No. 1343 February 4, 2000

The NGA's Misguided Plan to Tax the Internet and Create a New National Sales Tax

Adam D. Thierer

A heated showdown over the taxation of the Internet is taking place within the Advisory Commission on Electronic Commerce (ACEC), appointed by Congress under the Internet Tax Freedom Act of 1998 to study the feasibility of taxing the Internet and electronic transactions. The commission's final report to Congress is due in late April. So far, however, members have been unable to reach meaningful consensus on substantive recommendations, and they remain bitterly divided on the central issue: Should sales taxes be applied to electronic commerce?

Members of Congress therefore must prepare once again to address the issue of Internet taxation. As they do so, they should remember their constitutional obligation to protect both the sovereignty of state and local governments and the free flow of interstate commerce. The ACEC and Congress can achieve these objectives by adopting a plan that:

- **Does not impose** discriminatory or burdensome taxes on interstate commerce;
- **Eliminates** or radically reforms existing telecommunications sector taxes;
- **Protects** constitutional principles and Supreme Court precedents of fair taxation;
- **Adopts** a sound "nexus" standard that makes it clear which forms of sales taxation are legitimate;
- **Encourages** vigorous jurisdictional tax competition;
- **Does not violate** individual or corporate privacy; and
- **Allows** the Internet to continue to grow and thrive.

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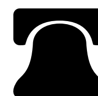

This paper, in its entirety, can be found at: *www.heritage.org/library/backgrounder/bg1343es.html*

On each of these counts, the leading plan currently before the ACEC moves in the opposite

direction. Offered by the National Governors' Association (NGA), this plan encourages the states to devise a system for the extraterritorial collection of sales taxes on Internet sales and, eventually, all forms of retail commerce. It is economically illogical and constitutionally suspect because it:

- **Creates** a new de facto national sales tax cartel;
- **Violates** constitutional first principles regarding tax fairness and commercial union;
- **Upsets** existing Supreme Court commercial jurisprudence;
- **Threatens** America's federalist structure of government by discouraging jurisdictional tax competition;
- **Creates** a "Trusted Third Party" tax collection system that could compromise individual and corporate privacy;
- **Is unnecessarily complex** and could be extremely costly to implement;
- **Is not "voluntary"** as the NGA claims; and
- **Is at odds** with the Clinton Administration's proposed "global free trade zone" for international commerce and could threaten American sovereignty.

The NGA plan is premised on two myths: that the Internet is a massive drain on state and local tax revenues and that it is unfair to exempt interstate vendors of commerce from taxes that Main Street businesses must pay. In reality, state and local tax revenues and budget surpluses are at an all-time high thanks to a high-tech Internet economy that has fueled unprecedented levels of economic growth and job creation. Additionally, out-of-state vendors of electronic commerce, though subjected to the same tax burdens that Main Street vendors must bear, would receive no benefits for the taxes they paid to state and local governments where they did not reside. This amounts to a form of taxation without representation.

The NGA proposal would subject Internet vendors—and all retail commerce—to an unprecedented, unconstitutional, and economically illogical system of sales tax administration. ACEC members and congressional policymakers would be wise to examine the NGA plan and others like it in light of a question posed by Federal Trade Commissioner Orson Swindle during the commission's New York City meeting: "Should policymakers apply a Depression-era tax system to the economy of the 21st Century?"

Because this is exactly what the NGA plan would do, both the ACEC and Congress should reject it and seek instead to establish a plan that allows state and local governments to impose sales taxes only on those Internet companies that have a physical presence or "taxable nexus" within their jurisdictions. Such an origin-based system of sales tax administration would be consistent with the Constitution and Supreme Court jurisprudence. It also would eliminate any perceived need to create the sort of inefficient and burdensome national sales tax system that has been proposed by the National Governors' Association.

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Adam D. Thierer

A heated showdown over the taxation of the Internet is taking place within the Advisory Commission on Electronic Commerce (ACEC) as opposing forces offer competing plans for eventual consideration by Members of Congress. The ACEC, which was appointed by Congress under the Internet Tax Freedom Act of 1998 to study the feasibility of taxing the Internet and electronic transactions, is required to submit its final report to Congress by late April of this year.

The commission, which consists of 19 members from the business community, government, and trade and political associations, has been unable to achieve any sort of meaningful consensus or substantive recommendations on these issues in meetings held in Williamsburg, Virginia; New York City; and San Francisco, California. A final meeting is scheduled for March 20 and 21 in Dallas, Texas.

Members of Congress must prepare once again to address the issue of Internet taxation since it appears increasingly unlikely that the bitterly divided ACEC will be able to produce a consensus plan before submitting its final report. Once the ACEC report is sent to Congress, federal lawmakers will have less than 20 months to consider what actions should be taken before the temporary three-year moratorium on "multiple" and "discriminatory" Internet taxes expires in October 2001.

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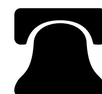

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As Members of Congress prepare for this battle, they should remember that they have a constitutional obligation to uphold the Founders' original federalist framework by protecting both the sovereignty of state and local governments and the free flow of interstate commerce. The ACEC and Congress can achieve these objectives by adopting a plan that:

- **Does not impose** burdensome new taxes on interstate commerce;

- **Eliminates** or radically reforms existing telecommunications sector taxes;
- **Protects** constitutional principles and Supreme Court precedents of fair taxation;
- **Adopts** a sound "nexus" standard that makes it clear what forms of sales taxation are legitimate;
- **Encourages** vigorous jurisdictional tax competition;
- **Does not violate** individual or corporate privacy; and
- **Allows** the Internet to continue to grow and thrive.

On each of these counts, the leading plan currently before the ACEC moves in the opposite direction. Offered by the National Governors' Association (NGA), this plan encourages the states to collude in devising a system for the extraterritorial collection of sales taxes on Internet sales and, eventually, all forms of retail commerce. The NGA plan is economically illogical and constitutionally suspect because it:

- **Creates** a new *de facto* national sales tax cartel;
- **Violates** constitutional first principles regarding tax fairness and commercial union;
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- **Is unnecessarily complex** and could be extremely costly to implement;
- **Is not "voluntary"** as the NGA claims; and
- **Is at odds** with the Clinton Administration's proposed "global free trade zone" for international commerce and could threaten American sovereignty.

ACEC members and congressional policymakers would be wise to consider the NGA plan and others like it in light of a question posed by Federal Trade Commissioner Orson Swindle during the commission's New York City meeting: "Should policymakers apply a Depression-era tax system to the economy of the 21st Century?"[1] Because this is exactly what the NGA plan would do, it should be rejected.

Instead, the ACEC and Congress should formulate a plan that allows state and local governments to impose sales taxes only on those Internet companies that have a physical presence within their jurisdictions. Such an *origin-based* system of sales tax administration would be consistent with the Constitution and Supreme Court jurisprudence. It also would eliminate any perceived need to create the sort of burdensome and inefficient national sales tax system that has been proposed by the National Governors' Association.

GRIDLOCK ON THE ADVISORY COMMISSION

In anticipation of the ACEC's recent San Francisco meeting, numerous proposals were submitted for its consideration. The two most notable plans were offered by two governors who serve on the commission—Mike Leavitt (R–UT) and James Gilmore (R–VA). Governor Gilmore also serves as chairman of the ACEC. Ironically, while Governors Leavitt and Gilmore share a common philosophy on most political issues, their plans for taxing the Internet are diametrically opposed to each other and have polarized opinions both on and outside of the commission.

Governor Leavitt champions a proposal introduced recently by the National Governors' Association, "A Streamlined Sales Tax System for the 21st

1. Orson Swindle, "Taxation of E-Commerce," address to the Browning Symposium, University of Montana, October 15, 1999, at *http://www.ftc.gov/speeches/swindle/montana.htm*.

Century."[2] Governor Leavitt also serves currently as chairman of the NGA. Many other state and local officials and representative groups, both on and outside of the commission, support the Leavitt–NGA plan.

The Leavitt–NGA plan proposes to expand existing sales tax collection requirements so that interstate or "remote" vendors of electronic commerce would have to collect and remit sales taxes to states and localities where they do not reside. To facilitate the collection of Internet taxes, independent "Trusted Third Party" tax collection agents would calculate and collect the taxes on e-commerce transactions using computer software. Although the NGA plan says this would be "voluntary," it also includes numerous incentives to encourage states and remote vendors to join the system. The states would have to develop a system of uniform product classification and work to harmonize other state tax policies through multi-state compacts to ensure that the system worked nationwide. Eventually, the plan would be extended to cover all retail merchants, including mail order catalog sales and more traditional "bricks-and-mortar" retail sales.

This proposal represents an unprecedented form of extraterritorial taxation by the states, yet the NGA argues that such a system is required to equalize the tax treatment of multi-state "cyber-vendors" and "Main Street" or "bricks-and-mortar" merchants. The governors further claim that this new sales tax system is needed to ensure that the continued growth of tax-free Internet commerce does not deprive state and local government of tax revenues as more and more consumers begin to shop on-line.

Although these "fairness" arguments are easily debunked, they continue to drive the debate over Internet taxation. In fact, the eagerness of many state and local officials to begin taxing Internet sales was evidenced dramatically during the recent ACEC meeting in San Francisco, when South Dakota Governor William Janklow (R), testifying on behalf of the National Governors' Association, warned that "the bottom line is ultimately we're going to start stopping little brown trucks and going to start examining these packages" delivered via UPS (and presumably Federal Express or the U.S. Postal Service) to determine whether taxes were paid on each purchase.[3]

Although it is unclear whether America's governors and mayors will begin to take such drastic steps to monitor commercial transactions, Governor Janklow's fears and frustrations regarding electronic commerce illustrate the prevailing mood among state and local officials. What is clear is that the NGA's claim that state and local revenues would be severely depleted without massive new Internet taxes is without merit. As the Internet sector has grown and created new businesses and jobs, state and local tax revenues have been increasing, not shrinking.

Taxing the Internet, therefore, could amount to "shooting the goose that lays the Golden Egg," since it might destroy the entrepreneurialism in this sector that has helped to fuel record levels of economic growth, which in turn has helped to fuel record levels of state and local budget surpluses. An important recent study by Austan Goolsbee, an economist with the University of Chicago, has shown that applying existing sales taxes to the Internet would reduce the number of on-line buyers by almost 25 percent and reduce on-line Internet spending by as much as 30 percent.[4]

Driven by this logic, considerable opposition to the NGA plan has developed, both within the ACEC and within the public policy arena.[5] Most notably, Governor Gilmore has introduced a "No

2. "Streamlined Sales Tax System for the 21st Century," National Governors' Association, November 1999, at *http://www.nga.org/Internet/Proposal.asp*.
3. Quoted in Joyce E. Cutler, "State, Local Governments Fear Tax Ban Will Threaten Revenues, Sovereignty," *BNA Daily Report for Executives*, December 16, 1999, p. GG1.
4. Austan Goolsbee, "In a World Without Borders: The Impact of Taxes on Internet Commerce," National Bureau of Economic Research *Working Paper* No. 6863, November 1998.

Internet Tax" proposal for the commission's consideration. [6] This plan:

- **Prohibits** sales taxes on remote Internet-based sales of goods, services, and information to consumers;
- **Recommends** that other federal, state, and local telecommunications taxes be abolished and that a clear legal "nexus" standard (or physical presence standard) be adopted by the commission to determine when a state or locality has the right to tax Internet companies;
- **Proposes** that the revenues generated from a portion of an existing federal excise tax on telecommunications companies be used to funnel roughly $1.7 billion back to the states this year (which, if the tax remained in place, Governor Gilmore estimates would redirect roughly $3.4 billion back to the states a decade from now);
- **Addresses** the so-called digital divide by allowing the states to spend federal welfare dollars to purchase computers and Internet access for poor families; and
- **Discourages** the imposition of international taxes and tariffs on electronic commerce.

While many other pro- and anti-tax proposals have been submitted to the commission for consideration, the Leavitt and Gilmore proposals are likely to define the framework for the ongoing debate over Internet taxation, not only within the public policy arena, but also more broadly within the media and the general public. The disagreement between Governors Leavitt and Gilmore, notes Associated Press tax reporter Curt Anderson, "mirrors the national debate involving billions of dollars in commerce that has split political parties, become an issue in the 2000 presidential race and pitted government officials against high-tech entrepreneurs."[7]

While Congress has been able to avoid taking sides in this heated feud, federal lawmakers must again prepare to address the issue of Internet taxation since it appears increasingly unlikely that the bitterly divided ACEC will be able to produce a consensus plan before issuing its final report to Congress in April. As the debate over Internet taxation once again resumes within Congress, policymakers will have the opportunity to discuss the problems associated with the current sales tax system and to determine whether and how to apply this system to the Internet sector and the modern Information Age economy in general.

WHY THE CURRENT SALES TAX SYSTEM MUST BE REFORMED

The NGA's proposed "Streamlined Sales Tax System for the 21st Century" begins with a candid assessment of sales tax administration within the United States:

> The current system of state and local sales tax administration is complex and burdensome. Differences in tax law among the states, coupled with the extensive use of the tax by local governments in many states, impose a significant compliance burden on multistate sellers, a burden for which they are not compensated in many instances. The tax system has not kept pace with changes in the U.S. and global economy and is particularly out of step with electronic commerce.... Substantial changes are necessary if the sales tax is to continue as an integral part of the state and local revenue system.[8]

5. See "Debate: NGA's Shafroth, Heritage's Thierer on Streamlined Proposal, Origin-Basing for E-Commerce," *State Tax Notes*, Vol. 18, No. 4 (January 24, 2000), pp. 279–290.
6. "No Internet Tax," A Proposal Submitted to the "Policies & Options" Paper of the Advisory Commission on Electronic Commerce, Governor James S. Gilmore III, November 8, 1999, at *http://www.state.va.us/governor/newsre/nitprop.htm*.
7. Curt Anderson, "GOP Govs. Divided on Internet Taxes," Associated Press, November 16, 1999, at *http://dailynews.yahoo.com/h/ap/19991116/tc/internet_taxes_3.html*. See also John Simons and John Harwood, "Bush Faces Wedge Issue as GOP Rivals Focus on Question of Taxing Internet," *The Wall Street Journal*, December 6, 1999, p. A36.

Few analysts would disagree with this critique. Ernst & Young tax economists Robert J. Cline and Thomas S. Neubig, for example, note in an important recent study that "the complex system of unique sales and use taxes in 46 different states and almost 7,500 local governments imposes significant compliance cost burden on retailers."[9] Moreover, "these figures represent the units of government imposing sales and use taxes today," and "there is potentially a much larger problem if every unit of government that exists chose to impose a sales and use tax."[10] To put this statement into perspective, as of 1997 there were 87,453 different units of government throughout the United States (3,043 counties, 19,372 cities, 16,628 townships, 13,726 school districts, and 34,683 special districts).

Table 1 B1343

Nearly 7,500 Local Governments Impose Sales and Use Taxes

Type of Jurisdiction	Number Imposing Sales Tax in 1999
State	46
Cities	4,696
Counties	1,602
Other Jurisdictions	1,113
Total	7,458

Source: Ernst & Young LLP.

Several factors associated with the current sales tax system combine to impose significant compliance costs on businesses, especially multi-state retailers. Cline and Neubig note that "high compliance costs result directly from complexities built into each component of the sales tax system: definitions of what is taxable, multiplicity of tax rates, numerous exemptions for specific buyers or uses, overlapping jurisdictions, filing requirements and audit procedures."[11] Specifically, "For firms selling nationally with collection responsibilities in all 46 states, the compliance costs range from 14 percent of sales tax collected for large retailers, to 48 percent for medium retailers, and 87 percent for small retailers."[12]

This is the "significant compliance burden on multi-state sellers" described in the opening paragraphs of the NGA proposal, yet the Leavitt–NGA plan does little to alter the nature of that system. In fact, although it calls for "substantial changes" to correct the existing system's flaws and make sure that state and local tax collection mechanisms keep pace with changes in the modern economy, the proposal would simply extend and expand the status quo.

The NGA plan would do this primarily by shifting the burden of collecting sales taxes from sellers to independent private-sector entities or "Trusted Third Parties." Over the next two to five years, the plan would then establish a "burdenless system of collecting sales taxes *that are owed by purchasers* [emphasis added]." This language is important because it makes clear the governors' intention, under the new system, to tax remote sales or out-of-state commerce in general.

In tax jargon, the NGA plan is a *destination-based* system of interstate sales tax collection. This means that the states would impose the tax at the buyer's rather than the seller's end of the transaction. For a variety of historical reasons, it has been argued that sales taxes are imposed at the point of

8. "Streamlined Sales Tax System for the 21st Century," National Governors' Association, at *http://www.nga.org/Internet/Proposal.asp*.

9. Robert J. Cline and Thomas S. Neubig, *Masters of Complexity and Bearers of Great Burden: The Sales Tax System and Compliance Costs for Multistate Retailers*, Ernst & Young LLP, September 8, 1999, p. i.

10. *Ibid.*, p. 12.

11. *Ibid.*, p. iii.

12. *Ibid.*

consumption instead of the point of sale. In reality, however, this is a distinction without a difference. For *intra*state sales—sales that take place entirely within a single state—the point of sale and point of consumption are virtually the same because the sale and consumption of a good or service typically take place in the same geographical area. In a sense, therefore, as Andrew Wagner, staff director of tax law with the FDX Corporation, and Wade Anderson, former director of tax policy for the Texas Comptroller of Public Accounts, have noted, "it can be strongly argued that the state sales taxes in most states already begin with a point-of-origin sales tax, then default to the destination state in the case of interstate sales."[13]

When a good or service is purchased through interstate means (mail order, catalogs, telephone sales, or the Internet), the logic of a destination-based system of sales taxation becomes more problematic. This is because relevant clauses of the U.S. Constitution and a variety of important Supreme Court tax decisions (see below) have prohibited states from collecting taxes from remote vendors outside their states.

This has not stopped state and local officials from attempting to find ways to collect taxes on remote sellers through other mechanisms. Specifically, many states and localities impose a "use tax" on out-of-state purchases by consumers, including mail order catalog sales, direct telephone or television sales, or magazine subscriptions. "Very simply, use taxes are levied on goods and/or services that are purchased out of state or out of town, but used or consumed within the state or locality," summarize Ronald John Hy and William L. Waugh, Jr., authors of *State and Local Tax Policies: A Comparative Handbook*.[14] "Use taxes permit states and localities to regain monies lost when firms or individuals choose to make purchases elsewhere to avoid local taxes or simply to avail themselves of lower prices."[15]

In practice, however, use taxes are difficult if not impossible to enforce since their administration is extremely complicated. As Saba Ashraf, an associate with the New York law firm of Winthrop, Stimson, Putnam & Roberts, has noted in the *Florida State University Law Review*, "Collecting the use tax from the purchaser, particularly where the purchaser is an individual, is often inefficient and not cost-effective. This is especially so because many consumers do not realize they are subject to the tax."[16] Consequently, few consumers comply with use tax requirements.

Moreover, note Hy and Waugh, "The problems inherent in defining locations of sale, delivery, and/or use of goods and services make it very difficult for a local government to administer a use tax effectively."[17] These problems are exacerbated by the rise of the Internet and electronic commerce, since it is becoming even more difficult to determine where "consumption" or "delivery" of goods and services takes place. For example, if a software program is electronically transmitted directly to a consumer and wirelessly uploaded directly onto the consumer's laptop computer while he or she is travelling by train, where is "delivery" of the good taken?

As Dean Andal, member of the ACEC and vice chairman of the California State Board of Equalization, has argued, "In the purely digital world, where both the consummation of the agreement and the exchange of the product or service occurs on-line, location is not just irrelevant; it can be

13. Andrew Wagner and Wade Anderson, "Origin-Based Taxation of Internet Commerce," *State Tax Notes*, July 19, 1999, p. 190.

14. Ronald John Hy and William L. Waugh, Jr., *State and Local Tax Policies: A Comparative Handbook* (Westport, Conn.: Greenwood Press, 1995), p. 102.

15. *Ibid*.

16. Saba Ashraf, "Virtual Taxation: State Taxation of Internet and On-Line Sales," *Florida State University Law Review*, Vol. 24, No. 3 (Spring 1997), p. 611.

17. Hy and Waugh, *State and Local Tax Policies: A Comparative Handbook*, p. 106.

impossible to determine."[18] Cline and Neubig note that

> Identifying where consumption occurs will become increasingly more difficult in the Internet environment where products can be delivered electronically without knowledge of the purchasers' residence and payment can be made in ecash. Ecommerce has the potential to create a large and growing set of retail transactions that may be impossible or costly to attribute to a specific location.[19]

The Key Issue: Nexus

Again, however, even if one assumes that enforcement of use taxes on out-of-state commerce is technically feasible (and many states are attempting to step up enforcement efforts), the constitutional question of taxable "nexus" remains. In such cases as *National Bellas Hess, Inc.* v. *Department of Revenue of State of Illinois* (1967),[20] *Complete Auto Transit, Inc.* v. *Brady* (1977),[21] and *Quill Corp.* v. *North Dakota* (1992),[22] the U.S. Supreme Court has held that a state or local government can tax a corporation only if it has a "substantial nexus," or clear physical presence, within the geographic confines of that state or locality.

In *Complete Auto Transit*, the Court established a four-part test to determine whether a state sales tax would be considered constitutional. Specifically, for a sales tax to pass constitutional muster, it:

1. Must be applied to an activity with a substantial nexus with the taxing state;
2. Must be fairly apportioned;
3. Must not discriminate against interstate commerce; and
4. Must be fairly related to the services provided by the state.

The logic behind the Court's framework in *Complete Auto Transit* flows directly from the Commerce Clause of the U.S. Constitution, which empowers Congress to keep the lanes of interstate commerce free of burdensome state taxation and regulation. "The very purpose of the Commerce Clause," as the Court noted in *National Bellas Hess*, "was to ensure a national economy free from…unjustifiable local entanglements. Under the Constitution, this is a domain where Congress alone has the power of regulation and control." In *Quill*—its last major decision dealing with interstate mail order sales—the Court found that "the underlying issue is not only one that Congress may be better qualified to resolve, but also one that Congress has the ultimate power to resolve."

As the law now stands, therefore, no matter how great their desire to tax remote vendors of commerce, state and local officials simply do not have the constitutional right to do so under current Supreme Court interpretations of the Constitution, particularly the Commerce Clause. As the Court concluded in *Quill*, "Congress is now free to decide whether, when, and to what extent the States may burden interstate mail-order concerns with a duty to collect use taxes."

Why the NGA Wants to Expand the Current System

Under an origin-based (or "seller-state") system, state and local governments could levy a sales tax at the point of sale on transactions made by companies that have a substantial physical presence within their borders, regardless of whether those sales were made to in-state or out-of-state

18. Dean Andal, *A Uniform Jurisdictional Standard: Applying the Substantial Physical Presence Standard to Electronic Commerce*, presentation to the Advisory Commission on Electronic Commerce, September 15, 1999, revised November 5, 1999, p. 13.

19. Cline and Neubig, *Masters of Complexity and Bearers of Great Burden*, p. 24.

20. 386 U.S. 753 (1967).

21. 430 U.S. 274 (1977).

22. 504 U.S. 298 (1992).

customers. They would not be allowed to tax sales by remote out-of-state vendors inside the state. In other words, they could tax the exports of companies based in their jurisdictions but not imports from other states. There would be no difference in tax treatment between a "Main Street" vendor and an Internet "cyber-vendor" within the state. Because all sales made by companies within a given jurisdiction would be taxed equally, a "level playing field" would exist.

Why, then, would the NGA want to apply destination-based sales or use taxes to Internet transactions or interstate transactions in general? The primary justification is political: It is more politically palatable to tax imports than to tax exports. Taxing electronic commerce (or any interstate transaction) at the destination or consumption end in an extraterritorial manner would allow state and local governments to target out-of-state vendors while simultaneously exempting companies located within their own taxing jurisdictions from sales taxes on the goods or services they sell and export out-of-state.

Many state and local officials feel that an origin-based system would constrain their ability to tax out-of-state vendors and force them to make tough political decisions within their own jurisdictions regarding how the tax burden is to be assessed. Governors, mayors, and other local tax officials also fear the vigorous jurisdictional tax competition that would exist under an origin-based system since companies would have the ability to "shop around" for more hospitable tax environments.

Consider the hypothetical case of a vitamin company that is located in South Dakota and has no stores or physical presence in any other state. The company engages in sales within South Dakota but also sells vitamins through mail order catalogs and an Internet site. Under an origin-based system, the firm would have to pay sales taxes only to South Dakota for each transaction. It therefore would need to know only the tax rate for South Dakota and the city or county within which it was located, and only the product classification and exemption rules for those jurisdictions in which it had a physical presence.

Under a destination-based system such as the Leavitt–NGA plan, however, the company would be subject to taxes levied by any state, county, city, or other taxing jurisdiction in which it sold its products to consumers. A portion of each sale would be remitted to jurisdictions in which the company has no physical presence and no voice in the democratic process. In addition, each tax jurisdiction typically has its own tax rates, product classifications, and exemption procedures, and health foods and nutritional supplements often receive favorable tax treatment by state and local officials. Therefore, the company would need to determine whether it was eligible for a sales tax exemption in each jurisdiction in which it sold products to consumers. When one considers that millions of companies and consumers engage in interstate transactions that pass through the tens of thousands of government tax jurisdictions across America, the staggering complexity of destination-based tax collection becomes evident.

The NGA plan purportedly would solve this problem by empowering third party tax collection agents to sort through the maze of tax rates, classifications, exemptions, and the like using sophisticated tax computation software. It also purportedly would simplify and harmonize tax collection systems to make sales tax administration more uniform nationwide. But even if significant simplification of sales tax systems and structures were achieved under this plan, it would be at the expense of efforts by local governments to tailor their sales tax systems to their own needs. This undercuts the NGA's argument that its system is based on protecting state *and local* tax sovereignty.

LEGAL AND ECONOMIC OBJECTIONS

In various sections of the Leavitt–NGA proposal, it is claimed that the newly proposed system will be "simple," "fair," "streamlined," "burdenless," "voluntary," and "constitutional." On each of these counts, however, the NGA is being at best deceptive and at worse fraudulent.

- **The NGA plan would not streamline the existing sales tax system; it would expand it**

significantly by creating a *de facto* national sales tax cartel.

The NGA proposal recommends the eventual expansion of its new system to *all* retail transactions, including not only Internet commerce and interstate catalog or mail order sales, but also all traditional forms of "Main Street" retail sales. This would be an unprecedented expansion of the existing sales tax system and possibly one of the biggest tax increases in American history. It is difficult to understand how such a plan can possibly represent a "streamlining" of the existing sales tax system.

The driving force behind this effort appears to be a desire for increased tax revenues. Expanding tax collection duties on interstate commerce in this fashion would allow state and local tax collectors to tax interstate catalog and mail order sales and other forms of interstate commerce that for decades they have been unable to reach thanks to the protection afforded by Congress and the Supreme Court.

The NGA apparently feels that "streamlining" tax rates and definitions, and making the collection process somewhat more administratively "simple," will allow state and local officials to evade the existing constitutional prohibitions on the taxation of remote vendors and begin implementing their system immediately. Despite the unambiguous interstate commerce issues at play in this debate, the NGA goes so far as to argue that no congressional action or approval is needed to implement this system immediately.

Such unilateral implementation by the states would represent a nearly complete end run around Congress's authority to oversee matters related to the free flow of interstate commerce. More profoundly, the NGA system would operate as a state-based tax cartel, with governors essentially agreeing to collude and tax electronic commerce, and eventually all interstate transactions, according to similar rates and standards.

In essence, as *The Wall Street Journal* noted recently, this means that "Mr. Leavitt's proposal is essentially a national sales tax—to be imposed on the most rapidly growing part of the economy to boot."[23] While the lanes of interstate commerce have been kept fairly clear of state-by-state tax meddling for most of America's history, the NGA plan with one Machiavellian blow would undermine the authority of Congress to legislate over these matters while instituting a stealth national sales tax on the American people.

- **The NGA proposal violates constitutional first principles**.

The Leavitt–NGA sales tax system would allow state governments to collect taxes beyond their geographic boundaries via third party collection agents. Its implementation would represent a betrayal of the Founders' original constitutional design. As *Wall Street Journal* columnist Paul A. Gigot has noted, "Mr. Leavitt's main problem…is that his view of interstate commerce went out with the Articles of Confederation."[24]

America's experiment under the Articles of Confederation proved to be disastrous precisely because the states attempted to create miniature kingdoms and violate the rights of their neighbors. "[S]tates had created extensive networks of public monopolies, franchises, and privileges, as well as wide arrays of local restrictions on trade and commerce," notes Richard A. Epstein of the University of Chicago Law School.[25] As Gerald Gunther concludes in his *Constitutional Law* textbook, "The poor condition of American commerce and the proliferating trade rivalries among the states were the immediate provocations for the calling of the Constitutional Convention."[26] Bernard H. Siegan,

23. "The E-Grinch," *The Wall Street Journal*, November 29, 1999, p. A28.

24. Paul A. Gigot, "The Net Changes Everything, Except Politicians," *The Wall Street Journal*, November 12, 1999, p. A19.

25. Richard A. Epstein, "Toward a Revitalization of the Contract Clause," *University of Chicago Law Review*, Vol. 51 (Summer 1984), p. 706.

26. Gerald Gunther, *Constitutional Law*, 12th ed. (Westbury, N.Y.: Foundation Press, 1991), p. 93.

distinguished professor of law at the University of San Diego, concurs: "The tariffs and other economic barriers erected by the states against each other, are widely alluded to as a major source of discontent with the existing Confederation."[27]

Historians Frederic A. Ogg and P. Orman Ray aptly summarize the overall effects of the Articles of Confederation in their 1932 textbook *Essentials of American Government*:

> The consequences were disastrous.... [N]o uniform commercial policy could be adopted; and the states laid duties, granted favors, and set up barriers as their individual interests dictated, sacrificing by their jealousies and bickerings splendid opportunities for advancing the new nation's trade, wealth, and prosperity. Enmeshed in a network of duties and tolls, trade languished; healthy commercial competition gave way to downright commercial welfare.[28]

This forced the Founders to call for a constitutional convention and abandon the Articles in favor of our modern Constitution, which contains numerous prohibitions on parochial state taxation and regulation of interstate commerce. For example:

1. **Article I, Section 8, Clause 3 (the Commerce Clause):** "The Congress shall have Power...To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

2. **Article I, Section 9, Clause 5 and Clause 6 (non-discrimination in shipping and trading):** "No Tax or Duty shall be laid on Articles exported from any State. No Preference shall be given by any Regulation of Commerce or Revenue to the Ports of one State over those of another: nor shall Vessels bound to, or from, one State, be obliged to enter, clear, or pay Duties in another."

3. **Article I, Section 10, Clause 2 and Clause 3 (additional shipping and trading protections):** "No State shall, without the Consent of the Congress, lay any Imposts or Duties on Imports or Exports...[or] lay any Duty of Tonnage...."

These clauses represent an unambiguous recognition of the need to protect interstate commerce and ensure commercial union among the states.[29] Although these provisions dealt primarily with water-borne interstate shipping and commerce, which was the primary form of interstate commerce in that age, the principles they represent are every bit as applicable to the current debate over taxation and regulation of the Internet.[30] As Dean Andal has summarized,

27. Bernard H. Siegan, "The Economic Constitution in Historic Perspective," in Richard B. McKenzie, ed., *Constitutional Economics: Containing the Economic Powers of Government* (Lexington, Mass.: Lexington Books, 1984), p. 40.

28. Frederic A. Ogg and P. Orman Ray, *Essentials of American Government*, 6th ed. (New York: Appleton–Century–Crofts, 1950), p. 10.

29. For a more extensive discussion of these issues, see "The Founders' Vision of Constitutional Federalism," in Adam D. Thierer, *The Delicate Balance: Federalism, Interstate Commerce, and Economic Freedom in the Technological Age* (Washington, D.C.: The Heritage Foundation, 1999), pp. 15–24.

30. It could be argued that a literal interpretation of these constitutional clauses prohibits *any* form of interstate taxation since the Founders seemed to outlaw duties and both imports and exports. In fact, this logic prevailed for roughly the first 150 years of America's existence. During the Great Depression and the New Deal, however, many states began to search for new revenue mechanisms and implemented the first sales taxes to supplement existing taxes, primarily property taxes. Since Congress or the Courts refused to authorize the collection of sales taxes on interstate transactions directly, use taxes were created as a surrogate mechanism and imposed on consumers at the destination-end of the transaction. The constitutionality of use taxes remains unclear under a strict reading of the Constitution, but little has been done to prohibit them because they remain difficult to administer and collect in practice. See also Terry Ryan and Eric Miethke, "The Seller-State Option: Solving the Electronic Commerce Dilemma," *State Tax Notes*, October 5, 1998, pp. 886–888.

> States that argue that…federalism protects their unrestrained regulation (and taxation) of interstate commerce are clearly misreading the Constitution and the writings of both [Alexander] Hamilton and [James] Madison. The model of unchecked State power in the regulation and taxation of interstate commerce was the Articles of Confederation…. [U]ltimately [this] idea of unlimited State power was decisively rejected.[31]

Finally, the NGA plan smacks of the very sort of taxation without representation that the Founders found so repugnant. By allowing states to tax corporations in other states—corporations with no physical presence within the taxing state and no voice in its democratic process—it would violate the most fundamental principle of tax fairness and good government that led to the founding of the American Republic.

- **The NGA proposal is at odds with Supreme Court commercial jurisprudence**.

In a similar vein, the NGA plan runs counter to Supreme Court jurisprudence in the field of interstate commerce. As noted above, in decisions such as *National Bellas Hess*, *Complete Auto Transit*, and *Quill*, the Court has found unambiguously and inescapably that the lanes of interstate commerce are not to be burdened with parochial state and local tax and regulatory schemes. The NGA, however, seems to be unwilling to accept this.

- **The NGA proposal threatens federalism by discouraging jurisdictional tax competition.**

The word "uniform" appears over 25 times in the NGA's short proposal to the ACEC. For example, the governors call for uniform product codes, uniform sourcing rules, uniform tax definitions, and uniform procedures for the administration of exemptions. Inevitably, the idea of bringing greater nationwide uniformity to sales tax collection will have great appeal for many merchants who dread the complexity of the current system.

But as Fred L. Smith, Jr., president of the Competitive Enterprise Institute, has noted, "harmonization of tax policy is not necessarily good policy. Competition is useful in the marketplace, but it is perhaps even more valuable in the political world."[32] Bringing greater uniformity to the current system may have some positive benefits, such as more straightforward tax administration, but these benefits would come at the expense of tax competition among the states.

In other words, the governors' advocacy of greater uniformity may be no more than a covert rationale for sustaining higher tax rates and expanding the current system to incorporate remote vendors of interstate goods and services. True federalism and jurisdictional tax competition would be sacrificed in exchange for the power to recoup tax revenue from interstate sales through a tax cartel masquerading as a uniform system of third party tax collection.

31. Andal, *A Uniform Jurisdictional Standard: Applying the Substantial Physical Presence Standard to Electronic Commerce*, p. 15. Andal is correct in his assessment of James Madison's and Alexander Hamilton's opposition to unconstrained state autonomy. In *The Federalist Papers*, Madison and Hamilton clearly articulated why certain restraints on state-based regulation and taxation were needed. As Hamilton noted in *Federalist* No. 22, "The interfering and unneighborly regulations of some states, contrary to the true spirit of the Union, have, in different instances, given just cause of umbrage and complaint to others, and it is to be feared that examples of this nature, if not restrained by a national control, would be multiplied and extended till they become not less serious sources of animosity and discord than injurious impediments to the intercourse between the different parts of the Confederacy." Madison concurred in *Federalist* No. 42: "The defect of power in the existing Confederacy to regulate the commerce between its several members is in the number of those which have been clearly pointed out by experience." More important, Madison went on to point out in *Federalist* No. 45 that "The regulation of commerce, it is true, is a new [national] power; but that seems to be an addition which few oppose and from which no apprehensions are entertained."
32. Fred L. Smith, "Rush to Tax Could Produce Net Loss," Competitive Enterprise Institute *CEI Update*, Vol. 12, No. 10 (November 1999), p. 9.

The NGA plan also would give rise to an illegal multi-state compact governed by an undefined, supra-state "consensus board." The NGA claims that "no action by the federal government" is necessary to implement its plan since it is "voluntary" in nature, but this claim is at best questionable.

To solve the problem of getting the states to join, the NGA plan says, "States that do not adopt this approach and mechanism by a fixed date will be denied the ability to collect taxes on remote sales until they adopt the uniform system." This *quid pro quo* arrangement and the supra-state organization or board that would administer it appear to violate the clear language of Article I, Section 10, Clause 3 of the U.S. Constitution: "No State shall, without the Consent of Congress…enter into any Agreement or Compact with another State…." In other words, without federal approval, the plan would be illegal.

Moreover, the NGA plan certainly has very little to do with protecting "states' rights." As Empower America Co-Director Jack Kemp cogently argues:

> [T]he NGA proposal does not appear to conform to its proponents' stated admiration for states' rights…. [T]he NGA proposal turns over some of the most important state powers—the power to formulate tax policy among them—to an ill-defined board or commission empanelled with representatives of unknown origin…. [T]he NGA system would create a sub-national, supra-state, extra-constitutional (and possibly unconstitutional) governance body that is inconsistent with the principles of federalism and state sovereignty.[33]

In short, concludes Kemp, "The [NGA] plan is the very antithesis of American Federalism."[34]

- **There is nothing trustworthy about a "Trusted Third Party" system of tax collection that could compromise individual and corporate privacy.**

The NGA plan would empower "Trusted Third Parties" (TTPs) to carry out sales tax administration and collection for vendors of electronic commerce in the short term and all retailers in the future. These TTPs (presumably tax or accounting firms with a particular expertise in tax computation and collection) would be chosen through a competitive bidding and negotiation process and would be paid on a per-transaction basis for each sale they process.

Essentially, the TTPs would become tax middlemen. According to the Leavitt–NGA plan, they would be responsible for:

- **Receiving** required information on transactions from a seller and providing software for determining the taxability of a transaction, the appropriate state and local tax rate, and the tax due;
- **Providing** tax information to sellers at the time of sale so that information on the tax due is available to a customer before completion of the transaction;
- **Entering into** arrangements with credit card and other electronic payment processors so that taxes owed to the state or local government may be remitted directly to the TTP for transmittal to the state;
- **Providing** all transaction and return information to the state and local governments along with the tax remittance; and
- **Providing** financial incentives to sellers to encourage them to use the system.

Although the governors claim that this process will be "burdenless" and "simple," using a software solution essentially to turn technology against itself is unlikely to work well in the long run. Many buyers and sellers will look for ways to evade burdensome new interstate taxes, perhaps through creative software solutions of their own. And because the TTP system is geared entirely to

33. Jack Kemp, "Taxation and the Cyber-Frontier: A Framework for Economic Growth," Submission to the Advisory Commission on Electronic Commerce, December 14, 1999, p. 19.

34. *Ibid.*, p. 14.

transactions made with credit cards, the question remains how it would work if a transaction involved cash, checks, e-money, or old-fashioned forms of barter.

Moreover, deputizing third parties to collect taxes on behalf of the government is an idea with an unsettling history. In the study of economics, Trusted Third Party systems are known more commonly as "tax farming" systems. Tax farming is the contracting-out of tax collection duties to private parties. Third party agents typically bid for the right to collect taxes on behalf of the government and take a certain share of the taxes collected to make the effort profitable.

From Greek and Roman times onward, many governments viewed tax farming as a more efficient way to collect taxes. However, it rarely worked as well as promised, and when it did, citizens came to despise it.[35] Third party tax collection creates a perverse incentive for deputized private-sector tax collectors to engage in overzealous enforcement to increase their own profits. Thus, tax farmers often engaged in such practices to collect more taxes, and most citizens rebelled against tax farming schemes or at least protested their existence as a serious threat to both property and privacy. Furthermore, the possibility of rampant fraud is always present. Simply stated, there are many government functions that should be privatized, but tax collection is not one of them.

The Leavitt–NGA plan's "Trusted Third Party" tax collection system could pose an equally serious threat to individual and corporate privacy if certain TTPs became overzealous tax collectors. Under the current *intra*state sales tax system, the typical transaction in a retail store requires the buyer and seller to exchange little more than money. Occasionally a vendor will ask for the buyer's zip code, but such information generally is not required to complete the transaction.

Under the NGA plan, however, there would have to be some way to track the location of the buyer at all times in order to remit money to the appropriate tax collectors. The NGA plan mentions the need to assign "geo-codes" to buyers according to their street address, but it does not specify how this would work. It also fails to mention how this "geo-code" would be assigned when street addresses are not given or are not relevant, as would often be the case for digital/electronic transactions.

In order to levy and collect taxes, TTPs would be required to collect information about buyers that is not now collected when consumers make routine retail transactions. This raises an important question: Could the NGA plan also require a typical Main Street vendor to ask for similar information and then remit taxes to out-of-state tax collectors if they sell goods in their stores to consumers from other states? Kaye Caldwell, public policy director for CommerceNet, argues that this would be inevitable under a plan like the one proposed by the NGA:

> If states are allowed to impose use tax collection obligations on out-of-state eCommerce and mail order merchants then in order to comply with the Equal Protection clause they will have to impose those obligations on Main Street merchants also. Imagine the administrative nightmare for local stores when a convention comes to town![36]

Consider another hypothetical example: a New Jersey resident who frequently crosses into the state of New York to shop in various New York City department stores. When making purchases in these stores, this New Jersey resident provides the department store vendor with cash, a check, or a credit card as payment. The sale includes both New York City and New York State sales taxes, which the vendor collects and remits to the government. The buyer's place of residence is

35. See Charles Adams, *For Good and Evil: The Impact of Taxes on the Course of Civilization* (London: Madison Books, 1993).

36. Kaye Caldwell, "A Message to Main Street Merchants: Be Careful What You Ask For," *The Public Policy Report: Electronic Commerce Core Series*, CommerceNet, Vol. 1, No. 9 (September 1999), p. 3.

irrelevant. It makes little difference whether this buyer is from New Jersey or New Delhi.

If the NGA's destination-based system was adopted and applied to all retail merchants, however, the department store vendor would be required to determine the buyer's place of residence (state or locality) before finalizing the sale. Once the New York vendor determined that the buyer was from New Jersey, the vendor would need to determine the sales tax rate for the state and for the specific city in which the buyer resided. (If the buyer were from outside the United States, it is unclear how this tax transaction would work under the NGA plan.)

More important, would the New York vendor be allowed to exempt the New Jersey buyer from New York City and New York State sales taxes, or would those taxes be levied *in addition to* the applicable New Jersey taxes? The second option would represent a clear case of multiple taxation as a result of the NGA plan.

The bottom line is that the NGA's Trusted Third Party tax collection system is neither administratively simple nor free of potential privacy violations. As summarized by Kaye Caldwell,

> [T]he message for Main Street is: That level playing field you want so badly? It will be much more level than you have yet imagined. You too will get to participate in the massively burdensome and costly use tax system, imposed on you by governments in other states where neither you nor your employees even get to vote.[37]

- **Both the cost of establishing this "zero burden" system and the complexity of carrying it out could be substantial.**

The NGA frames its proposal as a model of simplicity and efficiency: a "zero burden" or "burdenless" system of tax collection. In reality, it would spawn an entirely new cottage industry of tax software manufacturers and third party tax collectors who would be paid according to how much money they helped state and local government officials raise.

Exactly how much it would cost to get this system running is unclear. TTPs would have to determine the applicable tax rates on each transaction, the proper classification of all goods and services, how digitally delivered goods and services should be taxed, and what taxes were applicable or what exemptions were valid for each purchase made. Software systems would make it somewhat easier to administer this process, but they would not make it "burdenless."

It is likewise unclear just how much the TTPs would charge per transaction to administer this system. This is important because the NGA plan specifies that "State and local governments will also be responsible for paying all costs associated with the system so that costs and burdens will not be imposed on participating sellers." One portion of these costs would be the various "financial incentives" that TTPs would offer interstate vendors to induce them to sign up "voluntarily" for the new system. Because they would have to compensate TTPs for providing these incentives to private companies, state and local governments could find themselves spending two dollars to collect a dollar in taxes.

One thing is clear: The costs of this system would be passed on to companies and consumers. Moreover, in a much broader sense, these costs would be substantial for the Internet sector and the economy as a whole. A recent BizRate.com public opinion poll revealed that nearly 60 percent of on-line buyers would make fewer purchases if they had to pay a sales tax on all on-line purchases.[38] If Internet purchases are this sensitive to sales tax hikes, the NGA plan's consequences for on-line commerce and development could be devastating.

37. *Ibid.*, p. 4.

38. "Internet Taxes," *Flash Survey Report*, BizRate.com, December 1999, p. 3.

For the national economy, which has come to rely heavily on the high-tech sector for much of its recent growth, the NGA plan poses a triple threat.

1. By stifling the creativity and entrepreneurialism associated with the Internet sector, it would lead to decreased innovation, output, and job growth generally;
2. If applied more broadly throughout the national economy, as the NGA proposes, it would then burden other multi-state and Main Street retailers; and
3. By discouraging the continued expansion of the Internet sector and overall economic growth, it would lead to lower corporate and personal incomes, which would translate into lower state and local tax revenues.

The members of the National Governors' Association should think very carefully before inviting such a revenue shortfall.

- **The NGA proposal is not "voluntary."**

The NGA claims that participation in its new system would be "voluntary" for remote sellers and for participating states. It is not clear, however, why any state that currently has a sales tax would not begin immediately to use any system that allowed it to extend its tax reach extraterritorially. Moreover, all state and local governments would have to join for the system to succeed. The governors' plan makes it clear that the long-run goal is "a completely unified system," with "one classification system for products, one set of definitions on exemptions, and a one-stop audit process for all state and local governments."

As mentioned, the NGA plan includes a system of financial incentives to encourage companies to participate. These vendors would also be required to integrate their business systems with those of the TTPs so that the necessary tax information can be processed. The NGA claims that only periodic "system checks" would be needed to ensure that the process is working properly. It is likely, however, that the line between a system check and an audit would blur with time. In any event, few if any sellers could be expected to join the system voluntarily unless the financial incentives were great enough. Sooner or later, other ways to coerce companies to join would have to be found.

- **The NGA proposal is at odds with the Clinton Administration's proposed "global free trade zone" for international electronic commerce and could threaten American sovereignty.**

The NGA plan also threatens global tax harmonization. "Any proposed system for taxing the Internet should be evaluated in terms of whether it promotes or discourages global harmonization with other taxing systems," note Terry Ryan, director of state and local taxes for Apple Computer, and Eric Miethke, a partner with the Sacramento-based law firm of Nielsen, Merksamer, Parrinello, Mueller, & Naylor.[39] By this, they mean not harmonization in the sense of uniform tax rates, but harmonization of tax collection methodologies.

But the NGA plan is destination-based, and some foreign nations, especially European Union (EU) member states, have considered moving toward an origin-based system of tax collection. The EU has discussed the adoption of a definitive origin-based VAT (value-added tax) system at least for the taxation of digitally delivered products.[40] If adopted, such a system could serve as a model for future reforms of European tax collection systems.[41]

As Aaron Lukas, an analyst with the Cato Institute's Center for Trade Policy Studies, has argued, "Origin-based taxation on an international basis would offer the same advantages that it would within Europe. U.S. policymakers should thus

39. Ryan and Miethke, "The Seller-State Option: Solving the Electronic Commerce Dilemma," p. 882.

40. See *Indirect Taxation of Electronic Commerce: Position Paper*, Computer Systems Policy Project, July 1999, p. 6, at *http://www.cspp.org/projects/CSPP_Tax_Paper.pdf*.

41. See Tino Eggermont, "The Commission's Work Programme for the Gradual Introduction of the New Common VAT System," February 3, 1998, at *http://www.ecu-activities.be/1998_2/eggermont.html*.

actively encourage shifting to such a system as a viable option for dealing with the growth of electronic commerce."[42] Global adoption of an origin-based system would lead to simplified tax collection, the fair assessment of tax burdens, and the prevention of extraterritorial taxation on a global scale to preserve the sovereignty of countries and consumers alike.

Global adoption of a destination-based system like the NGA's, however, would allow foreign governments to extend the reach of their tax policies into the United States. For example, if a citizen of Paris, France, purchased a book from Amazon.com and the NGA plan was in effect globally, the city of Paris (and perhaps the government of France as well) could impose a tax on Amazon.com even though it is located in Seattle, Washington. This raises important sovereignty considerations. It also magnifies the problem of complexity.

For example, if the publisher of an on-line travel magazine sold an electronic version of the magazine to global travelers who are always on the move, what tax rate would apply? Would it be the rate in the buyer's home country? What if the buyer lived in different countries and had multiple residences? What if the buyer made the transaction while flying on a plane? Significant global coordination and a global tax collection body, created perhaps by the United Nations or a similar body, would be needed to administer this system. An origin-based system, by comparison, would require no such global coordination mechanism and no such sacrifice of sovereignty by individual nations or member states.

All of this flies in the face of recent proposals by the Clinton Administration and Members of Congress[43] to make the Internet a "global free trade zone" or a "tariff-free environment." The Clinton Administration's 1997 *Framework for Global Electronic Commerce* argues that "Any taxation of Internet sales should follow these principles":[44]

1. It should neither distort nor hinder commerce. No tax system should discriminate among types of commerce, nor should it create incentives that will change the nature or location of transactions.
2. The system should be simple and transparent. It should be capable of capturing the overwhelming majority of appropriate revenues, be easy to implement, and minimize burdensome record keeping and costs for all parties.
3. The system should be able to accommodate tax systems used by the United States and our international partners today.

Moreover, "Any such taxation system will have to accomplish these goals in the context of the Internet's special characteristics—the potential anonymity of buyer and seller, the capacity for multiple small transactions, and the difficulty of associating online activities with physically defined locations."[45]

It is obvious that, despite claims to the contrary, the NGA plan is anything but "simple and transparent." In addition to conflicting with emerging tax norms advocated by America's trading partners, it fails to take into account the Internet's special characteristics and is at odds with current U.S. principles and policy regarding Internet tax policy.

THE FAIRNESS MYTHS

The movement to tax the Internet is supported by certain myths propagated by state and local officials or retail merchants who fear the rise of the

42. Aaron Lukas, "Tax Bytes: A Primer on the Taxation of Electronic Commerce," Cato Institute *Trade Policy Analysis* No. 9, December 17, 1999, p. 38.

43. See "Cox–Wyden III Passes: House Approves Global Internet Tax Freedom 423–1," office of Representative Christopher Cox, at *HTTP://COX.HOUSE.GOV/PRESS/RELEASES/1999/1026COXWYDENIII.HTM*.

44. "A Framework for Global Electronic Commerce," The White House, July 1, 1997, at *http://www.ecommerce.gov/framewrk.htm*.

45. *Ibid.*

Internet and the electronic commerce marketplace generally. Specifically, two distinct arguments have been advanced by opponents of the Internet Tax Freedom Act in an attempt to win converts to the pro-tax camp. These arguments are based on mistaken assumptions and a misunderstanding of the nature of true tax fairness.

- **Fairness Argument #1:** It is not fair to exempt remote e-commerce vendors from taxes when "bricks and mortar" or "Main Street" businesses within a state are required to pay taxes on similar goods or services.

This argument misses an important point: Remote vendors do not use or deplete state or local resources that are supported by state or local taxes. It would be patently unfair to force out-of-state companies to pay taxes for government services or programs they do not use or from which they cannot benefit. As the Supreme Court noted in *State of Wisconsin* v. *J. C. Penney Co.* (1941) and reiterated in *National Bellas Hess* v. *Department of Revenue of State of Illinois* (1967), "The simple but controlling question is whether the state has given anything for which it can ask return."[46]

In other words, state and local businesses pay sales (and other) taxes because they can take advantage of the government programs or public services provided with those funds, such as roads, schools, parks, and police and fire protection. Remote vendors engaging in interstate electronic transactions do not benefit in a similar way either from these taxes or from the programs or services these taxes fund.

Moreover, Internet vendors *are* tangible "bricks and mortar" businesses that will continue to pay routine corporate income and property taxes where they reside. Even a permanent Internet tax moratorium would not prevent states and localities from imposing equal sales tax rates on companies within their own jurisdictions. Consequently, NGA arguments premised on "preserving state sovereignty" or "protecting local merchants" are dubious because, under current Supreme Court case law, there is nothing to stop state or local officials from imposing taxes on those companies that have taxable nexus within their jurisdiction.[47]

- **Fairness Argument #2:** It is not fair to deprive state and local governments of the revenues that could be collected by taxing the Internet or electronic sales.

This argument is equally flawed. The explosive rise of the Internet and electronic commerce has created an unprecedented level of entrepreneurialism and innovation in America, and this technological renaissance has been the driving force behind America's recent strong and sustained economic growth.

This presents policymakers with a paradox. The rise of this unregulated and, for the most part, untaxed industry sector has helped fuel the sustained growth of economic activity and government tax revenues. As Raymond J. Keating, chief economist of the Small Business Survival Commit-

46. *State of Wisconsin* v. *J. C. Penney Co.*, 311 U.S. 435 (1941); *National Bellas Hess* v. *Department of Revenue of State of Illinois*, 386 U.S. 753 (1967). Some scholars argue that *Quill Corp.* v. *Heitkamp*, 504 U.S. 298 (1992), partially overruled this sort of Due Process analysis, but the facts in *Quill* were not entirely analogous to Internet sales. It remains an open question whether the Court would overturn state-based efforts to tax remote Internet commerce on Due Process grounds or just rely on Commerce Clause considerations to strike down parochial tax schemes. There are good reasons to believe that more traditional Due Process analysis, such as the logic employed in the *J. C. Penney* and *National Bellas Hess* cases, would prevail if Internet vendors pushed a constitutional challenge on these grounds. See Ryan and Miethke, "The Seller-State Option: Solving the Electronic Commerce Dilemma," pp. 889–891.

47. Moreover, state and local governments that make such fairness arguments need to examine exactly how "level" the playing field is today within their own jurisdictions since most sales tax codes are riddled with exemptions and loopholes for favored political constituencies. For example, services are generally exempted from most state and local sales taxes; and agricultural producers, prescription drug vendors, and clothing manufacturers also receive generous exemptions from most tax jurisdictions. In this sense, the biggest "fairness" or "[un]level playing field" problem that governors or mayors face today is one of their own making, which they could correct immediately by applying sales taxes more evenly.

tee, noted in testimony before the ACEC on September 14, 1999, "federal, state and local governments have lost no revenues due to expanding e-commerce, but have gained revenues due to economic growth driven in part by information technologies."[48]

Recent studies of state and local tax collection during the 1990s support Keating's argument.

- *Investor's Business Daily* notes that between 1980 and 1995, state revenues grew 227 percent and local revenues grew by 193 percent.[49]
- Fiscal policy analysts Dean Stansel and Stephen Moore of the Cato Institute report that between 1992 and 1998, state tax revenues grew at almost twice the rate of inflation and population growth. "Today, almost without exception, state governments are awash in tax revenues."[50]
- Michael Flynn of the American Legislative Exchange Council confirms this finding and notes that states are "in their best financial health in over a decade" with $74 billion in windfall surplus tax revenues over the past four years.[51]

As Chart 1 illustrates, state and local sales tax collections have continued to grow through the mid- to late 1990s. At the same time, the Internet economy grew from roughly $5.3 billion in 1995 to $301 billion in 1998, according to a recent study by the Center for Research in Electronic Commerce at the University of Texas at Austin.[52] How can state and local governments be collecting record amounts of tax revenue if the rise of a tax-free Internet environment represents such a serious drain on governmental tax collections?[53]

The answer lies in simple economics. The rise of the Internet and the information economy has created new jobs and new business opportunities, and this increased economic activity and output has led to higher individual incomes and business profits. The result: new tax sources and higher revenues overall for all governments. As Stephen Kroes, vice president and research director for the California Taxpayers' Association, has noted,

48. Raymond J. Keating, "Testimony Before the Advisory Commission on Electronic Commerce on the Issue of E-Commerce Taxation," September 14, 1999.

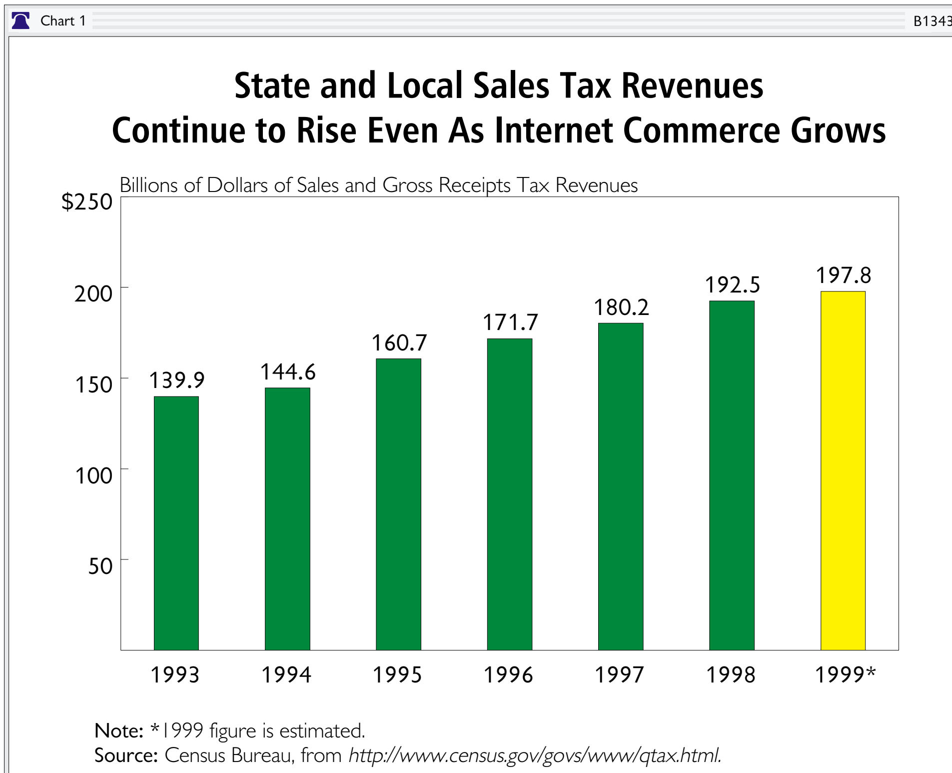
49. "Online Money Grab," *Investor's Business Daily*, September 9, 1999, p. A24.

50. Dean Stansel and Stephen Moore, "The State Spending Spree of the 1990s," Cato Institute *Policy Analysis* No. 343, May 13, 1999, p. 1.

51. Michael Flynn, "$74 Billion Windfall: Surplus Revenue in the States," American Legislative Exchange Council, *The State Factor*, Vol. 24, No. 5 (December 1998), p. 1. Despite these record surpluses, most states prefer to spend even more than they are taking in. The National Governors' Association recently reported that spending by the states will grow by 5.5 percent during 2000 even though revenues are estimated to grow by only 4.3 percent. See "State Spending Spree," *The Wall Street Journal*, January 12, 2000, p. A22.

52. Anitesh Barua, Jon Pinnell, Jay Shutter, and Andrew B. Whinston, *Measuring the Internet Economy: An Exploratory Study*, Center for Research in Electronic Commerce, Graduate School of Business, University of Texas at Austin, June 19, 1999, p. 8.

53. Although some studies have found that state and local governments have lost sales tax revenues because of the tax-free treatment of remote Internet sales, these losses appear to be fairly insignificant. A study by Robert J. Cline and Thomas S. Neubig of Ernst and Young LLP estimates that state and local governments lost less than $170 million in 1998 due to their inability to tax remote Internet commerce. This represents only one-tenth of 1 percent (0.1 percent) of total state and local sales tax collections for that year. See Robert J. Cline and Thomas S. Neubig, *The Sky Is Not Falling: Why State and Local Revenues Were Not Significantly Impacted by the Internet in 1998*, Ernst & Young LLP, June 18, 1999, p. i. Likewise, Austan Goolsbee of the University of Chicago and Jonathan Zittrain of Harvard Law School have estimated independently that state and local governments lost around $210 million in 1998, or one-quarter of one percent (0.25 percent) of total state and local tax revenues. See Austan Goolsbee and Jonathan Zittrain, *Evaluating the Costs and Benefits of Taxing Electronic Commerce*, unpublished manuscript, May 20, 1999.



> [E]conomic output is likely increasing because of growth in electronic commerce. As economic output increases, state and local governments reap greater tax revenues. These tax revenues can more than compensate for lost sales taxes, and it's time government officials start looking at the big picture and begin talking about e-commerce in a more balanced, rational way.[54]

CONSTRUCTIVE ALTERNATIVES

In view of the Leavitt–NGA plan's likely consequences for the Internet and the economy as a whole, the ACEC and Congress would be wise to consider more sensible proposals. Specifically, the following four proposals or recommendations would better achieve the ends the ACEC was empowered to study.

1. **Extend or broaden the current tax moratorium.**

Senator Robert Smith (R–NH) has introduced S. 328, which would make permanent the Internet Tax Freedom Act's current moratorium. It is important to stress, however, that while extending or making permanent this moratorium makes sense, it would not necessarily prohibit the imposition of all forms of taxation of the Internet, especially sales taxes. The ITFA prohibited "multiple and discriminatory taxes," as well as "access taxes," but did not outlaw all forms of Internet taxation.

In fact, Section 1101(b) of the ITFA went so far as to preserve state and local tax sovereignty by stating explicitly that

> Except as provided in this section, nothing in this title shall be construed to modify, impair, or supersede, or authorize the modification, impairment, or superseding of, any State or local law pertaining to taxation that is otherwise permissible by or under the Constitution of the United States or other Federal law and in effect on the date of enactment of this Act.

Therefore, even though "multiple and discriminatory" or "access" taxes would still be prohibited under an extended ITFA moratorium, Congress would have to do one of two things to keep a plan like the NGA's from taking effect: either prohibit all sales and use taxes on electronic commerce or Internet activity, or codify and clarify current Supreme Court jurisprudence regarding taxable nexus.

54. Stephen Kroes, "Electronic Commerce: Money Loser or Revenue Generator for Government?" *Cal-Tax Commentary*, October 1999, at *http://www.caltax.org/MEMBER/digest/oct99/oct99-7.htm*.

Representative John Kasich (R–OH) and Senator John McCain (R–AZ) have introduced legislation (H.R. 3552, S. 1611) that embodies the first option. However, although their approach has great appeal and would end the debate over Internet taxation, it also raises several concerns.

First, the Kasich–McCain bills would prohibit only sales taxes imposed on electronic commerce. But what about mail order sales, catalog sales, direct phone (1-800) sales, or other current or future forms of interstate retailing? Failure to grant these forms of interstate commerce similar protections would represent a serious breach of tax equity or regulatory parity.

Second, the Kasich–McCain approach could be found unconstitutional. The Supreme Court recently has held Congress to a much higher standard when federal legislators have tried to preempt state and local authority under the Commerce Clause.[55] University of Georgia law professor Walter Hellerstein has argued that "these [Supreme Court] decisions do not seriously inhibit the extensive power that Congress plainly possesses to deal with the broad range of problems raised by state taxation of electronic commerce."[56] Nevertheless, an argument can be made that the Kasich–McCain approach is too broad and would infringe on the sovereign rights of state and local governments to determine tax policies within their own jurisdictions.

2. **Adopt a clear and constitutional nexus standard.**

A better approach would be to clarify and codify constitutional and Supreme Court precedents regarding the taxation and regulation of interstate commerce. Congress could do this by adopting an unambiguous nexus standard that conforms to existing Supreme Court jurisprudence and constitutional objectives. Both Governor James Gilmore and Dean Andal have made presentations to the Advisory Commission that embody this approach.

Andal's "Uniform Jurisdictional Standard" asks the ACEC to lend its formal support to the Supreme Court's physical presence test, which makes it clear when state and local governments have the right to impose sales taxes.[57] Specifically, it would modify an existing federal law, Public Law 86–272, which deals with state *income* taxation of companies engaged in interstate commerce. The Andal proposal would broaden P.L. 86–272 to cover all forms of state and local taxation of interstate commerce, not merely income taxes, and clearly define what constitutes a "substantial physical presence" in a state or locality and when that test is not satisfied.

For example, the fact that an electronic transaction passes through a network of wires, computers, servers, or wireless satellite dishes that may be located within a given state does not by itself mean that a company has a substantial physical presence within that jurisdiction. Furthermore, the fact that a firm's Web page is advertised or promoted within a state or locality does not necessarily mean that the company is physically present within that jurisdiction.

Many state and local officials and tax officials have tried to replace traditional nexus standards with new theories, such as "attributional," "representational," or "agent" nexus, that attribute physical presence to a company in cases such as those

55. See, for example, *U.S.* v. *Lopez*, U.S. 93–1260 (1995), and *Printz* v. *United States*, U.S. 95–1478 (1997).

56. Walter Hellerstein, "The Law of Sales Taxes in a Cyber Economy," presentation to the Advisory Commission on Electronic Commerce, Williamsburg, Virginia, June 22, 1999, p. 10. In fact, a good argument can be made that a more traditional or literal reading of the Constitution would justify a sweeping prohibition along the lines of the Kasich–McCain approach. Most notably, Article I, Section 10 of the Constitution clearly states that "No State shall, without the consent of Congress, lay any imposts or duties on imports or exports…." If taken literally, this would proscribe *any* form of Internet taxation, whether destination-based or origin-based. To reiterate, however, while such a reading of the Constitution was commonplace throughout the first 150 years of the nation's existence, the Supreme Court has interpreted its language more broadly and pragmatically in the post-New Deal period to allow for certain types of import and export taxation.

57. Andal, *A Uniform Jurisdictional Standard: Applying the Substantial Physical Presence Standard to Electronic Commerce*.

discussed above. It is vital that the ACEC and Congress reject these new definitions. As Saba Ashraf notes, "By changing and expanding the definition of physical presence, and in effect equating non-physical presence in a state with physical presence, the state legislative bodies would be writing the constitutional requirement of physical presence out of existence."[58] Physical presence must mean what most rational individuals take it to mean: the actual, tangible presence of a company's buildings, employees, and related property within a state or locality.

3. **Require that any sales taxes imposed on Internet sales be origin-based so that they will be consistent with the Constitution and prevailing nexus standards.**

State and local leaders may fear that extending the Internet Tax Freedom Act and codifying a nexus standard would prohibit them from collecting any sales taxes on electronic transactions. As mentioned above, however, the ITFA and existing Supreme Court nexus jurisprudence do not prohibit all forms of taxation. What they do prohibit, respectively, is multiple or discriminatory Internet taxes and extraterritorial taxation of remote vendors of commerce in general—exactly the sort of burden that would be imposed by the NGA plan.

Adoption of an origin-based (or "seller-state") system of sales tax administration "technically would take care of a lot of these problems," argues ACEC member Gene Lebrun, former president of the National Conference of Commissioners on Uniform State Laws. "I think we've got to think outside the box to resolve these issues."[59]

Commissioner Lebrun is correct, because under an origin-based system, sales taxes would be collected at the source, or point of sale, instead of at the destination, or point of consumption. All commercial vendors (including Internet vendors and mail order companies) would be required to collect the sales taxes owed to governments within the state or location where they have a substantial physical presence. They would not be required to remit taxes to states or localities outside their home territory, where they have no physical presence.

Terry Ryan and Eric Miethke have detailed the many advantages an origin-based system would have in practice.[60] According to Ryan and Miethke, an origin-based or seller-state system would:

- **Minimize the burden on sellers** by requiring sellers to know and abide by only the tax rates and regulations within their principal place of business;
- **Maximize the amount of tax collected for states** by making compliance easier and incorporating activity (such as foreign shipments) that currently are untaxed;
- **Remove nexus uncertainty and constitutional concerns** by taxing only companies within a state or local government's borders;
- **Remove the threat of double taxation** by imposing taxes only once, at the point of sale;
- **Preserve local jurisdictional tax rights** instead of adopting a harmonization proposal like the NGA plan, which would create a *de facto* national sales tax;
- **Respect privacy rights** by not requiring that any special information be collected about a buyer and by not empowering a third party tax collector to collect information about buyers;
- **Respect federalism principles and preserve jurisdictional tax competition** by permitting

58. Ashraf, "Virtual Taxation: State Taxation of Internet and On-Line Sales," p. 628. For an excellent overview of these new nexus theories, see Karl A. Frieden and Michael E. Porter, *The Taxation of Cyberspace: State Tax Issues Related to the Internet and Electronic Commerce*, Part IV: Nexus Issues, December 1996, at *http://www.caltax.org/andersen/contents.htm*.

59. Quoted in "Sales Tax Calculation, Compliance a Heavy Load for Internet Businesses," *Electronic Commerce News*, Vol. 4, No. 37 (September 13, 1999).

60. Ryan and Miethke, "The Seller-State Option: Solving the Electronic Commerce Dilemma," p. 884.

each state to determine its own tax policies and encouraging healthy state-by-state tax rivalry; and

- **Be more politically feasible,** since it remains unlikely that Congress will alter existing nexus standards and allow extraterritorial taxation by state and local governments.

Andrew Wagner and Wade Anderson have submitted a formal proposal to the commission that outlines how such an origin-based system would work.[61] Though their proposal is tailored to the sale of digitized products sold over the Internet, they argue that an origin-based system could be applied to all types of sales.

Wagner and Anderson also conclude that an important advantage of an origin-based system is that it "represents a bottom-up approach to the question rather than a top-down approach."[62] There is no need to impose a confusing, top-down system of sales tax collection on America when state and local governments could move directly to a much more straightforward, bottom-up system of origin-based sales tax administration on their own.

Many state and local officials continue to fear that an origin-based system of sales taxation would cause a "race to the bottom" by encouraging some states or localities to lower tax rates, or even to create tax-free "tax havens" to attract commercial vendors to their jurisdictions. The question is: Why should this sort of vigorous jurisdictional tax competition be considered such a lamentable development?

Indeed, this is exactly what the Founders hoped would occur in the federalist system of government they created. By allowing states and localities to tailor their tax systems to their own needs and simultaneously allowing companies and consumers to "vote with their feet" by shopping around for favorable tax and regulatory environments, an origin-based system of sales taxation would enhance and reinvigorate federalism in the United States. If "race to the bottom" fears persisted, a revenue-sharing compact could be arranged among the states to redistribute revenue more evenly.

Arguments for destination-based use taxes on interstate commerce and against an origin-based sales tax system are parochial attempts to protect in-state vendors and avoid rigorous jurisdictional tax competition. As Dean Andal appropriately concludes, "The use tax is not a surrogate consumption tax as some would suggest. It was a device conceived to protect in-state merchants."[63]

4. Address broader telecommunications tax issues.

America's increasingly competitive communications sector also remains one of its most heavily taxed. As Progress and Freedom Foundation President Jeffrey A. Eisenach asks:

> [I]n a world in which building out the telecommunications infrastructure is policy goal Number One—why would we place discriminatory taxes on telecommunications? And we're not talking about small taxes, either. We're talking about levels of taxation between 20 and 40 percent, depending on the state and the locality.... We're talking about a level of complexity that is just stunning. There are 38 different kinds of taxes paid by telecommunications companies just in the telephone business.... The tax structure that we have is not only too high, it's also regressive. Virtually all of the taxes that we levy on telecommunications providers are excise taxes or line taxes, line charges, equivalent of poll taxes. And so they go directly against our objective of

61. Andrew Wagner and Wade Anderson, *Proposal of an Origin Based Tax Solution for the Possible Taxation of Digitized Products Sold Over the Internet*, proposal to the Advisory Commission on Electronic Commerce, November 8, 1999, at *http://www.ecommercecommission.org/proposal.htm*.

62. *Ibid.*, p. 6.

63. Andal, *A Uniform Jurisdictional Standard: Applying the Substantial Physical Presence Standard to Electronic Commerce*, p. 13.

making Internet access and the information revolution available to people regardless of their income.[64]

Among the taxes that most deserve the attention of Congress and members of the ACEC are the following:

- **The federal 3 percent excise tax on telecommunications.** Put in place during the time of the Spanish–American War of 1898, this tax is an anachronism and should be repealed immediately.
- **Discriminatory ad valorem taxation of interstate telecommunications.** Fifteen states tax telecommunications business property at rates higher than other property, driving up costs for consumers. Federal protections against such taxes—already in effect for railroads, airlines, and trucking—should be extended to telecommunications.[65]
- **Internet tolls.** These new taxes and fees levied on telecommunications providers and their customers when cable is installed along highways and roads can run up to 5 percent of gross receipts. They drive up costs for consumers and should be abolished. Congress should make clear that the 1996 Telecommunications Act intended only that state and local governments be reimbursed for actual costs incurred in managing public right of ways.
- **High state and local telecommunications taxes and complicated auditing and filing procedures.** Many governments are using consumer telephone bills as cash cows, imposing multiple and high taxes on services. Such taxes should be slashed to a single tax per state and locality, and filing and auditing procedures should be streamlined.
- **Internet access taxes.** The temporary federal ban on Internet access taxes should be made permanent. States and localities that imposed such taxes before the ban took effect should repeal any taxes on access to keep costs down for consumers.

Even if the ACEC and Congress do not reach agreement on the issue of Internet sales taxation in the short term, they should, at a minimum, undertake immediate action to eliminate or reform these costly telecom industry tax burdens.

THE OPPORTUNITY FOR FUNDAMENTAL TAX REFORM

In general, the Leavitt–NGA plan seeks (a) to effect a massive expansion of sales tax collection obligations and (b) to make it easier to impose sales taxes in general. Even worse, however, is the perverse incentive it would establish: States that do not have sales taxes would be encouraged to adopt them, and states that do have sales taxes would be encouraged to raise them. Under the NGA plan, there would be no escaping the reach of the tax collector.

The governors are correct when they argue that "The current system of state and local sales tax administration is complex and burdensome," and will require "significant simplification…to match the rapid evolution of the information economy and global trade." Their proposed solution, however, would make matters worse.

The problems associated with America's sales tax system will not be solved by expanding or attempting to modernize a system that is fundamentally broken. As R. Bruce Josten, executive vice president of government affairs for the U.S. Chamber of Commerce, has argued, "Putting new tires on a Model T tax code will not enable it to

64. Jeffrey A. Eisenach, "Speech Before Winter Meeting of the National Governors' Association," February 21, 1999, at *http://www.pff.org/NGA_speech_by_JAE_990221.htm.*

65. See also Dean Andal, *A Prohibition on Discriminatory Ad Valorem Taxation of Interstate Telecommunications: Encouraging Investment in Internet Infrastructure Through Equitable State Tax Treatment*, proposal to the Advisory Commission on Electronic Commerce, December 15, 1999.

catch a space age market."[66] More substantive and far-reaching reforms are in order.

State and local officials need to reform their tax systems in ways that will ensure their ability to pay for parochial social programs without imposing economically burdensome and legally unjust taxes on interstate transactions. One option would be for state and local governments to trim expenditures and reform costly government programs. Another would be to eliminate sales taxes altogether and find other revenue mechanisms that are more compatible with modern economic realities. Hal Varian, Dean of the University of California–Berkeley School of Information Management and Systems, has made such a proposal to the ACEC.[67]

To the extent that sales taxes continue to be imposed, however, only an origin-based method avoids the legal and economic problems associated with the current sales tax system. And only by switching to an origin-based system will state and local governments be able to tax Internet transactions.

Many state and local officials may not like the vigorous jurisdictional tax competition that would accompany a move to an origin-based system, but it represents the only constitutional option available outside of abandoning sales taxes altogether. The Advisory Commission for Electronic Commerce should use the opportunity it has been given to recommend that state and local governments move to such a system while simultaneously reforming or abolishing other communications industry taxes.

The choice for Congress is simple: Either adopt the NGA plan and create the equivalent of a national sales tax system for electronic commerce (and eventually all retail transactions) or uphold the Constitution and Supreme Court case law and encourage state and local governments to revise their tax collection schemes so that they impose taxes only on those parties that benefit from them.

Only by choosing the latter option will Congress protect the entrepreneurial and empowering nature of the Internet and stop the National Governors' Association's quest to impose an unprecedented national sales tax system on the American people.

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66. R. Bruce Josten, *E-commerce Taxation: Issues in Search of Answers*, submission to the Advisory Commission on Electronic Commerce, September 8, 1999, p. 17.

67. Hal Varian, *A Proposal to Eliminate Sales and Use Taxes*, proposal to the Advisory Commission on Electronic Commerce, November 12, 1999, at *http://www.ecommercecommission.org/proposal.htm*. See also Murray Weidenbaum, "Taxing E-Sales Without Hindering the 'Net,'" *Christian Science Monitor*, January 20, 2000, at *http://www.csmonitor.com/durable/2000/01/20/p9s2.htm*. Weidenbaum suggests the adoption of a savings-exempt income tax to continue to tax consumption without taxing goods and services.