

Internet Tax Simplification: *Is It Really That Simple?*

Don't be confused—the Internet access tax and sales tax are not the same thing. The persistent pairing of access tax and sales tax has created confusion for far too long. It's time to separate and define these issues in simple terms. Sales tax is what a purchaser pays as part of a transaction. Dial-up Internet access is already taxed for the universal service fund and by federal and state excise taxes, so a new internet access tax would amount to double taxation. New taxes on broadband Internet access would raise the cost of cable, wireless, DSL and satellite, putting them further out of reach for lower income households. With all the benefits that broadband access can bring to teleworkers and e-commerce users, our nation should not impede broadband adoption by adding new Internet access taxes.

Consumers buy from catalogs and websites because of better selection, information, convenience and savings -- not to avoid paying sales tax. Online and catalog consumers will stay and pay if remote sellers are forced to collect sales tax from out-of-state shoppers. But state and local governments will be sorely disappointed if they expect vast new revenues as a result of taxing their citizens' out-of-state purchases. The Direct Marketing Association released a study in March 2003 estimating that actual collections would amount to less than 10% of figures stated in a University of Tennessee study. The UT study assumed growth rates of internet bubble exuberance, and included B2B transactions which already have high compliance for the collection of use taxes. The idea of collecting sales tax on remote purchases may sound great, but states will discover it's less filling.

When weighing costs and benefits of remote sales tax, size matters. "Big box" retailers Wal-Mart, Toys"R"Us and Target made headlines in February 2003 by starting to collect sales tax on online purchases from states where they have operations. These retail giants aren't being sympathetic to state tax commissioners—they're responding to the market demands of cross-channel consumers. A Forrester study found that "83% of US cross-channel consumers say that the ability to return items purchased at online at offline stores is important."¹ Sales tax collection is inevitable for websites associated with national retailers, but smaller retailers have neither the nexus nor the necessary scale to justify collecting small amounts for so many tax jurisdictions. And while "tax simplification" effort may reduce the costs, there is nothing simple about integrating and maintaining the new system alongside existing retail web sites. The "simple" point is that costs borne by small sellers in collecting and remitting remote sales taxes may be too high to justify.

Policy recommendations for Internet tax

- **Extend the moratorium on Internet access taxes—separate from any action on remote sales tax collection.** Taxes on Net access would twice tax lower income dial-up users, and would retard broadband adoption and deployment. The moratorium on access tax should be made permanent to reduce costs for consumers and retain incentives for firms to keep deploying broadband infrastructure.
- **States don't need new powers to increase collection of sales taxes due.** Use tax compliance is extremely high on B2B purchases, and states can do more to collect use taxes on online and catalog sales. Many large, national chains already have nexus in most states, so their remote sales could be taxable without requiring any new powers from the federal government. Beyond B2B and national chain sales, there's just not much more to be gained by forcing smaller remote sellers to collect sales taxes.
- **Take into account differing burdens of small and large sellers.** Any federal mandate to require remote sales tax collection should be cognizant of the differing costs and potential collections for small versus big sellers. Ensure that smaller entrepreneurial e-commerce players aren't crippled with compliance costs by any plans to collect and remit for thousands of taxing jurisdictions.

¹ The February 7, 2003 Forrester Brief "The Internet Tax Man Cometh – Who Cares?"