



REPORT TO LAW & LEGISLATION COMMITTEE City of Sacramento

915 I Street, Sacramento, CA 95814-2671

Consent
August 9, 2007

Honorable Members of the
Law and Legislation Committee

**Title: Position on Federal Legislation: Oppose 1) S. 156/H.R. 743 and H.R. 1077
Relating to a Permanent Moratorium on Internet Access Taxes; and
Support 2) S. 1453 Relating to a Four-Year Extension of the Moratorium on
Internet Access Taxes**

Location/Council District: Citywide

Recommendation: Staff recommends that the Law and Legislation Committee adopt an oppose position on federal bills S. 156/H.R. 743 and H.R. 1077, which propose to make the current moratorium on Internet access taxes permanent, and support federal bill S. 1453, which would extend the Internet moratorium for four more years.

Contact: Susan West, Management Analyst, (916) 808-1246

Presenters: None

Department: Finance

Division: Administration

Organization No: 1111

Description/Analysis

Issue: The current Internet Tax Freedom Moratorium expires on November 1, 2007. The moratorium is a preemptive federal statute that prohibits any state or local tax: a) on Internet access; or b) that is a discriminatory tax on electronic commerce. The statute has been in place since 2003.

While the taxing jurisdictions in California have never taxed Internet access, they have always taxed charges for the use of communication networks. The current moratorium affects two different services: Internet access and broadband network service. It is the latter that has been causing a loss of UUT tax revenues for California cities for several years, and is expected to lead to more revenue loss in the future as traditional telephone customers switch from regular telephone service (which is taxable) to broadband and Voice Over Internet Protocol (VOIP) phone services (not taxable under the moratorium).

As the expiration date of the current moratorium approaches, Congress is considering whether to make the current moratorium permanent, or to extend the moratorium for four more years. Both have implications for cities with a local tax on telecommunications, where UUT/telephone service tax represents a significant portion of their tax base.

The following bills have been introduced in Congress relating to the Internet Tax Moratorium:

S. 156 (Wyden-OR) and H.R. 743 (Eshoo-CA): Permanent Internet Tax Freedom Act of 2007

These identical bills amend the Internet Tax Freedom Act to make permanent the ban on State taxation of Internet access and on multiple or discriminatory taxes on electronic commerce.

H.R. 1077 (Campbell-CA): Internet Consumer Protection Act of 2007

Amends the Internet Tax Freedom Act to make permanent the ban on state taxation of Internet access, and on multiple or discriminatory taxes on electronic commerce. Repeals provisions permitting states with Internet tax laws enacted prior to the ban on Internet taxes to continue enforcing such laws.

S. 1453 (Carper-DE): Internet Tax Freedom Extension Act of 2007

Amends the Internet Tax Freedom Act to extend until November 1, 2011: 1) the ban on state taxation of Internet access and on multiple or discriminatory taxes on electronic commerce; and 2) provisions allowing states with Internet tax laws enacted prior to the ban to continue enforcing such laws.

Policy Considerations: Federal legislation proposing to make the current Internet Tax Moratorium permanent will have a significant adverse impact on the City's UUT, as there will continue to be a major shift to Internet-provided communications and video programming services in the coming years. It is in the best interest of the City to ensure that any Internet tax proposal not be made permanent and further erode or eliminate the City's UUT.

The League of California Cities opposes any legislation that would make permanent an Internet Tax Moratorium, and supports legislation that would create an extension of the current Internet moratorium.

Environmental Considerations: None

Rationale for Recommendation: Given the potential of the current Internet Tax Moratorium to continue to erode the City's telecommunications tax base, a temporary extension of the current moratorium is preferable to making the moratorium permanent. Therefore, Staff recommends that the City oppose any legislation (current or future) that would make permanent an Internet Tax Moratorium, and support legislation that would create an extension of the current Internet moratorium.

Financial Considerations: As current telephone customers switch to VOIP, the City loses the tax revenues we had been receiving (or would have received) because our UUT Ordinance does not currently allow taxing VOIP.

The UUT is the third largest source of discretionary tax revenue in the General Fund. UUT applies to charges on electrical, natural gas, telephone (land line and cellular), and cable television services. For FY 2006-2007, revenue from the telephone user tax portion of the City's UUT is an estimated \$22.4 million. Revenues from all UUT sources are deposited into the General Fund and support critical City services.

Emerging Small Business Development (ESBD): None.

Respectfully Submitted by: 
Susan West, Management Analyst

Approved by: 
Russell Fehr, Director of Finance

Recommendation Approved:

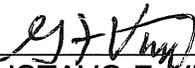

GUSTAVO F. VINA
Assistant City Manager

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Background

The Internet Tax Freedom Moratorium is a preemptive federal statute that prohibits any state or local tax: a) on Internet access; or, b) that is a discriminatory tax on electronic commerce. The current Moratorium expires on November 1, 2007.

The moratorium negatively impacts the City of Sacramento as follows:

- (1) As current telephone customers (or new customers) switch to VOIP, we lose the tax revenues we had been receiving (or would have received) because our UUT Ordinance does not currently allow taxing VOIP; and
- (2) It precludes the City from amending its UUT Ordinance in the future (with a Proposition 218 vote) to be able to capture such tax revenues in the future.

Proponents of the moratorium suggest that it has no financial impact on states and cities because these taxing jurisdictions have never imposed a tax on Internet Service Provider (ISP) services. This is not entirely accurate. While it is true that California jurisdictions have never taxed Internet access, it is also true that they have always taxed charges for the use of communication networks. The challenge is that the current moratorium affects two different services: Internet access and broadband network service. It is the latter that is causing a major loss of tax revenues for California cities for the past several years, and even more so in the future.

Consumers have more choices in telecommunications services today. As companies compete to offer services, customers migrate from traditional service providers to satellite, broadband, and others-- to which our UUT does not currently apply. This is why AT&T and Verizon experience significant losses in revenues each year, and why UUT cities are also experiencing a corresponding loss in tax revenues. This trend will likely accelerate until the broadband networks largely replace the old public-switched network. Those who point to the fact that cities do not tax Internet access are not acknowledging the loss of revenues when local tax cannot be applied to communication networks. Congress should be encouraged to understand why the current moratorium is rapidly eroding the existing tax base of California cities collecting a local tax on telecommunications. A permanent ban, or a continuation of the current moratorium, will cause the City of Sacramento to continue to lose UUT telecom revenues each year.

Given the potential of the moratorium to continue to erode the City's telecommunications tax base, a temporary extension of the current moratorium is preferable to making the moratorium permanent.

DATE

The Honorable _____
U.S. House of Representatives/U.S. Senate
_____ House Office Building/Senate Office Building
Washington, DC 20515

Subject: Impact of Permanent Extension of the Internet Tax Moratorium on California City Basic Services

Dear Congressman/woman/Senator _____:

On behalf of the City of Sacramento, I am writing to urge you to oppose federal legislation currently before Congress to permanently extend and expand the Internet Tax Moratorium (**S. 156/H.R. 743** and **H.R. 1077**); and to support alternate legislation providing for a short-term extension (**S. 1453**) of the current Internet Tax Freedom Act (PL 108-435).

The City of Sacramento would like to work with you to ensure that any Internet tax proposal not be made permanent and further erode or eliminate our City's Utility User Tax (UUT). In the City of Sacramento, revenue for the FY 2006-2007 telephone user tax portion (only) of the City's UUT is estimated at \$22.4 million. Revenues from all UUT sources are deposited into the General Fund and provide critical City services, including police, fire and emergency response.

Senator Dianne Feinstein is co-sponsoring **S. 1453**, the Internet Tax Freedom Extension Act of 2007. This bill would extend the current moratorium on Internet taxes to November 1, 2011. The current moratorium expires on November 1, 2007. This legislation will help preserve vital city services financed by UUT on telecommunications.

Thank you for your consideration of this important request.

Sincerely,

Sandy Sheedy, Chair
Law and Legislation Committee

cc: Senator Dianne Feinstein
Senator Barbara Boxer
Congresswoman Doris Matsui
Mayor Heather Fargo and Council
John Freshman
Genevieve Morelos – League of California Cities

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Permanent Internet Tax Freedom Act of 2007 (Introduced in Senate)

S 156 IS

110th CONGRESS

1st Session

S. 156

To make the moratorium on Internet access taxes and multiple and discriminatory taxes on electronic commerce permanent.

IN THE SENATE OF THE UNITED STATES

January 4, 2007

Mr. REID (for Mr. WYDEN (for himself, Mr. MCCAIN, and Mr. SUNUNU)) introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

A BILL

To make the moratorium on Internet access taxes and multiple and discriminatory taxes on electronic commerce permanent.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the `Permanent Internet Tax Freedom Act of 2007'.

SEC. 2. PERMANENT MORATORIUM ON INTERNET ACCESS

TAXES AND MULTIPLE AND DISCRIMINATORY TAXES ON ELECTRONIC COMMERCE.

Section 1101(a) of the Internet Tax Freedom Act (47 U.S.C. 151 note) is amended by striking `taxes during the period beginning November 1, 2003, and ending November 1, 2007:' and inserting `taxes:'.

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Permanent Internet Tax Freedom Act of 2007 (Introduced in House)

HR 743 IH

110th CONGRESS

1st Session

H. R. 743

To make the moratorium on Internet access taxes and multiple and discriminatory taxes on electronic commerce permanent.

IN THE HOUSE OF REPRESENTATIVES

January 31, 2007

Ms. ESHOO (for herself, Mr. GOODLATTE, Mr. CROWLEY, Mr. MACK, Mr. WESTMORELAND, Mr. NORWOOD, Mrs. MCMORRIS RODGERS, Mr. FARR, Ms. ZOE LOFGREN of California, Mr. MILLER of Florida, Mr. COHEN, Mr. SENSENBRENNER, Mr. KUHL of New York, Mr. FORTENBERRY, Mr. CHABOT, Mrs. JO ANN DAVIS of Virginia, Ms. JACKSON-LEE of Texas; Mr. CALVERT, Ms. HARMAN, Mrs. BLACKBURN, Mr. CAMPBELL of California, Mr. JORDAN of Ohio, Mr. MCHUGH, Mr. WILSON of South Carolina, Mr. WALBERG, Mr. UPTON, Mr. HERGER, Mr. HONDA, Mr. BOUCHER, Mr. JEFFERSON, Ms. LORETTA SANCHEZ of California, Mr. GRIJALVA, Mrs. TAUSCHER, Ms. HOOLEY, and Ms. HERSETH) introduced the following bill; which was referred to the Committee on the Judiciary

A BILL

To make the moratorium on Internet access taxes and multiple and discriminatory taxes on electronic commerce permanent.

Be it enacted by the Senate and House of Representatives of the United States of

America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the `Permanent Internet Tax Freedom Act of 2007'.

SEC. 2. PERMANENT MORATORIUM ON INTERNET ACCESS TAXES AND MULTIPLE AND DISCRIMINATORY TAXES ON ELECTRONIC COMMERCE.

Section 1101(a) of the Internet Tax Freedom Act (47 U.S.C. 151 note) is amended by striking `taxes during the period beginning November 1, 2003, and ending November 1, 2007:'. and inserting `taxes:'.

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Internet Consumer Protection Act of 2007 (Introduced in House)

HR 1077 IH

110th CONGRESS

1st Session

H. R. 1077

To amend the Internet Tax Freedom Act to make permanent the moratorium on certain taxes relating to the Internet and to electronic commerce.

IN THE HOUSE OF REPRESENTATIVES

February 15, 2007

Mr. CAMPBELL of California (for himself, Mr. DANIEL E. LUNGREN of California, Mr. CANTOR, Mr. FEENEY, Mr. GOODE, Mr. GOHMERT, Mr. PRICE of Georgia, Mr. DOOLITTLE, Mr. LAMBORN, Mr. SALI, Mr. GOODLATTE, Ms. ZOE LOFGREN of California, Mr. MILLER of Florida, Mr. MACK, Mr. GARRETT of New Jersey, Mr. GARY G. MILLER of California, Mr. SESSIONS, Mr. MCCARTHY of California, Mr. ROHRABACHER, Mrs. BLACKBURN, Mr. FOSSELLA, Mr. DREIER, Mr. PENCE, Mr. KLINE of Minnesota, Mr. WILSON of South Carolina, and Mr. BARRETT of South Carolina) introduced the following bill; which was referred to the Committee on the Judiciary

A BILL

To amend the Internet Tax Freedom Act to make permanent the moratorium on certain taxes relating to the Internet and to electronic commerce.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the `Internet Consumer Protection Act of 2007'.

SEC. 2. AMENDMENTS TO THE INTERNET TAX FREEDOM ACT.

The Internet Tax Freedom Act (47 U.S.C. 151 note) is amended--

(1) in section 1101(a) by striking `during the period beginning November 1, 2003, and ending November 1, 2007', and

(2) by striking section 1104.

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ITFA Extension Act of 2007 (Introduced in Senate)

S 1453 IS

110th CONGRESS

1st Session

S. 1453

To extend the moratorium on taxes on Internet access and multiple and discriminatory taxes on electronic commerce imposed by the Internet Tax Freedom Act, and for other purposes.

IN THE SENATE OF THE UNITED STATES

May 23, 2007

Mr. CARPER (for himself, Mr. ALEXANDER, Mrs. FEINSTEIN, Mr. VOINOVICH, and Mr. ENZI) introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

A BILL

To extend the moratorium on taxes on Internet access and multiple and discriminatory taxes on electronic commerce imposed by the Internet Tax Freedom Act, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the 'ITFA Extension Act of 2007'.

SEC. 2. FOUR-YEAR EXTENSION OF INTERNET TAX MORATORIUM.

(a) IN GENERAL- Section 1101(a) of the Internet Tax Freedom Act (47 U.S.C. 151 note) is amended by striking `2007:' and inserting `2011:'.

(b) GRANDFATHERING OF STATES THAT TAX INTERNET ACCESS- Section 1104(a) (2)(A) of such Act is amended by striking `2007.' and inserting `2011.'.

SEC. 3. DEFINITION OF INTERNET ACCESS.

(a) IN GENERAL- Section 1105(5) of the Internet Tax Freedom Act (47 U.S.C. 151 note) is amended to read as follows:

`(5) INTERNET ACCESS- The term `Internet access'--

`(A) means a service that enables users to connect to the Internet to access content, information, or other services offered over the Internet;

`(B) may include incidental services directly related to the provision of the service described in subparagraph (A), such as electronic mail or instant messaging; and

`(C) does not include--

`(i) telecommunications services (as defined in section 3(46) of the Communications Act of 1934 (47 U.S.C. 153(46))), except to the extent such services are purchased, used, or sold by a provider of Internet access to provide Internet access described in subparagraph (A) or (B); or

`(ii) voice service or any other good or service utilizing Internet protocol or any successor protocol, except services described in subparagraph (A) or (B).'

(b) CONFORMING AMENDMENT- The Internet Tax Freedom Act (47 U.S.C. 151 note) is amended by striking section 1108 and redesignating section 1109 as section 1108.

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