

Cite as 8 WTD 427 (1989)

BEFORE THE DIRECTOR
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petitions) F I N A L
For Correction of Assessment of) D E T E R M I N A T I O N
) No. 88-378A
) Registration No. . . .
) . . . /Audit No. . . .

[1] RETAILING B&O & RETAIL SALES TAX -- COST-PLUS
TELEPHONE SERVICE AND CHARGES TO HOTEL GUESTS --
DISALLOWANCE OF "CONDUIT" EXEMPTION. Hotel's
provision of telephones, telephone equipment, and
access to local and long distance phone networks to
guests at cost-plus rates does not qualify for
"conduit" exemption/deduction of guest receipts.

[2] RCW 82.04.065 AND WAC 458-20-245: HOTEL'S TELEPHONE
SERVICE BUSINESS -- RETAILING B&O & RETAIL SALES TAX
--TAX ON WHOLESALE COSTS. Hotel's provision of
telephones, telephone equipment, and access to local
and long distance phone networks to guests at cost-
plus rates constitutes the activity of Telephone
Service, subject to Retailing B&O and retail sales
tax and eligible for credit for retail sales tax
mistakenly paid on wholesale purchase.

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: . . .
 . . .

HEARING CONDUCTED BY DIRECTOR'S DESIGNEES:
 Edward L. Faker,

Assistant Director,
Interpretations and Appeals
Garry G. Fujita,
Former Assistant Director

DATE OF CONFERENCE: January 4, 1989

NATURE OF CASE

A hotel operating company appeals the imposition of Retailing business and occupation tax and retail sales tax on unreported local and long distance telephone receipts charged to and collected from taxpayer's hotel guests.

FACTS AND ISSUES

Faker, A.D. -- . . . (Taxpayer), doing business at the . . . , was audited for the period of April 1, 1983 through September 30, 1986. The taxpayer was assessed \$. . . for Retailing B&O tax and retail sales tax on unreported telephone charges to guests.

On October 7, 1988, in Determination 88-378, the I & A Division denied taxpayer relief on its challenge to the taxability of its telephone charges to guests. The matter is now before us for Director Review.

The factual circumstances and legal arguments of this case (pertaining to this and other issues) were fully reported in Determination 88-378 and will not be repeated here. Briefly restated, the taxpayer provided its guests with telephones and telephone access to local and long distance telephone service, networks and exchanges. It then charged the guests for guest originated calls, both local and long distance.

The taxpayer provided the guests with phones and phone service by operating a telephone switchboard capable of timing and tracking guest calls. It leased telephone equipment and purchased local and long distance service and service access. To the extent such was available, the taxpayer utilized WATS line long distance service; sometimes, however, it was compelled to utilize the local telephone company's long distance service.

The taxpayer itself received regular monthly billings (including retail sales tax amounts) from the various telephone service providers. No segregation of taxpayer

business calls from guest originated calls was made on the monthly service provider billings. Based on the rates and charges to it, the taxpayer assessed its guests flat charges (cost plus) for each guest-originated call, based upon time and distance records independently kept by the taxpayer through its switchboard.

The taxpayer excluded from its tax measure the total guest payments made for telephone calls. The Auditor required inclusion of such guest payments and characterized them as receipts derived from "services related to lodging." Accordingly, Retailing B&O tax and retail sales tax were assessed.

The issues for review by the Director are:

1. Does taxpayer act solely as collection agent for the underlying telephone service and telephone network access providers, such that the taxpayer is entitled to deduct from its B&O tax measure collections made by the taxpayer as a "conduit"?
2. Is the taxpayer engaged in business as a Telephone Service provider itself, buying at wholesale telephone services and telephone network access and reselling the same at retail to its guests, whereby it is entitled to credit for retail sales taxes it previously paid to the underlying suppliers of telephone services and telephone network access?

TAXPAYER'S OBJECTIONS

1. The taxpayer re-asserts that it acted solely as collection agent or conduit of funds paid through it to the underlying telephone service providers. Thus, guest monies paid through the taxpayer to the underlying service providers for telephone services rendered should be deducted from the taxpayer's tax measure as exempt from B&O and sales taxes.
2. In the alternative, the taxpayer re-argues that, as to telephone related receipts, it was itself an intermediary "telephone service" provider, as defined in RCW 82.04.050(5) and WAC 458-20-245. While subject to Retailing B&O and to retail sales tax on receipts, it would also be eligible for credit for sales tax it paid to the underlying telephone companies on its own monthly telephone service bills.

DISCUSSION

[1] The taxpayer urges us to believe that it acted solely as agent for the telephone service providers in the collection and passage through of telephone charge receipts from the taxpayer's guests. That relationship is a prerequisite to the taxpayer's argument for deduction of so-called "conduit" payments from guests passed on to the phone companies.

The factors the taxpayer must prove to maintain this argument are that the taxpayer (1) had no real business relationship or involvement with any of the parties, the phone service, or the billing, and (2) did in fact merely pass through the funds received from its guests to the underlying telephone service providers. The taxpayer would have us believe that its only role was that similar to a paymaster merely receiving and dispensing the funds of others (guests) to satisfy their telephone debts.

The taxpayer's contention can not be accepted in light of the following material facts: The taxpayer acquired in its own name telephone equipment and access to local and long distance telephone service networks. At no point were the underlying telephone service providers ever made aware of the identity and billing address of any of the actual guest callers or users. Thus, the service providers were unable to charge the actual user guests, even were they so inclined.

Further, the taxpayer obligated itself for all service and long distance calls made, regardless of whether such calls were originated by the taxpayer or by its guests. The taxpayer did not request separate designations of guest versus taxpayer phone calls. Consequently, the underlying telephone companies did not segregate guest from the taxpayer service calls. Instead, it simply identified all calls and billed the taxpayer therefor. Thus, the taxpayer was solely responsible for paying the underlying monthly telephone service and long distance costs and charges.

Next, the taxpayer acquired the telephone equipment and services for reason of its needs in conducting its own business activities (management, room rentals, supply and resupply, and other business activities) and in order to solicit business and advertise its hotel as a full service establishment. The hotel was interested for its own reasons in obtaining full service phone and telecommunication capabilities.

Finally, the taxpayer assessed its guests an amount greater than the actual costs charged by the underlying service providers. It levied and collected a flat time and distance

rate estimated to be equal to and/or in excess of the actual cost of guest calls. The extra charges were set to cover the cost of taxpayer's employees, lease materials, and equipment expenses incidental to the provision of the phone service.

In the face of these circumstances, it is clear that the taxpayer's "conduit" contention must fail. It was acting for itself, and not as an agent for the telephone service providers or for anyone else. Essentially, the taxpayer had sole and separate responsibility for the acquisition of and payment for telephone service and telephone network access. It was actively involved in the provision and metering of service to its guests and it levied additional charges for that involvement.

For these reasons, the taxpayer can not be considered a mere "conduit" simply paying over to the service providers the guest phone receipts. No "conduit" exemption or deduction is allowed.

[2] The taxpayer has also contended that it acted as a middle level telephone service provider, under RCW 82.04.065 and WAC 458-20-245. According to the taxpayer, it purchased and/or leased the phone equipment and obtained the phone access and related services at wholesale for ultimate retail sale to its guests.

In making this argument, the taxpayer admits that it owes Retailing B&O tax on its gross receipts from telephone services provided. Moreover, it acknowledges retail sales tax liability on all service charges billed to the guests. However, the taxpayer also believes itself entitled to, and argues for, credit for any sales taxes mistakenly paid by it to the underlying service providers.

RCW 82.04.065 defines "network telephone service" as:

. . . 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.

Further along, that statute also makes clear that persons providing network telephone service are engaged in the telephone business.

(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.

After reviewing the facts in this case, and the June 26, 1989 letter of the taxpayer's accountant, we find that the taxpayer's telephone activities vis-a-vis its guests constitute that of a retail "telephone business." The taxpayer provides a "network telephone service" by accessing for its guests "local telephone network(s)," "local telephone network switching service(s)," and "toll service(s)" including interstate communications billed locally. This determination is in accord with prior departmental rulings. In Determination 89-111, ____ W.T.D. ____ (1989), we held

The taxpayer's business activity of providing to its customers access to a local telephone network is "network telephone service." The taxpayer's income from such business activity is subject to Retailing B&O tax measured by the amounts billed to the customer which includes the taxpayer's handling charge. There is no deduction from the measure of the tax for any of taxpayer's expenses including amounts paid by the taxpayer for purchase of the telephone service, which the taxpayer resells to its customers/consumers, from local telephone companies.

Consequently, under WAC 458-20-245, the taxpayer owes Retailing B&O tax and retail sales tax on its telephone service revenues. The taxpayer, however, is entitled to a retail sales tax credit for any retail sales taxes paid by it to the underlying wholesale telephone service and network access providers on charges for calls by hotel guests.

Finally, in the future, the taxpayer is advised to comply with WAC 458-20-102 and obtain the necessary resale certificates for use at the time it purchases those basic telephone services for resale.

DECISION

The taxpayer's "conduit" theory for exemption from its B&O tax measure of its telephone service charges to guests is denied. The taxpayer's second request for characterization and taxation of its activities as a "telephone business" is granted. Credit for retail sales taxes previously paid by the taxpayer to the underlying telephone service providers shall be computed by the Audit Section. Following recomputation of the balance of the taxpayer's liability, Audit Section will notify the taxpayer of its revised liability.

DATED THIS 7th day of December, 1989.