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**Subject:** Hawaii Bill 1405 - Dean Takamine

Dean Takamine

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Online Advertising & Marketing

### **Dear Hawaii House of Representatives and Senators:**

I have taken a lot of time to write this letter and would greatly appreciate it if you would spend a few minutes of your precious time to read it.

I am writing in opposition to **HB1405** (the "Amazon Tax"), which would drive hundreds of U.S. companies to exclude Hawaii publishers from their advertising budgets. The lost income tax will exceed any sales tax collected.

#### **1. The Problem: Sales & Use Tax Evasion**

At the outset, I must acknowledge the "real problems." First, the U.S. Supreme Court ruled in the *Quill Corp. v. North Dakota* that a company's mailing of thousands of catalogs to a state's residents, plus solicitations and other contacts by telephone, and shipment of orders into the state were an insufficient "nexus" to permit the state to impose the burden of sales-tax collection on an out-of-state company. *Quill* instead requires "physical presence" before a state may impose sales- or use-tax collection duties on that merchant.)

Second, the "use tax" is ignored and is not paid by more than 99% of consumers who purchase products from out-of-state retailers.

The solution to these problems is clear (but not simple): Hawaii should initiate or join a "multistate sales tax" effort. That hasn't happened.

#### **2. HB1405's Apparent Intent:**

I believe HB1405 was intended to capture sales taxes in the same way as New York's "Amazon Tax." Sales tax collection duties would be imposed on any out-of-state company which pays Hawaii residents who "solicit" customers. New York's salestax

collection agency has interpreted this law to apply only to “solicitation” activities and not ordinary advertising. The “Amazon tax” laws focus on a popular form of “commission-based advertising,” generally referred to as an “affiliate program.”

These laws are widely referred to as “The Amazon Tax” not only because Seattle based Amazon.com is the largest company selling to many states without collecting sales taxes, but also because the sales taxes “newly collected” by Amazon.com are widely expected to exceed the total of new sales taxes collected by *all other companies combined*.

The “Amazon Tax” identifies (or fabricates) a Hawaii “physical presence,” to require sales-tax collection without challenging *Quill*.

### 3. HB1405’s Overbreadth (Initial Draft Defects)

As drafted, HB1405 is absurdly overbroad. It would impose sales-tax collection duties on any company which places **any advertising** through **any publisher or broadcaster** in Hawaii (including ads through Google’s AdWords system, which is used by nearly all e-commerce retailers worldwide). HB1405 would thus require that **every** out-of-state company compute, collect, report, and remit sales taxes for **all** of its Hawaii customers, *unless* the company can persuade Hawaii that all of its Hawaii advertising combined drove less than \$10,000 in sales to Hawaii residents. This reaches far beyond the scope of *Quill*.

Worst are the vague phrases “or other consideration,” “or otherwise,” and “directly or indirectly refers potential customers.” As drafted, HB1405 would impose sales-tax collection requirements on tens of thousands of companies which lack any “nexus” with Hawaii under *Quill*. (The “saving language” in the final sentence won’t make the bill valid – not only because it is completely vague, but also because it imposes an administrative or legal “proof” requirement on companies with no “nexus.”)

I won’t attempt a detailed legal analysis of the first draft of HB1405. If passed as written, the law would be stricken by *any* court. (And yet, a future ruling would **not** help tens of thousands of Hawaii web publishers terminated by hundreds of out-of-state merchants when the law passes.)

I assume that during the legislative process, HB1405 will be **amended** to conform with *Quill*, and to more closely mirror the New York law (as interpreted by New York’s sales-tax collection agency), so that HB1405 would apply only to “solicitation” activities which are “something more than ordinary advertising.”

However, I will continue to oppose an amended bill: **any** version of an “Amazon Tax” will cause hundreds of out-of-state companies to cancel their relationships with Hawaii publishers (including me).

#### 4. An “Amazon Tax” will *not* increase Hawaii tax revenues.

##### A. Sales Tax Collections Would Increase – Nominally.

In response to the New York “Amazon Tax,” Amazon reportedly began collecting and remitting sales tax on orders shipped to New York residents. I assume that this amounted to “millions of dollars” and I assume that Amazon would collect “*more* millions of dollars” for Hawaii if HB1405 passes. Dozens of much smaller out-of-state retailers also began collecting New York sales taxes because of the law; the total sales taxes collected by *all* those firms *combined* is almost certainly less than the amount collected by Amazon alone.

##### B. Income Taxes Would Be Lost.

###### i. Hawaii Publishers Will Be Terminated.

When New York’s “Amazon Tax” was enacted, **several hundred** companies responded by immediately **terminating** their relationships with **all** New York web publishers (affiliates).

**Among these firms were:** Overstock.com [UT], NetShops [NE], CSN Stores [MA], Luggage.com [MA], Home, Shopping Network [FL], Oriental Trading [NE], OnlineShoes.com [WA], Fingerhut [MN], Northern Tool [MN], Musician’s Friend [OR], Footsmart [GA], DVD Planet [IL], uBid.com [IL], Woodwind & Brasswind [IN], Gaiam.com, [CO], MyTwinn [CO], LinenSource [FL], ReStock It [FL], J&P Cycles [IA], Leaps And Bounds [IL], One Step Ahead [IL], Spilsbury [IL], Garden’s Alive [IN], Gurneys [IN], Henry Fields [IN], Tিরerack [IN], Shopper’s Choice [LA], Karmaloop [MA], Acorn Media [MD], ShopNBC [MN], ustoy.com <<http://ustoy.com>> [MO], Silhouettes [NJ], Michigan Bulb [OH], Palo Alto Software [OR!], Eastwood Company [PA], Spring Hill [TN].

Hundreds of out-of-state merchants concluded that the burden of collecting sales taxes from New Yorkers was greater than their lost sales from terminating all New York affiliates. Ironically, many of these firms would probably never be required to collect tax, under the New York or Hawaii laws – but the “compliance costs” to document the law’s non-applicability, combined with audit risks, possible retroactive imposition of taxes and penalties, and costs to dispute any assessment, were far too great for these firms to accept.

After these merchants announced that they would be terminating their New York affiliates, some New York residents actually **moved** from New York to other states, in order to continue their successful advertising relationships with these merchants. Amazon.com has already stated that if Hawaii passes this bill it will terminate their

Hawaii affiliates.

If HB1405 is passed, these same companies, and many more, will almost certainly choose to terminate their relationships with Hawaii publishers. As a result, tens of thousands of Hawaii residents (including me) would lose income, and some Hawaii residents (those with the most earnings) would move to another state to maintain their business relationships with these merchants.

ii. Reduced Income Means Reduced Income Tax

Hawaii collects substantial **income taxes** from Hawaii residents (including me) who are web publishers participating in “affiliate programs.” Nobody really knows how much.

There is no specific “classification” that would enable the state to identify (for example, from tax-return data) the amount of the income or taxes associated with commission-based advertising or “affiliate program” activity by Hawaii web publishers; indeed, there is no way to isolate advertising revenue associated with “web publishing” from other forms of publishing and advertising revenue.

Of course, individual out-of-state retailers like Amazon.com know how much they pay to Hawaii publishers through their “affiliate programs,” and how many dollars of sales those affiliates influence – but there are *tens of thousands* of such companies, few of whom are likely to cooperate with Hawaii’s efforts to optimize sales tax collection. (Most of these firms would probably not technically be included by the Hawaii law, if their affiliate-driven sales to Hawaiians fall below the \$10,000 threshold). There are also several dozen “affiliate networks” and “affiliate technology providers” (like Santa Barbara’s Commission Junction) who possess data from hundreds of individual retailers who utilize their technology – but such firms probably can’t lawfully disclose this confidential information.

I simply don’t know how much revenue is earned by Hawaii web publishers from affiliate programs. Nor can we identify, with reasonable confidence, the amount of income tax paid on those earnings. We just don’t know.

I believe that the total sales taxes collected as a result of HB1405 would be **less than** the amount of income tax lost due to the law’s passage. But I don’t have “hard data” to persuade you. (If someone claims to have “hard data,” I’d be glad to explain why their data is actually “soft.”)

## 5. Who am I? How would HB1405 affect me?

Since 2004, I have been self-employed as a “**web publisher**” and online advertising consultant. I produce original content (articles and directories) which I publish on

my own web sites. I also do online advertising consulting for many online companies on the mainland and get paid by commission.

We refer to commission-based advertising programs as "**affiliate programs**" (Amazon calls theirs an "Associates Program"; a few companies call them "partner programs"). Commission-based advertising isn't new or unique to the internet: it has been used in newspapers and magazines for more than a century, and in radio and television for decades.

This type of income makes up more than 95% off my income.

**If HB1405 passes, my business will be wiped out over night.** As explained below, I expect many of my merchants who currently work with to terminate their relationship with me if I remain a Hawaii resident. If this occurs, I would need to find some other source of income to support myself.

**If HB1405 passes, I will no doubt have to move my company out of Hawaii.**

Which is very unfortunate for me because I was born and raised in Hawaii. I was educated by the Hawaii public school system then later graduated from the University of Hawaii with a Computer Science degree. 99% of my income comes from out of the state of Hawaii which means my company brings money into the Hawaii economy. I strongly believe this bill is a lose-lose situation.

## **6. Conclusion.**

As drafted, HB1405 is absurdly overbroad and unconstitutional. Even if it is amended to more closely mirror New York's "Amazon Tax" law, HB1405 would still result in a loss of income for many of Hawaii residents, and I believe that the income tax lost would exceed the new sales tax revenue collected.

**Please vote against this bill.** Thank you for your consideration.

Sincerely,  
Dean Takamine

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