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To the Congress of the United States:

When Congress established the Commission, it decided to include representatives of a wide variety of groups – setting the bar very high for achieving supermajority support on the Commission for making formal “recommendations” to Congress.

With that in mind, I am pleased that there was in fact so much consensus on critical matters before the Commission, although, like others, I am disappointed that strong and serious efforts at negotiation from Commissioners representing the business community – even extending beyond our last formal meeting in Dallas – were unable to garner the additional votes necessary to reach a supermajority consensus.

Most important, however, eleven Commissioners agreed on a solid package of proposals which, if adopted by Congress and the States, would provide a fair and sensible way of addressing critical issues regarding Internet taxation. This report and the views of other Commissioners have highlighted these proposals, and there is no need to repeat them all here.

It is appropriate, though, to elaborate somewhat on the ideas behind these proposals. In developing them, we have been motivated by the Hippocratic imperative: “first, do no harm.” Many Commissioners and other observers are legitimately troubled by the appearance of different rules for the sale of the same good and believe that this system is not sustainable. Others note that tax burdens on different types of sellers must be equal for a tax system to be truly equitable. Clearly, any new system must not disproportionately burden any type of seller. Therefore, we recommend a process under which each State provides a clear and accountable measure of whether an increased tax burden would be established by the collection of taxes on remote sales. This is one reason why we believe so strongly that simplification of tax systems must be a prerequisite for any expanded collection duties.

Despite the dramatic growth of e-commerce, particularly business-to-business e-commerce, it is still early days. The Commerce Department reported that in the fourth quarter of 1999, Internet sales amounted to only 0.64% of total retail sales of \$821.2 billion.<sup>1</sup> Because it is so difficult to predict the future of e-commerce with clarity at this point – and because of the overriding imperative not to take action at this time that would hinder the development of e-commerce – it is likewise difficult to ascertain the wisdom of expanded collection duties without any definitive information on the impact on the economy.

The majority proposal, then, permits the Nation to assess, after a period necessary to adopt tax simplification and other desirable reforms, whether it is possible or wise to

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<sup>1</sup> “Retail E-Commerce Sales for the Fourth Quarter 1999 Reach \$5.3 Billion, Census Bureau Reports,” U.S. Department of Commerce News, March 2, 2000; <http://www.census.gov/Press-Release/www/2000/cb00-40.html>.

achieve equality of tax rates and tax burdens without danger to the general economy or to the growth of electronic commerce.

On a personal note, I am pleased that over the course of the Commission's work, it has spent so much effort addressing factors that contribute to the "digital divide." One such factor is excessive taxation on telecommunications services. According to one study, a consumer's purchase of telecommunications services is subject to a nationwide average effective rate of taxation of 18% (including Federal, State, and local taxes).<sup>2</sup> Nineteen States have local telecommunications transactions tax rates greater than 10%; ten States have State telecommunications transactions tax rates greater than 10%. Ten States have combined State and local telecommunications tax rates greater than 20%. Taxation at this level cries out for reform. High telecom taxation widens the digital divide.

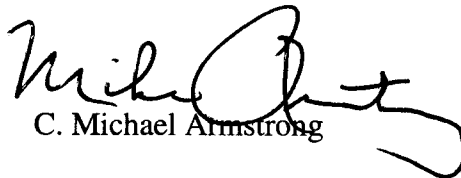
The National Governors' Association and the National Conference of State Legislatures have recognized the need to reform taxes on telecommunications and have worked cooperatively with the telecommunications industry. To take AT&T as an example, the Company files over 99,000 State and local tax returns each year. This places an unnecessary burden on businesses in complying with antiquated and complex taxing statutes. Lessening this burden will reduce the barriers to entry in providing telecommunications services and increase competition in the industry. AT&T looks forward to continuing cooperative efforts to reform the telecommunications tax structure.

The 3% Federal excise tax on telecommunications, a "tax on talking" that dates back to the Spanish-American war when telephones were a luxury item, is also – and very importantly – effectively a tax on accessing the Internet. Repealing this tax will help to bridge the digital divide and also encourage the greatest possible use of the Internet, including its e-commerce applications.

Reform of the telecommunications tax system at all levels would benefit primarily not telecommunications companies, but instead the American consumers who bear these taxes. It would enable telecommunications companies throughout the Nation to fulfill their mission of bringing low-cost services to all Americans.

I commend the majority report to your deliberations and thank you, with particular thanks to the Senate Democratic leader, for the honor of having served on the Commission.

Respectfully,

  
C. Michael Armstrong

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<sup>2</sup> Committee on State Taxation ("COST") study presented to the Advisory Commission on Electronic Commerce, September 14, 1999.