

The Federal Internet Tax Freedom Act Amendments Act of 2007 and its Effect on the New York Sales Tax and Telecommunications Excise Tax

General

The sale of *Internet access service* is not subject to the state and local sales taxes under Articles 28 and 29 of the Tax Law or to the telecommunications excise tax imposed by section 186-e of the Tax Law (see Tax Law, §§ 179 and 1115[v], and TSB-M-97(1.1)C and TSB-M-97(1.1)S).

The federal moratorium against the imposition of state and local taxes on *Internet access*, originally enacted by the 1998 Internet Tax Freedom Act (ITFA) and extended by the Internet Tax Nondiscrimination Act (ITNA), has been extended again, until November 1, 2014, under the federal Internet Tax Freedom Act Amendments Act of 2007 (Public Law 110-108) (ITFAA).

In addition, ITFAA amended the federal definition of *Internet access* for purposes of the moratorium to include certain closely related Internet communications services, such as electronic mail services and instant messaging services.

This memorandum describes how the amended federal definition of *Internet access* affects New York State and local sales taxes and the telecommunications excise tax.

Federal definition of *Internet access*

Under the new federal law *Internet access* includes:

- (A) a service that enables users to connect to the Internet to access content, information, or other services offered over the Internet;
- (B) the purchase, use, or sale of telecommunications by a provider of a service described in (A) to the extent those telecommunications are purchased, used, or sold to provide that service or to otherwise enable users to access content, information or other services offered over the Internet;
- (C) services that are incidental to the provision of the service described in (A) when furnished to users as part of that service, such as a home page, electronic mail and instant messaging (including voice- and video-capable electronic mail and instant messaging), video clips, and personal electronic storage capacity; and
- (D) a homepage, electronic mail and instant messaging (including voice- and video-capable electronic mail and instant messaging), video clips, and personal electronic storage capacity, that are provided independently or not packaged with Internet access.

Internet access does **not** include voice, audio or video programming, or other products and services (except services described in (A), (B), (C), or (D)) that utilize Internet protocol or any successor protocol and for which there is a charge that is either separately stated or aggregated with the charge for those services.

Impact of ITFAA amendments on New York State and local sales taxes and the telecommunications excise tax

As previously described, *Internet access*, for purposes of the federal moratorium, now includes the following services: home page, electronic mail, instant messaging, video clips (e.g., movie previews and portions or short clips of a complete video); and personal electronic storage capacity. These services are included in the federal moratorium regardless of whether they are furnished as part of the Internet connection service, **or if they are purchased and furnished separately**. The following examples illustrate the exempt status of *Internet access* as it applies to New York State and local sales taxes and the telecommunications excise tax.

Example: Customer A purchases high-speed Internet access service from Company X. In addition to the Internet connection, this service includes the provision of electronic mail services, instant messaging and access to video clips. All of these services constitute Internet access that is covered by the federal moratorium and therefore, they are not subject to New York State and local sales taxes or to the telecommunications excise tax.

*Example: Customer B purchases high-speed Internet access service from Company Y. In addition to the Internet connection, this service includes the provision of electronic mail services, instant messaging and access to video clips. Customer B also purchases a **separate** electronic mail service and an instant messaging service from Company T. All of these services purchased by Customer B constitute Internet access that is covered by the federal moratorium and therefore, they are not subject to New York State and local sales taxes, or to the telecommunications excise tax.*

However, any form of telephony (e.g., private telecommunications networks), including Voice over Internet Protocol (VOIP), network services and data transmission services, other than telecommunications services used by an Internet Service Provider (ISP) to connect customers to the Internet, **are not** included under the federal moratorium. Accordingly, these forms of telephony continue to be subject to New York State and local sales taxes and the telecommunications excise tax.

Grandfather provisions

ITFAA also amended the grandfather provisions of the Internet Tax Freedom Act of 1998 (ITFA) for taxes on *Internet access*. These grandfather provisions, which were extended by ITNA, allowed, under certain conditions, state and local taxes to continue to be imposed on services that are otherwise covered by the ITFA moratorium. Under ITFAA, the four-year grandfather provision

of ITNA was extended to November 1, 2014 (the date on which the federal moratorium will expire). In addition, this provision now applies to *Internet access* as originally defined by the Internet Tax Freedom Act enacted on October 21, 1998. This definition generally included only the charges by the ISP to its customer. However, these charges were expressly **exempted** from sales tax by Tax Law section 1115(v) and from the telecommunications excise tax by Tax Law section 179. Furthermore, prior to enactment of section 1115(v), charges for *Internet access services* were not subject to New York's sales or telecommunications excise taxes as a matter of administrative interpretation. (See TSB-M-97(1)S issued January 24, 1997). Therefore, the extended new seven-year grandfather provision has no effect for sales and telecommunications excise tax purposes.

ITFAA also amended the application of the two-year grandfather provision enacted by ITNA. This provision now applies to the definition of *Internet access* as amended by ITNA, which includes telecommunications services *to the extent that such services are purchased, used, or sold by a provider of Internet access to provide Internet access*. Since these services were previously exempt from state and local sales taxes, this new provision has no effect on those taxes. (See TSB-M-07(2)S, issued April 2, 2007.)

However, the ITFAA amendments, as added by section 1104(c)(2) of IFTA, **do affect** New York State's telecommunications excise tax. Under the ITFAA amendments, telecommunications services purchased, used or sold by ISPs to provide Internet access will continue to be subject to New York State's excise tax until June 30, 2008. Beginning July 1, 2008, telecommunications services as described in the preceding sentence do fall under the federal moratorium and, as of that date, will no longer be subject to New York's excise tax. However, as previously stated in this memorandum, telephony such as VOIP is not covered by the federal moratorium. See NYT-G-07(2)C, NYT-G-07(3)S, *Taxation of Internet Telephony*, for more information on the application of state and local sales tax and telecommunications excise tax to the sale of VOIP.

The Internet Tax Freedom Act and its subsequent amendments have no effect on the state and local sales tax treatment of goods or services sold and purchased over the Internet.

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