

# INSIDE *A*LEC

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## SPECIAL ISSUE

**INTERNATIONAL RELATIONS +  
TELECOMMUNICATIONS &  
INFORMATION TECHNOLOGY**

**Promoting U.S. Competitiveness  
through 21st Century Trade  
Agreements**

By Gina Vetere

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**In a Battle Over Internet Taxes,  
Both Sides Invoke States' Rights**

By Steve DelBianco

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**ALEC Alumni Spotlight**

By U.S. Rep. Tom Graves (GA)

# In a Battle Over Internet Taxes, Both Sides Invoke States' Rights

BY STEVE DELBIANCO

It's hard enough to wade through political rhetoric to get to the core issues of a legislative debate, but that becomes much harder when both sides sing the same tune to rally support for opposite positions.

At their annual meetings in August, two national groups focused on state legislation—the American Legislative Exchange Council (ALEC) and the National Conference of State Legislatures (NCSL)—took up the thorny issue of helping states collect more taxes on Internet transactions. One

law could at the same time undermine and uphold states' rights, one of the most valued legal concepts in our republic?

For the answer, we need a little background. Article 1 of the U.S. Constitution has a key provision known as the Commerce Clause, which precludes states from impeding interstate commerce. That was an essential condition of unifying the independent states back in 1787, as a way to prevent tariffs and trade barriers favoring in-state businesses.

Fast-forward to the 1960s when states demanded that catalog retailers collect

state's businesses and citizens against tax burdens imposed by foreign states. But lawmakers and tax collectors at NCSL say *Quill* impairs them from collecting all the sales tax due on Internet and catalog purchases. And they want Congress to overturn *Quill* so that Amazon and others will start moving that money from consumers' pockets to the state treasury.

Just how much money are we talking about here? The U.S. Commerce Department reports that 93 percent of e-commerce is business-to-business, where state tax auditors already collect any unpaid sales

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group opposed the national “streamlined” sales tax proposal and the other endorsed it.

And they both invoke the same reason for these opposing views: States' rights.

At the center of the debate is the *Main Street Fairness Act* introduced in Congress during the heat of July's debt ceiling debate. This legislation would let states collect more taxes on Internet sales, by establishing a “streamlined” collection system for sellers. But Internet advocates, my organization among them, point out that the measure imposes severe collection burdens, and actually swings the fairness needle in the wrong direction, helping big box retailers, while imposing new costs on small businesses who use the Internet to find new customers.

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their sales taxes, even where those catalogs had no operations in the state. The Supreme Court ruled then—and later affirmed in the *Quill* case—that state sales tax regimes were so complicated that they presented an unreasonable burden on interstate commerce.

Consequently, businesses are required to collect sales taxes only for states where they have a physical presence. So while consumers owe a “use tax” for out-of-state catalog and online purchase, states cannot force the businesses to collect the tax. However, when the business has physical presence, they must collect the sales taxes. That's why Amazon, for example, collects sales tax for only the five states where they have a physical presence.

Most ALEC members look at *Quill* and see a Constitutional way to protect their

tax. Another 4 percent of e-commerce goes to government customers, who don't typically pay sales tax. That leaves just 3 percent of total e-commerce on which sales tax is due from everyday consumers.

But every day, consumers are doing more of their online shopping at websites of multi-channel retailers like Walmart and Target, for the added convenience of in-store pickups and returns. Under *Quill*, these websites already collect sales tax for all states where they have stores or other facilities. In fact, 17 of the top 20 e-retailers are already collecting sales tax for at least 38 states.

So, if Congress overturned *Quill* and forced retailers to collect on all consumer e-commerce, the extra sales taxes would add only half of one percent to total state & local tax revenue.

Clearly, overturning *Quill* is no silver bullet for strapped state budgets, but it's become a major lobbying campaign for some state legislators and big-box retailers.

And both sides have some basis to cite “states rights” to either uphold or upend the *Quill* standard of physical presence. But in this summer's debate among legislators, not once did a sales tax advocate acknowledge that *Quill* and the Commerce Clause arose from necessary constitutional protections for interstate commerce.

Reasonable people on both sides can disagree on whether a voluntary group of states have sufficiently simplified their sales tax systems to justify overturning *Quill*. We're talking here about the *Streamlined Sales Tax Project (SSTP)*, a 10-year effort to simplify state and local sales taxes and get Congress to require retailers to collect for SSTP member states.

But SSTP advocates seldom acknowledge that this federal law would impose collection burdens on businesses in all 50 states—including those in states that don't join SSTP and those in states that don't even have a sales tax. To the contrary, many pro-tax advocates sought to reassure legislators that they would retain their state sovereignty, telling them, “you don't have to join SSTP,” and “you can drop out any time you want.”

But if Congress mandates SSTP, lawmakers in all 50 states would lose the sovereign right to protect their citizens and businesses from tax burdens imposed by other states. If these new collection burdens are hurting businesses in a state, their legislators won't be able to rescue them once Congress makes it mandatory.

This comes as a surprise to many lawmakers who are just getting their arms around the SSTP and its accompanying



Congressional mandate. And it will come as a complete shock to businesses all around the country if they have to start collecting for 9,000 tax jurisdictions.

That's when lawmakers and retailers will be singing the blues over the loss of

constitutional protection from foreign state tax burdens. SSTP advocates, however, will be singing the refrain from *Hotel California*, where “You can check-out any time you like, but you can never leave”. 🎷

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