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Tax rebate deals are bad news for communities

Amazon.com has finally agreed to pay sales taxes to the state of California, but that doesn't mean it has stopped trying to weasel out of...

By Chris O'Brien

San Jose Mercury News

Commentary |

Amazon.com has finally agreed to pay sales taxes to the state of California, but that doesn't mean it has stopped trying to weasel out of paying everything it should. The Seattle-based company is reportedly trying to strike deals with two local communities that would cut the sales taxes it pays, according to recent media reports.

Outrageous, sure, but not unprecedented. In the San Francisco Bay Area, there are several companies that either have similar deals or have their hands out asking for them, including Apple and Netflix. In such an arrangement, a company agrees to funnel more of its sales through a city and the city agrees to refund some portion of the extra sales-tax money it's getting back to the company.

Nobody knows how common such arrangements are. California State Sen. Mark DeSaulnier, a Democrat who is thinking of introducing a bill to stop or limit such deals, said his office is trying to figure out the extent of their use.

"It really hurts the general public who are their customers and shareholders because our infrastructure is falling apart," DeSaulnier said.

Here's the background, based on stories in both the Los Angeles Times and The Sacramento Bee that have reported on Amazon's plans.

After ducking sales taxes for years, Amazon reached a settlement last year with the state of California to start collecting them. That will add roughly \$150 million a year to state coffers. But it's trying to cut that tax bill. Here's how:

The state collects sales taxes of 7.25 percent. It returns 1 percentage point of that haul back to the city where the sales occurred.

The question is how Amazon will split its California sales between the two cities in which it is building distribution centers, Patterson and San Bernardino. So to sway Amazon's decision, both are reportedly considering offering big tax rebates.

Offering such deals is tempting for the cities, because even after the rebate they could get a big boost in sales-tax revenue. It's a great deal for Amazon, which cuts its total sales tax bill. But the city not picked could get far less tax revenue than it had expected.

Other companies

Amazon's not alone. Last year, San Jose, Calif., agreed to negotiate such a deal to entice Netflix to move its DVD division from Los Gatos, Calif. — where it paid sales taxes on DVD rentals but not video streaming — to San Jose. The city was planning to offer to refund Netflix 50 percent of new sales taxes it collected from the move the first year, 40 percent the second year, and 30 percent the third year, capped at a total of \$5 million.

That deal fell through when Netflix decided not to spin off its DVD business (the ill-fated "Qwikster" deal). Instead, Los Gatos will pocket about \$1.5 million in sales-tax revenue it expected to lose if the San Jose move had happened.

Kim Walesh, San Jose's director of economic development, said this was the first time the city had extended such a deal, and it did so only because the state's decision to end redevelopment agencies has left local governments with few economic incentives to offer.

"I wouldn't say we had qualms about doing this," Walesh said. "Sharing net new revenue you wouldn't have otherwise, it's a logical thing for a city to do."

Apple's deal

The size of the Netflix deal, however, would have been dwarfed by the one that exists between Apple and Cupertino, Calif. The city signed the original five-year deal in 1997, when Apple was contributing only \$50,000 annually in sales-tax revenue to the town.

Cupertino agreed to refund half of the Apple sales taxes it received in exchange for Apple assigning more of its sales to Cupertino.

The city renewed the deal in 2002 and again in 2007. It's set to expire this year, but this week the City Council is expected to grant a temporary extension to give city staff time to negotiate a new one. Under the most recent deal, the percentage of revenue Cupertino gives back to Apple increases as new tax revenues increase.

For instance, if Apple generated \$250,000 in new sales taxes for Cupertino, the city would refund \$62,500. If Apple generated more than \$2 million in new sales taxes in a given year, Cupertino would return as much as \$862,500.

Apple's actual sales-tax bill is unknown because that information is not public. The company had no comment.

And in fairness, the company has been loyal to Cupertino, rising to become the city's largest source of sales-tax revenue.

Question of need

And yet, I can't help but wonder: Does the world's most valuable technology company really need such a break at this point?

Carol Atwood, Cupertino's director of administration, said the city has been happy with the deal and a second similar deal it offered to another tech company, but otherwise has discouraged other companies from requesting them. "We've said, 'No, thank you,' " Atwood said.

Still, other cities may be more amenable. Now is the time for the state to stop them. Local governments have enough problems without cannibalizing each other's already shrinking pies.

Chris O'Brien is a columnist at

the San Jose Mercury News.

He can be reached at cobrien@mercurynews.com