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Personal Statement of Stanley S. Sokul

As a Member of the Commission I represented the Association for Interactive Media (“AIM”), a trade association of companies that do business on the Web. AIM has some large, well-known members, but its heart and soul are smaller e-businesses whose daily struggles make the Internet economy such a dynamic place.

Internet sales taxation affects AIM members directly. The wonderful thing about the Internet – its instant national market access – also makes state tax designs potentially devastating to Web businesses. Most people do not realize that Internet sales are already subject to tax in the 7,600 state and local jurisdictions with a sales tax. The controversy exists because states can and do force in-state merchants to collect sales taxes, but they cannot force out-of-state merchants to do the same. The Supreme Court has twice ruled that imposing *every* state’s tax system on a company with cross-border sales would place an unconstitutional burden on interstate commerce. Under these rulings, only if the company has some form of physical presence, or “nexus,” in a state, can that state force the business to collect its taxes.

Consequently, the Internet sales tax issue is actually a collection issue, not a taxability issue, and involves the scope of state tax powers. Our Founding Fathers confined state tax powers to their borders a long time ago, and nothing about the Internet calls for abandoning their basic wisdom. To solve the Internet tax “problem,” states seek new nationalized tax authority to force out-of-state businesses to collect their taxes. The Commission refused to endorse this power quest. I hope Congress will do the same.

While states and localities complain of revenue shortfalls and some “local” and mass retailers complain of “unfairness,” the issue really boils down to whether electronic merchants should be subject to the full weight of every state and local tax system – including those jurisdictions in which they have no presence, receive no services, and enjoy no political representation. Knowing every jurisdiction’s definitions of taxable items and exemptions, and collecting and remitting appropriate taxes, would be burdensome enough. Being subject to the audit and enforcement machinery of every state and locality as well is downright frightening.

Also frightening are the privacy implications of taxing electronic commerce. The Commission process exposed, but did not resolve, some difficult privacy issues. Internet merchants know first-hand the high sensitivity consumers have to privacy matters. The specter of the government forcing the collection of private purchase information, in large multi-state databases for tax purposes, may cause consumers to flee e-commerce in droves.

Furthermore, the proposed expansion of tax burdens that would confront U.S. electronic merchants could never be enforced internationally as a practical matter. Thus, our global competitors would perversely gain new advantage in our domestic marketplace.

For all these reasons, granting states the nationalized tax powers they seek would significantly discriminate against electronic commerce. A solid majority of the Commission wisely sought the opposite result. Extending the Internet Tax Freedom Act would prevent electronic commerce from being subject to specific, discriminatory taxes. Asking states to simplify their Depression-era tax systems highlights the proper problem: namely, the overly burdensome nature of those tax systems themselves. The major success of the Commission process was to reveal the current condition of state and local tax systems – and they are not a pretty sight. Additionally, telecommunications tax simplification and the elimination of the federal communications excise tax would make the Internet backbone less expensive, and thus Internet access more affordable to help close the Digital Divide.

The need to clarify nexus standards with bright line safe harbors deserves particular mention. Such clarification would halt the constant churning of litigation that results from the states' relentless push to chip away, state-by-state, at nexus protections in the courts. The reality of aggressive nexus interpretations, and the associated filing or threats of litigation, are real problems for AIM members and a growing drag on electronic commerce. Small businesses do not have the wherewithal to fight, and thus bear the brunt of questionable tax burdens.

Finally, Congress cannot forget the big picture. The Internet is driving a dynamic economy under which retail sales are surging and state coffers are overflowing. Congress should do nothing to undermine this engine of record prosperity, but rather act decisively to preserve it.

It was an honor to serve on this Commission. I thank Senator Trent Lott for his appointment, and hope I lived up to the trust he placed in me.



Stanley S. Sokul