Cite as Det. No. 92-273, 12 WTD 243 (1993).

BEFORE THE INTERPRETATION AND APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In The Matter of the Petition For Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 92-273
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .

[1] RULE 245, RCW 82.04.065: B&O TAX--RETAIL SALES TAX--NETWORK TELEPHONE SERVICE--"REPEATER" INCOME. Gross receipts derived from the activity of providing two-way voice communications via repeaters is within the definition of network telephone services and taxable under the retailing B&O tax classification.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

TAXPAYER REPRESENTED BY: . . .

DATE OF CONFERENCE: . . .

NATURE OF ACTION:

Taxpayer protests the reclassification on the repeater income and the resulting additional tax liability. Moreover, the taxpayer protests the additional tax liability on the grounds that even if the reclassification is warranted, such reclassification should only be imposed prospectively.

FACTS AND ISSUES:

Hesselholt, Chief A.L.J. -- The taxpayer, . . . , was audited for the period July 1, 1987 through December 31, 1990. As a result of the audit, the taxpayer was assessed a total of $ . . . . The Audit Division found that the taxpayer had misclassified the income received from the "repeater" rental income (i.e., the fees charged for access to the "repeater" tower) as taxable under the Service and Other Activities business and occupation tax

classification, and reclassified the income as taxable under the Retailing B&O tax classification and assessed the resulting additional tax liability.

The taxpayer offers two-way radio communication services to various customers. In particular, the taxpayer's business involves the selling, installing, and repairing of radios, radiophones, and pagers. Additionally, the taxpayer provides customers access to mountain top radio towers ("repeaters") for a basic fee.

These "repeaters" enable taxpayer's customers to use radios and radiophones for two-way communication by allowing a customer's mobile unit (such as an automobile or truck) to transmit a radio signal to the tower and the signal will be "repeated" back to the customer's other mobile units or base, or, for an additional fee, it may interconnect the signal with public telephone networks. Customers utilizing the taxpayer's communication services are required to be licensed by the Federal Communications Commission (FCC).

DISCUSSION:

The taxpayer protests the Audit Division's reclassification of taxpayer's "repeater rental" income from being taxable under the service B & O classification to being taxable under the retailing B & O classification. Specifically, taxpayer claims that its communication activities should not be considered as "telephone business" or "telephone service" subject to the Retailing B & O tax.

"Retail sale" is defined at RCW 82.04.050. Section five of the statute states "[t]he term [retail sale] shall also include the providing of telephone service, as defined in RCW 82.04.065, to consumers." (Brackets and emphasis added.) RCW 82.04.065 provides as follows:

> (1) "Competitive telephone service" means the providing by any person of telecommunications equipment or apparatus, or service related to that equipment or apparatus such as repair or maintenance service, if the equipment or apparatus is of a type which can be provided by persons that are not subject to regulation as telephone companies under Title 80 RCW and for which a separate charge is made.
>
> 2) "Network telephone service" means the providing by any person of access to a local telephone network, local telephone network switching service, toll service, or coin telephone services, or the providing

> of telephonic, video, data, or similar communication or transmission for hire, via a local telephone network, toll line or channel, cable microwave, or similar communication or transmission system. "Network telephone service" includes interstate service, including toll service, originating from or received on telecommunications
> equipment or apparatus in this state if the charge for the service is billed to a person in this state. "Network telephone service" does not include the providing of competitive telephone service, the providing of cable television service, nor the providing of broadcast services by radio or television stations.
>
> (3) "Telephone service" means competitive telephone service or network telephone service, or both, as defined in subsections (1) and (2) of this section.
>
> (4) "Telephone business" means the business of providing network telephone service, as defined in subsection (2) of this section. It includes cooperative or farmer line telephone companies or associations operating an exchange.

The proceeds of the taxpayer's activities are therefore subject to both the retailing B&O and retail sales tax.

The taxpayer contends that offering two-way voice communication to customers through radios and mountain top repeaters is not a "telephone business" or a "network telephone service" and, therefore, should not be taxable as a retailing activity. In support of its contention, the taxpayer advances two general arguments: (1) that RCW 82.04.065 (the statute) was intended to cover "traditional" telephone services and since the taxpayer does not offer "traditional" telecommunications services, the statute and supporting rule should not be applicable to its activities; and (2) that the legislative intent in enacting the statute was to make telephone services, previously taxable under the public utility tax, taxable under the retailing classification. Since the taxpayer was not previously taxable under the public utility tax, then it should not be presently taxed under the statute.

First, the taxpayer divines a legislative intent that the statute and supporting rule should not be applicable to it:

> It is clear that the term `network telephone service' is intended to cover `traditional' telecommunications

> services such as those provided by AT&T, US West Communications, ..., etc.

The taxpayer believes that because its customers must apply for and receive a license from the FCC and that its two-way communication service is a private activity not accessible to the public on a "for hire" basis are both dispositive for being considered "non-traditional". Furthermore, the taxpayer avers that its two-way communication system, except in limited circumstances, does not access or offer transmission over a local telephone network,
switching, or toll service. To the extent that the taxpayer does provide customers with interconnect service to a local telephone network (a service which entails a separate, additional charge), the taxpayer concedes that the retailing classification is appropriate. However, the taxpayer maintains that the balance of the charges for the non-interconnect two-way communication services (i.e., the basic charge for communications between mobile unit(s) and/or base unit) should not be considered a retailing activity.

The Audit Division concluded that the taxpayer was engaged in providing network telephone service since the taxpayer's "radios, radio telephones, and repeaters enable two-way voice communication between separate locations in a specific area. Additionally, the radio telephones provide access to a local telephone network."

In Determination No. 89-352, 8 WTD 79 (1989), it was observed that

> the definition of `network telephone service' of RCW 82.04.065(2) is broader in scope than merely including traditional telephone companies. It includes several business activities which may be performed ... without entailing the ownership or operation of a traditional telephone system.

The taxpayer in that case utilized a computerized "secretarial" system for rerouting calls in order to save on toll calls. Briefly the scenario involved was as follows: in an effort to eliminate long distance charges on frequent calls between location "A" and location "C", the taxpayer in that case set up an office in location "B" which was located in a local call area to both "A" and "C". The result was that a customer at "A" could call "B" with only local charges applicable and the computer at "B" would reroute the call to "C", again with only local charges applicable. The taxpayer argued that the computer was simply replacing a receptionist at the transfer point (office), who, if present, could simply perform the same function manually.

Nevertheless, it was concluded that this computerized rerouting was a local telephone network switching service and, thereby, taxable as a retail sale.
In Determination No. 87-328, 4 WTD 191 (1987), affirmed by Det. No. 87-328A, 8 WTD 89 (1989), which dealt with a somewhat similar type of telephone answering service ("cross connecting"), it was found that the computer in that case was serving the function of a local telephone network since the computer was

> assuming a role analogous to that of an old-time switchboard operator by making it possible for two parties on different telephone lines to talk to each other. The only real difference is that the taxpayer uses a computer to accomplish the connection whereas the old-time operator did it with jacks and wires.

It was concluded that this type of network activity was retailing as well.

In the present case, the fact that the taxpayer was not engaged in "traditional" telephone services is not dispositive for finding that the taxpayer was not engaged in "network telephone service". Both the statute, RCW 82.04.065, and the rule, WAC 458-20-245, are highly inclusive as to what types of communication activities are considered to be taxable as retailing. The present taxpayer sells communication services to business customers. The fact that those customers must be licensed by the FCC and that the customers must subscribe to the service prior to actual use does not change this outcome.

The taxpayer's claim that "the nature and characteristics of two-way communication service is significantly distinguished from `regular' telephone service", would seem to evidence an erroneous presumption that actual phone cables, operators, and other indicia of "regular" telephone company service are prerequisite to applicability of the statute and rule.

Second, the taxpayer next argues that the state legislature, when enacting RCW 82.04.065 in 1983, did not intend to apply the Retailing classification to businesses which offered services similar to that of the taxpayer (i.e., businesses reporting its state taxes under the "service" classification). Specifically, taxpayer contends that the statute was <u>solely</u> designed to impact businesses which offered telephone services previously taxable under the "public utility" classification.

Taxpayer bases its argument, in respect to this point, on one passage from a Department publication titled "Summary of 1983 Tax Legislation" (Summary). This publication purportedly detailed the application and scope of the changes relating to the taxes

imposed on telephone services. The passage quoted by the taxpayer reads:

> Consistent with extending sales tax to most telephone services, the gross receipts of telephone business will become subject to the retailing classification of the B & O tax (0.00471), instead of the higher public utility tax rates. (Emphasis added by taxpayer.)

The taxpayer not only contends that the above passage "makes it quite clear that, effective July 1, 1983, telephone businesses that paid taxes under the `public utility' category, were required to begin paying taxes under the `retailing' category," but also that in writing the above passage "even the Department acknowledged that only those businesses paying state taxes under the public utility tax laws, chapter 82.16 RCW, were impacted by the 1983 law." The taxpayer also argues that the 1983 statute was simply a progression of reclassifying public utility to retailing. This progression
purportedly began in 1981, when "competitive" telephone service was made subject to the "retailing" taxes. Finally, taxpayer maintains that prior to July 1, 1983, it properly paid taxes under the "service" category of the B & O tax, not the public utility tax.

At least one major fallacy is present in the taxpayer's argument-- that the statute was designed to solely impact entities previously paying public utility tax. First, the taxpayer completely ignores the opening clause of the passage quoted from the Summary - "Consistent with extending sales tax to most telephone services, ..." Second, in a preceding passage of the Summary the legislation enacted in 1981 is described as "broaden[ing] the application of sales tax to charges for network, toll, and switching services,...." There is absolutely no mention in the publication of restricting this "broadening" to entities previously taxed as public utilities. A more plausible reading of the Summary is that the legislation represents a compromise between "public utility" telephone companies and the state. Finally, the summary is simply a summary and not an indication of the legislature's intent.

The taxpayer's service of providing two-way communication is correctly categorized as "network telephone service." The fact that the taxpayer's activities would or would not be considered "traditional" telephone services is irrelevant for finding applicability of the Retailing B & O rate. Moreover, it does not appear that the legislature, in enacting RCW 82.04.065, intended to exclude the type of two-way communication service offered by the taxpayer from subjection to the retailing B & O tax and the retail sales tax.

If it is found to be properly taxable under the retailing classification and liable for the collection of retail sales tax, the taxpayer protests the retroactive application of the tax. Specifically, the taxpayer claims that even if the reclassification is ultimately upheld, the resulting additional liability should only be imposed prospectively.

We recognize that the Department has not previously ruled with finality upon this matter of first impression. This case arises in an industry of rapid and radical technological change, and the methods by which the "telephone services" included in RCW 82.04.065 may be examined, reviewed, and evaluated are not easily circumscribed.

In the interest of fairness and due notice, to the taxpayer and to the public, the Department has determined that the aforesaid application of RCW 82.04.050 and RCW 82.04.065, as well as WAC 458-20-245 (Rule 245), will be prospective only. This application has been formulated to achieve industry wide uniformity and consistency in the application of excise taxation. It is in the best interests of the public and will promote the efficient and uniform administration of the law.
As to the petitioner in this case, the Department will accept the taxpayer's reporting and payment of B & O tax under Service and Other Business Activities on its gross receipts for calls made for periods up to the date of this determination.

DECISION AND DISPOSITION:

The taxpayer's petition is denied in part and granted in part.

DATED this 6th day of October 1992.