

**Larry Eichel / The Body Politic**

# Internet raises a taxing issue for the presidential candidates

If you've done any shopping on the Internet, you've encountered one of the joys of e-commerce.

No sales tax.

Therein lies a set of political questions that may not be huge now but will be sooner or later. And they're not going to be easy to resolve.

Why should an item bought online be treated differently than the same item purchased in a store? Should state sales taxes apply to transactions made in cyberspace? More generally, what impact will the Internet have on the way governments raise money?

The matter arose in two recent GOP presidential debates. Safe in the knowledge that a Republican can't go wrong opposing taxes, all the candidates, with the notable exception of George W. Bush, declared that the Internet should remain a tax-free zone.

John McCain is leading the anti-tax charge. Hailing the Internet as "the greatest engine of economic growth in our time," the Arizona senator says that "we must resist the temptation to choke off" its growth through taxation.

But even some e-commerce purveyors acknowledge it's not that simple. And you can bet that owners of "brick-and-mortar stores," who probably don't refer to themselves in exactly those words, will be howling for a level playing field as Internet sales to continue to grow.

For now, a moratorium on taxing e-commerce is in place and a commission is studying what to do. Both are the result of the federal Internet Tax Freedom Act of 1998, which also banned taxes on Internet access fees. The moratorium will be in place for two more years; the commission is supposed to report in April.

The argument in favor of taxing Internet (and catalogue) sales is being spearheaded by the National Governors' Association, with the support of organizations representing the nation's cities and counties. No surprise there. State governments

get more than 40 percent of their revenue from sales taxes. They're the ones that take the hit when you buy that new video camera on-line rather than from the store at the mall.

Aside from complaining about lost revenue, the governors raise questions of fairness — not just for local merchants but also for people of modest means. The argument is this: The poor are less likely than the rich to have the ability to buy online. So exempting Internet sales from taxation, the governors say, "disproportionately benefits wealthy consumers."

Bush, who's one of those governors, would like to see the states get a piece of the action. And he's put off taking a formal stand until the commission completes its work. For that, he's getting hammered by McCain and Steve Forbes. They say he lacks the foresight to give the Internet the chance to realize its potential.

Frank Shafroth, director of state-federal relations for the governors' group, dismisses such talk: "Those poor, infant e-commerce companies, AOL, Microsoft and Amazon. They really need our protection."

Counters Dave McClure, executive director of the U.S. Internet Industry Association: "In the era of the global economy, a 1930s-style, horse-and-buggy, sales-and-use tax doesn't make any sense."

In essence, the industry's case rests on two points, only one of which has merit.

Point one, the weak one. An Internet business shouldn't pay local sales tax because it doesn't use local services. This is utterly specious. The tax is paid by the buyer, not the seller, and the money raised provides services for the area in which the buyer lives.

The better argument concerns practicality. Requiring on-line businesses, especially start-ups, to collect sales tax based on the buyer's home address would be a logistical nightmare. Each state has its own tax rates, often with variations from county to county, its own exemptions and its own arcane ways of defining those exemptions. Is a bag of marshmallows food and exempt, or is it candy and taxable? It depends on where you are. In some places, it depends on the size of the marshmallow.

The governors acknowledge that sales taxes must be simplified and standardized. And sophisticated software, they say, should make it possible for e-businesses to collect the right amounts and send them along to each state.

Making accommodations won't be easy for either camp. But ultimately, something will have to be done.

If not, the result will be higher state income taxes, higher local property taxes or fewer government services. None of those sounds like a price worth paying.

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