

BEFORE THE DIRECTOR
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of Requested)	<u>F</u> <u>I</u> <u>N</u> <u>A</u> <u>L</u>
Ruling of Tax Liability of)	<u>D</u> <u>E</u> <u>T</u> <u>E</u> <u>R</u> <u>M</u> <u>I</u> <u>N</u> <u>A</u> <u>T</u> <u>I</u> <u>O</u> <u>N</u>
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RULE 245, RCW 82.04.065: TELEPHONE BUSINESS -- NETWORK TELEPHONE SERVICE -- SWITCHING SERVICE -- "HOOK FLASH" CROSS CONNECTIONS -- PROSPECTIVE APPLICATION. An electronic, computerized system which connects local telephone access lines to reroute telephone calls and avoid toll call charges constitutes a "local telephone network switching service" under RCW 82.04.065(2). Charges for providing such "hook flash" cross connects are retail sales, subject to sales tax. Prospective application granted.

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: . . .

DEPARTMENT REPRESENTED BY:

Garry G. Fujita, Assistant Director
Edward L. Faker, Sr. Administrative Law Judge

DATE OF HEARINGS: March 21 and 27, 1989

FACTS AND ISSUES:

Faker, Sr. A.L.J. -- The taxpayer has requested a prior ruling of tax liability under Section 18 of WAC 458-20-100 (Rule 100). At both attended and telephoned conferences on the dates referenced earlier, the taxpayer explained the technical methodology by which it provides its computer facilitated services to customers. The taxpayer's supplemental petition submitted on March 28, 1989

corrected earlier misunderstandings and explained its services, in pertinent parts, as follows: (The taxpayer's business name has been replaced by the bracketed inclusions for reasons of confidentiality.)

1. Again, it is helpful to begin with an analogy. Assume that a company in [Zone 1] wishes to call to [Zone 2] often enough so that a flat monthly charge is more economic than per call toll charges. One solution could be the establishment of an office in [an area overlapping both Zone 1 and 2] staffed with a secretary and the acquisition of [Zone 2] telephone line. In that situation the [Zone 1] company could call its [central] office, tell the secretary the desired number in [Zone 2] and ask her to dial that number and hook the lines together by pushing a button on her telephone.

. . .

2. [The taxpayer's] computer services simply takes the place of the secretary, in what amounts to a very simple function. A [Zone 1] customer, after calling the customer's own [central] office where the [taxpayer's] computer is located, identifies itself to the computer and tells it (by dialing) the desired [Zone 2] number. The computer merely records the number dialed by the customer and repeats the dialing on the [Zone 2] line.

Thus, [taxpayer] does not . . . achieve the more economic routing of telephone calls by a kind of computer wizardry. Instead it achieves its function simply by being in the customer's [central] office. The key to the desired routing of the call is that the [central] office is overlapped by the EAS zone that includes [Zone 1] and also by the EAS zone that includes [Zone 2].

[Taxpayer's] computer "secretary" is, of course, more economic than the employment of a real person for the same purpose. Further economies can be realized by the customer by sharing office space with other customers (which [taxpayer] facilitates by subleasing to them). The customers can also economize vis-a-vis the telephone company by sharing telephone lines.

Again, it should be emphasized that all telecommunications facilities and services needed for the desired routing are acquired by the customer from the telephone company. The customer's own lines, [to Zone 1] and [Zone 2], are used and the call transfer occurs at the telephone company's central office.

In addition, the taxpayer's original petition explained:

(1) [Taxpayer] does not own, operate or manage facilities used to transmit information by wire for hire. It does not own, operate or manage telephone lines, a telephone network, toll line or channel, cable, two-line patching equipment, microwave or similar communication or transmission system. Nor does it resell the use of these facilities.

(2) [Taxpayer] does not transmit information or voice communications. It does not provide telephonic, data, video or similar communications or transmissions for hire.

(3) [Taxpayer's] customers have, as have the persons that such customers wish to reach, already paid existing telephone businesses for the services and facilities described in (1) and (2) above. Such services and facilities are put in place by other businesses prior to the rendition of [taxpayer's] services. Their provision of those telecommunication facilities, and the customers' use of them, are already fully subject to the retail sales tax.

Finally, the taxpayer's original petition states:

1. Consistent with what we believe to be correct practice, the industry presently pays taxes under RCW 82.04.290 and WAC 458-20-224 ("Rule 224") on the service it provides and does not collect sales taxes from its customers. However, if the Department were to impose a sales tax collection obligation, the result would be to require the industry to pay the past sales tax liability of its customers from whom it has not collected such taxes. The result would be financial disaster for our client and its infant industry.

In the March 27 teleconference the taxpayer further explained that its computer is a "hook flash" machine which actually redials a number which is outside of the caller's EAS (access) zones, within which zones the call can be made toll free. The system simply replaces a receptionist at the transfer point or office, who, if present, could simply perform the same function manually.

The sole issue for our ruling is whether this service constitutes a sale at retail subject to retail sales tax or a personal service which is not sales taxable.

The Department has entertained this original petition for a final ruling at the Director's level of consideration.

DISCUSSION:

We have thoroughly reviewed the information provided and we conclude that the taxpayer's business activity is a local telephone network switching service under RCW 82.04.065(2). As such, it is expressly included within the definition of "retail sale" at RCW 82.04.050.

Telephone network switching services are precisely the functions which the taxpayer provides through its computerized system. Moreover, it is immaterial whether such switching services are electronically or manually provided. In all cases it is the result of the function which determines its nature as a switching service. The common and ordinary meaning of the terms "telephone network switching service," as that language is used in the statute, as well as the technical meaning of these terms within the industry are clear and unambiguous. The system results in switching telephone lines and cross connecting calling and called parties.

We fully recognize that the taxpayer itself does not own or operate telephone lines or operate a communications or transmissions system for hire. However, 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 by persons, manually or electronically, without entailing the ownership or operation of a traditional telephone system.

We also recognize that the Department has not previously ruled upon this matter of first impression. Moreover, in an industry of rapid and radical technological change, the methods by which the services included in RCW 82.04.065 may be provided are not easily circumscribed. Thus, the Department will accept the taxpayer's reporting of B&O tax under the Service and Other Business Activities for past periods. Retailing B&O tax and retail sales tax shall apply prospectively from the date of this Final Determination.

DATED this 7th day of July 1989.