

ORIGINAL

1 EXECUTIVE COMMITTEE MEETING ON MARKUP ON S. 442, THE  
2 INTERNET TAX FREEDOM ACT  
3 TUESDAY, JULY 28, 1998  
4 U.S. Senate,  
5 Committee on Finance,  
6 Washington, DC.

7 The meeting was convened, pursuant to notice, at  
8 10:34 a.m., in room SD-215, Dirksen Senate Office  
9 Building, Hon. William V. Roth, Jr. (Chairman of the  
10 Committee) presiding.

Gilmour  
35 pp.

11 Also present: Senators Chafee, Hatch, Nickles, Gramm,  
12 Mack, Moynihan, Baucus, Conrad, Graham, Bryan, and  
13 Kerrey.

14 Also present: Franklin Polk, Staff Director and  
15 Chief Counsel; Mark A. Patterson, Minority Staff Director  
16 and Chief Counsel.

17 Also present: Mr. Grant Aldonas, Chief Trade  
18 Counsel; Mr. Mark Prater, Chief Tax Counsel; Ms. Brig  
19 Pari, Tax Counsel; Mr. Faryar Shirzad, Trade Counsel; Mr.  
20 Jeff Kupfer, Tax Counsel; and Mr. Joseph H. Guttentag,  
21 Deputy Assistant Secretary, International Tax Affairs.

22 Also present: Mr. Donald Abelson, Chief Negotiator,  
23 U.S. Trade Representative.

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1 OPENING STATEMENT OF THE HON. WILLIAM V. ROTH, JR., A  
2 U.S. SENATOR FROM DELAWARE, CHAIRMAN, COMMITTEE ON  
3 FINANCE

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5 The Chairman. The committee will please be in  
6 order.

7 We are going to try to proceed as expeditiously as  
8 possible because it is my understanding there will be  
9 another vote, probably within a half hour. And, of  
10 course, we are anxious to report this bill out.

11 As you know, the Internet Tax Freedom Act was  
12 referred to the Finance Committee and we have to act on  
13 the bill by July 30. Towards accomplishing this, the  
14 Finance Committee held a hearing to look at tax and  
15 international trade issues related to the Internet on  
16 July 16. Based on information received in that hearing,  
17 we are now prepared to mark up a substitute to the  
18 Internet Tax Freedom Act.

19 The Chairman's mark we would begin with establishes,  
20 I believe, a sound foundation upon which Congress can  
21 appropriately address the issue of taxation and Internet  
22 commerce that brings together the objectives and concerns  
23 expressed by the parties involved in this important  
24 issue.

25 The Chairman's mark imposes a three-year moratorium

1 on taxes relating to the Internet. This period seems  
2 like the one most members feel comfortable with, and it  
3 provides adequate time for proper study and  
4 recommendations.

5 This mark also establishes a commission to study and  
6 make recommendations for international, Federal, State,  
7 and local government income and excise taxes of the  
8 Internet, and other comparable sales.

9 I am laying down a modification to the mark which  
10 increases the number of members on the commission from 13  
11 to 16. Finally, my mark includes international trade  
12 provisions that help ensure no unfair trade barriers or  
13 tariffs.

14 So, I believe this is a solid beginning. In the  
15 effort to meet the deadline that has been proposed, I do  
16 ask my colleagues to work constructively towards moving  
17 this mark forward.

18 So we will now proceed. We do not have Senator  
19 Moynihan here. Senator Kerrey, would you like to  
20 proceed?

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1 OPENING STATEMENT OF THE HON. J. ROBERT KERREY, A U.S.  
2 SENATOR FROM NEBRASKA

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4 Senator Kerrey. We could have some fun here today,  
5 could we not, Mr. Chairman? [Laughter.] Well, I do not  
6 know. I was intending to offer three or four amendments,  
7 Mr. Chairman, but the only two I really have a strong  
8 interest in getting adopted in the committee prior to  
9 reaching the floor is the one that would reduce it  
10 further from three years to two years, that Senator  
11 Chafee and I were going to offer.

12 The second, is just to get some report language in  
13 having to do with universal service, to make certain that  
14 the Universal Service Fund is not adversely affected by  
15 this language. I have been assured that it does not, but  
16 I am interested in getting report language to make  
17 certain that that does not happen.

18 So the only amendment that I would want to offer  
19 today, this morning, would be the one Senator Chafee and  
20 I had to reduce the time from three years to two.

21 The Chairman. We will instruct the staff to work  
22 with you on providing the language within the report.

23 Senator Kerrey. On the report language. Thank you.

24 The Chairman. With that, I will now call on Brig to  
25 walk us through the tax provisions.

1 Ms. Pari. Thank you, Senator. The Chairman's mark,  
2 very briefly, would impose a three-year moratorium on  
3 taxes imposed by States and local governments on services  
4 or electronic commerce after today.

5 The taxes subject to this moratorium are taxes on  
6 Internet access, bit taxes, and any multiple or  
7 discriminatory taxes on electronic commerce. This  
8 moratorium would apply to taxes imposed before July 29,  
9 1998.

10 The Chairman's mark includes a sense of the Congress  
11 that no new Federal taxes, like the State and local taxes  
12 subject to the three-year moratorium, should be enacted  
13 on Internet activity during the moratorium.

14 The Chairman's mark would establish a commission to  
15 study and make recommendations for international,  
16 Federal, State, and local government taxes on the  
17 Internet, as well as comparable interstate or  
18 international sales activities. The commission would  
19 have two years to submit its findings to Congress.

20 The Chairman's mark has been modified in two ways  
21 with respect to this commission. First, the commission  
22 would be made up of 16 members, as follows: four  
23 representatives from the Federal Government, the  
24 Secretaries of Treasury, Commerce, State, and the USTR;  
25 six representatives of State and local governments would

1 be appointed; two members each by the Speaker of the  
2 House of Representatives and the Majority Leader of the  
3 Senate; and one member each by the Minority Leader of the  
4 House and the Minority Leader of the Senate; and then six  
5 representatives of the electronic industry and of  
6 consumer groups would be appointed in the same manner.

7 The second modification to the Chairman's mark would  
8 require two-thirds majority for the commission to adopt  
9 a position.

10 I would now like to turn to the Finance Committee's  
11 Chief Trade Counsel, Grant Aldonas, to describe the trade  
12 provisions in the mark.

13 Mr. Aldonas. Mr. Chairman, the trade provisions of  
14 the Chairman's proposal would reinforce current  
15 administration efforts to keep the Internet free of  
16 either tariff or non-tariff barriers. The proposal would  
17 provide a clear statement of Congress' intent in that  
18 regard, and then outline the U.S. trade negotiating  
19 objectives.

20 Those objectives would be three-fold: first, assuring  
21 our trading partners do not impose either tariff or non-  
22 tariff barriers on electronic commerce itself; second,  
23 eliminating existing barriers to trade in goods and  
24 services via the Internet; and third, eliminating  
25 barriers to trade in goods and services, such as

1 telecommunications equipment and services that are  
2 essential to the future growth of electronic commerce.

3 Finally, the Chairman's proposal would amend Section  
4 181 of the Trade Act of 1974 to ensure that the U.S.  
5 Trade Representative included barriers to electronic  
6 commerce within the National Trade Estimates Report that  
7 it provides on an annual basis that provides a catalog of  
8 barriers that the USTR will target in future  
9 negotiations. Thank you.

10 The Chairman. Thank you, Grant.

11 We do have a roll call vote, so the committee will be  
12 in recess. We will reconvene promptly at the end of that  
13 vote.

14 [Whereupon, at 10:40 a.m., the hearing was recessed.]

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1 AFTER RECESS

2 [10:59 a.m.]

3 The Chairman. The committee will please be in  
4 order. We are now open to amendments. We have five  
5 here, so we can proceed.

6 Senator Kerrey. Mr. Chairman?

7 The Chairman. Senator Kerrey.

8 Senator Kerrey. Mr. Chairman, I would offer an  
9 amendment. I believe staff has the amendment. I do not  
10 know if they have distributed it, or I can just explain  
11 it to you.

12 In your mark, you have got three years. In the  
13 amendment I would offer, it would reduce it from three  
14 years to two years and require a report to be produced in  
15 18 months.

16 I would just say to my colleagues that I think  
17 Senator Chafee wants to offer this. This was originally  
18 his amendment, so I presume that he is still willing to  
19 do it. I was originally going to go just two years  
20 without the 18-month report, so I am basically offering  
21 Senator Chafee's amendment.

22 Members are very much familiar with complicated  
23 issues where we have dealt with it in even less time than  
24 this. I appreciate very much the Chairman changing the  
25 original bill from six years to three years, because I

1 think you are heading in the right direction. I would  
2 just urge colleagues that this is an unprecedented  
3 interference.

4 Maybe unprecedented is a bit strong. We, from time  
5 to time, intervened in State and local taxing issues. We  
6 did so in 1976, with the RRRR Act, and it created a  
7 tremendous amount of problem. I have had to live with  
8 some of the problems with property tax evaluations that  
9 occurred when we intervened on behalf of the railroads in  
10 1976 with the RRRR Act.

11 We generate almost \$700 million a year in sales tax  
12 in Nebraska. We are taxing all kinds of retail  
13 transactinos. I have a difficult enough time explaining  
14 at home why I would want to put a moratorium on an arae  
15 of sales where there is 30 percent real growth per month  
16 and I am not willing to put a moratorium--they are saying  
17 to me, if you have got to have a moratorium, why do you  
18 not put it on retail sales for automobiles, the retail  
19 sales for something we are selling there at home. But to  
20 put a long period of time for that moratorium, it seems  
21 to me, is not a good idea. I appreciate very much the  
22 Chairman going towards three years, and this amendment  
23 woudl take it to two.

24 Senator Moynihan. Would the Senator yield for a  
25 question?

1 Senator Kerrey. Yes, sir.

2 Senator Moynihan. Simply to say that the IRS  
3 Commisison, of which you and Senator Grassley were such  
4 distinguished members, did its work in 18 months. The  
5 Medicare Commission, of which Senator Breaux is a member,  
6 has, I think, 18 months. If you have to look into a  
7 question, your mind will begin to wander after 18 months.  
8 [Laughter.]

9 The Chairman. Yes. Any further comment? Senator  
10 Gramm.

11 Senator Gramm. Mr. Chairman, we have got a  
12 situation where the Commerce Committee has done six  
13 years. I would certainly have no objection to setting a  
14 shorter time limit on the condition for it, but I think  
15 we ought to have a three-year moratorium. I think when  
16 we finally get the report, it is going to take time for  
17 us to make a decision.

18 I think this is a very complicated area, and I have  
19 to admit that I am very much torn on many of the issues  
20 related to this. I think the bottom line is, we have a  
21 general area where we do not allow the taxation or the  
22 so-called moratorium, is we are dealing with a new--in  
23 any case, the logic of the moratorium is, we are dealing  
24 with a new and powerful tool and we do not want its  
25 growth stunted by action taken without people totally

1 understanding its potential. So, from that point of  
2 view, I am opposed to the amendment.

3 Senator Kerrey. Mr. Chairman, if I could add one  
4 additional point. There is no evidence that the growth  
5 of Internet sales is stunted today, that there is any  
6 barrier to the sales; quite the contrary, the growth of  
7 sales is impressive.

8 What this does, if we put a moratorium on taxing  
9 retail sales, what that does, is it means you are going  
10 to have a disproportionate burden that is going to fall  
11 on normal retail sales. There are \$740 million worth of  
12 sales tax applied to transactions in Nebraska, of that,  
13 almost \$400 million on retail trade.

14 We are offering no moratorium to those individuals,  
15 so that tax will continue. My guess is, if we showed the  
16 sales growth of normal retail trade versus Internet  
17 trade, you would see a rather substantial growth in  
18 Internet trade and rather modest growth--in some cases  
19 not at all--in other retail trade.

20 So, I mean, I just do not find the evidence to be  
21 overwhelmingly on the side of those who were saying that  
22 this is a fragile industry in its infancy that deserves  
23 special attention because it is struggling to reach its  
24 sales targets.

25 Senator Graham. Mr. Chairman?

1 Senator Chafee. Mr. Chairman?

2 The Chairman. Senator Chafee.

3 Senator Chafee. Mr. Chairman, this is not an  
4 industry that is exactly in swaddling clothes. Let us  
5 take a look at it. This is from testimony that we had  
6 the other day from the America Online people themselves:  
7 more than 100 million individuals worldwide are connected  
8 to Internet; 23 million American households have access  
9 to Internet, and network traffic doubles every 100 days.

10 They process 32 million pieces of e-mail to 105  
11 million recipients every day. This is not just some  
12 little venture, some thing that they are starting out,  
13 feeling their way along. Online consumer sales are  
14 projected to be \$20 billion by the year 2000. That is a  
15 year and a half away, an increase of 233 percent over  
16 today's levels.

17 So, Mr. Chairman, I do not think we have to weep  
18 tears over this organization. I think we are doing  
19 awfully well to give them a moratorium on State and local  
20 taxes for as long as suggested by this amendment. So, I  
21 very much hope that the amendment will be approved.

22 Senator Baucus. Mr. Chairman?

23 The Chairman. Senator Baucus.

24 Senator Baucus. Mr. Chairman, I would like to ask  
25 the author a question. Is it two years after which the

1 commission completes its study, and then the moratorium is  
2 over?

3 Senator Kerrey. Two-year moratorium, and the  
4 commission makes its report in 18 months.

5 Senator Baucus. I see. I was going to suggest two  
6 years, and then with a three-year moratorium. Two years  
7 for the study. But you have 18 months for the study, and  
8 just two years for the moratorium.

9 Senator Kerrey. Yes.

10 Senator Baucus. And that begins when?

11 Senator Kerrey. I presume it would begin upon  
12 enactment of the legislation.

13 Senator Baucus. So two years would be two years  
14 from now, end of the next Congress.

15 Senator Kerrey. Yes. Whenever it becomes law.

16 Senator Baucus. Assuming that it is enacted this  
17 year, the two years would be up near the end of the next  
18 Congress.

19 Senator Kerrey. That is correct.

20 Senator Baucus. I was just wondering if that is  
21 wise. It might make sense to have it end in the  
22 following Congress. I have some sympathy with the  
23 argument of the Senator from Texas, that this is  
24 extremely complicated and I do not know if we are going  
25 to get it resolved that quickly or not, frankly.

1 Senator Kerrey. Mr. Chairman.

2 The Chairman. Senator Kerrey.

3 Senator Kerrey. Mr. Chairman, let me just challenge  
4 this idea. I do not think it is any more complicated  
5 than Medicare. I do not think by any stretch of the  
6 imagination this is comparable to the complexity of  
7 Medicare.

8 We are supposed to finish our work in 18 months and  
9 get back to Congress with our recommendation. I mean,  
10 what is complicated about this? Describe the complexity  
11 of this. This is a fairly straightforward question: if I  
12 purchase something, do I have to pay tax on it?

13 I understand the industry is saying, it is  
14 complicated, if I collect it. Come on. I mean, this is  
15 the industry that is writing software. They know that  
16 they can solve almost any complicated problem with rather  
17 simple software.

18 The complexity here, is you have people that do not  
19 want to have tax collected on their transactions. That  
20 is where it gets complicated. The question is, do you  
21 want to tax them, not how do you unravel the----

22 Senator Baucus. Well, the reason I ask, is  
23 different jurisdictions may tax so much differently, that  
24 it could be a huge problem.

25 Senator Kerrey. Well, I will tell you what I think

1 is a huge problem. A huge problem is when I have got  
2 retailers out in Nebraska being taxed to the tune of \$400  
3 million a year. They would like a moratorium, too.

4 They will describe how complicated it is to collect  
5 the sales tax and remit it to the State, and gee, all the  
6 forms they have got to fill out. That is pretty darn  
7 complicated as well.

8 Why not impose a moratorium there until we can sort  
9 out the various complexities of collecting sales tax on  
10 my merchants at the local level? They are signing  
11 leases, they are building buildings, they are creating  
12 jobs at the local community. I think if we are going to  
13 have a moratorium based upon need, you would put a  
14 moratorium on Main Street today, not on Internet  
15 transactions.

16 The Chairman. We do want to try to report this out  
17 this morning. Let me just make a very brief statement,  
18 then we will call for a vote.

19 I do think there is a rather broad consensus on the  
20 three years. We have brought it down from six years to  
21 three years. That is a substantial reduction. One can  
22 talk at great length, but there is no question but what  
23 this is a two-fold problem.

24 In the first place, it is one of the most promising  
25 developments. I mean, one thing our economy can very

1 well depend upon is growth and prosperity as to what  
2 happens in this area.

3 Second, it is complex. It is extraordinarily  
4 complex, as Senator Baucus has pointed out, because if we  
5 begin to burden it at the local, county, and State level,  
6 as well as international, we could have some very  
7 significant problems.

8 But I think we have heard the argument, so I would  
9 ask the Clerk to call the roll.

10 The Clerk. Mr. Chafee?

11 Senator Chafee. Aye.

12 The Clerk. Mr. Grassley?

13 The Chairman. No, by proxy.

14 The Clerk. Mr. Hatch?

15 Senator Hatch. No.

16 The Clerk. Mr. D'Amato?

17 The Chairman. No, by proxy.

18 The Clerk. Mr. Murkowski?

19 The Chairman. No, by proxy.

20 The Clerk. Mr. Nickles?

21 Senator Nickles. No.

22 The Clerk. Mr. Gramm, of Texas?

23 Senator Gramm. No.

24 The Clerk. Mr. Lott?

25 The Chairman. No, by proxy.

1 The Clerk. Mr. Jeffords?  
2 The Chairman. Yes, by proxy.  
3 The Clerk. Mr. Mack?  
4 Senator Mack. No.  
5 The Clerk. Mr. Moynihan?  
6 Senator Moynihan. Aye.  
7 The Clerk. Mr. Baucus?  
8 Senator Baucus. Aye.  
9 The Clerk. Mr. Rockefeller?  
10 Senator Moynihan. Aye, by proxy.  
11 The Clerk. Mr. Breaux?  
12 Senator Moynihan. Aye, by proxy.  
13 The Clerk. Mr. Conrad?  
14 Senator Conrad. Aye.  
15 The Clerk. Mr. Graham, of Florida?  
16 Senator Graham. Aye.  
17 The Clerk. Ms. Moseley-Braun?  
18 Senator Moynihan. Aye, by proxy.  
19 The Clerk. Mr. Bryan?  
20 Senator Bryan. Aye.  
21 The Clerk. Mr. Kerrey?  
22 Senator Kerrey. Aye.  
23 The Clerk. Mr. Chairman?  
24 The Chairman. No.  
25 The Clerk. The votes are 11 yeas, 9 nays.

1 The Chairman. The amendment is agreed to.

2 Senator Graham. Mr. Chairman? Mr. Chairman?

3 The Chairman. Yes, Senator Graham.

4 Senator Graham. Thank you. Mr. Chairman, I offer  
5 the amendment relative to the collection of State and  
6 local sales tax on out-of-State sales.

7 Mr. Chairman, this legislation would require, as the  
8 Supreme Court has authorized subject to Congressional  
9 action, out-of-State direct-marketers to collect sales  
10 and local sales tax under two conditions: when the  
11 company solicits business in the State; and second, where  
12 it delivers products into the State.

13 There is a diminimus provision which would exempt a  
14 company if its nationwide sales are less than \$3 million.  
15 There is also a one-rate-per-State provision, which  
16 provides for a blended rate in the event that a State has  
17 sales taxes at different levels, such as municipal as  
18 well as State.

19 It has a filing frequency that out-of-State companies  
20 have to file their tax returns once per quarter. There  
21 is a toll-free information service available to provide  
22 out-of-State companies with necessary information and  
23 forms.

24 Mr. Chairman, the rationale behind this amendment,  
25 when I came this morning, I thought was primarily going

1 to be that it creates parity of treatment among various  
2 forms of retail sales.

3 Today, the person who occupies the retail store on  
4 Main Street pays these taxes. His competitor, who may be  
5 hundreds of miles away and is selling through a catalog,  
6 does not. There had originally been some thought that  
7 that was a constitutional issue.

8 The Supreme Court has clarified that. It is a policy  
9 issue, and we are the policy as to whether we believe it  
10 is appropriate to continue that unfairness or to rectify  
11 it, which this amendment would do.

12 I would suggest, further, that this has a major  
13 adverse effect, not only on the retail merchant on Main  
14 Street, but on all the people who depend upon that retail  
15 merchant.

16 It creates a distinct advantage and disincentive to  
17 that person who is in the community, contributing to the  
18 well-being of his own citizens, and benefits by giving an  
19 unfair tax advantage to the out-of-State catalog sales  
20 company.

21 It also represents a substantial impact on State and  
22 local governments. \$3.3 billion in tax revenue is  
23 estimated to be lost annually to those mail-order sales,  
24 which means that all the other taxpayers have to make up  
25 those funds in order to pay for the police, the schools,

1 and all of the responsibilities of State and local  
2 government. Those were the arguments as we commenced  
3 this session.

4 I would now add another. If we think that the issue  
5 of Internet sales is complex and will require as much  
6 learning as possible in order to determine what the  
7 appropriate response of the Federal Government should  
8 be-----

9 Senator Moynihan. Would my friend from Florida  
10 yield for just a comment?

11 Senator Graham. Yes.

12 Senator Moynihan. The Chairman hopes to have a vote  
13 on final passage and I understand you would like to have  
14 a vote on this amendment before.

15 Senator Graham. First.

16 Senator Moynihan. If we could hurry up; Senator  
17 Kerrey has to leave.

18 Senator Graham. All right. Then just my last point  
19 is, this will help give us some information about what  
20 the complexities of out-of-State sales are that might  
21 reduce the difficulties of the commission that we are  
22 just establishing.

23 The Chairman. I will be very brief in my opposition  
24 to this amendment. I would just point out that this  
25 amendment assumes an answer to what we are having the

1 commission study. The whole purpose of the commission is  
2 to determine what should be done in such situations, and  
3 I do not think we have that information available at this  
4 time to draw what conclusion is appropriate.

5 So I would urge my colleagues to oppose this  
6 amendment, and I would ask the Clerk to call the roll.

7 Senator Graham. If I could just, Mr. Chairman,  
8 state that this amendment has the support of virtually  
9 every State and local organization, including the  
10 National Governors' Association, the National Association  
11 of Counties, the Conference of Mayors, and major national  
12 retail groups such as the International Council of  
13 Shopping Centers, the National Home Furnishings  
14 Association, et cetera.

15 I urge the adoption of this amendment.

16 The Chairman. The Clerk will call the roll.

17 The Clerk. Mr. Chafee?

18 Senator Chafee. No.

19 The Clerk. Mr. Grassley?

20 The Chairman. No, by proxy.

21 The Clerk. Mr. Hatch?

22 Senator Hatch. No.

23 The Chairman. No, by proxy.

24 The Clerk. Mr. Murkowski?

25 The Chairman. No, by proxy.

1 The Clerk. Mr. Nickles?  
2 Senator Nickles. No.  
3 The Clerk. Mr. Gramm, of Texas?  
4 Senator Gramm. No.  
5 The Clerk. Mr. Lott?  
6 The Chairman. No, by proxy.  
7 The Clerk. Mr. Jeffords?  
8 The Chairman. No, by proxy.  
9 The Clerk. Mr. Mack?  
10 Senator Mack. No.  
11 The Clerk. Mr. Moynihan?  
12 Senator Moynihan. Aye.  
13 The Clerk. Mr. Baucus?  
14 Senator Baucus. No.  
15 The Clerk. Mr. Rockefeller?  
16 Senator Rockefeller. [Pass.]  
17 The Clerk. Mr. Breaux?  
18 Senator Moynihan. Aye, by proxy.  
19 The Clerk. Mr. Conrad?  
20 Senator Conrad. Aye.  
21 The Clerk. Mr. Graham, of Florida?  
22 Senator Graham. Aye.  
23 The Clerk. Ms. Moseley-Braun?  
24 Senator Moynihan. Aye, by proxy.  
25 The Clerk. Mr. Bryan?

1 Senator Bryan. Aye.

2 The Clerk. Mr. Kerrey?

3 Senator Kerrey. No.

4 The Clerk. Mr. Chairman?

5 The Chairman. No.

6 The Clerk. The votes are 6 yeas, 13 nays.

7 The Chairman. The amendment is not agreed to.

8 Before we go to further amendments, we would like to  
9 report out the legislation, subject to any further  
10 amendment that may be adopted.

11 So I move that the committee favorably report the  
12 Chairman's mark, as modified, as a substitute for the  
13 amendment, in the nature of a substitute to S. 442.

14 Senator Moynihan. I second the motion.

15 The Chairman. The Clerk will call the roll.

16 The Clerk. Mr. Chafee?

17 Senator Chafee. Aye.

18 The Clerk. Mr. Grassley?

19 The Chairman. Aye, by proxy.

20 The Clerk. Mr. Hatch?

21 Senator Hatch. Aye.

22 The Clerk. Mr. D'Amato?

23 The Chairman. Aye, by proxy.

24 The Clerk. Mr. Murkowski?

25 The Chairman. Aye, by proxy.

1           The Clerk.   Mr. Nickles?  
2           Senator Nickles.   Aye.  
3           The Clerk.   Mr. Gramm, of Texas?  
4           Senator Gramm.   Aye.  
5           The Clerk.   Mr. Lott?  
6           The Chairman.   Aye, by proxy.  
7           The Clerk.   Mr. Jeffords?  
8           The Chairman.   Aye, by proxy.  
9           The Clerk.   Mr. Mack?  
10          Senator Mack.   Aye.  
11          The Clerk.   Mr. Moynihan?  
12          Senator Moynihan.   Aye.  
13          The Clerk.   Mr. Baucus?  
14          Senator Baucus.   Aye.  
15          The Clerk.   Mr. Rockefeller?  
16          Senator Moynihan.   Aye, by proxy.  
17          The Clerk.   Mr. Breaux?  
18          Senator Moynihan.   Aye, by proxy.  
19          The Clerk.   Mr. Conrad?  
20          Senator Conrad.   Aye.  
21          The Clerk.   Mr. Graham, of Florida?  
22          Senator Graham.   No.  
23          The Clerk.   Ms. Moseley-Braun?  
24          Senator Moynihan.   Aye, by proxy.  
25          The Clerk.   Mr. Bryan?

1 Senator Bryan. Aye.

2 The Clerk. Mr. Kerrey?

3 Senator Kerrey. Aye.

4 The Clerk. Mr. Chairman?

5 The Chairman. Aye.

6 The Clerk. The votes are 19 yeas, 1 nay.

7 The Chairman. The committee has favorably reported  
8 the Chairman's mark, as modified.

9 Senator Conrad. Mr. Chairman?

10 The Chairman. Yes.

11 Senator Conrad. Might I offer my amendment, Mr.  
12 Chairman?

13 The Chairman. Please proceed.

14 Senator Conrad. I thank the Chair. I will be very  
15 brief.

16 I am offering an amendment that would simply provide  
17 a grandfather to those States and local governments who  
18 already have imposed taxes on these transactions.

19 Mr. Chairman and members of the committee, it seems  
20 to me Federal preemption is a step that should only be  
21 taken for the most compelling reasons. I do not think we  
22 have a reason for preempting the decisions of States that  
23 have already been made.

24 This has already been the determination in the  
25 Commerce bill, this has already been the determination in

1 the bill passed unanimously in the House of  
2 Representatives. So, I hope we would do the same thing  
3 here as well.

4 There are seven States that have been named  
5 specifically in the House provision. There are three  
6 other States that may have laws that qualify under the  
7 grandfather provision. I would hope this would be  
8 considered a non-controversial amendment.

9 Senator Nickles. Can you identify those?

10 Senator Conrad. The States?

11 Senator Nickles. Yes.

12 Senator Conrad. In the House-passed bill: Iowa, New  
13 Mexico, North Dakota, Ohio, South Dakota, Tennessee, and  
14 Wisconsin. Not listed, but some have asserted that they  
15 too have laws, are South Carolina, Connecticut, and  
16 Texas, and certain home-rule cities in Colorado.

17 Senator Nickles. Is that a tax on all Internet  
18 transactions in the State?

19 Senator Conrad. No, just access. These are taxes  
20 on access to the Internet, not on Internet transactions.

21 Senator Nickles. Just a tax on Internet access, not  
22 on sales transactions.

23 Senator Conrad. That is correct.

24 Senator Nickles. So if you hook up with an Internet  
25 access provider, America Online or something, that the

1 State would tax that?

2 Senator Conrad. They already have. And the  
3 question is, do we preempt that? In both the Commerce  
4 Committee and in the House bills, they have made a  
5 determination that it would be inappropriate for us to  
6 preempt State actions that have already been taken.

7 It is one thing to declare a moratorium going forward  
8 from here, it is another thing for us to preempt  
9 decisions that have already been made at the State level.

10 The Chairman. Any further comment?

11 [No response.]

12 The Chairman. I would oppose the amendment by the  
13 distinguished Senator from North Dakota. As I understand  
14 it, there are two parts. The first component does limit  
15 the moratorium to new taxes and Internet access. As  
16 such, it would grandfather any existing taxes on Internet  
17 access, making these taxes exempt from the moratorium.

18 I oppose it because, first, the purpose of this  
19 legislation is to call a time-out from taxes on Internet  
20 access or on electronic commerce, to study the issue, and  
21 hopefully come up with some policy recommendations about  
22 how, or if, the Internet should be taxed.

23 The mere fact that some States were more aggressive  
24 in taxing Internet access does not mean that these States  
25 should be favored over others. There is no substantive

1 policy rationale for making such a distinction.

2 Second, as our negotiators work to ensure that other  
3 countries do not throw up barriers to Internet access and  
4 electronic commerce, we want to make sure that we provide  
5 a good example. If we simply grandfather existing taxes  
6 on the Internet, it will be more difficult to convince  
7 other countries not to impose such taxes or tariffs.

8 We may encourage other countries, as a matter of  
9 fact, to quickly impose new taxes or tariffs under the  
10 assumption that they have an existing tax on the books,  
11 and it will be simple to grandfather them under any new  
12 agreement.

13 I might say, that happened in past experience. In  
14 the GATT, for instance, we grandfathered numerous trade  
15 barriers and then we spent the next 50 years trying to  
16 eliminate them. So, I would urge we not set that  
17 precedent.

18 The second part of the amendment would ensure that  
19 the moratorium would not impair the ability of any State  
20 or local government to continue collecting taxes that  
21 were generally imposed and actually enforced under State  
22 or local law before July 28, 1998.

23 My mark does provide the same provision, so we have  
24 no objection to that aspect. But, because of the first  
25 part, I would urge my colleagues to vote no.

1 Senator Gramm. Mr. Chairman?

2 Senator Graham. Mr. Chairman?

3 The Chairman. Senator Gramm.

4 Senator Gramm. Mr. Chairman, I have to admit that I  
5 always feel a little bit queasy on the sales tax question  
6 in terms of collecting sales tax on the purchase of  
7 goods. I have not quite decided where it ought to be  
8 paid, whether where the goods are from or where they are  
9 bought. I think there is a legitimate debate there. I  
10 do not personally feel very comfortable in helping people  
11 collect taxes, if you want to know the truth.

12 But on this issue, I have no divided loyalty, so to  
13 speak. I do not think we ought to be taxing people who  
14 are interconnecting to the Internet. The Federal  
15 Government is literally spending hundreds of millions--  
16 billions of dollars, ultimately--collecting every library  
17 and every school because we believe that this is a  
18 powerful instrument for communication and commerce.

19 I do not think State and local governments ought to  
20 be taxing the interconnect. It is one thing to collect  
21 taxes if I buy a fruitcake through the Internet, or I buy  
22 a book through the Internet, which I often do, but it is  
23 quite another thing to impose a tax on people that are  
24 signing up for the Internet.

25 So I am just against that tax, period. I hope, as a

1 result of this moratorium, that we conclude that we  
2 should not allow that tax. I feel very comfortable in  
3 overriding those taxes that have been imposed.

4 Again, I want to emphasize, this is not a case where  
5 States are collecting--and I think they have a legitimate  
6 right to collect sales taxes when you buy something using  
7 the Internet. But the idea of taxing people to hook up  
8 to the Internet, I think, is something that I am  
9 fundamentally opposed to. I think it is a tax on  
10 technology and exactly the wrong kind of tax to be  
11 imposing.

12 Senator Graham. Mr. Chairman?

13 The Chairman. Senator Graham.

14 Senator Graham. I have some questions that the  
15 Senator from Texas' remarks just brought to my mind.

16 The moratorium that we are imposing in this bill is  
17 both a moratorium on a tax to connect to the Internet,  
18 and a moratorium on collecting taxes that might be  
19 generated by a transaction through the Internet. Is that  
20 correct?

21 The Chairman. Yes.

22 Senator Graham. Now, let me assume that transaction  
23 is through a company which both has a physical presence  
24 in the State and also makes sales through the Internet.  
25 For instance, Barnes & Noble has bookstores in almost

1 every community. So they, today, have a presence in the  
2 State which would make them subject to State sales taxes.

3 Under this moratorium, would they be exempt from  
4 collecting those sales taxes in a State which were the  
5 result of an Internet sale?

6 Ms. Pari. No. The way the moratorium is meant to  
7 work, is no discriminatory taxes or higher taxes should  
8 be charged on a good, whether you buy it through the mail  
9 or whether you buy it through the Internet. That's the  
10 concept.

11 A State is still free to tax goods that are sold  
12 within their jurisdiction. Other States have a use tax  
13 that is imposed on goods that are shipped into their  
14 jurisdiction. That is the concept behind the moratorium.

15 Senator Graham. So if a Barnes & Noble sale on the  
16 Internet is subject to State taxes today because Barnes &  
17 Noble has a presence in the State, this moratorium would  
18 not affect the State's continued ability to make those  
19 collections. Is that correct?

20 Ms. Pari. That is correct.

21 Senator Baucus. Mr. Chairman?

22 Senator Chafee. Mr. Chairman?

23 The Chairman. Senator Chafee.

24 Senator Chafee. Mr. Chairman, I just want to ask a  
25 question of the staff, because I want to make sure I

1 definitely understand this. It is my understanding that  
2 the moratorium we are talking about here today applies  
3 solely to State and local taxes on Internet access. In  
4 other words, the \$20 a month or whatever it is America  
5 Online charges, and the taxes on electronic commerce.  
6 But it is my understanding the moratorium does not cover  
7 taxes currently imposed on telecommunications and cable  
8 services. Is that right?

9 Ms. Pari. That is correct, Senator.

10 Senator Chafee. Because it is my understanding that  
11 sometimes they have a bundle situation, where you can get  
12 the Internet, you can get the telephone, you can get the  
13 cable all in one package. But that State would still be  
14 able to collect its tax on the telephone and on the  
15 cable, is that right?

16 Ms. Pari. Yes, sir. That is right.

17 Senator Chafee. All right. Now, is that clear in  
18 the language?

19 Ms. Pari. We can work with you on language to make  
20 that crystal clear.

21 Senator Chafee. Because, certainly, my State would  
22 be terribly distressed if we were passing casually here a  
23 moratorium on taxes that they are currently collecting on  
24 telephone service, for example.

25 Senator Baucus. Mr. Chairman?

1           The Chairman.    Senator Baucus, then we would like to  
2 take a vote.

3           Senator Baucus.   Mr. Chairman, I favor the  
4 amendment, and I understand your concerns about the  
5 international ramifications. My concern, however, is  
6 that our experience with other countries is, they are  
7 going to pretty much do what they want to do, and then  
8 tend to be a little bit more protective of themselves and  
9 little less internationalists, or less of free trade, in  
10 a certain sense, than we.

11           If we do not at least grandfather in current  
12 practices, my guess is we are going to handcuff ourselves  
13 because other countries are going to at least, I am sure,  
14 grandfather some of their current practices.

15           I think it is unlikely that other countries are going  
16 to go as far as the spirit of the underlying bill, and  
17 for that reason I support the amendment.

18           Senator Moynihan.   Mr. Chairman, could I just note  
19 for the record that the WTO, in May, went on record  
20 saying they were opposed to tariffs on electronic  
21 commerce.

22           The Chairman.    Thank you, Senator Moynihan.

23           The Clerk will call the roll.

24           The Clerk.    Mr. Chafee?

25           Senator Chafee.    No.

1 The Clerk. Mr. Grassley?  
2 The Chairman. No, by proxy.  
3 The Clerk. Mr. Hatch?  
4 Senator Hatch. No.  
5 The Clerk. Mr. D'Amato?  
6 The Chairman. No, by proxy.  
7 The Clerk. Mr. Murkowski?  
8 The Chairman. No, by proxy.  
9 The Clerk. Mr. Nickles?  
10 Senator Nickles. No.  
11 The Clerk. Mr. Gramm, of Texas?  
12 Senator Gramm. No.  
13 The Clerk. Mr. Lott?  
14 The Chairman. Yes, by proxy.  
15 The Clerk. Mr. Jeffords?  
16 The Chairman. No, by proxy.  
17 The Clerk. Mr. Mack?  
18 Senator Mack. No.  
19 The Clerk. Mr. Moynihan?  
20 Senator Moynihan. Aye.  
21 The Clerk. Mr. Baucus?  
22 Senator Baucus. Aye.  
23 The Clerk. Mr. Rockefeller?  
24 Senator Moynihan. Aye, by proxy.  
25 The Clerk. Mr. Breaux?

1 Senator Moynihan. Aye, by proxy.  
2 The Clerk. Mr. Conrad?  
3 Senator Conrad. Aye.  
4 The Clerk. Mr. Graham, of Florida?  
5 Senator Graham. Aye.  
6 The Clerk. Ms. Moseley-Braun?  
7 Senator Moynihan. Aye, by proxy.  
8 The Clerk. Mr. Bryan?  
9 Senator Bryan. Aye.  
10 The Clerk. Mr. Kerrey?  
11 Senator Moynihan. Aye, by proxy.  
12 The Clerk. Mr. Chairman?  
13 The Chairman. No.  
14 The Clerk. The votes are 10 yeas, 10 nays.  
15 Senator Conrad. It passes. The Conrad rule.  
16 [Laughter.]  
17 The Chairman. The amendment is not agreed to.  
18 Are there any other amendments?  
19 [No response.]  
20 The Chairman. If not, we stand adjourned.  
21 [Whereupon, at 11:26 a.m., the meeting was  
22 concluded.]  
23  
24  
25

**DESCRIPTION OF S. 442,  
THE "INTERNET TAX FREEDOM ACT,"  
AND A PROPOSED CHAIRMAN'S AMENDMENT  
IN THE NATURE OF A SUBSTITUTE**

Scheduled for Markup

by the

SENATE COMMITTEE ON FINANCE

on

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Prepared by the Staff

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JOINT COMMITTEE ON TAXATION

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JCX-58-98

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## INTRODUCTION

S. 442, the "Internet Tax Freedom Act," was reported by the Senate Committee on Commerce, Science, and Transportation on May 5, 1998 (S. Rept. 105-184). S. 442 would impose a moratorium on the ability of States and local governments to impose taxes with respect to Internet activity, both access to and transactions conducted on the Internet. S. 442 further would direct the Secretaries of State, Treasury, and Commerce, in consultation with private business and appropriate Congressional committees, to undertake a study of the appropriate taxation of Internet activity, and would provide that it is the sense of the Congress that Internet activity be a tariff-free zone. Consistent with the jurisdiction of the Committee on Finance (the "Finance Committee") over issues related to interstate taxation by States and local governments and international taxation and trade, S. 442 has been sequentially referred to the Finance Committee through July 30, 1998.

Similar legislation, H.R. 4105, was passed by the House of Representatives on June 23, 1998.

The Finance Committee has scheduled a markup on July 28, 1998, to consider an amendment in the nature of a substitute to S. 442. This document,<sup>1</sup> prepared by the staff of the Joint Committee on Taxation, provides an overview description of S. 442 and H.R. 4105 (Part I), an overview of present law (Part II), and a description of a proposed amendment in the nature of a substitute to be offered by Chairman Roth (Part III).

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<sup>1</sup> This document may be cited as follows: Joint Committee on Taxation, *Description of S. 442, the "Internet Tax Freedom Act," and a Proposed Chairman's Amendment in the Nature of a Substitute to S. 442* (JCX-58-98), July 24, 1998.

## I. OVERVIEW OF S. 442 AND H.R. 4105

### S. 442

S. 442 (the "Internet Tax Freedom Act") would prohibit States and local governments from imposing any tax, license, or fee directly or indirectly on the Internet or interactive computer services between the date of the bill's enactment and January 1, 2004. This moratorium would not apply to taxes on net income derived from the Internet (including interactive computer services), to fairly apportioned business taxes applied to businesses having a business location within the taxing jurisdiction, or to the authority of States or local governments to impose any sales or use tax on transactions effected through the Internet if the taxes (1) are generally applicable taxes and (2) are imposed in the same manner as is permitted on sales or transactions effected by mail order, telephone, or other remote means.

S. 442 would direct the Secretaries of State, Treasury, and Commerce to consult with appropriate Congressional committees and the private sector to develop policy recommendations on the appropriate taxation (domestic and international) of Internet activity. These recommendations would be required to be provided to the President within 18 months after the bill's enactment, and the President would be directed to transmit legislative recommendations to the Congress within two years after enactment.

Further, S. 442 would declare that it is the sense of the Congress that international agreements be negotiated providing that international use of the Internet is free from tariffs and taxation.

### H.R. 4105

H.R. 4105 would prohibit States and local governments from imposing any taxes on Internet access, any "bit" taxes, or any multiple or discriminatory taxes on electronic commerce during the three-year period beginning on the date of the bill's enactment. The bill would exempt from this moratorium certain taxes currently imposed by the States of Connecticut, Wisconsin, Iowa, North Dakota, New Mexico, Tennessee, and Ohio, if those taxes are expressly re-enacted during the one-year period beginning on the date of the bill's enactment. A bit tax is defined as any tax on electronic commerce expressly imposed on or measured by the volume of digital information transmitted or the volume of such information per unit of time transmitted electronically.<sup>2</sup> A discriminatory tax is defined as any tax on electronic commerce that is not generally imposed on transactions accomplished by other means or is not imposed at the same rate as other such transactions.

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<sup>2</sup> Taxes on telecommunication services (e.g., telephone access) would be specifically excluded from the moratorium.

H.R. 4105 would establish an Advisory Commission on Electronic Commerce, composed of 31 members representing the Federal Government, States and local governments, and the private sector to develop legislative recommendations (to be submitted to the Congress within two years after the bill's enactment) on the appropriate taxation of Internet activity and other remote area transactions (e.g., mail order or catalog sales). The recommendations, once submitted to the Congress, would be considered under special, expedited legislative procedures. The bill includes specific provisions identifying associations and industry groups to be represented on the commission, and detailed rules governing actions of the commission.

As with S. 442, H.R. 4105 would declare that it is the sense of the Congress that international agreements be negotiated providing that international use of the Internet is free from tariffs and taxation.

H.R. 4105 also contains provisions, not within the jurisdiction of the Finance Committee, regarding Federal regulation of the Internet and imposition of user fees.<sup>3</sup>

H.R. 4105 was passed by the House of Representatives on June 23, 1998.

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<sup>3</sup> Authorizing committees of the Congress may impose, or authorize executive agencies to impose non-tax, or true, user fees that agencies may charge for specific services they provide. In general, a true user fee is a charge levied on a class that directly avails itself of a governmental program, and is used solely to finance that program rather than to finance the costs of Government generally. The amount of the fee charged to any payor may not exceed the direct costs of providing the services with respect to which the fee is charged. There must be a reasonable connection between the payors of the fee and the agency or function receiving the fee. Those paying a fee must have the choice of not utilizing the governmental service or avoiding the regulated activity and thereby avoiding the charge. In other words, the fee can be viewed as payment for a special privilege, as opposed to a mandatory charge (e.g., tax) imposed on the public at large for general or specified governmental purposes.

## **II. OVERVIEW OF PRESENT FEDERAL INCOME TAX, EXCISE TAX, AND TARIFF PROVISIONS RELATING TO THE INTERNET AND STATE AND LOCAL GOVERNMENT TAXATION OF INTERNET AND SIMILAR INTERSTATE SALES ACTIVITIES**

### **Federal tax provisions**

#### **Income taxation of the Internet**

There are no special Federal income taxes on Internet services. The Federal income tax applies to Internet services in the same manner that it applies to any other provision of services. Accordingly, the income received by an Internet service provider is includible in that provider's income for Federal income tax purposes. Similarly, a business that pays amounts to an Internet service provider generally may deduct or amortize (as appropriate) those amounts as an ordinary and necessary business expense (assuming the other prerequisites for a deduction or amortization are satisfied).

#### **Federal excise taxation of the Internet**

Present law imposes no special excise taxes on Internet services. Access to and transactions conducted on the Internet are subject to generally applicable Federal excise taxes in the same manner as other taxable activities. For example, present law imposes a three-percent excise tax on certain communications services (i.e., local and long distance telephone service). Thus, amounts paid for telephone service connecting users to the Internet are subject to this excise tax in the same manner as other payments for telephone service. Charges for actual Internet service are not subject to this tax, as long as the service provided does not otherwise fall within the statutory provisions governing the communications excise tax (e.g., voice quality local or toll service).

### **International trade provisions**

Present law provides no direction to the President regarding Congress' interest in or intent with respect to the conduct of international negotiations regarding barriers to electronic commerce. Nothing in the law directs the President to include barriers to electronic commerce among the barriers cataloged annually in the National Trade Estimates report prepared by the United States Trade Representative. The National Trade Estimates report serves as a compendium of foreign barriers to U.S. commerce and a presumptive target for future negotiations with our trading partners.

### **State and local government taxation of interstate transactions**

Under the Constitution, a State or local government may impose taxes on sales that occur within its jurisdiction or on the use of property within its jurisdiction. Approximately 6,600

State and local jurisdictions impose sales and use taxes.<sup>4</sup> A limited number of States have applied their sales or other excise taxes to Internet activity. The allowable sales tax authority of a State or local government extends to mail order sales by out-of-State vendors to residents of the State if the sale is deemed to take place within the taxing jurisdiction.<sup>5</sup> There are, however, limitations on the methods State and local jurisdictions may employ to collect sales and use taxes.

State and local sales and use taxes are levied on the final purchaser, but are collected primarily through the vendor. In the case of a sale by an out-of-State vendor, the U.S. Supreme Court has held that a State or local government cannot constitutionally require the vendor to collect and remit use taxes unless the vendor has a sufficient business nexus with the State.<sup>6</sup> In the *National Bellas Hess* case, the Court found that the required nexus was not present if the vendor's only connection with customers in the State was by common carriers or the United States mail.<sup>7</sup> The Court based this conclusion on due process considerations and on the Commerce Clause of the United States Constitution, which reserves to Congress the power to regulate and control interstate commerce.<sup>8</sup> The required nexus has been held to exist when the vendor arranges sales through local agents or maintains retail stores in the taxing State.

Subsequently, in 1992, the U.S. Supreme Court ruled that an out-of-state mail-order house with neither outlets nor sales representatives in the State is not required to collect and pay use tax on goods purchased for use in the State.<sup>9</sup> The Court ruled that the due process clause did not bar enforcement of the State's use tax, but held that enforcing the State's use tax would be inconsistent with the Court's commerce clause jurisprudence. The Court concluded by observing that "the underlying issue is not only one that Congress may be better qualified to resolve, but also one that Congress has the ultimate power to resolve."<sup>10</sup>

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<sup>4</sup> Advisory Commission on Intergovernmental Relations, *Significant Features of Fiscal Federalism, Vol. 1* (1995), table 27.

<sup>5</sup> See, e.g., *McLeod v. J.E. Dilworth Co.*, 322 U.S. 327 (1944).

<sup>6</sup> *National Bellas Hess, Inc., v. Department of Revenue of the State of Illinois*, 386 U.S. 753 (1967) (henceforth referred to as *National Bellas Hess*).

<sup>7</sup> *Id.* at 754.

<sup>8</sup> *Id.* at 760.

<sup>9</sup> *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

<sup>10</sup> *Id.* at 318.

### III. DESCRIPTION OF CHAIRMAN'S AMENDMENT IN THE NATURE OF A SUBSTITUTE

The Chairman's amendment would substitute the provisions described below for the provisions of S. 442, as reported by the Committee on Commerce, Science, and Transportation.

#### **State and local tax moratorium**

In lieu of the approximately six-year moratorium provided in S. 442, the Chairman's amendment would prohibit imposition of State and local taxes on the Internet for a period of three years, beginning on the date of the bill's enactment.<sup>11</sup> Taxes to which the moratorium would apply include any taxes on Internet access, any bit taxes, or any multiple or discriminatory taxes on electronic commerce.

The Chairman's amendment further would provide that this moratorium applies only to taxes imposed after July 28, 1998 (the date of Finance Committee action). Thus, the amendment would not affect the ability of States or local governments to collect tax with respect to transactions occurring before July 29, 1998, or the rights of parties in any dispute concerning State and local taxation of Internet activity during periods before July 29, 1998. Unlike H.R. 4105, the Chairman's amendment would not grandfather any existing State or local taxes on Internet activity during the period of the moratorium.

#### **Sense of the Congress resolution on new Federal Internet taxes**

The Chairman's amendment would provide that it is the sense of the Congress that no new Federal taxes like the State and local government taxes to which the three-year moratorium would apply should be enacted on Internet activity during the moratorium.

#### **International trade provisions**

Like S. 442 and H.R. 4105, the Chairman's amendment would express the sense of Congress that the President should continue efforts to ensure that electronic commerce remains free of tariffs, discriminatory taxation, and any form of discriminatory regulation.

Unlike S. 442 and H.R. 4105, the Chairman's amendment would amend existing law to direct the United States Trade Representative, under existing statutory authority, to include barriers to electronic commerce, among the barriers designated annually in the National Trade Estimates report.

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<sup>11</sup> The moratorium does not affect taxes, fees, and other charges imposed pursuant to Federal law.

### Establish national advisory commission

Similar to the provisions of H.R. 4105, the Chairman's amendment would establish a national advisory commission to study and recommend appropriate rules for international, Federal, State, and local government income and excise taxation of the Internet and other comparable interstate or international sales activities, as well as appropriate tariff treatment of such activities.

The commission would be comprised of 13 members, as follows:

Federal Government representatives.—The Secretaries of State, Treasury, and Commerce, the Attorney General, and the United States Trade Representative, or the designee of each such cabinet member would represent the Federal Government.

State and local government representatives.—A total four representatives of State and local governments would be appointed, one member each by the Speaker of the House of Representatives, the Minority Leader of the House, the Majority Leader of the Senate, and the Minority Leader of the Senate.

Electronic industry and consumer representatives.—A total of four representatives of the electronic industry and of consumer groups would be appointed, one member each by the Speaker of the House of Representatives, the Minority Leader of the House, the Majority Leader of the Senate, and the Minority Leader of the Senate.

Legislative history accompanying the bill would suggest that the Congressional leadership coordinate their appointments to the commission to assure the broadest possible State and local government and private sector representation.

The commission would be directed to submit its findings, with legislative recommendations, to the Congress within two years of the date of the bill's enactment. Unlike H.R. 4105, the Chairman's amendment would not provide any expedited procedures for consideration of the commission's recommendations.

The Chairman's amendment further would direct the President to continue negotiations currently under way in a variety of fora regarding the regulation of the electronic commerce. The amendment would establish a set of concrete trade negotiating objectives designed to guide the President in future negotiations. Those negotiating objectives would include the removal of barriers to trade in goods and services that are essential to the delivery of electronic commerce as well as barriers to electronic commerce itself.

## MODIFICATION TO CHAIRMAN'S MARK

The Chairman's Mark is modified in the following two ways with respect to the national advisory commission:

1. The commission would be comprised of 16 members, as follows:

Federal Government representatives.-- The Secretaries of Treasury, Commerce and State and the United States Trade Representative, or the designee of each such cabinet member would represent the Federal Government.

State and local government representatives.-- A total of six representatives of State and local governments would be appointed, two members each by the Speaker of the House of Representatives, and the Majority Leader of the Senate, and one member each by the Minority Leader of the House and the Minority Leader of the Senate.

Electronic industry and consumer representatives.-- A total of six representatives of the electronic industry and of consumer groups would be appointed, two members each by the Speaker of the House of Representatives, and the Majority Leader of the Senate, and one member each by the Minority Leader of the House and the Minority Leader of the Senate.

2. The commission may not adopt a position with respect to a matter unless at least two-thirds of the members agree.

1

## POSSIBLE CHAFEE AMENDMENT #1

### PRESENT LAW

No federal preemption exists for the imposition of state or local taxes on Internet access or transactions conducted on the Internet.

### CHAIRMAN'S MARK

The Chairman's mark imposes a 3-year moratorium on the states' ability to impose taxes on Internet access, any bit taxes, or any multiple or discriminatory taxes on electronic commerce.

### CHAFEE AMENDMENT

The Chafee amendment strikes that portion of the Chairman's mark which imposes a moratorium on a state's ability to impose taxes on Internet access charges. The moratorium in the Chairman's mark would continue to apply to bit taxes, or any multiple or discriminatory taxes on electronic commerce.

2

## POSSIBLE CHAFEE AMENDMENT #2

### PRESENT LAW

No federal preemption exists for the imposition of state or local taxes on internet access or transactions conducted on the Internet.

### CHAIRMAN'S MARK

The Chairman's mark imposes a 3-year moratorium on a states' ability to impose taxes on Internet access, any bit taxes, or any multiple or discriminatory taxes on electronic commerce. The mark also establishes a national advisory commission to study and recommend appropriate rules for international, Federal, State and local government income and excise taxation of the Internet and other comparable interstate or international sales activities. The commission is directed to submit its findings, including legislative recommendations, within two years of the bill's date of enactment.

### CHAFEE AMENDMENT

The Chafee amendment limits the moratorium on a state's ability to impose taxes on internet access, any bit taxes, or any multiple or discriminatory taxes on electronic commerce to 2 years. The amendment directs the advisory commission established under the Chairman's mark to submit its findings within 18 months of the bill's enactment.

3

Hatch Amendment #1

To expand the size of the Commission.

4

Hatch Amendment #2

To modify the make-up of the Commission.

5

Hatch Amendment #3

Modify the definition of taxation. [Use House bill with some modifications]

6

Hatch Amendment #4

Relevant.

7

**Amendment by Senator Conrad**

Modify the Chairman's Mark to provide that the moratorium applies only to new taxes imposed on Internet access services delivered after July 28, 1998, and that the moratorium would not impair the ability of any State or local government to continue collecting taxes on Internet access that were generally imposed and actually enforced under State or local law (including any law of a home-rule community) before July 28, 1998.

8

## Graham Amendment to Internet Tax Freedom Act

### Collection of State and Local Sales Tax on Out-of-State Sales (Previously known as S 1586)

This amendment would require out-of-state direct marketers to collect state and local sales taxes (use taxes) when the company:

- a. Solicits business in the state;
- b. Delivers products into the state.

#### De Minimus Provision

A company will be exempt if its nationwide sales are less than \$3 million.

#### One Rate Per State

Local sales taxes often vary within a state. Companies will have the option of collecting a blended rate which covers all state and local taxes.

#### Filing Frequency

Out-of-state companies only have to file tax returns once per quarter.

#### Toll Free Information Service

States must establish toll-free information service to provide out-of-state companies with necessary information and forms.

**SUGGESTED AMENDMENT TO CHAIRMAN'S AMENDMENT TO S. 442**

Suggested additional subsection added to section creating a moratorium:

In no event shall the moratorium created by this section apply to any tax imposed by a State or political subdivision thereof on (1) the sale of personal property or services, or (2) the provision or use of content, information, or other data; provided that the tax is imposed at the same rate as is imposed on transaction or services not accessed through the Internet.

Rationale: When state or local governments may otherwise tax the sale of personal property or services, or the charges for utilizing information on a database, providers should not be able to escape otherwise applicable taxes merely because the transaction utilizes the Internet. For example, stores should not be able to avoid state and local sales taxes by making sales from an on-line catalog accessed through the Internet. Similarly, a credit reporting service otherwise subject to a state or local service or transaction tax should not escape taxation merely because it permits its reports to be downloaded rather than mailed out. In Chicago, for example, our lease transaction tax applies to those who obtain information from databases, and without this amendment any provider who moves his database onto the Internet would escape taxation. The moratorium should apply to what is charged to enable users to access sites on the Internet, but not to the charges of those who operate sites and who are otherwise subject to applicable state and local taxes because of their nexus to the taxing jurisdiction. Without the amendment, providers will be encouraged to relocate to the Internet en masse, with unpredictable and potentially serious erosion in state and local revenues. At a minimum, lengthy and expensive litigation will be required to clarify the scope of the moratorium absent an amendment, and state and local governments will experience considerable budgetary uncertainty during the course of that litigation.

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## KERREY AMENDMENT #1

In contrast to the three years provided for in the Chairman's amendment in the nature of a substitute, provide for a two-year moratorium on the imposition of State and local taxes on the Internet, beginning on the date of enactment. Also, provide for a two-year, not three-year, national advisory commission to study and recommend appropriate rules for international, Federal, State and local government income and excise taxation of the Internet and other comparable interstate or international sales activities, as well as appropriate tariff treatment of such activities.