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TAXWATCH

Use what?

You probably never think of the 'use' tax, but it's likely you owe it

By [Andrea Coombes](#), MarketWatch

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SAN FRANCISCO (MarketWatch) -- It's not a tax many of us think about, but if you've bought anything over the Internet, from a catalog or abroad, it's likely you owe it.

It's called the "use" tax, and state tax agencies are ramping up their efforts to collect it from taxpayers who often have no idea what it is.

The use tax is the difference between what you would have paid in sales tax if you purchased an item in your own state versus what you actually paid on the purchase. If your state doesn't collect sales tax on a certain item, then you don't owe use tax on it.



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For the most part, states' efforts focus on educating consumers. But states also share information and work with retailers and customs agents to track down taxpayers who've made pricey purchases and never paid sales tax.

As with most things tax, the use tax confuses plenty of people. For instance, many taxpayers think that items they buy on the Internet are untaxed. But it's simply that the retailer is not required to collect the tax.

Retailers are required to collect sales tax if they have a significant presence in the "ship-to" state, but they're not required to if they don't. The buyer is still supposed to pay state sales tax.

"You are supposed to pay it. Do a lot of people not pay it? Yes," said Carol Kokinis-Graves, an analyst in the sales and use tax division at CCH Inc., a Riverwoods, Ill., tax publisher.

"It's incumbent on you to file a sales-and-use tax return and indicate your liability and make your payment, but a lot of people don't," Kokinis-Graves

said. "Do revenue departments find a lot of people? In all likelihood, probably not."

Instead, states focus on large, pricey purchases. Florida, for instance, looks at the bills of lading for trucks heading into the state. State officials "can go through that to see what's on the truck, where it's going and see if the tax has been paid," said Verenda Smith, government affairs official with the Federation of Tax Administrators, an association of tax agencies.

North Carolina and Virginia share information on furniture purchases, she said. "Furniture that gets shipped into Virginia, [taxpayers] are likely to see a bill on that," she said.

States work with customs officials

But plenty of people ignore their use-tax obligations. Many states now include a line on their income-tax return specifically for reporting use taxes, said Bob Scharin, a New York-based senior tax analyst with RIA, of Thomson Tax & Accounting.

The instructions will say, "If you don't have any, put zero," he said. That puts you on the hook, he said. "You can't say, 'Oh, I missed that line.'"

If you buy high-priced items, you'll want to think about the use tax. States often target jewelry purchases, said Diane Yetter, president of Yetter Consulting Services in Chicago, which offers sales-tax consulting to businesses.

Some jewelers offer to ship jewelry specifically so customers can avoid sales tax. Some even take it one step further, offering to ship an empty box to avoid the sales tax, but still let the customer walk out of the store with the item, Yetter said.

"Ironically, how a lot of jewelers get caught is they fail to insure the box, because they're shipping an empty box," she said. Tax auditors now often ask for merchants' shipping documentation and, say, a \$20,000 item shipped without insurance tends to catch their attention.

State revenue departments also work with customs officials to collect tax on purchases made overseas.

"When you come through customs, you report purchases," Yetter said. Customs reports that information to the state revenue department, which then contacts you. "You recently came through customs, you reported \$380 dollars worth of purchases from your recent trip abroad. If any of these items are subject to the use tax," you need to pay, Yetter said.

"I've had some high-wealth individuals that have gotten stuck with that," Yetter said. "They declared \$1,200 worth of goods" and owed a tax of about \$60.

Meanwhile, other states, including Ohio and Tennessee, work with retailers to collect unpaid sales taxes, Yetter said. Some retailers "send records of sales and deliveries to customers within that state to the department of revenue and then the department of revenue sends out bills," she said.

Internet taxes

An effort to simplify states' complex sales tax systems is gaining some ground, making it easier for online retailers to collect sales taxes in more states.

"As a consumer all that means to you is the company you are buying from is more likely to collect the tax from you than they were in the past," Smith said.

Don't confuse the various efforts related to curbing Internet taxes with the use tax. Internet tax discussions often refer to taxing access to the Internet. "That's different from owing use tax if sales tax has not been collected," Scharin said.

What to do

Taxpayers eager to follow the letter of the law should record all purchases they make that are sales-tax free -- if those purchases would generally incur sales tax at home.

In particular, record the large-ticket items that might garner attention from the state's tax collector.

There are other reasons to consider the use tax. "One of my favorite stories comes out of Florida: A man got a bill for jewelry that he had bought overseas," Smith said.

The state tax office heard from customs about the purchase, and sent a bill for the use tax to the man's house. "His wife got the bill -- and it wasn't her jewelry," Smith said. "Things for your girlfriend that you don't want your wife to know about -- that would be a good thing to pay your use tax on."

Sales taxes can be complex. For instance, in California the software you download online is often sales-tax-free but you'll pay sales tax if you buy the same software in a store, Yetter said.

Look on your state's revenue department Web site for more information on what items are subject to sales tax in your area. But consumers don't need to worry all that much about the questionable items, Yetter said.

"If consumers reported tax on the tangible things that they ordered online and had delivered through the mail, I think the states would be ecstatic if they saw the tax on that coming in," she said.

Also, check out the instructions that go with your state's "use tax return" -- they should clarify what you need to include and what you don't. In general, "it's what you pay when you walk out the door and buy it," Smith said.

In some states, such as Illinois, the use tax rate is lower than the sales tax rates. "In Illinois, I only have to pay the state [sales] tax, not all the local taxes, under the use-tax project," Yetter said. ■

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