108TH CONGRESS *1st Session*	SENATE	REPORT 108–155

INTERNET TAX NON-DISCRIMINATION ACT OF 2003

R E P O R T

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

on

S. 150

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SEPTEMBER 29, 2003.—Ordered to be printed

Mr. MCCAIN, from the Committee on Commerce, Science, and Transportation, submitted the following

REPORT

[To accompany S. 150]

The Committee on Commerce, Science, and Transportation, to which was referred the bill (S. 150) to make permanent the moratorium on taxes on Internet access and multiple and discriminatory taxes on electronic commerce imposed by the Internet Tax Freedom Act, having considered the same, reports favorably thereon with an amendment (in the nature of a substitute) and recommends that the bill (as amended) do pass.

PURPOSE OF THE BILL

The primary purpose of S. 150, as amended, is to extend permanently the current Federal moratorium on State and local taxation of Internet access under the Internet Tax Freedom Act of 1998 (ITFA or the Act) and to ensure that the moratorium is applied in a technology neutral fashion.

BACKGROUND AND NEEDS

In 1998, the ITFA was enacted to impose a temporary moratorium on certain taxes that could have a detrimental effect on the continued expansion of Internet use in the United States. A grandfathering provision was included in the ITFA to allow States that were imposing such a tax as of October 1, 1998, to continue to do so. At the time, 26.2 percent of United States households had Internet access, according to the Department of Commerce (DOC). The DOC reports that by September 2001, prior to the renewal of the ITFA for a two-year period, 50.5 percent of United States households had Internet access. Forrester Research, a technology industry research firm, estimates that in 2002, 64 percent of United States households had Internet access, more than twice the

number of households with Internet access at the time the ITFA was enacted.

Despite the significant growth rate of Internet use in the United States since 1998, the penetration rate of Internet access still lags behind other basic technologies. For example, and in contrast to the Internet access rates cited above, 95.3 percent of American households have telephone service, according to the Federal Communications Commission (FCC). In addition, many of the households with Internet access have only basic dial-up access, and have not migrated to broadband access services, which offer higher bandwidth connections that permit faster data transmission and thus facilitate and enhance services such as streaming audio and video. The Yankee Group, a technology industry research firm, estimates that in 2002 only 15 percent of American households had broadband access, while most users connected through dial-up modem access. Accordingly, there remains a need to ensure that taxes on Internet access will not pose a hurdle to the continued adoption of basic dial-up access or to the migration from basic Internet access to broadband Internet access.

Since the enactment of the ITFA, e-commerce also has grown significantly. For example, in the fourth quarter of 1999, e-commerce retail sales totaled $5.39 billion, according to the DOC. By contrast, in the first quarter of 2003, the DOC estimates that e-commerce retail sales totaled $11.92 billion. Nevertheless, e-commerce remains a small fraction of overall economic activity in the United States. According to the DOC, in the fourth quarter of 1999, e-commerce accounted for 0.7 percent of total retail sales in the United States. By the first quarter of 2003, this percentage had more than doubled to 1.5 percent of the United States' total retail sales. However, e-commerce still remains an emerging component of the economy. As such, it merits the guarantee of fair and equal tax treatment that the ITFA provides through its provisions regarding multiple and discriminatory taxes on e-commerce.

To avoid impeding the growth of Internet use and of e-commerce in the United States, the Senate Committee on Commerce, Science, and Transportation (the Committee) believes that the ITFA's Internet tax moratorium should be made permanent. However, the extension of the ITFA moratorium is intended to prohibit only taxes on Internet access, as well as multiple and discriminatory taxes on e-commerce. The permanent extension of the ITFA would not affect States' and localities' current right and ability to collect sales taxes on e-commerce transactions or any other taxes not prohibited by the United States Constitution, the ITFA, or any other Federal law.

In addition, the Committee believes that the current definition of Internet access under the Act requires clarification to ensure that States and localities do not attempt to circumvent the moratorium on Internet access taxes by taxing individual components of access such as telecommunications services used to provide Internet access. To date, some States have interpreted narrowly the definition of Internet access under the ITFA in order to impose taxes on certain types of Internet access or components thereof. For example, certain States tax the transmission component of digital subscriber line (DSL) Internet access.

S. 150, as amended, would update the language of the ITFA in recognition of the significant technological developments in the methods used to access the Internet since 1998. The bill would ensure that all such methods, whether in the form of dial-up, DSL, cable, satellite, wireless, or any other technology platform, as well as components used to provide Internet access, would be covered by the Internet access tax moratorium and, therefore, would be exempt from State and local taxation. Specifically, section 2(c) of S. 150, as amended, would modify the definition of "Internet access" to include only telecommunications services that are used to provide Internet access within the scope of the tax exemption provided by the ITFA.

The Committee does not intend for the removal of section 1101(d) of the ITFA and the modification to the definition of Internet access as set forth in section 2 of S. 150, as amended, to affect the State and local governments' authority to assess and collect taxes that do not fall within the tax categories set forth in section 1101(a) of the ITFA, such as traditional sales and use taxes, excise taxes, property taxes, corporate income taxes, gross receipts taxes, business and occupational taxes, and other such taxes that are generally applied and not enumerated in section 1101(a) of the Act.

The Committee intends for the tax exemption for telecommunications services to apply whenever the ultimate use of those telecommunications services is to provide Internet access. Thus, if a telecommunications carrier sells wholesale telecommunications services to an Internet service provider that intends to use those telecommunications services to provide Internet access, then the exemption would apply.

The modified definition of Internet access would clarify that all transmission components of Internet access, regardless of the regulatory treatment of the underlying platform, are covered under the ITFA's Internet tax moratorium only when the transmission component is used to provide Internet access. For example, the FCC has determined that the transmission component of cable modem service constitutes "telecommunications" (as defined in the Communications Act of 1934, as amended (1934 Act)) not offered separately from the Internet access and is thus not a "telecommunications service" (as defined in the 1934 Act). By contrast, the FCC currently classifies the transmission component of Internet access via DSL as a "telecommunications service" (as defined in the 1934 Act). By modifying the definition of Internet access, the Committee seeks to clarify that, under the ITFA, neither Internet access nor the transmission component of Internet access is subject to taxation.

By approving S. 150, the Committee neither condones nor rejects the FCC's decisions regarding the regulatory classification of any services. The revised definition of "Internet access" would apply only to the term as used in S. 150. It is not intended to affect in any way existing laws, regulations, policies, or regulatory decisions by the FCC or any other agency. Specifically, the revised definition of Internet access does not reflect any intention on the part of the Committee to influence any regulatory decisions made by the FCC or any other agency regarding the classification of Internet access as "information services" (as defined in the 1934 Act), "tele-

communications services" (as defined in the 1934 Act), or otherwise.

Further, the modified definition of Internet access is not meant to affect State and local taxation of traditional telecommunications services and other services that are not used to provide Internet access. For example, the moratorium does not allow an Internet access provider to claim or to seek immunity from State or local taxes for the provision of other services—such as cable television programming—that are separate from Internet access. Nor does the moratorium exempt telecommunications services provided over the same facilities that are not used to provide Internet access.

Likewise, the modified definition of Internet access does not exempt from State or local taxation otherwise taxable products or services that are bundled with Internet access. The Committee intends that this clarification will be narrowly construed to include only those telecommunications services that are actually being used to provide Internet access. The Committee does not intend to include telecommunications services that are being used to provide services other than Internet access, regardless of whether those other services are offered separately or as part of a package that includes Internet access. In addition, the Committee intends for the words "to the extent that" to constitute words of limitation that clarify that a particular medium can deliver services other than Internet access. The language makes clear that when a particular medium is used to provide services other than Internet access, neither that medium nor those services fall under the ITFA's tax exemption. For example, a package of services that includes local voice, long distance voice, and Internet access would be covered under the Internet tax moratorium only with respect to the portion of the package that actually constitutes Internet access. In addition, the modified definition would not affect the taxability of voice telephony over the public switched telephone network (so-called "plain old telephone service" or "POTS").

Finally, the Committee does not intend for the lapse of the grandfathering protection to affect the authority of State and local taxing authorities to assess and collect traditional sales and use taxes, excise taxes, property taxes, corporate income taxes, gross receipts taxes, business and occupational taxes, and other such taxes that are generally applied and are not enumerated in section 1101(a) of the ITFA.

SUMMARY OF PROVISIONS

As reported, S. 150 would:

- Extend permanently the current Federal moratorium on State and local taxation of Internet access under the ITFA.
- Make permanent the current Federal prohibition under the Act on multiple and discriminatory State and local taxes relating to e-commerce transactions.
- Extend by three years, from October 1, 2003, the current grandfathering provision in the ITFA that permits States that imposed or enforced a tax on Internet access prior to the passage of the legislation in 1998 to continue doing so.
- Supplement the definition of Internet access to ensure that all Internet access is free from State and local taxes regardless of the technology used to provide such access.

• Ensure the FCC's and the States' ability to collect and remit Universal Service funds as authorized by section 254 of the Communications Act of 1934 would not be affected.

LEGISLATIVE HISTORY

The ITFA was signed into law on October 21, 1998 (P.L. 105–277; included as titles XI and XII of the Omnibus Appropriations Act of 1998). It imposed a three-year moratorium on State and local government taxes on Internet access, as well as on any multiple or discriminatory State and local taxes on Internet-based transactions. In 2001, Congress voted to amend the ITFA by extending the tax moratorium through November 1, 2003, under the Internet Tax Nondiscrimation Act (H.R. 1552). The extension was enacted on November 28, 2001 (P.L. 107–075).

The House of Representatives Judiciary Committee reported H.R. 49, the Internet Tax Nondiscrimination Act, to the full House of Representatives on July 17, 2003. H.R. 49 would extend permanently the moratorium on Internet access taxes and on discriminatory and multiple taxes on e-commerce transactions. The only amendment to H.R. 49 that was approved by the House of Representatives Judiciary Committee clarifies that States and localities cannot tax any form of Internet access, including certain telecommunications services under particular circumstances. Specifically, the amendment would insert ", except to the extent such services are used to provide Internet access" to the language in the ITFA that permits States and localities to continue taxing telecommunications services. On September 17, 2003, by voice vote, the full House of Representatives approved H.R. 49 as reported by the House of Representatives Judiciary Committee.

Senator Wyden introduced a companion bill to H.R. 49, S. 52, the Internet Tax Nondiscrimination Act of 2003, on January 7, 2003. Senator Allen introduced S. 150 shortly thereafter on January 13, 2003. Both S. 52 and S. 150 would amend the ITFA to establish a permanent Internet tax moratorium and eliminate, after three years, the grandfathering protection for States that imposed Internet access taxes prior to the passage of the ITFA.

On July 16, 2003, the Committee held a full Committee hearing on S. 150 and S. 52. The following individuals testified at the hearing: Joseph Ripp, Vice Chairman, America Online, Inc.; Paul Misener, Vice President for Global Public Policy, Amazon.com, Inc.; Billy Hamilton, Deputy Comptroller, Texas Comptroller of Public Accounts; and Mark Beshears, Assistant Vice President of State and Local Tax, Sprint Corporation.

On July 31, 2003, the Committee held an executive session at which it considered S. 150. The bill was ordered reported by a voice vote with an amendment in the nature of a substitute co-sponsored by Senators Allen, Brownback, Stevens, Sununu, and Wyden.

ESTIMATED COSTS

In accordance with paragraph 11(a) of rule XXVI of the Standing Rules of the Senate and section 403 of the Congressional Budget Act of 1974, the Committee provides the following cost estimate, prepared by the Congressional Budget Office:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, September 9, 2003.

Hon. JOHN MCCAIN,
Chairman, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for S. 150, the Internet Tax Nondiscrimination Act.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Sarah Puro.

Sincerely,

DOUGLAS HOLTZ-EAKIN,
Director.

Enclosure.

S. 150—Internet Tax Nondiscrimination Act

Summary: S. 150 would permanently extend a moratorium on certain state and local taxation of online services and electronic commerce, and after October 1, 2006, would eliminate an exception to that prohibition for certain states. Under current law, the moratorium is set to expire on November 1, 2003. CBO estimates that enacting S. 150 would have no impact on the federal budget, but beginning in 2007, it would impose significant annual costs on some state and local governments.

By extending and expanding the moratorium on certain types of state and local taxes, S. 150 would impose an intergovernmental mandate as defined in the Unfunded Mandates Reform Act (UMRA). CBO estimates that the mandate would cause state and local governments to lose revenue beginning in October 2006; those losses would exceed the threshold established in UMRA ($64 million in 2007, adjusted annually for inflation) by 2007. While there is some uncertainty about the number of states affected, CBO estimates that the direct costs to states and local governments would probably total between $80 million and $120 million annually, beginning in 2007. The bill contains no new private-sector mandates as defined in UMRA.

Estimated cost to the Federal Government: CBO estimates that enacting S. 150 would have no impact on the federal budget.

Intergovernmental mandates contained in the bill: The Internet Tax Freedom Act (ITFA) currently prohibits state and local governments from imposing taxes on Internet access until November 1, 2003. The ITFA, enacted as Public Law 105–277 on October 21, 1998, also contains an exception to this moratorium, sometimes referred to as the "grandfather clause," which allows certain state and local governments to tax Internet access if such tax was generally imposed and actually enforced prior to October 1, 1998.

S. 150 would make the moratorium permanent and, after October 1, 2006, would eliminate the grandfather clause. The bill also would state that the term "Internet access" or "Internet access services" as defined in ITFA would not include telecommunications services except to the extent that such services are used to provide Internet access (known as "aggregating" or "bundling" of services). These extensions and expansions of the moratorium constitute

intergovernmental mandates as defined in UMRA because they would prohibit states from collecting taxes that they otherwise could collect.

Estimated direct costs of mandates to state and local governments: CBO estimates that repealing the grandfather clause would result in revenue losses for as many as 10 states and for several local governments totaling between $80 million and $120 million annually, beginning in 2007. We also estimate that the change in the definition of Internet access could affect tax revenues for many states and local governments, but we cannot estimate the magnitude or the timing of any such additional impacts at this time.

UMRA includes in its definition of the direct costs of a mandate the amounts that state and local governments would be prohibited from raising in revenues to comply with the mandate. The direct costs of eliminating the grandfather clause would be the tax revenues that state and local governments are currently collecting but would be precluded from collecting under S. 150. States also could lose revenues that they currently collect on certain services, if those services are redefined as Internet access under the bill.

Over the next five years there will likely be changes in the technology and the market for Internet access. Such changes are likely to affect, at minimum, the price for access to the Internet as well as the demand for and the methods of such access. How these technological and market changes will ultimately affect state and local tax revenues is unclear, but for the purposes of this estimate, CBO assumes that over the next five years, these effects will largely offset each other, keeping revenues from taxes on Internet access within the current range.

The grandfather clause

The primary budget impact of this bill would be the revenue losses—starting in October 2006—resulting from eliminating the grandfather clause that currently allows some state and local governments to collect taxes on Internet access. While there is some uncertainty about the number of jurisdictions currently collecting such taxes—and the precise amount of those collections—CBO believes that as many as 10 states (Hawaii, New Hampshire, New Mexico, North Dakota, Ohio, South Dakota, Tennessee, Texas, Washington, Wisconsin) and several local jurisdictions in Colorado, Ohio, South Dakota, Texas, Washington, and Wisconsin are currently collecting such taxes and that these taxes total between $80 million and $120 million annually. This estimate is based on information from the states involved, from industry sources, and from the Department of Commerce. In arriving at this estimate, CBO took into account the fact that some companies are challenging the applicability of the tax to the service they provide and thus may not be collecting or remitting the taxes even though the states feel they are obligated to do so. Such potential liabilities are not included in the estimate.

It is possible that if the moratorium were allowed to expire as scheduled under current law, some state and local governments would enact new taxes or decide to apply existing taxes to Internet access during the next five years. It is also possible that some governments would repeal existing taxes or preclude their application to these services. Because such changes are difficult to predict, for

the purposes of estimating the direct costs of the mandate, CBO considered only the revenues from taxes that are currently in place and actually being collected.

Definition of Internet access

Depending on how the language altering the definition of what telecommunications services are taxable is interpreted, that language also could result in substantial revenue losses for states and local governments. It is possible that states could lose revenue if services that are currently taxed are redefined as Internet "access" under the definition in S. 150. Revenues could also be lost if Internet access providers choose to bundle products and call the product Internet access. Such changes would reduce state and local revenues from telecommunications taxes and possibly revenues from content currently subject to sales and use taxes. However, CBO cannot estimate the magnitude of these losses.

Estimated impact on the private sector: This bill would impose no new private-sector mandates as defined in UMRA.

Previous CBO estimate: On July 21, 2003, CBO transmitted a cost estimate for H.R. 49, the Internet Tax Nondiscrimination Act, as ordered reported by the House Committee on the Judiciary on July 16, 2003. Unlike H.R. 49, which would eliminate the grandfather clause upon passage, S. 150 would allow the grandfather clause to remain in effect until October 2006. Thus, while both bills contain an intergovernmental mandate with costs above the threshold, the enactment of S. 150 would not result in revenue losses to states until October 2006.

Estimate prepared by: Impact on State, Local, and Tribal Governments: Sarah Puro. Federal Costs: Melissa Zimmerman. Impact on the Private Sector: Paige Piper/Bach.

Estimate approved by: Peter H. Fontaine, Deputy Assistant Director for Budget Analysis.

REGULATORY IMPACT STATEMENT

In accordance with paragraph 11(b) of rule XXVI of the Standing Rules of the Senate, the Committee provides the following evaluation of the regulatory impact of the legislation, as reported:

NUMBER OF PERSONS COVERED

S. 150 would extend permanently the current Internet tax moratorium under the ITFA. The revised definition of Internet access under the bill, as reported, would clarify that the definition of Internet access is meant to include all forms of Internet access, regardless of the medium by which such access is provided. However, the measure is not expected to have an effect on the number of persons regulated.

ECONOMIC IMPACT

S. 150 would preserve State and local taxing authorities' ability to impose traditional sales and use taxes, excise taxes, property taxes, corporate income taxes, gross receipt taxes, business and occupational taxes, and other such taxes that are generally applied and are not enumerated in section 1101(a) of the ITFA. Because these taxes make up the vast majority of State and local tax reve-

nues, any adverse economic impact that the moratorium would have on States is expected to be relatively minimal. S. 150, as amended, would terminate the current grandfather clause after three years; therefore, after that time the States that are currently grandfathered may lose collectively between $80 million and $120 million in annual revenues beginning in 2007, according to CBO's initial analysis of S. 150.

It is expected that S. 150 would continue to facilitate the growth of e-commerce and to encourage increasing numbers of Americans to access the Internet via various technological means. Accordingly, the permanent extension of the Internet tax moratorium is expected to create benefits for the economy.

PRIVACY

S. 150 is not expected to have an adverse effect on the personal privacy of any individuals that will be impacted by this legislation.

PAPERWORK

S. 150 would have a minimal impact on current paperwork levels.

SECTION-BY-SECTION ANALYSIS

Section 1. Short title

This section provides that the bill may be cited as the "Internet Tax Non-discrimination Act".

Section 2. Permanent extension of Internet Tax Freedom Act moratorium

This section would extend permanently the current Federal moratorium on State and local Internet access taxes and on State and local multiple or discriminatory taxes on e-commerce. In addition, this section would make certain changes to the ITFA relating to the permanent extension of the tax moratorium. Significantly, this section also would amend the definitions of "Internet access" and "Internet access service" contained in the ITFA by adding ", except to the extent such services are used to provide Internet access" at the end of the second sentence of each of sections 1101(e)(3)(D) and 1104(5) of the ITFA. Those sentences would thus read, "Such term does not include telecommunications services, except to the extent such services are used to provide Internet access." [1]

The permanent extension of the moratorium is consistent with the majority view of the Advisory Commission on Electronic Commerce (ACEC) established pursuant to the ITFA that the current moratorium on Internet access taxes should be extended permanently.

Section 3. Three-year sunset for pre-October 1998, tax exception

This section would extend by three years, from October 1, 2003, the current grandfathering provision that permits States that imposed or enforced a tax on Internet access prior to October 1, 1998,

[1] Though this report focuses specifically on the modified definition of "Internet access," the discussion of that modified definition generally applies also to the modified definition of "Internet access service."

to continue taxing Internet access. Thereafter, the grandfathering protection would be eliminated.

The elimination of the grandfathering protection is consistent with the majority view of the ACEC that the grandfathering protection of the ITFA should be abolished.

Section 4. Universal service

This section states that nothing in the ITFA shall prevent the imposition or collection of any fees or charges used to preserve and advance universal service or similar State programs authorized by section 254 of the Communications Act of 1934.

CHANGES IN EXISTING LAW

In compliance with paragraph 12 of rule XXVI of the Standing Rules of the Senate, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new material is printed in italic, existing law in which no change is proposed is shown in roman):

INTERNET TAX FREEDOM ACT.

[Pub. L. 105–277, Div. C, Title XI, 112 Stat. 2681–719; as amended by Pub. L. 107–75, 115 Stat. 703 (47 U.S.C. 151 nt)**]**

SEC. 1100. SHORT TITLE.

This title may be cited as the "Internet Tax Freedom Act".

SEC. 1101. MORATORIUM.

[(a) MORATORIUM.—No State or political subdivision thereof shall impose any of the following taxes during the period beginning on October 1, 1998, and ending on November 1, 2003—

[(1) taxes on Internet access, unless such tax was generally imposed and actually enforced prior to October 1, 1998; and

[(2) multiple or discriminatory taxes on electronic commerce.**]**

(a) MORATORIUM.—No State or political subdivision thereof may impose any of the following taxes:

(1) Taxes on Internet access.

(2) Multiple or discriminatory taxes on electronic commerce.

(b) PRESERVATION OF STATE AND LOCAL TAXING AUTHORITY.—Except as provided in this section, nothing in this title shall be construed to modify, impair, or supersede, or authorize the modification, impairment, or superseding of, any State or local law pertaining to taxation that is otherwise permissible by or under the Constitution of the United States or other Federal law and in effect on the date of enactment of this Act.

(c) LIABILITIES AND PENDING CASES.—Nothing in this title affects liability for taxes accrued and enforced before the date of enactment of this Act, nor does this title affect ongoing litigation relating to such taxes.

[(d) DEFINITION OF GENERALLY IMPOSED AND ACTUALLY ENFORCED.—For purposes of this section, a tax has been generally imposed and actually enforced prior to October 1, 1998, if, before that date, the tax was authorized by statute and either—

[(1) a provider of Internet access services had a reasonable opportunity to know by virtue of a rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that such agency has interpreted and applied such tax to Internet access services; or

[(2) a State or political subdivision thereof generally collected such tax on charges for Internet access.]

[(e)]*(d)* EXCEPTION TO MORATORIUM.—

(1) IN GENERAL.—Subsection (a) shall also not apply in the case of any person or entity who knowingly and with knowledge of the character of the material, in interstate or foreign commerce by means of the World Wide Web, makes any communication for commercial purposes that is available to any minor and that includes any material that is harmful to minors unless such person or entity has restricted access by minors to material that is harmful to minors—

(A) by requiring use of a credit card, debit account, adult access code, or adult personal identification number;

(B) by accepting a digital certificate that verifies age; or

(C) by any other reasonable measures that are feasible under available technology.

(2) SCOPE OF EXCEPTION.—For purposes of paragraph (1), a person shall not be considered to making a communication for commercial purposes of material to the extent that the person is—

(A) a telecommunications carrier engaged in the provision of a telecommunications service;

(B) a person engaged in the business of providing an Internet access service;

(C) a person engaged in the business of providing an Internet information location tool; or

(D) similarly engaged in the transmission, storage, retrieval, hosting, formatting, or translation (or any combination thereof) of a communication made by another person, without selection or alteration of the communication.

(3) DEFINITIONS.—In this subsection:

(A) BY MEANS OF THE WORLD WIDE WEB.—The term "by means of the World Wide Web" means by placement of material in a computer server-based file archive so that it is publicly accessible, over the Internet, using hypertext transfer protocol, file transfer protocol, or other similar protocols.

(B) COMMERCIAL PURPOSES; ENGAGED IN THE BUSINESS.—

(i) COMMERCIAL PURPOSES.—A person shall be considered to make a communication for commercial purposes only if such person is engaged in the business of making such communications.

(ii) ENGAGED IN THE BUSINESS.—The term "engaged in the business" means that the person who makes a communication, or offers to make a communication, by means of the World Wide Web, that includes any material that is harmful to minors, devotes time, attention, or labor to such activities, as a regular course of such person's trade or business, with the objective of earning a profit as a result of such activities (although

it is not necessary that the person make a profit or that the making or offering to make such communications be the person's sole or principal business or source of income). A person may be considered to be engaged in the business of making, by means of the World Wide Web, communications for commercial purposes that include material that is harmful to minors, only if the person knowingly causes the material that is harmful to minors to be posted on the World Wide Web or knowingly solicits such material to be posted on the World Wide Web.

(C) INTERNET.—The term "Internet" means collectively the myriad of computer and telecommunications facilities, including equipment and operating software, which comprise the interconnected world-wide network of networks that employ the Transmission Control Protocol/Internet Protocol, or any predecessor or successor protocols to such protocol, to communicate information of all kinds by wire or radio.

(D) INTERNET ACCESS SERVICE.—The term "Internet access service" means a service that enables users to access content, information, electronic mail, or other services offered over the Internet and may also include access to proprietary content, information, and other services as part of a package of services offered to consumers. Such term does not include telecommunications [services.] *services, except to the extent such services are used to provide Internet access.*

(E) INTERNET INFORMATION LOCATION TOOL.—The term "Internet information location tool" means a service that refers or links users to an online location on the World Wide Web. Such term includes directories, indices, references, pointers, and hypertext links.

(F) MATERIAL THAT IS HARMFUL TO MINORS.—The term "material that is harmful to minors" means any communication, picture, image, graphic image file, article, recording, writing, or other matter of any kind that is obscene or that—

(i) the average person, applying contemporary community standards, would find, taking the material as a whole and with respect to minors, is designed to appeal to, or is designed to pander to, the prurient interest;

(ii) depicts, describes, or represents, in a manner patently offensive with respect to minors, an actual or simulated sexual act or sexual contact, an actual or simulated normal or perverted sexual act, or a lewd exhibition of the genitals or post-pubescent female breast; and

(iii) taken as a whole, lacks serious literary, artistic, political, or scientific value for minors.

(G) MINOR.—The term "minor" means any person under 17 years of age.

(H) TELECOMMUNICATIONS CARRIER; TELECOMMUNICATIONS SERVICE.—The terms "telecommunications carrier"

and "telecommunications service" have the meanings given such terms in section 3 of the Communications Act of 1934 (47 U.S.C. 153).

(f) ADDITIONAL EXCEPTION TO MORATORIUM.—

(1) IN GENERAL.—Subsection (a) shall also not apply with respect to an Internet access provider, unless, at the time of entering into an agreement with a customer for the provision of Internet access services, such provider offers such customer (either for a fee or at no charge) screening software that is designed to permit the customer to limit access to material on the Internet that is harmful to minors.

(2) DEFINITIONS.—In this subsection:

(A) INTERNET ACCESS PROVIDER.—The term "Internet access provider" means a person engaged in the business of providing a computer and communications facility through which a customer may obtain access to the Internet, but does not include a common carrier to the extent that it provides only telecommunications services.

(B) INTERNET ACCESS SERVICES.—The term "Internet access services" means the provision of computer and communications services through which a customer using a computer and a modem or other communications device may obtain access to the Internet, but does not include telecommunications services provided by a common carrier.

(C) SCREENING SOFTWARE.—The term "screening software" means software that is designed to permit a person to limit access to material on the Internet that is harmful to minors.

(3) APPLICABILITY.—Paragraph (1) shall apply to agreements for the provision of Internet access services entered into on or after the date that is 6 months after the date of enactment of this Act.

* * * * * * *

SEC. 1104. PRESERVATION OF PRE-OCTOBER, 1998, STATE AND LOCAL TAX AUTHORITY UNTIL 2006.

(a) IN GENERAL.—Section 1101(a) does not apply to a tax on Internet access that was generally imposed and actually enforced prior to October 1, 1998, if, before that date, the tax was authorized by statute and either—

(1) a provider of Internet access services had a reasonable opportunity to know by virtue of a rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that such agency has interpreted and applied such tax to Internet access services; or

(2) a State or political subdivision thereof generally collected such tax on charges for Internet access.

(b) TERMINATION.—This section shall not apply after October 1, 2006.

(c) TAX ON INTERNET ACCESS.—Notwithstanding section 1105(10), in this section the term 'tax on Internet access' includes the enforcement or application of any preexisting tax on the sale or use of Internet services if that tax was generally imposed and actually enforced prior to October 1, 1998.

SEC. [1104.] *1105.* DEFINITIONS.

For the purposes of this title:

(1) BIT TAX.—The term "bit tax" means any tax on electronic commerce expressly imposed on or measured by the volume of digital information transmitted electronically, or the volume of digital information per unit of time transmitted electronically, but does not include taxes imposed on the provision of telecommunications services.

(2) DISCRIMINATORY TAX.—The term "discriminatory tax" means—

(A) any tax imposed by a State or political subdivision thereof on electronic commerce that—

(i) is not generally imposed and legally collectible by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means;

(ii) is not generally imposed and legally collectible at the same rate by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means, unless the rate is lower as part of a phase-out of the tax over not more than a 5-year period;

(iii) imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or information accomplished through other means;

(iv) establishes a classification of Internet access service providers or online service providers for purposes of establishing a higher tax rate to be imposed on such providers than the tax rate generally applied to providers of similar information services delivered through other means; or

(B) any tax imposed by a State or political subdivision thereof, if—

(i) [except with respect to a tax (on Internet access) that was generally imposed and actually enforced prior to October 1, 1998,] the sole ability to access a site on a remote seller's out-of-State computer server is considered a factor in determining a remote seller's tax collection obligation; or

(ii) a provider of Internet access service or online services is deemed to be the agent of a remote seller for determining tax collection obligations solely as a result of—

(I) the display of a remote seller's information or content on the out-of-State computer server of a provider of Internet access service or online services; or

(II) the processing of orders through the out-of-State computer server of a provider of Internet access service or online services.

(3) ELECTRONIC COMMERCE.—The term "electronic commerce" means any transaction conducted over the Internet or through Internet access, comprising the sale, lease, license, offer, or de-

livery of property, goods, services, or information, whether or not for consideration, and includes the provision of Internet access.

(4) INTERNET.—The term "Internet" means collectively the myriad of computer and telecommunications facilities, including equipment and operating software, which comprise the interconnected world-wide network of networks that employ the Transmission Control Protocol/Internet Protocol, or any predecessor or successor protocols to such protocol, to communicate information of all kinds by wire or radio.

(5) INTERNET ACCESS.—The term "Internet access" means a service that enables users to access content, information, electronic mail, or other services offered over the Internet, and may also include access to proprietary content, information, and other services as part of a package of services offered to users. Such term does not include telecommunications [services.] *services, except to the extent such services are used to provide Internet access.*

(6) MULTIPLE TAX.—

(A) IN GENERAL.—The term "multiple tax" means any tax that is imposed by one State or political subdivision thereof on the same or essentially the same electronic commerce that is also subject to another tax imposed by another State or political subdivision thereof (whether or not at the same rate or on the same basis), without a credit (for example, a resale exemption certificate) for taxes paid in other jurisdictions.

(B) EXCEPTION.—Such term shall not include a sales or use tax imposed by a State and 1 or more political subdivisions thereof on the same electronic commerce or a tax on persons engaged in electronic commerce which also may have been subject to a sales or use tax thereon.

(C) SALES OR USE TAX.—For purposes of subparagraph (B), the term "sales or use tax" means a tax that is imposed on or incident to the sale, purchase, storage, consumption, distribution, or other use of tangible personal property or services as may be defined by laws imposing such tax and which is measured by the amount of the sales price or other charge for such property or service.

(7) STATE.—The term "State" means any of the several States, the District of Columbia, or any commonwealth, territory, or possession of the United States.

(8) TAX.—

(A) IN GENERAL.—The term "tax" means—

(i) any charge imposed by any governmental entity for the purpose of generating revenues for governmental purposes, and is not a fee imposed for a specific privilege, service, or benefit conferred; or

(ii) the imposition on a seller of an obligation to collect and to remit to a governmental entity any sales or use tax imposed on a buyer by a governmental entity.

(B) EXCEPTION.—Such term does not include any franchise fee or similar fee imposed by a State or local franchising authority, pursuant to section 622 or 653 of the

Communications Act of 1934 (47 U.S.C. 542, 573), or any other fee related to obligations or telecommunications carriers under the Communications Act of 1934 (47 U.S.C. 151 et seq.).

(9) TELECOMMUNICATIONS SERVICE.—The term "telecommunications service" has the meaning given such term in section 3(46) of the Communications Act of 1934 (47 U.S.C. 153(46)) and includes communications services (as defined in section 4251 of the Internal Revenue Code of 1986).

(10) TAX ON INTERNET ACCESS.—The term "tax on Internet access" means a tax on Internet access, including the enforcement or application of any new or preexisting tax on the sale or use of Internet [services unless such tax was generally imposed and actually enforced prior to October 1, 1998.] *services.*

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