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GUEST EDITORIAL

Taxing Internet sales is a recipe for big government

Unwilling to cut spending in the face of shrinking revenues, state governments nationwide are getting creative about taxing purchases made over the Internet.

North Carolina, which announced that its 1999 personal income tax form would require taxpayers to report and pay use taxes on items purchased out of state, has a bill pending that would interpret existing laws as requiring companies having local "marketing affiliates" to collect state sales taxes on items purchased from remote retailers. Amazon.com immediately dropped its North Carolina affiliates and other Internet businesses, such as Overstock.com and Blue Nile, Inc., have threatened similar action.

Legislative creativity is needed because the Supreme Court ruled in *Quill Corp. v. North Dakota* that requiring retailers located in one state to collect sales taxes from customers residing in another unconstitutionally burdens interstate commerce. As a result of that ruling, sales taxes are due on mail-order and Internet purchases only if the seller has a substantial "physical presence" in the customer's state of residence. Although buyers in every state that imposes a retail sales tax are obliged to report and pay "use" taxes on items purchased elsewhere, that proviso is difficult to enforce and, hence, few consumers willingly comply.

The proponents of taxing Internet commerce claim that it is simply a matter of "fairness". Under the current Internet-tax-free regime, brick-and-mortar retailers supposedly are placed at a competitive disadvantage because they must collect sales taxes from their customers, while their rivals located in other states do not.

So what? Brick-and-mortar retailers have competitive advantages of their own. They offer customers opportunities to "touch and feel" their products, to make comparisons on the spot, to accept immediate delivery and to avoid paying sometimes hefty shipping and handling charges.

The goal of promoting a level playing field is nothing more than a money-grab. North Carolina state senator David Hoyle admitted as much when he said that collecting sales taxes from out-of-state retailers would yield between \$150 million and \$200 million in additional revenue per year.

But "leveling the sales tax playing field" has serious consequences for our federal system of government. A retailer in, say, the State of Washington, who sells a product to a customer located in North Carolina, imposes few, if any, burdens on the local public sector. That remote retailer's children do not attend North Carolina's public schools, nor do its employees use the state's roads or place demands on any of the state's other public goods or services. On the other hand, the common carrier that delivers the remote retailer's orders already does pay local taxes.

The bottom line is that Internet taxes break the link between benefits received and taxes paid. An e-tailer located in the State of Washington, required to collect North Carolina sales taxes on an item shipped to a customer there, receives nothing in return. Moreover, that Washington e-tailer has no political voice in North Carolina and therefore has no influence over how high its taxes will be or how prudently tax revenue is spent. Insulated from competitive market forces by a policy that all retailers, wherever located, be required to collect North Carolina sales taxes on items shipped there, local retailers, in turn, have little incentive to oppose increases in local tax rates. Facing less political opposition to higher levels of spending and higher taxes to finance it, North Carolina's politicians predictably have a freer hand to pursue their own parochial self-interests.

When the playing field is leveled by forcing Internet companies to raise their prices by collecting sales taxes and remitting them to the treasury of the state where the purchaser resides, the inter-jurisdictional tax-rate competition is short-circuited and taxpayers become more vulnerable to exploitation by big government.

As Chief Justice John Marshall once said, "the power to tax is the power to destroy". The Internet is one critical constraint on that power.

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