) (2015).

The second additional reform option is on much firmer ground. All states should at least adopt statutes or administrative rules that relieve consumers from use-tax liabilities if they have a meaningful use of the property first in another state. This type of exception would address many of the difficulties inherent in trying to comply with state use taxes. At a minimum, it would limit taxpayers' recordkeeping requirements. This type of exception would certainly act to disalign state sales and use taxes, but it would not result in any meaningful lost revenue and it would remove an impediment to respect for the use-tax system.²¹⁵

C. Decriminalizing Use-Tax Noncompliance

As an alternative or complement to the suggestions above, states could address the morality and equity issues currently present in our use-tax system by simply ratcheting down the classification of use-tax noncompliance. Taxpayers who file a tax return knowingly reporting use tax incorrectly are often committing fraud and/or perjury, which are often felonies. That fact alone is problematic. We cannot have an unenforced tax that turns Washingtons into criminals. A state not intending to reform or enforce their taxes should, at the very least, modify how use-tax noncompliance is penalized. If states are going to treat use-tax noncompliance like speeding, noncompliance should carry the same consequences. It should technically be a minor violation carrying with it the same stigma and social cost. This should again, however, be measured with respect to the attitude of our Washingtons. They may not represent the norm, but they represent the ideal. States that can affirmatively reduce the severity of the use-tax offense would go a long way toward addressing the moral and psychological problems with the current use-tax regime.

VI. CONCLUSION

Use-tax noncompliance is rampant, and that situation is generally viewed with helplessness. Obtaining compliance at the individual level seems like a fool's errand while vendor-centric approaches appear to show promise. States have thus focused their energies on the latter by adopting expansive nexus rules and by lobbying for congressional intervention to extend their power. This Article establishes, however, that this generally accepted approach cannot stand. The nonenforcement of state use taxes raises significant economic, moral, and psychological concerns. From an economic perspective, the most probable form of federal intervention would likely close less than one-

²¹⁵ Of course, some intent carve-out could be applied so that taxpayers with very significant purchases could not simply use their property in a low or no tax state for a year and then move it to its final resting place. This practice is used with respect to high-value art, for example. See Graham Bowley & Patricia Cohen, *Buyers Find Tax Break on Art: Let It Hang Awhile in Oregon*, N.Y. TIMES, Apr. 13, 2014, at A1.

half of the use-tax gap. From a moral perspective, states' nonenforcement postures are inconsistent with generally accepted notions regarding the proper exercise of government power. From a psychological perspective, those postures also likely undermine taxpayers' motivations to comply with their existing tax obligations.

Those problems can only be solved, and must be solved, by adopting a consumer-centric approach to the use tax. That approach will require states to reform their use taxes such that compliance will be possible and to enforce those taxes against those who do not comply. This proposal certainly goes against modern thought on how to best address the use-tax gap, but it is the only way to salvage the validity of the use tax and to save it from being the tax on honesty that it currently represents.