

Electronic commerce

BY KEON S. CHI

In the past few years, the number of businesses and consumers shopping online has increased at an astonishing rate. Two years ago, for example, only 5 million households purchased goods and services via the Internet. In the next four years, an estimated 49 million U.S. households are expected to shop electronically. Online retail sales of \$20 billion in 1999 are expected to increase to \$184 billion by 2004. Today's typical electronic customers are male, better educated and have higher incomes, but the gap in buyers based on gender, age and Internet access — the so-called "digital divide" — is narrowing. More women, teen-agers and people without household Internet access are expected to join the rising tide of e-commerce.

Much is speculation, however. U.S. Secretary of Commerce William M. Daley wrote in *The Emerging Digital Economy II*, "We are not able to give a complete picture of the Internet's effects on our economy."

To develop rational tax policies on e-commerce at all levels of government, Congress passed and President Clinton signed the Internet Tax Freedom Act of 1998. The act created the Advisory Commission on Electronic Commerce and charged it to report to Congress by this April. In the meantime, the federal government placed a three-year moratorium on state and local taxation on e-commerce.

Representatives of state and local government organizations argued before Congress that the moratorium unfairly pre-empted their authority. At Advisory Commission meetings, state and local governments have called for levying state sales and use taxes on e-commerce on several grounds:

- Internet remote sellers should not be given a tax advantage over and should be treated the same as local merchants.
- Imposition of sales and use taxes on e-commerce is necessary for a level playing field for all customers.
- If left untaxed, e-commerce as it grows would further erode the sales-tax base of many state and local governments.
- Although dealing with numerous taxing jurisdictions is challenging for multistate, remote sellers, there is software available to do the job.
- If states and local governments cannot collect sales and use taxes on e-commerce, the substantial revenue losses would affect public services.

Opponents of e-commerce taxation contend that sales and use taxes on e-commerce would reduce the volume of online retail sales, negatively affecting the economy.

The strongest arguments against taxing e-commerce relate to the administrative burdens imposed on sellers by differing tax rates and tax collections for more than 7,000 state and local taxing jurisdictions.

So, the issue is: How can state and local governments reform their sales tax systems to deal more effectively with e-commerce? Many reformers propose the following:

- Adopt uniform policies on tax rates (such as a single tax per state), vendor registration, tax remittance and audit requirements, exemptions for business purchases and definitions of products and services.
- Simplify state and local sales and use tax systems by eliminating tax compliance burdens for remote sellers, especially in tax returns, payments, tax audits, tax-rate monitoring and record-keeping requirements.
- Shift e-commerce sales tax administration to third-party entities, such as software and credit card companies. For example, software would automatically figure out the sales tax on an Internet purchase based on destination and then charge it to the buyer's credit card. The credit-card company would then isolate and transfer the taxes to the state or local taxing jurisdiction.

• Adopt uniform legislation on e-commerce taxation either on a regional or national basis by states themselves before Congress makes permanent the current moratorium on e-commerce taxation.

States should be aware of what is taking place in Congress with regard to e-commerce. Recently, Congress passed a resolution urging the U.S. government to seek an international ban on e-commerce taxes. Some members of Congress filed bills to outlaw any attempts to impose sales taxes on online purchases.

States should resist a tax-free zone for e-commerce. Creating such a tax-free zone would be the beginning of the end of state and local sales taxes in most states.

Finally, states should review the proceedings and final report of the Advisory Commission on Electronic Commerce. They should work with representatives of state and local government organizations to launch regional or national campaigns to streamline current sales and use tax systems to preserve their authority to tax e-commerce.

Note. Available is a new CSG report *Electronic Commerce: Revenue Implications for States*, C200-9900, \$20 from publications sales, (800) 800-1910 or CSG's online store, www.csg.org.



A federal ban on taxing e-commerce sales threatens state and local government revenues.

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