

# E-Commerce Taxation Practices In Of United States Of America

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## Abstract

The study highlights the E-commerce practices followed in United States and highlights the taxation principles adopted in United States of America which will help us in understanding different taxation concepts and how to apply them in domestic taxation compliance in developing world especially in Pakistan. Global principles of taxation that are applicable and comparing it with the applicable tax laws in E-commerce sector in Pakistan is the goal of this study. US E-commerce tax practices could be pointed out as a example to the developing countries that this sector needs galvanization, there is also a need of comprehensive policy for collecting taxes from E-commerce sector. Furthermore, facilitation of E-commerce export business will help Pakistan in creating wealth and employment opportunities to people.

**Key Words:** E-commerce, tax, policy, E-market, payment

## (i) Introduction

Globally in the year 2017 alone, it is estimated that about one quarter of the population of the world purchased online goods from different platforms. This amounted to the unprecedented peak of \$29 trillion. It is the highest income derived from online businesses. United States is among the

top users of E-commerce platforms that alone has online sales of \$9 trillion (UNCTD, 2019). Such E-commerce transactions include 88% in terms of Business-to-Business (B2B) transactions and 22% in terms of Business to Consumer (B2C) transactions.

Such big market is transacting online business at global level, and it allows global economies to harvest tax benefit from such big online marketplace (UNCTAD, 2019)

## **(ii) Overview of Taxation in United States**

As a general principle there are two methods of collecting taxes from online sources that is collecting taxes from online marketplaces that offers platforms for buyers and purchasers, the second method of collecting taxes is through online E-commerce stores.

Both these types of taxes are levied on the online platforms and are collected by such stores.

Taxes are levied and collected by the respective states in which such E-commerce stores are registered.

### **(a) Tax Nexus**

There is a concept of nexus through which a state levies tax. There was a shift in policy adopted after *South Dakota vs. Wayfair Inc.* Previously the adopted practice as precedented by *Quill Corp vs. North Dakota* was that the tax will be only levied by the state in which the business had a physical presence. The physical presence of business was held mandatory for taxation and for catalog businesses that went to other states for selling goods, such states could not levy sales tax as the business was registered in another state. However, the shift in the policy was made by the *South Dakota vs Wayfair Inc.* case in which the Supreme Court of United States held that sales tax will be collected by the state in which the consumer resides irrespective of the physical presence of the business. This principle was changed the way taxation was conducted in United States. This new principle is known as nexus taxation. In nexus taxation, an online E-commerce store should be taxed also outside the state jurisdiction. The taxes levied on the online stores is now deductible by the state in which the goods are transferred electronically or via mail order irrespective of where the business is registered. This principle is now applicable for E-commerce stores that have physical presence in one state and are selling their products in other states (*SOUTH DAKOTA v. WAYFAIR, INC., ET AL., 2018*).

### **(b) Exemptions on Tax Nexus**

The precedent set out under *South Dakota v. Wayfair Inc.* laid out many new tax related complications. The E-commerce businesses that were in their infancy period could not cope up with filing tax returns in each state as it would be detrimental for the infant businesses to flourish and compete in the industry. Therefore, it was difficult to levy and comply with the new requirements after the decision. To protect new small and medium sized E-commerce business including small brick and mortar E-commerce stores and other new entrants in the field a minimum

threshold tax rule was applied by many states so the process of registration of E-commerce business will be held mandatory when the business reaches a minimum threshold on transactions. This exemption creates room for economic growth of new entrants and small and medium Ecommerce stores. It also gives them leverage of not filing and auditing tax returns for all the states in which they transact business via online platform.

This exemption is applied by each state differently, some states offer minimum threshold of transactions, and some states offer minimum threshold in terms of transaction revenue.

### **(c) Taxation in States of Registration**

Although there are exemptions on interstate E-commerce transaction, still, taxation is carried out in states where the business is registered. There is a requirement of registration of online business in any one of the state at the minimum. The sales tax levied on E-commerce businesses on online transactions are of three types:

#### **County Tax**

County tax is imposed by the municipality under which such business is registered, and a license is obtained for doing business under such county.

#### **District Tax**

District tax is imposed by the district in which such business is registered and is transacting business.

#### **State Tax**

It is the highest that is imposed by the state in which the business is registered, and each state has different taxation rate for sales, and it varies from state to state.

### **(iii) Destination Structure**

In US, the mode of taxation is a destination taxation structure. When an online product is purchased from any business, the tax will be levied on the place where such product or service is received and not where such product or service is at source. This approach is also diversified in United States. Some states offer destination structure of taxations that is tax should be levied where the product is received or consumed whereas other states suggest that tax should occur at the source from where the product is delivered. This divide on taxation in E-commerce also creates a confusion among other states and the chance of double taxation increases when tax is levied by a state other than the state of registered business where the state comes in the list of source tax

collection. Therefore, mixed taxation system also prevails in United States and comparing it with Pakistan, the service tax levied by the provinces in Pakistan is also the same (Agrawal, 2017).

**(iv) Double Taxation**

There is also a chance of double taxation in United States as some states offer source taxation that is taxation at origin and some states offer taxation at destination. The conflict between states especially in E-commerce business where there is always an influx of interstate transactions taking place. It is very important to understand the dynamics in which USA reports tax evasion is due to the levied double taxation. The same issue is prevalent in Pakistan, and it is always better to take precautionary measures than being at loss.

**(v) Source Based Taxation vs. Destination Taxation**

In source-based taxation, the tax is levied on the business irrespective of where the Ecommerce entity is selling whether in the same state or in any other state. The destination-based structure is based on the principle of taxing where the goods are received and used irrespective of the location of the store. The major issue that comes in destination taxation is regarding tax evasion. The companies liable to pay service tax in states where there is a requirement of a minimum threshold, such E-commerce companies may limit their presence in other states under the given threshold and limit their sales on such states once the limit is capped. As an Ecommerce business is capable to conduct business anywhere in the world and in any state, it is very easy for such businesses to shift their sales from one state to another (Andonga, 2019).

On the other hand, the same principle cannot be applied when the tax is accounted for origin or source of the business. As it is the requirement by law to collect tax from the source in some states. Therefore, it is very easy for such states to collect taxes from the businesses working under their jurisdiction no matter where they are sending their E-commerce products. This approach is also easy for the E-commerce retailers as they must abide by a single tax regime authority of a single state and only have to comply with the requirements of a single state (Andonga, 2019).

**(vi) United States E-Commerce Payment Gateways**

The biggest plus point that can be attributed to the United States E-commerce tax system lies within their payment gateways. There are multiple payment gateways available in the United States that work internationally. These systems are seamless and can be integrated with the Ecommerce system through which the collection and audit of tax return filing has become more efficient than other conventional methods. All these E-commerce stores can keep a track of their online transactions and as most of the transactions occur through proper channel the measurement of tax on transaction with the addresses of the consumers becomes easy. There are hundreds of payment gateways that work in United States and most of these gateways are protected. Compliance of tax becomes easy with such gateways, and it stops tax evasion and growth of informal economy.

### **(vii) Successful Economic Growth**

Many of the big tech giants are from United States including Google, Apple, and Amazon. All these tech giants have contributed to the economic growth of the United States. United States is one of the key contributors in global E-commerce including goods and services. The Ecommerce sector is a growing sector and tax compliance of such platforms are gives economic growth to the country at the best. Such big giants have also provided employment opportunities to many people. Apart from this the growth of E-commerce companies leads to wellbeing of the state.

### **Conclusion**

As we have seen in the study that a minimum threshold of taxation is applicable on states in US and before reaching such threshold, no E-commerce business is required for registration in other states for filing tax returns. It is a major issue is E-commerce taxation, most of the infant Ecommerce businesses could not bear such expenses and it is also against the free marketplace initiative. Tax exemption of small business owners is required for a minimum threshold amount.

As E-commerce is expanding the issues relating to online shopping are also on the rise. This has twofold impact on the E-commerce sector. Number one, the rights of the individuals are violated when any fraudulent act has been encountered by them during online shopping experience. Secondly, once a customer is frauded by any online platform, it creates a bad name for the entire platform. Both these two factors are life threatening to E-commerce growth. As these platforms are taxed, the government should take initiative in creating an online portal for registration of complaints regarding E-commerce frauds.

All taxes leviable on the E-commerce stores should come with easy filing and auditing procedures. Registered businesses can easily comply with the tax requirements. For marketplaces acting as a facilitator should be collecting taxes on behalf of the seller and remitting the same in the sales return. As WHT or withholding tax is the applicable sales tax on the products or services delivered. In marketplace model, such tax should be retained by the marketplace holder and then remitted and filed in the concerned tax collection authority.

Developing countries like Pakistan needs to increase national IT parks throughout the country and initiate provision of certifications for E-commerce as it will provide millions of new jobs if it is done as per international requirements and rules and regulations (Government of Pakistan Ministry of Commerce & Textile, 2019).

Tax compliance should be made but with subject to the Taxation rules. Although the case in USA for taxation held that all states of US can take taxes, there are some bars also and there is a minimum threshold transaction limit after which such tax can be collected and that also varies from state to state (SOUTH DAKOTA v. WAYFAIR, INC., ET AL., 2018)

As discussed above Pakistan, Unlike US, is still in its infancy period of E-commerce and there is yet a lot to be achieved in this sector. Many international marketplaces and payment gateways, operating in US, are not available in Pakistan. The big E-commerce giants are not conducting

business in Pakistan that creates a vacuum, it also creates vacuum as E-commerce is deprived to follow such practices as applied by E-commerce giants. This also deprives Pakistan from earning income from foreign sources and increasing federal reserves of the country (UNCTAD, 2019).

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