

# IMPACT OF E-COMMERCE LEGISLATIONS ON BUSINESS

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## Abstract

*In recent years, electronic commerce has seen widespread adoption and growth. It is estimated that online sales have surpassed \$2 billion and is growing rapidly. Apart from companies that purely perform their business on the Internet, other companies have in many cases established an electronic storefront. With this growth in business, states have enacted legislation that applies primarily to electronic commerce. Unlike other forms of conducting business, electronic commerce cuts across state lines and therefore it is vital for companies to know the legislation in various states. Such knowledge will assist them in formulating their business strategy and be in compliance with the law. This paper analyzes and compares the variances of electronic commerce legislations between states. In addition, it also studies the strategic and legal ramifications of this variance on organizations implementing e-commerce in their business practices. Overall, it was found that there is lesser variation between states when dealing with e-commerce legislations on trademarks/copyrights and privacy/security when compared to legislations dealing with taxation and digital signatures.*

**Keywords:** e-Commerce, legislation, digital signature, taxation

## INTRODUCTION

In recent years, electronic commerce has seen widespread adoption and growth. It is estimated that online sales have surpassed \$2 billion and is growing rapidly. Apart from companies that purely perform their business on the Internet, other companies have in many cases established an electronic storefront. Examples of such businesses range from book sellers such as Barnes and Noble to retailing giant such as WalMart.

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### **Electronic Commerce defined**

Electronic commerce includes a wide variety of activities including interactive order processing at established web sites and electronic data interchange of business transactions between present and future business partners, and secure electronic funds transfer (EFT) payment systems (6).

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### **State-to-State Comparison of Electronic Commerce Legislation**

Some of the benefits of e-commerce include the ability of businesses to move away from the time consuming, paperbound business practices and into the paperless transaction based future that will save money on all fronts and give equal footing to small and large businesses alike. Firms can now choose from vendors without regard to location. In addition, increased possible speed to market and reduced costs of access may also lead to added scope for innovation by firms that can compete effectively for customers' attention. The technology itself makes possible methods of purchase, and forms for delivery of services that are new (2). Due to increased reliance of e-commerce in organizations, it has become imperative to understand the laws governing such transactions.

To understand electronic commerce legislation we need to analyze the components or areas that such legislation will affect. For example, consider a company headquartered in New York with sales operations in California, database and web servers in Virginia and the shipping operations are in Georgia. The first critical question is, which state's laws should be applied? Traditionally, the law of the state where the transaction occurs is applied. The issue becomes complicated when B2B transactions are made in multiple states. In that case, the application of the law can be ambiguous.

In addition to this, important e-commerce issues are: a. what is the validity of electronic and digital signatures/transactions? b. how will electronic commerce be taxed?, c. what are the issues related to electronic commerce privacy and security? and, d. what are the issues related to copyrights, trademarks/the uniform trade secret act? This leads us to further analyze the state-to-state comparison of e-commerce legislation in the following sections.

#### *Digital/Electronic Signature*

Most states have similar definitions of electronic signatures. It is a symbol or a series of symbols logically associated with a record and executed or adopted by a person with the intent of signing the record. Some states (e.g., Mississippi) have extended the definition of digital signatures to include electronic sounds and processes. A digital signature is synonymous with an electronic signature, however; typically there is an added requirement that some form of encryption scheme be used with the electronic signature to make it a digital signature.

The legislation in almost all states work with the fundamental premise that the goal of the definition as well as the laws that govern electronic/digital signatures will be to facilitate electronic commerce and not impede it. However, the legislation in these states also makes the use of electronic transactions voluntary. Moreover, even if two parties agree on some form of electronic transfer of documents an electronic signature is not necessary. In some states like Alaska, where laws relating to electronic signature are still being developed, handwritten signature should follow the electronic version. Several states, however, authorize the general use of electronic signatures only for transactions involving government entities. Delaware and

Maryland are the states in this category. Besides that, New Jersey has statutes that authorize the use of electronic signatures only for certain categories of transaction, which are medical records. Therefore, only business related to medical field may take this advantage and benefit of having the electronic signature.

States that have accepted electronic signature have given it the same force as that of a written signature. In most cases certain conditions apply. This includes verifiability, in which it can definitely be verified that the signature belongs to the person in the agreement. Uniqueness is another typical requirement, so that no other person or entity can have the same electronic signature.

The Uniform Electronic Transaction Act (UETA) (7) is an act that allows for the e-transaction and signature to have the same binding contractual effects as a paper transaction with a written signature. Currently 42 out of the 50 states have adopted this act. The states that have not adopted this legislation are: Alaska, South Carolina, Washington, New York, Georgia, Massachusetts, Illinois, and Wisconsin. All of these states have currently enacted legislation of their own design allowing for the validity of electronic and digital signatures to be equal to that of a written signature.

#### *Taxation of Electronic Commerce*

In 1998 the US House of Representatives passed the Internet Tax Freedom Act which creates a body designed to consider possible changes in the law of taxation on the Internet (8). This Act included provisions for a ban on new local and state taxes that discriminate against electronic commerce. It also called for the US Administration to put pressure on other countries to refrain from taxation of the Internet.

According to the Information Technology Association of America, there should be no discrimination between products on the basis of whether they were sold on-line or by conventional means. They single out the case of purchasing tangible goods over the Internet, which are later delivered. These, says the ITAA(5), should be treated in the same way as mail order purchases.

Taxation of electronic commerce is still evolving. While in general, most states have some taxation on either goods or services (or both) transactions over the Internet, some do not. Even in states that have taxes for Internet goods or services, there are many exemptions. Typically, taxation issues can be classified into the following categories: a. internet access charges. b. sales of goods purchased over the Internet and, c. information/software purchased via downloading from the Internet.

In most states, Internet access charges are not considered a taxable telecommunications service and are therefore not subject to either sales tax or other taxes. One time set up charges is not taxable. In some cases (California, for example), there is a moratorium on these charges. Once the moratorium ends, charges may be imposed or the status quo maintained. In 1998, the federal government declared a 3-year moratorium on Internet access charges. This barred state or local governments from taxing Internet access. The handful of states that had already taxed Internet

access (for example, Texas) could continue to do so, if they could demonstrate that their taxes had been “generally imposed “and actually enforced” prior to October 1, 1998. This was reauthorized for two more years as the Internet Tax Nondiscrimination Act. Currently ISPs are seeking a permanent ban (1). In the meantime, some states like Texas eliminated its tax on Internet access priced below \$25 a month. What eventually happens is yet to be seen. There is also a sense that there should be no federal taxes for Internet access. Some states (e.g., Ohio) do not have Internet access charges for individual customers but have an Internet access charge for businesses.

Different states apply different sales and use taxes in various goods and services. The majority of the 50 states tax sales of goods or services as if the sale had taken place physically within the state. In other cases, the sale of goods is taxed only if the business has sufficient nexus in the state. In these cases, an e-business has to determine states in which it has nexus for sales and use tax purposes. Some states like Oregon, Delaware, New Hampshire, and Alaska do not have sales tax for Internet sales transactions. Other states such as Hawaii have special sales tax legislation regarding the Internet. Hawaii has a special 4% sales tax on e-commerce transactions.

In some states, including California, taxation is subject to the rules of nexus. In this case, the retailer should have sufficient nexus to require collection of use tax. A retailer’s advertisement and taking of orders through the Internet web site is not considered for determining nexus. Therefore if a retailer has no other presence in the state, it will not be required to collect use tax from its California customers. Alaska does not have a sales tax; however, individual localities have the right to impose their own taxes. In the states where there is a sales tax, sales of goods purchased over the Internet are treated the same as sales of tangible personal property and are subject to sales/use tax laws. Tangible personal property is something that can be seen, weighed, measured, felt or touched (e.g., Idaho). In most cases, intangible personal property is exempt from taxes. Intangible personal property lacks physical existence but represents or has evidence of value. This includes copyrights, patents and software. Examples of tax exempt intangible personal property will be, shares of stocks and bonds traded over the Internet

While software is treated as intangible personal property, states may or may not tax software. Consideration also has to be given to whether the information/software was downloaded from the Internet or not. Most states do not have taxes for software downloaded from the Internet. Some states, like Arizona have a policy of charging use tax. Idaho has a policy of charging tax on downloading of information/software over the Internet. Utah considers software as taxable tangible personal property regardless of the form in which it is transferred or purchased. Connecticut provides an interesting example for information/software purchased over the Internet. Beginning 7/1/97 sales and use taxes on computer and data processing services were phased out over a six-year period. Initially, the tax rate was 5%. From 7/1/02, these services became totally exempt from sales/use tax. Canned software is considered tangible personal property.

The lack of uniform state laws governing e-commerce transactions led to the development of UCITA(Uniform Computer Information Transactions Act). This is a contract law statute developed by the National Conference of Commissioners on Uniform State Laws (NCCUSL) that would apply to computer software, multimedia products, computer data and databases,

online information, and other such products. It was designed to create a uniform commercial contract law for these products and calls itself "a cyberspace commercial statute." It covers contracts that are generally known as "shrink-wrap licenses."

Although UCITA was introduced in a number of legislatures in 2000, only two enacted it, both with amendments. In Virginia, UCITA was enacted with a delayed effective date of July 1, 2001 and creation of a commission to look into user concerns in the meantime, so there may be amendments before the effective date. During the Virginia legislative consideration, several industry groups such as MPAA, newspaper and magazine publishers, music recording companies and telecommunications--negotiated exclusions from UCITA. To deal with general user concerns, the commission was set up as a compromise, to put off reckoning with the mounting opposition expressed in Virginia by many business users, library organizations and consumer advocates, among others.

UCITA also was enacted in Maryland, with an October 1, 2000, effective date. In addition to the exclusions in the Virginia version, the insurance industry got a partial exclusion from UCITA's scope in the Maryland version, but neither insurance regulators nor industry representatives were fully satisfied. The Maryland attorney general was unsuccessful, however, in efforts to use the strategy of industry groups and have consumer transactions excluded from UCITA. The largest volume of transactions covered by UCITA will be consumer contracts.

UCITA has two prominent features. First, it validates terms held back until after payment and delivery, presented in so-called "shrinkwrap" or "clickwrap" contracts. Second, it re-characterizes software and digital content contracts as "licenses" of use, rather than sales of copies, raising two issues that will require a great deal of litigation to resolve. The first issue is whether consumer protection laws applicable to "sales" of goods and services apply to these transactions. The second is whether software and digital content providers can use license terms to rewrite users' basic intellectual property deal, for example by taking away the right to transfer a copy, criticize a product or quote content. Both of these features are harmful to consumer welfare.

Legislation has yet to scratch the surface of dealing with taxation on individual Internet e-commerce transactions. Businesses emerge daily under the guise of C2C sales. Individuals purchase merchandise wholesale, repackage and/or reconfigure the products and then resell them over the Internet, paying no attention to the various laws that regulate the same activity in the brick and mortar business world. Currently there are few laws to stop these kinds of transactions from taking place.

### *Electronic Commerce Privacy and Security*

Many states such as Alaska, Hawaii, Louisiana, Oregon and Washington follow the federal online privacy laws. Others states such as California and Arizona have legislation to address this issue. Most states provide Internet security and privacy legislation based upon the interception of personal communication. This excludes businesses or other agencies monitoring email. This also excludes any interception necessary to the protection of children. The Children's Online Privacy

Protection Act specifically protects the privacy of children under the age of 13 by requesting parental consent for the collection or use of any personal information of the users (3).

Consumer Protection is a continuous fight in the e-commerce community. There is currently legislation prohibiting the misuse of consumers personal and credit card information. Online businesses understand the need to keep financial information private up to a point. Their ability and responsibility to do is always a concern. Many companies have yet to view using insecure software/processes akin to a bank leaving the safe open and the front doors unlocked, even though the end result is the same. Keeping consumers email addresses private is another matter altogether.

Spam mail is the latest consumer privacy concern. The Unsolicited Electronic Mail Act was passed in July of 2000 will bar email marketers from sending Spam unless the message gives identification that it's an unsolicited commercial advertisement; the bill also will support the enforcement of opt-out measures (4). This bill requires that businesses pushing their solicitations include a return email address that consumers can respond in order to be removed from the distribution. What remains to be regulated is the sale and purchasing of bulk email addresses by those companies.

#### *Copyrights and Trademarks/ Uniform Trade Secret Act*

Copyright ability, gives the author the ability to enforce certain exclusive rights in a work. These include the exclusive right to reproduce work, to distribute copies, and to prepare derivative works (17 USC #106 (1982)). The question of whether computer programs are copyrightable subject matter has been extensively debated (17 USC 301 (1982)). Computer programs are within the scope of copyright law (17 USC 301 (1982)).

In order to address the issue of copyright ability, virtually all states have adopted a portion of or modified version of the Uniform Trade Secrets Act, which was drafted by the National Conference of Commissioners on Uniform State Laws in 1970 and amended in 1985 (4).

The UTSA provides the protection of information, including a formula, pattern, program, device, method, technique, or process that has economic value, either actual or potential. Federal Copyright and Trademark statutes include software and have been adopted by most states. What this means is computer code is treated like works of literature in regards to ownership, reuse, repurposing or theft (9)

Currently the Internet community is in an uproar over P2P (Peer to Peer) music file sharing. The RIAA (Recording Industry Association of America) is waging a war on the activity based on the UTSA and the federal courts have upheld their request for subpoenas for individual user names from Internet service providers, alleged to be involved. Traditional businesses have learned to deal with shoplifting just as e-commerce must find a way to address the threat of collective theft of copyrighted works facilitated by the electronic medium.

## CONCLUDING REMARKS

Overall, it was found that there is greater uniformity between states when dealing with e-commerce legislations on trademarks/copyrights and privacy/security when compared to legislations dealing with taxation and digital signatures. Businesses need to make critical business decisions based on the laws of a particular state. For example, an ISP needs to know when and where taxes should be added for Internet access. In some cases a signature on paper has to follow a digital signature for a valid contract. In some other cases, the digital signature is sufficient. Similarly, businesses need to know when and how to assess taxes on goods and products sold. Corporate policies on how e-business has to be conducted stem directly from these laws because failure to comply with laws of the states may lead to expensive lawsuits.

In conclusion, e-commerce has brought the small town supplier into the view of the big city firm. Legislation gives the advantage of worldwide exposure to all firms and businesses along with the protection afforded those in the physical market place. An entirely new industry has come along with this new virtual world. Increasing not only the need for specific and specialized skill sets but also allowing for more innovative thinkers in the workforce. People are more important than ever in this virtual environment. The fear of people losing jobs to automated processes has been replaced with the race to find and hire skilled employees to maintain, manipulate, and grow the virtual enterprise.

Business between client and vendor is not the only aspect of business that has been moved into an electronic format. Many companies now use the Internet to provide a wide variety of products and services ranging from tangible good such as automobiles and furniture to intangible goods such as education and legal advice. There is no boundary as to what types of transactions can exist in e-commerce; Products, services, and in the case of eLearning even skills can be transferred over the Internet. Life in this virtual market place is constantly changing, and so is the legislation intended to keep us grounded.

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