



NATIONAL CONFERENCE *of* STATE LEGISLATURES

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TESTIMONY OF  
HONORABLE PHIL MONTGOMERY  
STATE REPRESENTATIVE, WISCONSIN

CHAIRMAN,  
NATIONAL CONFERENCE OF STATE LEGISLATURES'  
COMMITTEE ON COMMUNICATIONS, FINANCIAL SERVICES  
& INTERSTATE COMMERCE

ON BEHALF OF THE  
NATIONAL CONFERENCE OF STATE LEGISLATURES

REGARDING  
VOIP : WHO HAS JURISDICTION TO TAX IT?  
VOIP SOURCING ACT OF 2009

BEFORE THE  
SUBCOMMITTEE ON COMMERCIAL  
AND ADMINISTRATIVE LAW  
COMMITTEE ON THE JUDICIARY  
UNITED STATES HOUSE OF REPRESENTATIVES

MARCH 31, 2009

**SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW  
COMMITTEE ON THE JUDICIARY  
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**TESTIMONY OF THE HONORABLE PHIL MONTGOMERY  
CHAIRMAN  
NCSL COMMITTEE ON COMMUNICATIONS, FINANCIAL SERVICES  
& INTERSTATE COMMERCE**

Chairman Cohen, Ranking Member Franks and members of the Subcommittee on Commercial and Administrative Law, I appreciate the invitation to testify before you today on behalf of the National Conference of State Legislatures (NCSL). I am Phil Montgomery, a member of the Wisconsin Assembly and I serve as Chairman of NCSL's Standing Committee on Communications, Financial Services & Interstate Commerce. As you know Mr. Chairman, the National Conference of State Legislatures is the bi-partisan national organization representing every state legislator from all fifty states and our nation's commonwealths, territories, possessions and the District of Columbia.

Mr. Chairman, I also am pleased to acknowledge your long history as an active member of NCSL, especially during your service on NCSL's Executive Committee. Speaking on behalf of your colleagues in state legislatures, we are proud of your past service as a state Senator and now your leadership in Congress. We hope that during your tenure as a member of Congress and your chairmanship of this Subcommittee, we will have numerous opportunities to work together to foster a strong federal-state partnership on issues of mutual concern.

I am pleased to have the opportunity to appear before you today to discuss Voice over Internet Protocol and the problems related to the assessment and collection of taxes on VoIP related services. I also am here to express NCSL's support for draft legislation - the "Voice over Internet Protocol Sourcing Act of 2009" - and I want to commend you

Mr. Chairman for your willingness to sponsor this important legislation that goes directly to strengthening the federal-state partnership.

### **Mobile Telecommunications Sourcing Act (MTSA)**

Mr. Chairman, you may recall that while you were a member of the Tennessee Senate, you voted to implement Public Law 106-252, the Federal Mobile Telecommunications Sourcing Act (MTSA). This legislation established a national framework that when implemented by the states between 2001-2002 provided a mechanism on how mobile telecommunications calls involving multiple jurisdictions should be assigned or sourced for tax purposes.

Prior to the enactment of the MTSA, the Supreme Court decision in *Goldberg vs. Sweet* governed the question of which jurisdiction has authority to tax all interstate calls, both wireline and wireless. Under the Goldberg rule, a jurisdiction could impose a tax on a call if the call either originated or terminated in the jurisdiction and the call was charged to a "service address" in that jurisdiction.

Because of the mobile nature of wireless telecommunications, it had become more difficult to determine whether wireless calls met the two-out-of-three "Goldberg" rule of origination or termination plus service address, calling into question states' ability to tax such calls. Furthermore, as customers increasingly selected single rate, fixed-usage plans, the wireless industry's determination of which jurisdiction has authority to tax the calls become more complicated. With the growing popularity of the single rate plans, there was a decreasing need to track individual calls for billing purposes. Tracking individual calls solely for tax purposes unnecessarily wastes company resources.

The MTSA solved both of these problems. It created the concept that the customer has a "place of primary use," which is the jurisdiction with the right to tax wireless calls, even if the call neither originates nor terminates in that jurisdiction. Thus,



the federal law allows states and localities to tax calls that they could not have taxed under the "Goldberg" rule and precludes their ability to tax other calls that they may have historically taxed.

The MTSA also provided a means to avoid another very contentious fight between state and local governments, Congress and industry as was the case just two short years before its enactment. You may recall, that in 1998 in response to an effort by some states to tax access to the Internet, Congress passed and President Clinton signed into the law the first Internet Tax Freedom Act. The new law prohibited taxation of access to the Internet by any government, federal, state or local. The legislation did grandfather approximately 13 states, but the number is now down to 9 to 10 states. With the rapid growth of the Internet in the late 1990's, some state tax departments merely extended the taxation schemes that existed in their states' telecommunications statutes without any recognition of the impact on a new interstate communications service. Applying the old tax scheme to an emerging technology led to protests and complaints from communications providers and Internet service providers. While Congress intended the original moratorium to be a temporary measure, it has now been extended until 2014 and will likely be made permanent. The MTSA is a model in avoiding another Internet Tax Freedom Act type battle between Congress, state and local governments and industry. It is for this reason that we seek quick congressional action to pass legislation that would extend the sourcing provisions of the MTSA to Voice over Internet Protocol and get it to the President's desk for his signature.

The MTSA was a "win-win" for both industry and government. State and local governments supported the MTSA to prevent "nowhere taxation" and to bring administrative simplicity and cost savings to tax administration. Furthermore, government organizations supported the legislation to avoid potential Congressional preemption of state taxing authority based on the above mentioned burdens on Interstate Commerce.

The wireless industry supported the legislation to prevent multiple taxation; to achieve administrative simplicity and cost savings in the billing process; to avoid expensive audit and litigation exposure when multiple states claim jurisdiction to tax the same call; and to avoid class action lawsuits from customers who claim that companies are improperly collecting taxes even when they are merely complying with state laws.

The MTSA was enacted in July 2000 and in two years, all fifty state legislatures and the Council of the District of Columbia passed legislation to bring their states into compliance with the federal legislation. The MTSA has served state and local governments well as it ensured a vital revenue stream and provided clarity and uniformity for providers in collecting our taxes and fees on wireless services. The MTSA has served as a model of federal, state and private sector cooperation.

NCSL is once again pleased support and urge passage of legislation to extend the MTSA provisions to VoIP. We will work with the other state and local organizations to obtain their support for a VoIP sourcing rule. This legislation will merely clarify how VoIP calls involving multiple jurisdictions should be sourced for state and local tax purposes; it will not change the tax status of any VoIP provider.

As is the case with wireless calls, it is just as important for VoIP communications that there be clear, national rules for determining what jurisdiction is permitted to tax the call, and thus avoid situations where multiple jurisdictions may try to tax the same call or that a call might escape taxation all together. While the thought of tax free communications may be appealing, we must acknowledge that if a government taxes communications services, as policymakers we have an obligation to ensure that all providers, regardless of the medium used, should be treated similarly for tax purposes. Taxes on communications services must be applied in a competitively neutral manner, without being used to benefit one provider over another in the marketplace. This legislation endeavors to ensure competitive neutrality.

## **Voice over Internet Protocol**

Ten years ago when negotiations were taking place between state and local governments and providers on the sourcing of wireless calls, few had any notion that soon another developing technology would provide another medium for voice communications that would once again challenge the way government taxes communications services.

Voice over Internet Protocol or VoIP enables packet transmission over data networks which in essence converts voice to data and allows for voice transmission over the Internet. I will leave the basics and types of VoIP transmissions to the experts on this panel. However, as a legislator and an advocate for enhanced communications services, I am concerned about how my colleagues in state governments may attempt to collect taxes on VoIP communications service. Under what “tax rule” will state tax departments attempt to assess VoIP services for taxation? It certainly does not meet the standard of the Goldberg rule I mentioned above and while in some respects the mobile telecommunications sourcing rules could apply, VoIP technology also has differences from wireless technology that will need to be addressed.

The legislation to source VoIP services provides the clarity that state and local governments need to assess and collect taxes on VoIP services. It ensures that well meaning tax officials do not try to impose existing tax regimes on VoIP that will only lead to confusion, litigation, lost revenue and possibly federal preemption.

This legislation will expand the sourcing rule adopted in the Mobile Telecommunications Sourcing Act to VoIP services. This will ensure consistent tax treatment of VoIP across all states. It will provide consumers, vendors and state and



local governments with certainty, thus avoiding needless litigation. It ends the likelihood of multiple taxation of the same call and eliminates the possibility of “nowhere” taxation.

As with the Mobile Telecommunications Sourcing Act, this legislation allows the jurisdiction the customer identifies as their place of primary use (PPU) to tax VoIP services and conforms with the sourcing provisions of the Streamlined Sales and Use Tax Agreement.

VoIP providers may offer VoIP services that provide multiple telephone numbers only a limited amount of capacity or lines for making calls outside of the internal network. With VoIP it is important to understand that telephone numbers do not necessarily equal a traditional wireline access line. Therefore the VoIP sourcing rule will only count those lines that a customer can make simultaneous calls as a line for tax purposes.

As I mentioned previously, what this legislation does not do is change the taxability of VoIP services. If VoIP is already taxable in a jurisdiction, this legislation only provides certainty in how services will be sourced for tax purposes, it does not force a state or local government to impose any new taxes. As VoIP service is an Internet protocol, it is possible that a VoIP service provider may not have nexus in a state where it has customers. If a VoIP service provider does not have nexus in a state, this legislation does not provide any new authority to the state or local governments in that state to tax the service provided by the non-nexus VoIP service provider.

## **Conclusion**

Last year, the National Conference of State Legislatures held a total of three hearings on the question of assessing taxation on VoIP services in which we invited all stakeholders to express their concerns. At our annual meeting last summer, NCSL’s membership unanimously approved a request to Congress for legislation which would

extend the MTSA sourcing provisions to Voice over Internet Protocol. A copy of the NCSL resolution is attached to my testimony.

The legislation to extend the MTSA provisions to VoIP should be considered non-controversial and should move without any opposition. For this reason, we also would request that the Voice over Internet Protocol sourcing legislation not become a vehicle for non-germane or slightly related amendments that would only slow and probably keep the legislation from enactment.

Mr. Chairman, thank you for inviting me to express the concerns of the National Conference of State Legislatures with regard to the assessment of taxation on VoIP services and our support for legislation on a national sourcing rule. We stand ready to work with you and the other members of this Subcommittee to ensure quick congressional passage of a sourcing rule for VoIP

Thank you.