



Taxation of E-Commerce

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The question of taxing e-commerce has been addressed in a number of forums. The main issue concerns jurisdiction: which governmental entity shall have the authority to tax a transaction that spans several jurisdictions? The goal of a comprehensive e-commerce taxation policy framework is two-fold: to avoid either double-taxation or non-taxation; and to avoid disparate treatment of off-line versus on-line transactions.

Organization for Economic Cooperation and Development

Perhaps the most important work on taxation of e-commerce has been done by the OECD. See <http://www.oecd.org/oecd/pages/home/displaygeneral/0,3380,EN-document-101-nodirectorate-no-21-1564-22,FF.html> for detailed information.

Key principles for the taxation of electronic commerce were agreed to at the OECD Ministerial Conference in Ottawa in 1998. The OECD concluded that the taxation principles that guide governments in relation to conventional commerce should also guide them in relation to electronic commerce.

- In the tax treaty area, the OECD framework provides that the present international norms are capable of being applied to electronic commerce, but that some clarifications should be given as to how these norms, and in particular the Model Tax Convention, applies.
- In the consumption tax area, the framework provides that taxation should occur in the jurisdiction where consumption taxes place, and that the supply of digitised products should not be treated as a supply of goods.

In the tax administration area, information reporting requirements and tax collection procedures should be neutral and fair, so that the level and standard is comparable to what is required for traditional commerce (although different means may be necessary to achieve those requirements). http://www1.oecd.org/daf/fa/e_com/e_com.htm

European Union

Based on these principles, European Commissioner Frits Bolkestein claimed in a speech in Sept 2000, "We have international agreement on the principle that for consumption taxes the rules should result in taxation in the jurisdiction where consumption takes place."
http://europa.eu.int/comm/internal_market/en/speeches/spch312.htm

In a 1998 Commission communication (COM(1998)374), the EU endorsed three main principles drawn from the OECD framework.

- The first is that no new or additional taxes need be considered for e-commerce but that existing taxes – and specifically VAT - should be adapted so that they can be applied to e-commerce.
- The second principle is that, for consumption taxes, electronic deliveries should not be considered as goods. In the case of the EU VAT system, they should be treated as supplies of services.
- The third principle is that only supplies of such services consumed in Europe should be taxed in Europe (i.e., that taxation should take place in the jurisdiction where consumption takes place).

Thus, within the EU, e-commerce is to be taxed neutrally in relation to conventional trade. For VAT purposes, sales of good online are treated in the same way as any other form of distance sales (e.g., from catalogues, by phone, post, etc.). VAT will be applied at the place of consumption, subject to a number of adjustments. There are well established channels for taxing these transactions –

- goods purchased from third countries are taxed at import,
- exported goods are zero-rated, and
- intra-Community sales of goods are taxed, under a special regime for distance sales, either in the Member State of the seller or the buyer (dependent largely on the volume of such trade carried out by the seller).

Electronic transmissions, on the other hand, will be taxed as services.

However, specific rules for translating these general principles into reality have not been fully resolved. Materials on EU policy are available at <http://europa.eu.int/ISPO/ecommerce/legal/taxation.html> , including a 2000 proposal to amend Directive 77/388/EEC as regards the value added tax arrangements applicable to certain services supplied by electronic means.

United States

The US does not have a VAT, but rather has sales taxes imposed by most but not all states and by many local governments. Internet taxation issues remain unresolved in the US.

In 1998, the US adopted the Internet Tax Freedom Act "(ITFA)", which prohibited the states of the United States from imposing any tax on Internet access (unless such tax was generally imposed and actually enforced prior to October 1, 1998) or any multiple or discriminatory taxes on electronic commerce. (Congress has authority to do this under its power to regulate interstate commerce.) The ITFA's moratorium initially ran for three years, until October 2001. In

November 2001, the US Congress extended the moratorium until November 1, 2003. H.R. 1552, Public Law 107-75

The ITFA exempts Internet access services from state and local taxes, such as sales tax. In addition to Internet access, this ban extends to many Internet-based services. However, the ban on taxation of Internet access is not complete. The eight or so states that taxed Internet access prior to October 1, 1998 can continue to do so. The ITFA also prohibits multiple and discriminatory taxation of electronic commerce.

However, the ITFA does not directly affect sales of tangible products over the Internet. States can still tax intra-state e-commerce (i.e., any state can require online retailers physically located in that state to collect taxes on items sold to residents of that state). However, under the provision in the US Constitution preventing states from erecting barriers to interstate commerce, as interpreted by the Supreme Court, a state currently cannot require remote sellers (retailers, including Internet sellers, without a physical store or warehouse or other presence in that state) to collect sales tax on sales into that state. Congress could, if it wanted, set up a framework for states to collect taxes on Internet and mail order commerce. In order to provide the basis for federal action, a number of states have developed a harmonised sales tax regime, but they have failed to convince Congress to endorse it. So the moratorium remains, a compromise between those who want to permanently prohibit the states from taxing e-commerce, and those who want to allow states to tax Internet sales as soon as enough of them sign up to a broad simplification of sales taxes.

When Congress first enacted the ITFA, it created an the Advisory Commission on Electronic Commerce to develop recommendations on electronic commerce and tax policy. The Commission was not able to reach general consensus, but its report did include a series of findings and recommendations. <http://www.ecommercecommission.org>

For a background paper dated April 2000, largely from the US perspective, see http://www.internetpolicy.org/briefing/4_00_story.html

For more information, contact: James X. Dempsey, jdempsey@cdt.org