

To: Compliance Review and Interpretations Committee

From: Scott Peterson and Pam Cook

Re: Preliminary report on 2009 Annual Recertification

Date: 9/24/09

Arkansas (no 30 day rule for rate changes)

No issues.

Indiana (no 30 day rule for rate changes)

The statutes do not contain a provision relieving sellers and CSPs from liability for errors in the taxability Matrix (section 328) or rate information (section 306).

State response: The state has drafted legislation that addresses the relief for errors in the taxability matrix issue. Indiana has no local taxes so there is no need for relief for errors in rates, boundaries, or taxing jurisdiction assignments as there are no databases.

The statute cited for the rounding rule give a bracket system.

State response: The draft legislation addresses this.

There is no rule regarding taxation of digital codes nor is there a definition.

State response: The draft legislation addresses this.

Telecommunications nonrecurring charges are exempt according to the taxability matrix, but services necessary to complete the sale are not. The statute does not define or specifically exempt telecommunications nonrecurring charges.

State response: The draft legislation addresses this.

Dietary supplements are excluded from the exemption for food and food ingredients but not excluded from the definition.

State response: The draft legislation addresses this.

The taxability matrix indicates that mobility enhancing equipment is exempt but the statute does not list it in the medical equipment and supplies exemption.

State response: The draft legislation addresses this.

Iowa (no 30 day rule for rate changes)

Bundling language is still in sales price definition.

State response: Department of Revenue has a proposed amendment to strike for 2010 session.

Rule 701-18.20(7)(d)(3) includes one-way paging as a non-taxable service. The definition of paging includes one-way and two way paging. Since “paging” is a defined product, it has to be either all taxable or all non-taxable.

The taxability matrix indicates that optional maintenance contracts for non-prewritten software which include updates which are not delivered electronically are taxable. The statute and rules do not specifically address such contracts. The rules only address canned software contracts and the statute (423.2(1)(a)(4)) taxes “sales of optional service or warranty contracts, except residential service contracts regulated under chapter 523C, which provide for the furnishing of labor and materials and require the furnishing of any taxable service enumerated under this section. The sales price is subject to tax even if some of the services furnished are not enumerated under this section.” Is it assumed that materials are provided with custom software updates?

Kansas

No issues.

Kentucky (no 30 day rule for rate changes)

Digital products are sourced to place of primary use. The Agreement sources such transactions under section 310.

State response: As part of the adoption of digital property definitions in 2009, Kentucky also adopted the definition of “transferred electronically” which means accessed or obtained by the purchaser by means other than tangible storage media. This definition is based upon Rule 332.2 B.4. This rule elaborates further that “it is not necessary that a copy of the product be physically transferred to the purchaser. So long as the purchaser may access the product, it will be considered to have been electronically transferred to the purchaser. The term “transferred electronically” has a broader meaning than the term “delivered electronically” used in the computer related definitions.” This concept of accessing by means other than tangible storage media beyond an electronic download is not included within the current sourcing scheme of Section 310. With this definition in mind, Kentucky adopted a placeholder provision to accomplish the intent of our legislation until Section 310 can be appropriately updated. We would appreciate any further guidance on how to properly clarify our sourcing provisions within the Agreement requirements.

Staff response: Section 309 paragraph A provides that “Each member state shall agree to require sellers to source the retail sale of a product in accordance with Section 310. The provisions of Section 310 apply regardless of the characterization of a product as tangible personal property, a digital good, or a service.”

The provision for when a cause of action against a seller accrues does not specify that the notification to the seller has to be in writing.

The state exempts “rate increases” for the school tax and any other taxes and surcharges relating to telecommunications service. The school tax and many of the other charges are imposed on the provider of the service and the definition of sales price includes them. Sales price only excludes such charges if they are imposed directly on the consumer.

State response: Below is further comment regarding the exemption in KRS 139.470(9) for certain charges for residential telecommunications service. We have not regarded this exemption as a change to the definition of sales price, but an exemption as it relates to specific telecom charges.

- This provision has been in KY code since 1979 and was not amended in our initial conforming bill back in 2003. Even though the sales price definition has been amended subsequently, we do not believe these amendments have substantively changed the sales price requirements regarding our provision for residential telecom services.
- In 2007 we amended the statute to include the SST definition of residential telecommunications service. We use this definition in the exemption according to the provisions of Sections 316 and 327.
- Nothing in Sections 316 or 327 seems to prohibit this type of exemption affecting a residential telecom bill. There are no definitions used in this provision that are contrary to established SST terms.
- We agree that the sales price definition explicitly excludes any taxes legally imposed directly on the consumer that are separately stated on the invoice, bill of sale or similar document given to the purchaser. However, the definition of sales price does not include a definition for the terms within our statute (any rate increase for school taxes and any other charges or surcharges added to the total for residential telecom). It is correct that the exemption in question takes out of the computation of tax what is routinely part of sales price. However, any exemption from sales tax affects the treatment of sales price for the transactions affected.

Staff response: This issue needs further discussion. Such charges are not defined in the telecommunications definitions and therefore cannot be exempted as a telecommunications service. If these items represent an “other expense of the seller” under B. of the sales price definition, can they be excluded from the sales price?

Michigan (no 30 day rule for rate changes)

The statute for taxing interstate telecommunications service excludes one-way paging service. Paging service is defined in the Agreement and includes both one-way and two-way service. It should be all taxable or all exempt.

The bundling definition and rules only apply to telecommunications services. In its response last year the state said there was no need for bundling definitions and rules for other transactions. However, the de minimis rule should apply as would the food and drug, etc. provision (food and food ingredients and certain medical items including drugs are exempt). Also, mobile wireless services are specifically taxed in a separate section of the statute, but the provision for transactions including telecommunications service, Internet access, ancillary service or video or audio programming service is in another section of the statute which appears to only apply to other types of telecommunications service.

As noted in their recertification letter, the state does not have a provision allowing sellers and CSPs 10 days to correct errors as provided in section 502E.

Minnesota (no 30 day rule for rate changes-proposed 2010 legislation)

The taxability matrix indicates that digital audio works are not taxable in general but that ringtones are. Digital audio works is a product definition that includes ringtones. Ringtones is defined “for purposes of the definition of “digital audio works”” and is not set out as a separate definition that can be treated as a product definition. No change was made in the 2009 session. Unless there is a special session, they will be out of compliance on 1/1/2010.

Nebraska

Nebraska taxes all computer software. Could not find the definition for computer software in the statute cited as it was the imposition statute. The definition in Reg. 1-088 is not the Agreement definition (does not conflict with it though).

The rule cited on the taxability matrix for various telecommunications services is out of date and uses terms not in the Agreement. It also indicates that certain fees and surcharges are excluded from the tax which is in conflict with the definition of “sales price” which only excludes such charges if they are imposed directly on the purchaser and not the seller.

State response: Until Nebraska expands its sales tax base from the more narrow “telephone communications services” to cover the broader “telecommunications services”, the terminology will not match up exactly with the Agreement language. The last sentence of Regulation 1-065.02 indicates that taxes and surcharges imposed on the purchaser are not included in the tax base. Regulation 1-007.01S indicates that sales tax applies to the seller’s cost of materials, and “any other expense”. Therefore, taxes, fees, and surcharges imposed on the

seller are included in the sales price. We have historically not taxed fees and surcharges which are collected concurrently with the sales tax from the customer. While we do not use the exact wording found in the "Sales Price" definition, the effect is the same.

Staff response: According to your statute, Nebraska does tax intrastate telecommunications service as defined in the Agreement. There is no definition for telephone communication service in the Agreement.

77-2701.16 Gross receipts, defined. (1) Gross receipts means the total amount of the sale or lease or rental price, as the case may be, of the retail sales of retailers.

(a)(i) In the furnishing of telephone communication service, other than mobile telecommunications service as described in section 77-2703.04, the gross income received from furnishing ancillary services, except for conference bridging services, and intrastate telecommunications services, except for value-added, nonvoice data service;

With respect to the fees and surcharge issue, are the surcharges for the hearing impaired and the universal service fund imposed on the customer? They are usually imposed on the provider who is permitted to pass them on to the customer. (See staff response to Kentucky on this issue.)

Nevada

The state has not fully implemented ACH credit payments.

State response: The state is in the process of completing (within two months) the full implementation of ACH credit.

New Jersey (no 30 day rule for rate changes)

The statute taxes "digital products" which it defines as "electronically delivered music, ringtones, movies, books, audio and video works and similar products, where the customer is granted a right or license to use, retain or make a copy of such item." These are all included in the definitions of specified digital products but the definitions are not used. The Taxability Matrix indicates that they tax other products delivered electronically.

North Carolina (no 30 day rule for rate changes, but did comment that provided relief in this situation in 2007)

The statute defines prepaid telephone calling service to include prepaid wireline calling service and prepaid wireless calling service. There is no definition for prepaid calling service (which includes both wireline and wireless service) and prepaid wireline calling service is not a defined term.

The statute exempts pay telephone service but does not define it. There is a definition in the Agreement.

The statute cited for providing relief from liability from errors in the taxability matrix for sellers and CSPs (section 328) and purchasers (section 331) only relates to errors in information on rates, boundaries and taxing jurisdiction assignments. There is no provision for errors in the taxability matrix.

North Dakota

It was noted in last year's review that there was no definition of prepaid calling service. The state indicated that the rules would be updated to include the definition. This has not been done yet. The recertification letter states that an updated rule is being drafted and is expected to go into effect by January 1, 2010.

The state taxes communication service which is defined to include telecommunications service. Under the statute one-way communication services are not taxable. Paging services are a defined product under telecommunications service and there are one-way and two-way paging services. They would have to be all taxable or all exempt.

Oklahoma (no 30 day rule for rate changes)

There is no provision for sourcing of ancillary services.

State response: The state was unaware that this was missed. An emergency rule was adopted on 9/10/2010.

The rule for telecommunications services excludes from taxation "Regulatory assessments and charges, including charges to fund the Oklahoma Universal Service Fund, the Oklahoma Lifeline Fund and the Oklahoma High Cost Fund ". If these charges are imposed on the telecommunications provider and not the purchaser, this provision is not in compliance with the definition of "sales price."

State response: This issue was discussed with the telecommunications industry when we adopted the telecommunications services definitions when required under the Agreement. Under our old law, the regulatory assessments and charges were not considered telecommunications services. The new definition required us to bring them into the levy. To avoid a new tax on consumers, it was understood that it was permissible to include the charges in our list of telecommunications services that are exempted from the tax.

Staff response: This issue needs further discussion. Such charges are not defined in the telecommunications definitions and therefore cannot be exempted as a telecommunications

service. If these items represent an “other expense of the seller” under B. of the sales price definition, can they be excluded from the sales price?

Rhode Island (no 30 day rule for rate changes)

It was noted in last year’s review that there was no provision for sourcing of ancillary services. CRIC was told that a rule would be promulgated. The state indicated in its recertification letter that they are now in the process of promulgating a rule which should be complete by early fall.

State response: A draft of the rule that is being promulgated was provided.

The taxability matrix indicates that telecommunications nonrecurring charges are not taxable and refers to the statute excluding installation from the definition of sales price. The Agreement requires telecommunications nonrecurring charges to be separately defined and excluded from the sales price definition when services necessary to complete the sale are included in the sales price.

State response: The response to Telecommunication nonrecurring charges incorrectly indicated that such charges were excluded from sales price. This has been corrected to state that these charges are included in sales price.

South Dakota (no 30 day rule for rate changes)

The taxability matrix indicates that transportation, shipping and similar charges for direct mail are not taxable but the code section cited only refers to postage.

The statute specifically taxes ancillary services. The state failed to define conference bridging services when they moved their definitions from the rule to the statutes.

State response: This will be done next session.

Tennessee (no 30 day rule for rate changes)

The effective date for the conforming provisions for the following sections of the Agreement was changed from 7/1/09 to 7/1/11:

Section 302 State and local tax base

Section 305 Local rate and boundary change

Section 308 State and local tax rates

Section 310 General sourcing rules

Section 311 General sourcing definitions

Section 313 Direct mail sourcing

Section 314 Telecom sourcing rule – for prepaid calling service and prepaid wireless calling service

Section 317 Administration of exemptions – drop shipments

Section 318 Uniform tax returns – only allows use of simplified returns if no location in TN

Section 322 Sales tax holidays – bundling provision

Section 323 Caps and thresholds

Section 330 Bundled transactions

Definitions – Bundled transactions

Vermont (no 30 day rule for rate changes, but state indicates will comply)

On the Certificate of Compliance, the response in section 310.1, Election for Origin-Based Sourcing still indicates “yes”. The statute provides for destination sourcing.

Under section 314, a regulation is cited for sourcing prepaid wireless calling service, but the current regulation does not address it. This was an issue last year and the state has indicated that a regulation is being promulgated.

Under section 314, the regulation cited for sourcing ancillary services defines “receive” and “receipt”. It does not address ancillary services. No other regulation sourcing ancillary services was identified.

The regulation section cited for treatment of software maintenance contracts deals with bundles including telecommunications services, ancillary services, Internet access or audio or video programming services. The bundling regulations do not address software maintenance contracts.

Is the reference to “direct mail charges” in the statutory definition of delivery charges referring to charges for direct mail service itself or to charges for direct mail delivery? The definition of delivery charges includes the following: Direct mail charges that are separately stated on an invoice or similar billing document given to the purchaser are excluded from the definition of “delivery charges”. The Taxability Matrix indicates direct mail delivery charges are taxable.

Washington

The statute sourcing prepaid calling and prepaid wireless calling services only refers to prepaid calling service in the rules for receipt at seller's place of business and for receipt at the location delivered to the customer.

State response: We understand your comments regarding prepaid wireless calling services. The term was inadvertently left out of portions of our telecom sourcing statute when it was enacted in 2007. That is, RCW 82.32.520(3)(c) clearly provides:

(c) A sale of **prepaid calling service** or a sale of a **prepaid wireless calling service** is sourced as follows:..[.]

However, two of the subsequent statutory sourcing rules explicitly reference "prepaid calling service" but not "prepaid wireless calling service":

(i) When a **prepaid calling service** is received by the purchaser at a business location of the seller, the sale is sourced to that business location;

(ii) When a **prepaid calling service** is not received by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser or the purchaser's donee, designated as such by the purchaser, occurs, including the location indicated by instructions for delivery to the purchaser or donee, known to the seller;

We intend to propose legislation that would put the term into RCW 82.32.520(3)(c)(i) and (ii). That said, RCW 82.32.520(3)(c) already provides that sourcing rules (i) - (ii) apply to both prepaid calling services and prepaid wireless calling services consistent with existing SSUTA rules for prepaid wireless. We apply the language in that manner.

The statute excludes local service from the tax on telecommunications service. Local service is defined to mean ancillary service and telecommunications service excluding toll service. The taxability matrix shows all telecommunications services as being taxable other than local service and coin operated telephone serviced. The Agreement does not define toll service. Other than the services traditionally thought of as toll service, telecommunications service includes local private communications service, prepaid calling service, prepaid wireless calling service, mobile wireless service, fixed wireless service, paging service and value-added non-voice data service. Are all these included in the definition of local service?

State response: Regarding the exemption for local service, we view the exemption to be compliant with the Agreement. The last sentence in the Telecommunications section of Part II of the Library of Definitions provides:

A member state that specifically imposes tax on, or exempts from tax, local telephone or local telecommunications service may define "local service" in any manner in accordance with section 327 of the Agreement, except as limited by other sections of this Agreement.

We view our treatment of local service to be in accord with section 327. That section provides in part:

Except as specifically provided in Sections 316 and 332 and the Library of Definitions, a member state shall impose a sales or use tax on all products or services included within each Part II or Part III(B) definition or exempt from sales or use tax all products or services within each such definition.

In turn, section 316(C)(3) provides:

A member state may enact an entity-based exemption for an item if Part II of the Library of Definitions does not have a definition for such item but has a definition for a product that includes such item.

The Agreement gives great latitude to states in how to define local service and also allows states to provide entity-based exemptions for items within a defined product category. The Washington definition of local service requires that it be "provided to an individual subscribing to a residential class of telephone service" so the exemption provided is based on entity. See *RCW 82.08.028*. It might have been incorrect to include the local service exemption in the Taxability Matrix since that is focused on product taxability. However, it does alert sellers to the exemption.

For some background, I have enclosed an Excise Tax Advisory (ETA) dealing with the comparable sales tax exemption from network telephone service, the term we formerly used for what is now telecommunications service. The ETA needs to be updated to reflect our adoption of SSUTA telecommunications terms now codified in statute.

Regarding your question about "local private communications service, prepaid calling service, prepaid wireless calling service, mobile wireless service, fixed wireless service, paging service and value-added non-voice data service", these items would not fall under local service because they are not tariffed services provided to an individual subscribing to a residential class of service.

West Virginia (no 30 day rule for rate changes)

Statutes providing relief from liability for sellers and CSPs relying on incorrect information on rates, boundaries and taxing jurisdictions limits the relief to sellers and CSPs that are registered under the Agreement. This was an issue last year and the state indicated that the statute would be changed.

The Certificate of Compliance cites the same section of the statute for relief from liability for relying on erroneous information in the taxability matrix. The section does not include the taxability matrix.

Both the Certificate of Compliance and the taxability matrix do not contain information on statute references in several instances. For example, no statute is given for section 331 purchaser relief from liability. After reviewing the statutes, the provision was found. There were also several other errors in statute references given. In addition, there is an error in the taxability matrix where interstate prepaid calling service is marked taxable. This should have been interstate prepaid wireless service. Prepaid calling service is not taxable.

The statute does not define “delivered electronically”. Instead it defines “delivered” using the definition in the Agreement for “delivered electronically”.

Wisconsin (By law, rate changes have to provide 30 day notice)

No issues

Wyoming (By law, rate changes have to provide 60 day notice)

There is no provision for sourcing of ancillary services. The statute given on the certificate of compliance is for sourcing of telecommunications service.

State response: All telecommunications services and ancillary services are sourced to the primary place of use. We do not tax interstate telecommunications so by default the primary place of use is implied.

Staff response: The definition of “telecommunications service” excludes ancillary services. Sourcing for ancillary services needs to be specifically provided in the statute or rules.

The statute cited for sourcing of prepaid wireless calling service only addresses prepaid calling service. There is no provision for sourcing prepaid wireless calling service.

State response: The state taxes both prepaid calling services and wireless calling services as we do tpp. It is not specifically stated for Prepaid Wireless but only makes sense that it would follow our sourcing under section 310. We will add it directly to the telecom sourcing if that is necessary but it does comply with the intent of the law.

Staff response: Sourcing for prepaid wireless calling service needs to be added to the statute or rules.

The taxability matrix shows delivery charges for transportation, shipping, postage and similar charges and for direct mail as not included in the definition of sales price. The definitions for sales price and delivery charges in the statutes include such items.

State response: Delivery charges are included in sales price but are specifically exempted as a transportation charge as long as it is separately stated. The matrix is correct.

The state currently taxes specified digital products as TPP. Effective 1/1/2010, the statutes define specified digital products and the individual products under that category. There is no new statute specifically taxing them however. To continue taxing them would mean they are being taxed as TPP absent a law change.

State Response: Specified Digital Products are currently taxed as TPP but once the definition is valid they will be specifically excluded from taxation until the legislature decides whether they want to tax them or not. This was done to force action on their part.

The taxability matrix shows intrastate paging as not taxable and has a comment that paging is not included in the definition of taxable communication service. The statute taxes intrastate telecommunications service and paging is included in the definition of telecommunications service in the Agreement.

State response: Wyoming specifically exempts them under 39-15-105(a)(viii)(K).

Staff response: The statute exempts sale of the service of transmitting radio waves to a one-way paging unit. The definition of paging in the Agreement includes both one-way and two-way paging. The state would need to either exempt all paging or tax all paging.