

**NCSL Communications, Financial
Services & Interstate Commerce
Committee**

**The “Digital Goods and Services Tax
Fairness Act of 2011”**

**A National Framework to Ensure Fair
Taxation of Digital Commerce**

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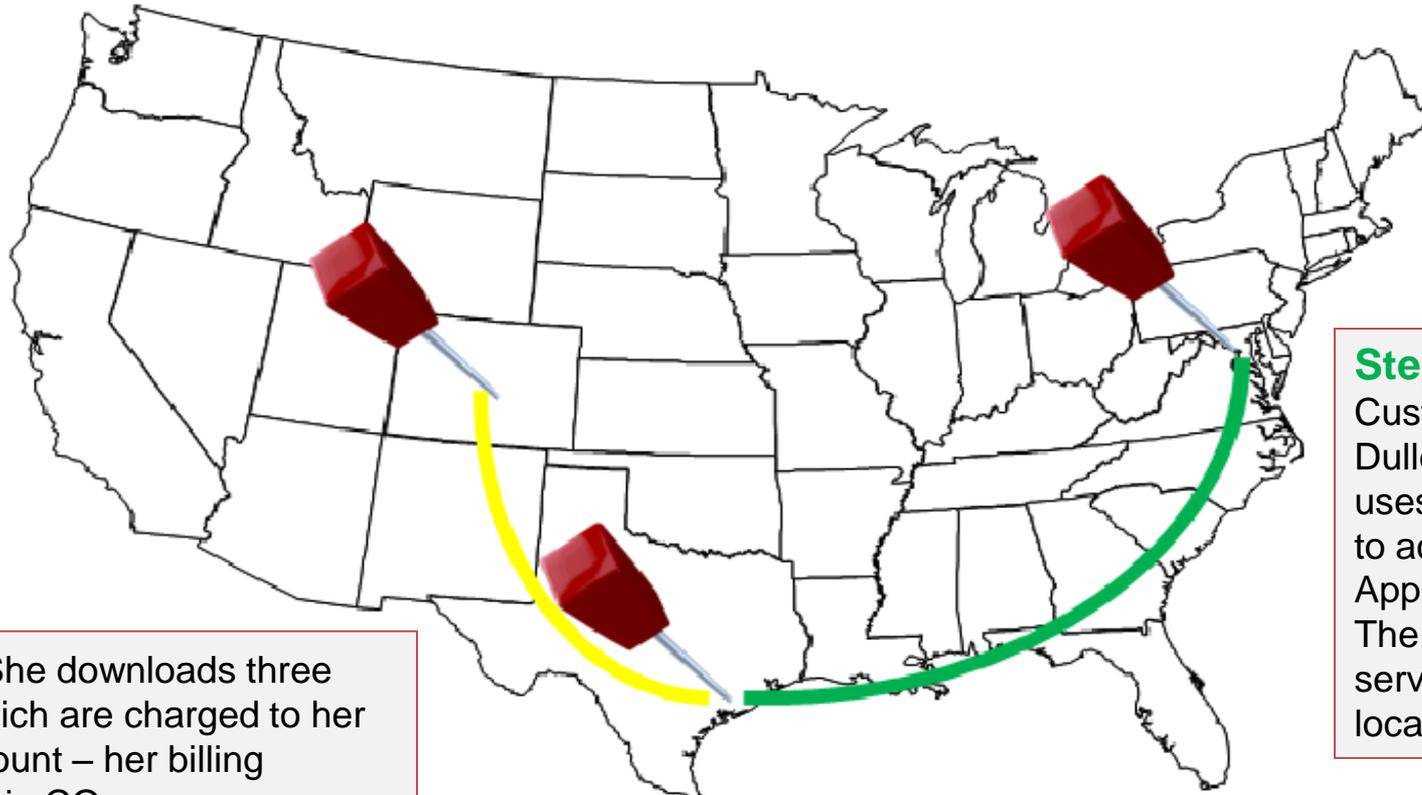
The Need for a National Framework for Fair Taxation of Emerging Technologies, Products and Services

- **Technological Convergence and Innovation + 20th Century state tax systems = increasing risk of no taxation, multiple taxation, inequitable and/or excessive taxation**
 - **Early 21st Century:** Convergence of cable, telephone, satellite and wireless industries – generally voice, data and video services...
 - **2011:** New entrants are competing to provide new digital goods and services, such as music downloads, digital books, video and more...
- **Federal legislation establishing National Framework would ensure fair taxation of digital commerce**
 - By ensuring digital commerce sold over global networks will not be subject to tax by multiple jurisdictions
 - By providing clear rules identifying which jurisdiction has the right to tax, precluding arguments that no jurisdiction might have the right to tax digital transactions
 - Retains State autonomy to choose to tax or not tax digital goods/services
 - Will preclude legacy taxes imposed on traditional communications providers from being imposed on digital goods/services ensuring equitable taxation by competing providers

State of Confusion – How to “Source” Tax Revenues – Which State has the Right to Tax?

The example below illustrates how complicated it can be to identify which jurisdiction has the right to tax digital good and services:

A customer uses the Wi-Fi at Dulles Airport to download movies from the Apple Store to her i-Touch – the movies are downloaded from servers located in Texas and her bill sent to Colorado.



Step 2: She downloads three movies which are charged to her Apple account – her billing address is in CO.

Step 1: A Customer at Dulles Airport uses her Wi-Fi to access the Apple store. The Apple store server is located in TX.

Digital Goods and Services Tax Fairness Act

- Provides clear rules for which tax jurisdiction authorized to tax digital goods and services sold over interstate communications networks
- Mobile Telecommunications Sourcing Act (MTSA) is model for general rule of taxing at the purchaser's place of primary use (customer location)
- Congressional action is needed to authorize a jurisdiction to tax transactions that arguably do not occur within their borders just like MTSA
- Sourcing rules are consistent with SSTP rules
- Ongoing discussions with FTA and others to ensure clear and administrable rules and address any definitional concerns

Digital Goods and Services Tax Fairness Act

- Would preclude legacy communications taxes from being imposed upon digital commerce
- Digital goods and services should be subject to the same state and local taxes, regardless of who provides such services, which is consistent with NCSL principles
- Digital goods and services should be subject to the same taxes imposed on other tangible goods and comparable services
- State coalition is working with states legislators to enact legislation that eliminates existing “discriminatory” taxation consistent with the federal legislation (e.g., Nebraska taxation of digital goods under local business license tax)

State of Confusion – Problems with Imposing 20th Century Telecom Tax System on Digital Commerce

Most states tax games as software -- if sold at a store, the retail sales tax applies. But if sold by a wireless provider, it could be taxed at a much higher communications services tax rate.

Federal law preempts Internet access and certain digital services (email) from state and local taxation (0%).

Text messages are taxed as telecom services (subject to higher rates).



Tones

Tunes

Games

Web

TV

Text



iPhone



iTouch

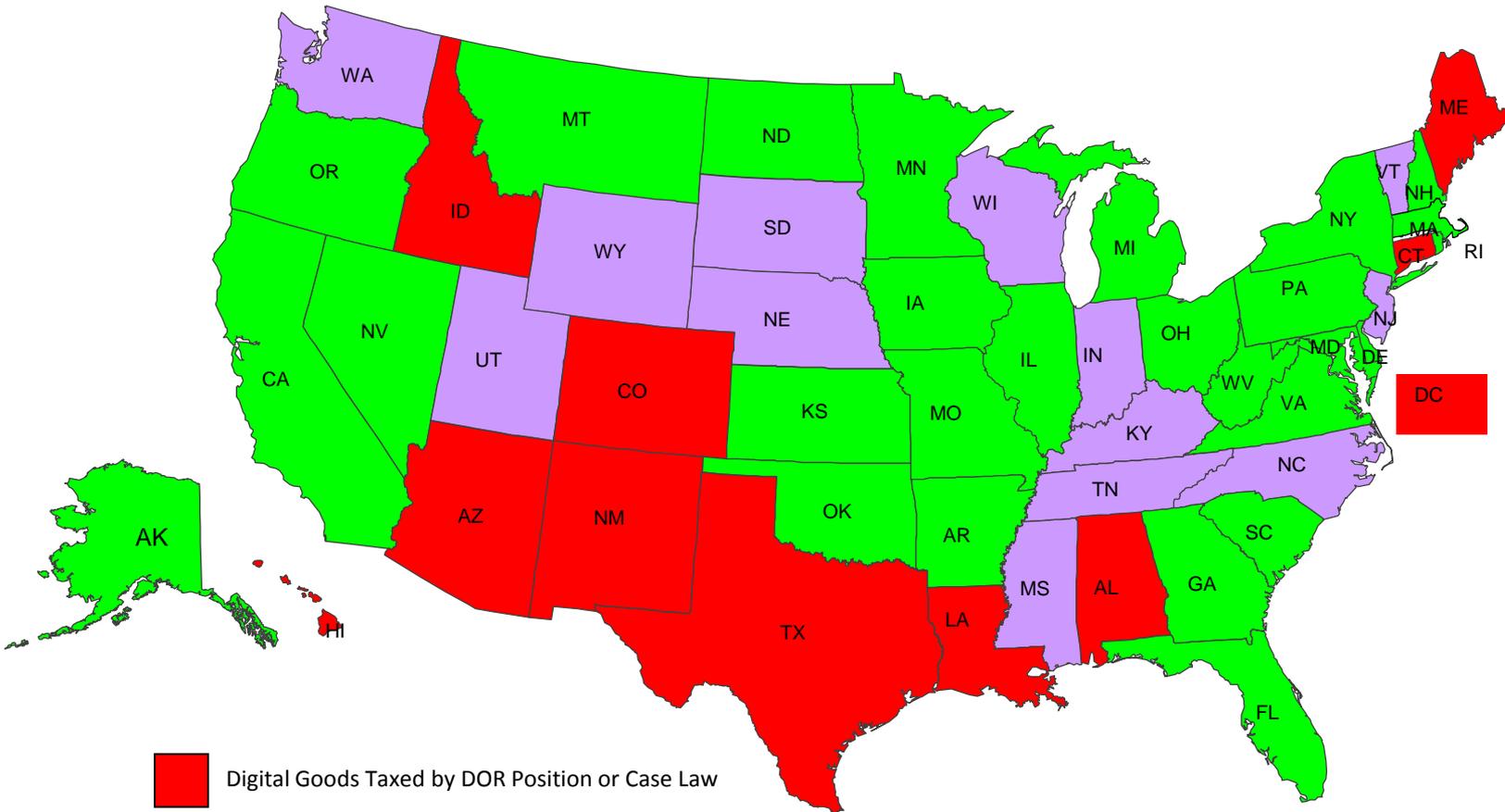
In one state, ring tones are taxed at the higher communications services tax rate when sold by a wireless provider.

...But you can download the entire song to an iTouch and just pay the retail sales tax rate.

Digital Goods and Services Tax Fairness Act

- **Rules to avoid tax pyramyding**
 - 20th Century state and local sales tax statutes applicable to the manufacturing economy included sale for resale exemptions and exemptions for business inputs to avoid tax pyramiding
 - National framework would establish clear rules to ensure that digital commerce is subject to same rules as tangible goods
 - Ensures digital goods and services are not subject to multiple taxation in course of producing/providing such goods and services
- **Rules to govern commerce over global networks**
 - Federal government has jurisdiction over international commerce (communications networks enable global commerce)
 - States need to work with Federal government to ensure U.S. subnational transaction tax system can be administered with respect to new digital services, such as cloud computing
 - Consumers have the ability to access digital services anywhere, anytime on any device – businesses need clear, simple and uniform rules to collect taxes on behalf of government

State of Confusion – Inconsistent State Laws Confuse Consumers and Hamper Consumer Access to the Digital Economy



-  Digital Goods Taxed by DOR Position or Case Law
-  Digital Goods Non-Taxable under Sales Tax
-  Digital Goods Taxed by Sales Tax Statute

Digital Goods and Services Tax Fairness Act

- **Congress should establish a national framework to preclude multiple and discriminatory state and local taxation of digital commerce**
 - Ensure fair taxation by clearly identifying which jurisdiction has the right to tax digital transactions, preventing multiple states from taxing the same transaction and claims that no state has the right to tax these transactions
 - Preclude discriminatory taxes imposed on other legacy services at excessive rates from being imposed on digital goods and services
- **Congress and states should ensure that 20th Century regressive and confusing tax systems are not expanded to Digital Commerce**
 - Digital Commerce is delivered over Global communications networks crossing numerous state and local boundaries – uniform 50 state system is critical
 - Congress has a clear role in taxation of International/Interstate commerce
- **Establishes clarity for consumers purchasing new innovative services, states and local governments seeking to impose taxes on these new goods and services, and businesses that collect tax for governments**
- **A National Framework would not preclude states from taxing this segment of the new economy under generally applicable taxes (e.g., sales taxes) and would provide certainty to state and local governments regarding tax revenues received from digital commerce**