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**Resales, Exemptions and Bundled  
Transactions: An Update on Current Sales  
Tax Issues for the Telecommunications  
Industry**

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# DEFINITION

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- Telecommunications services include such things as telephone and telegraph services, mobile telecommunication devices, the internet, and other similar services. In the majority of instances, telecommunications services also include sales taxation.



# IMPOSITION

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- All but a handful of the states with broad-based sales taxes impose sales taxes on telecommunications services.
- While the imposition of a sales tax on telecommunications services is an exception to the general rule that state sales taxes are limited to sales of tangible personal property, it is consistent with the widespread exception to that rule for utility services.



# Who Imposes Telecommunication Taxes?

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- Internal Revenue Service
- State & Local Departments of Revenue
- Federal Communications Commission
- State Public Utility
- Public Service Commissions



# Taxes Imposed on Telecommunications Services

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- States have found ways to uniquely deal with the intangible nature of telecommunications services in order to apply a services-related tax. Often referred to as:
  - Sales Tax
  - Excise Tax
  - Use Tax
  - Services Tax
  - Gross Receipts Tax
- Regardless of the name, the practical result is a sales tax.



# RESALES

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- Tax generally does not apply to sale of telecommunications services for resale.
- Sale of telecommunications service to provider of information services or other enhanced services may not be excluded sales for resale.



# RESALES

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- Maintenance of resale certificates prerequisite for exclusion from tax.
- Resale certificate requirements vary by jurisdiction and within jurisdictions.



# RESALES

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- Spirit of law is to tax product one time on sale to the end-user, presumably at highest value of transaction.
- Sale of telecommunications service to provider of information services or other enhanced services may not be excluded sales for resale.





# RESALES: Certificates

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- Contributions are due on end-user revenue, not resale revenue.
- The FCC has recently imposed a heavy amount of paperwork and compliance obligations for providers reporting resale revenue
  - Must collect & retain annual customer certifications
  - Must have documented procedures



# RESALES: Certificates

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Mass. Regs. Code 64H.1.6(6)(d):

- Any vendor that purchases telecommunications services for resale must provide its wholesale vendor with a resale certificate (Form ST-4) and must collect tax from its retail customers on the sales price that it charges those retail customers for the telecommunications services.
- If a purchaser that has given a resale certificate to its wholesale telecommunications vendor itself consumes some of the telecommunications services that it purchased tax free under the resale certificate, it must file use tax returns and pay tax on the sales price of the telecommunications that it consumes.



# RESALES: Statutes

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- "Retail sale of prepaid wireless telecommunications service" means a sale of prepaid wireless telecommunications service by a seller for any purpose other than resale. Ariz. Rev. Stat. Ann. § 42-5401.
- "Prepaid retail transaction" means the purchase of prepaid wireless telecommunications service from a seller for any purpose other than resale. Ala. Code § 11-98-5.3(a)(2).



# RESALES: Statutes

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- “Retail transaction” means a purchase of prepaid wireless telecommunications service from a seller for any purpose other than resale. Conn. Gen. Stat. § 28-30b(5).
- “Retail transaction” means the purchase of prepaid wireless telecommunications service from a seller for any purpose other than resale. Del. Code Ann. § 10110(5).
- “Retail transaction” means the purchase of prepaid wireless telecommunications service from a seller for any purpose other than resale. D.C. Code Ann. § 34-1801(7A).



# RESALES: Cases

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## *Sprint Communications Co. v. Finance and Administration Cabinet Dept. of Revenue*

- Issue: Whether Sprint's communications services ("access services") were exempt from sales and use tax because they were sold for resale.
- Analysis: A KY regulation was enacted in 2001 that stated switch access services could not be exempted as for resale. 103 KAR 28:140. In 2005, KY statute was amended so that tax was **not** imposed upon switch access revenues.
- Holding: The court was bound by the 2001 regulation because the taxpayer did not show the 2001 regulation detracted from the taxing statutes at the time.



# RESALES: Cases

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*In the Matter of Securities Industry Automation Corp.*

- Issue: Whether the Per End User Fee is exempt from New York City Utility Tax (UT) as a sale for resale.
- Analysis: The taxpayer argued that Service Providers purchased SFTI access from it and then resold that access to Third-Party Users. As a result, Taxpayer charged the Per End User Fee as a privilege of reselling SFTI.
- Holding: The Per End User Fee is not exempt, because the Fee does not constitute a sale of SFTI access. The Fee is based only on the number of users, not their actual consumption.



# EXEMPTIONS

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Exemptions vary by jurisdictions and within jurisdictions by tax type.

- Common Exempt Customers:
  - Federal Government
  - State/Local Government
  - Private Nonprofit Charitable, Educational, or Religious Organization
  - Disabled veterans
  - Foreign Diplomats
- Common Exempt Categories:
  - Data Center and Equipment
  - Resale
  - Residential



# EXEMPTIONS: Equipment

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*Southwestern Bell Tel. Co. v. Dir. of Revenue*, 78 S.W.3d 763 (Mo. 2002)

- Facts: Bell filed claims for refund of use tax on purchases of machinery and equipment used in transmitting and processing information required for telephone communications and services.
- Issue: Whether the machinery and equipment are used directly in manufacturing a product that is intended to be sold ultimately for final use or consumption, within Section 144.030.2.
- Holding: Telephone services constitute the “manufacturing” of “products”.





# EXEMPTIONS: Equipment

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Ariz. Rev. Stat. Ann. §42-5061(B)(3):

- There is an exemption from transaction privilege (sales) tax and use tax for the following TPP sold to persons engaged in telecommunications businesses including (effective January 1, 2015) a person representing or working on behalf of such a person in a manner described in Ariz. Rev. Stat. Ann. §42-5075(O)), and consisting of:
  - central office switching equipment;
  - switchboards;
  - private branch exchange equipment;
  - microwave radio equipment; and
  - carrier equipment including optical fiber, coaxial cable and other transmission media.



# EXEMPTIONS: Equipment

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- Colorado FYI Sales 94 (3/01/2015): A broadband provider can claim a sales and use tax refund for equipment used in providing broadband service in a rural area. Claims for the 2014 calendar year must be received by April 1, 2015.
- Missouri Mo Sec 144.810: Effective August 28, 2015, a state and local sales and use tax exemption is provided for all machinery, equipment, computers, electrical energy, gas, water and other utilities, including telecommunication and internet services, used in new or expanded data storage center facilities. An application is required.



# EXEMPTIONS: Equipment

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- North Dakota: H.B. 1089, Laws 2015, effective retroactively and applicable to taxable events occurring after December 31, 2014, and effective through December 31, 2020. Enterprise information technology equipment and computer software purchased for use in a qualified data center are exempt from North Dakota sales tax. The exemption includes upgraded or replacement enterprise information technology equipment and computer software purchased for use in a qualified data center. An application is required.



# EXEMPTIONS: Equipment

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- Illinois Admin. Hearing TC-15-01 (1/6/2015): ALJ for IL Dep't of Rev. ruled that a telecommunications retailer's credit request for telecommunication excise tax and fees was properly denied, finding the department is precluded from issuing a credit or refund for erroneous payments made before January 1, 2003, under the general SOL. As the taxpayer did not keep accurate records, they were not able to refute the state's assertions.



# BUNDLED TRANSACTIONS

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- Selling taxable and non-taxable in a combined package
- Combines the purchase of two separate types of property –
  - Tangible: equipment
  - Intangible: services



# BUNDLED TRANSACTIONS

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- Priced in a variety of ways
  - Lump sum amount
    - Representing a single value for both components
  - Separately assigned prices
    - Each component's fair market value



# BUNDLED TRANSACTIONS

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- To address the treatment of bundled transactions, taxpayers may:
  - Rely on books and records exceptions
  - Request a letter ruling or administratively issued guidance
  - Rely upon legislation



# BUNDLED TRANSACTIONS

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Mobile Telecommunications Sourcing Act, amending 4 USC 123:

- If a taxing jurisdiction does not otherwise subject charges for mobile telecommunications services to taxation and if these charges are aggregated with and not separately stated from charges that are subject to taxation, then the charges for nontaxable mobile telecommunications services may be subject to taxation unless the home service provider can reasonably identify charges not subject to such tax, charge, or fee from its books and records.
- If a taxing jurisdiction does not subject charges for mobile telecommunications services to taxation, a customer may not rely upon the nontaxability of charges for mobile telecommunications services unless the customer's home service provider separately states the charges for nontaxable mobile telecommunications services from taxable charges or the home service provider elects, after receiving a written request from the customer in the form required by the provider, to provide verifiable data based upon the home service provider's books and records that are kept in the regular course of business that reasonably identifies the nontaxable charges.





# BUNDLED TRANSACTIONS: Computing Receipts

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Ark. Regs. GR-7:

- In the case of a bundled transaction that includes a telecommunications service, the following rules will apply:
  1. If the price is attributable to products that are taxable and products that are nontaxable, the portion of the price attributable to the nontaxable products is also subject to tax unless the provider can identify, by reasonable and verifiable standards, the portion of the products that are nontaxable from its books and records.
  2. If the price is attributable to products that are subject to tax at different tax rates, the total price is attributable to the products subject to the highest tax rate unless the provider can identify, by reasonable and verifiable standards, the portion of the price attributable to the products subject to the lower tax rate from its books and records.



# BUNDLED TRANSACTIONS: Computing Receipts

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Cal. Code Regs. 1585(b)(3):

- Tax applies to the gross receipts from the retail sale of a wireless telecommunication device sold in a bundled transaction, measured by the unbundled sales price of that device.
- Tax applies to the unbundled sales price whether the wireless telecommunication device and utility service are sold for a single price or are separately itemized.
- Tax does not apply to charges in excess of the unbundled sales price made for telecommunications services.



# BUNDLED TRANSACTIONS: Computing Receipts

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Colo. Code Regs. 1 CCR 201-3:

- Gross receipts attributable to the sale of a telecommunication or ancillary service sold as part of a bundled transaction are in this state when such gross receipts would be this state in accordance with the provisions of sections Colo. Code Regs. 1 CCR 201-3(d)(i) through (vii).



# BUNDLED TRANSACTIONS: Computing Receipts

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Colo. Code Regs. 1 CCR 201-3(d)(viii)(1):

- The amount of gross receipts attributable to the sale of a telecommunication service sold as part of a bundled transaction is equal to the price charged for the service when sold separately, adjusted by an amount equal to the quotient of:
  - a) the difference between:
    - 1) the price charged by the taxpayer for the bundled transaction, and
    - 2) the sum of the prices charged by the taxpayer for each of the included products when sold separately, and
  - b) the number of products included in the bundled transaction.



# BUNDLED TRANSACTIONS

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*People v. Sprint Nextel Corp.*, 26 N.Y.3d 98 (N.Y. 2015)

- Facts: Sprint unbundled the portion of the fixed monthly charge it attributed to intrastate mobile services and did not collect taxes on the interstate or international calls.
- Issue: Whether Sprint knowingly violated Tax Law by failing to collect sales tax on the portion of the flat-rate charge that was attributable to interstate and international voice services.
- Holding: All of Sprint's receipts from the sales of interstate voice service were subject to sales tax.

# IMPLEMENTATION:

## What To Look For

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1. Always have legal support and understand the strength of support
2. Implementation costs can add up quickly
3. Develop a short-term and long-term risk profile
4. Explain the risk profile and inherent assumptions to parties providing opinions and decision makers
5. Avoid promising decision makers certainty of results



# Questions?

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