

ST 14-0043-GIL 08/11/14 TELECOMMUNICATIONS EXCISE TAX ACT

This letter provides an overview of items subject to the Telecommunications Excise Tax Act. See 35 ILCS 630. (This is a GIL.)

August 11, 2014

Dear Xxxx:

This letter is in response to your letter dated March 24, 2014, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings (“PLRs”) are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department’s regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter (“GIL”) is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

I am writing on behalf of COMPANY, EIN: XX-XXXXXXX (“COMPANY”), to request a private letter ruling as to whether, under the facts described below, arrangements between COMPANY and its customers will be subject to the Illinois Telecommunications Excise Tax.

This request, made pursuant to 2 Ill. Adm. Code 1200.110, relates to the tax period commencing Month X, 20XX, and all subsequent tax periods. No audit or litigation is currently pending with the Illinois Department of Revenue (the “Department”) with respect to COMPANY. To the best of my knowledge and to the best of COMPANY’s knowledge, the Department has not previously ruled on the same or a similar issue for COMPANY and neither COMPANY nor any of its representatives have previously submitted the same or a similar issue to the Department but withdrew it before a letter ruling was issued. The relevant facts, authorities and analysis relating to this request are fully set forth below.

FACTS

COMPANY is an Illinois limited liability company formed through the filing of articles of organization effective Month2 XX, 20XX. COMPANY was established with the expectation that it would eventually assume ownership and operation of a broadband network developed and implemented by UNIVERSITY (“UNIVERSITY”). The network was built using federal and state grant funds for the purpose of bringing high-speed Internet services to underserved communities and organizations where current market capabilities do not offer access to higher speeds of Internet service. COMPANY took ownership of the network assets and became fully operational effective as of Month X, 20XX.

COMPANY's customer base (current and prospective) includes the following:

- The vast majority of COMPANY's clients (in terms of both number and network usage) consist of governmental, public and nonprofit organizations, including without limitation municipalities, schools, universities, community colleges, medical and healthcare facilities, public safety organizations, libraries, museums and community support organizations ("Category 1 Users"). Through lit fiber strands, Category 1 Users access the Internet directly, without need for an additional arrangement with a commercial Internet service provider (ISP) such as COMPANY1, COMPANY2, etc. Category 1 Users use the Internet access solely for purposes of their own internal operations and do not re-sell network access to third parties. COMPANY charges Category 1 Users a fee based on per-megabit cost.
- On a limited basis, COMPANY provides lit fiber strands to ISPs ("Category 2 Users"), who in turn re-sell Internet access to their own customers. COMPANY has established a separate pricing approach for Category 2 Users that offers Internet connectivity at a graduated cost per unit.
- Also on a limited basis, COMPANY provides certain other commercial organizations ("Category 3 Users") with dark fiber strands on a long-term lease basis pursuant to Irrevocable Rights of Use. The lighting of the strands are [sic] the responsibility of the lessee, although ongoing maintenance is handled by COMPANY in exchange for an annual fee.

We have enclosed a representative copy of the service agreements entered into with each category of customer, redacted to remove customer-specific identifying information pricing figures.

ANALYSIS

A. Illinois Statutory and Regulatory Provisions.

The Illinois Telecommunications Excise Tax, 35 ILCS 630/1 et seq. (the "Act"), is imposed on the act or privilege of originating or receiving telecommunications by a person in the State of Illinois, if purchased by such person at retail from a retailer. 35 ILCS 630/3 and 630/4. The Telecommunications Excise Tax is technically imposed on those who originate or receive telecommunications, but responsibility for collecting the tax rests with retailers maintaining a place of business in the State of Illinois; such retailers are liable for the tax whether or not they have collected it from the taxpayers. See 35 ILCS 630/5. An understanding of the scope of the Telecommunications Excise Tax requires a careful parsing of the terms used in the statute and their stated definitions. For these purposes, the term "telecommunications" is broadly defined, including:

. . . messages or information transmitted through use of local, toll and wide area telephone service; private line services; channel services; telegraph services; teletypewriter; computer exchange services; cellular mobile telecommunication service; specialized mobile radio; stationary two way

radio; paging service; or any other form of mobile and portable one-way or two-way communications; or any other transmission of messages or information by electronic or similar means, between or among points by wire, cable, fiber-optics, laser, microwave, radio, satellite or similar facilities. . . . Carrier access charges, right of access charges, charges for use of inter-company facilities, and all telecommunication resold in the subsequent provision of, used as a component of, or integrated into end-to-end telecommunications service shall be non-taxable as sales for resale.

35 ILCS 630/2(c).

The other key definition is that of “sale at retail,” which means:

. . . the transmitting, supplying or furnishing of telecommunications and all services and equipment provided in connection therewith for a consideration to persons other than the Federal and State governments, and State universities created by statute and other than between a parent corporation and its wholly owned subsidiaries or between wholly owned subsidiaries for their use or consumption and not for resale.

35 ILCS 630/2(k). By administrative rule, the Department has elaborated upon the foregoing provisions, stating, for example, that the exemption for State governments and universities extends only to telecommunications purchased by such entities for their own use (*e.g.*, by a university’s faculty and staff in the course of their duties); the university would have to collect and remit the Telecommunications Excise Tax on any sale by the university of telecommunications services to students in university dorms. See 86 Ill. Adm. Code 495.105.

In other administrative rules, the Department has elaborated on the application of the Telecommunications Excise Tax to Internet service providers. Specifically, 86 Ill. Adm. Code 495.100(m) provides as follows:

Generally, persons that provide customers access to the Internet (“Internet Service Providers” or “ISPs”) and who do not, as part of that service, charge customers for the line or other transmission charges that are used to obtain access to the ISP’s server or other point of access, are not considered to be telecommunications retailers from these activities. This is the case so long as such ISPs do not, as part of their billing, charge customers for such line charges and instead pay their telecommunication suppliers all transmission costs that they incur in providing the Internet service. In this situation, an ISP’s customer pays his telecommunications supplier for all transmission costs incurred while using the service. The single monthly fee charged by the ISP, which often represents a flat charge for a package of items including Internet access, e-mail, and electronic newsletters, would generally not be subject to tax. If, however, the ISP charges customers for line or other transmission charges, it should provide its telecommunication suppliers with Certificates of Resale and should collect and remit the tax. For example, if an ISP provides customers with Internet access, as described in this subsection, but also

provides customers the use of a 1-800 service to access the ISP, and separately assesses customers per minute charges for the use of the 1-800 service, the ISP is considered a telecommunications retailer and incurs Telecommunications Excise Tax on the charges made for the 1-800 service. If the charges are not disaggregated [as provided elsewhere in this rule], all charges are subject to the Telecommunications Excise Tax.

B. Preemption by Federal Law

The Act recognized that the Telecommunications Excise Tax may be preempted by federal law. See 35 ILCS 630/3 and 630/4. In that regard, the federal Internet Tax Freedom Act (“ITFA”) provides that, “No State or political subdivision thereof may impose any of the following taxes during the period beginning November 1, 2003, and ending November 1, 2014: (A) Taxes on Internet access . . .” 47 U.S.C. § 151 note § 1101(a). The ITFA defines “Internet access” as “a service that enables users to connect to the Internet to access content, information, or other services offered over the Internet,” but specifically excludes voice services provided over Internet protocol, so providers of VoIP services are not covered by the ITFA tax moratorium. *Id* at § 1105(5). On its face, the ITFA preempts the application of the Telecommunications Excise Tax to Internet access providers.

C. Interpretations by the Department.

The Department has published various ruling addressing the application of the Telecommunications Excise Tax to Internet or Internet-related activities. Most such rulings have been in the form of General Information Letters (“GILs”) issued under 2 Ill. Adm. Code 1200.120, which contain general discussion of tax principles or applications, but are not binding on the Department and may not be relied upon by taxpayers. We have summarized certain of the rulings below.

- ST-06-0154-GIL (7/31/06) – This ruling involves a company providing residential realtors with online access to a product that generated maps and related marketing materials to permit subscribers to market their own services. The Department pointed the taxpayer to regulations providing that charges for automated information retrieval and data processing (including access to on-line computer databases, as described here) are not taxable, unless the taxpayer also imposes a line charge or other fee for transmission of the data; the latter would be subject to the Telecommunications Excise Tax, or the entire charge if such amounts are not separately stated. Observing that ISPs who do not charge their customers for line or other transmission charges are generally not considered to be telecommunications retailers, the Department stated, “It is our general understanding that most Internet access providers do not, as part of their billing, charge customers for such line charges, but instead, pay all transmission costs to their telecommunications providers.”
- ST-08-0033-GIL (3/19/08) – This ruling involved a satellite-based Internet service provider. The Department offered the same statements as in the 2006 ruling (above), almost verbatim, with the additional clarification that an Internet access provider may point to either a customer invoice or its own books and records to

support a delineation between amounts charged for transmission (taxable telecommunications gross charges) and other non-taxable services.

- ST-10-0008-GIL (2/25/10) – This ruling responded to a request regarding the taxation of wireless Internet services that were either bundled with voice and other taxable services or sold separately. The Department reviewed the federal moratorium created pursuant to the ITFA and observed that, while *some* telecommunications would fall within the ITFA definition of “Internet access” (*i.e.*, a service that enables users to connect to the Internet to access content, information or other services offered over the Internet) and thus be non-taxable, other telecommunications services would not so qualify and thus would remain subject to the Telecommunications Excise Tax. The Department reiterated that the non-taxable charges must be disaggregated and separately stated from other charges in the books and records of the services provider.
- ST 10-0053-GIL (6/7/10) – In a ruling issued to what appears to be the same taxpayer described in ST-10-0008, the Department further addressed the application of the Telecommunications Excise Tax to a 24-hour medical consultation service accessible via the Internet. The online offerings include a database of prerecorded messages on various health topics, plus the opportunity for customers to use a “chat line” to speak directly with a health professional. The Department stated that the Telecommunications Excise Tax would not apply to amounts charged to access content, information or other services offered over the Internet, but may apply to any transmission charges imposed on customers using the chat line.
- ST 10-0120-GIL (12/21/10) – This ruling responded to a request from a taxpayer that sold GPS tracking devices, which were piggybacked to a third party’s cellular network. The devices would be installed on a customer’s vehicles and would permit the vehicles to be tracked via mapping software at the customer’s office. The Department stated that it could not determine, based on the information provided, whether the taxpayer was a *retailer* of telecommunication services or a *user* of telecommunication services who owed the Telecommunications Excise Tax to its own telecommunication supplier.
- ST 11-0028-GIL (4/6/11) – This ruling was issued to a taxpayer that purchased mobile broadband data plans from cellular and PCS wireless carriers (*e.g.*, Verizon, AT&T, Sprint), then resold the wireless broadband Internet access to its own customers. The arrangements did not entail mobile telecommunication services, but rather were limited solely to data plans for wireless broadband Internet access. The Department again reviewed the moratorium created by the ITFA, stating that the exemption would apply *only* to telecommunications that are purchased, used or sold to enable users to connect to the Internet or to otherwise enable users to access content, information or other services offered over the Internet. Any *other* telecommunications services would be fully subject to the Telecommunications Excise Tax. The Department reminded the taxpayer that the Internet access charges must be separately identified from charges for taxable telecommunications services in order to avoid the entire charge being taxable.

- ST 13-0048-GIL (9/11/13) – This ruling was requested by a taxpayer providing web-based services such as online group meetings, webinars, and training sessions. The services included, at no additional charge, an option for customers to add voice or video communications features to an online session; however, customers would need to use their own telecommunications services (Internet and/or long-distance telephone service) to access such features and presumably would be paying that telecommunications provider separately for the same. The Department concurred that the provision of web-based services is not the provision of telecommunications; rather, the taxpayer should be considered a *user* of telecommunications and should be paying the Telecommunications Excise Tax in connection with its purchase of telecommunications from its own provider.

D. Applicability to COMPANY.

Based on the foregoing statutory and regulatory provisions, as well as the various interpretations offered by the Department in its published rulings, we believe that the arrangements between COMPANY and its customers should not be subject to the Telecommunications Excise Tax, as further discussed below.

1. Category 1 Users

COMPANY is not providing any “telecommunications” service to Category 1 Users, within the meaning of the Act and consistent with interpretations offered by the Department in the various GILs above. The applicable regulations specifically provide that ISPs who do not charge their customers for the line or other transmission charges that are used to obtain access to the ISP’s server or other point of access are not considered to be telecommunications retailers. See 86 Ill. Adm. Code 495.100(m). Moreover, even if the provision of Internet access *would* be considered as “telecommunications” within the meaning of the Act and corresponding regulations, the ITFA, in its current form and for so long as it continues in effect, precludes the imposition of tax on telecommunication that are purchased, used or sold to enable users to connect to the Internet or to otherwise enable users to access content, information or other services offered over the Internet. This is precisely, and solely, what COMPANY is providing to its Category 1 Users – nothing less and nothing more.

2. Category 2 Users

COMPANY is not providing its Category 2 Users with a taxable “telecommunications” service, provided that it does not charge the ISPs for line or other transmission charges used to obtain access to COMPANY’s network. See 86 Ill. Adm. Code 495.100(m). Moreover, even if the provision of Internet access *would* be considered as “telecommunications” within the meaning of the Act and corresponding regulations, the arrangements between COMPANY and its Category 2 Users should be protected by the ITFA moratorium, at least for so long as it remains in effect.

Even if the ITFA is allowed to expire in November 2014, the Department presumably would continue to adhere to the position set forth in its existing regulations, unless and until modified. If such regulations are modified to reflect an expansive application of the

Telecommunication Excise Tax to the provision of Internet access, COMPANY *still* may be able to avoid application of the tax insofar as its dealings with Category 2 Users are not “at retail” within the meaning of the Act, but rather constitute sales for resale. In particular, the transactions between the Category 2 Users and their ultimate customers would be the pertinent “retail” transaction, with the Category 2 users collecting and remitting the Telecommunications Excise Tax in connection with their resale of Internet access to their own customers.

3. Category 3 Users

In the case of the Category 3 Users, COMPANY provides fiber strands that are unlit, meaning that such strands will not transmit messages or information at all – the essential starting point for the definition of “telecommunications” under the Act. Insofar as the Telecommunications Excise Tax is imposed on the act or privilege of originating or receiving telecommunications in the State of Illinois, COMPANY’s provision of dark fiber strands that, for so long as they remain dark, convey no messages or information whatsoever, should be squarely outside the scope of the Telecommunications Excise Tax. If Category 3 Users assume responsibility for lighting the strands at some point, COMPANY should still not be liable for collecting the Telecommunications Excise Tax because: (i) COMPANY itself is not the provider of the telecommunications services; (ii) the annual fees paid by Category 3 Users to COMPANY do not constitute “gross charges” within the meaning of the Act (to which the tax is applied), *i.e.*, the amounts are not paid for the act or privilege of originating or receiving telecommunications, but rather were paid for unlit dark fibers without regard to whether they are ever used; and/or (iii) the arrangement constitutes the provision of Internet access and thus should be exempt under the same analyses set forth with respect to Category 1 and/or Category 2 Users above (depending on who the Category 3 Users are and what they will do with the access achieved via the fibers, once lit).

While we believe the above analysis is correct, and we have not been able to identify any authorities contrary to such views, COMPANY has authorized us to request a private letter ruling on its behalf to obtain more certainty with respect to application of the Telecommunications Excise Tax.

If you have any questions about or wish to discuss this request, please contact me at the telephone number or e-mail address above.

DEPARTMENT’S RESPONSE:

The Department’s regulation “Public Information, Rulemaking and Organization” provides that “[w]hether to issue a private letter ruling in response to a letter ruling request is within the discretion of the Department. The Department will respond to all requests for private letter rulings either by issuance of a ruling or by a letter explaining that the request for ruling will not be honored.” 2 Ill. Adm. Code 1200.110(a)(4). The Department recently met and determined that it would decline to issue a Private Letter Ruling in response to your request. We hope however, the following General Information Letter will be helpful in addressing your questions.

The Illinois Telecommunications Excise Tax Act imposes a tax on the act or privilege of originating or receiving intrastate or interstate telecommunications by persons in Illinois at the rate of 7% of the gross charges for such telecommunications purchased at retail from retailers by such persons. 35 ILCS 630/3 and 4. The Simplified Municipal Telecommunications Tax Act allows municipalities to impose a tax on the act or privilege of originating in such municipality or receiving in such municipality intrastate or interstate telecommunications by persons in Illinois at a rate not to exceed 6% for municipalities with a population of less than 500,000, and at a rate not to exceed 7% for municipalities with a population of 500,000 or more, of the gross charges for such telecommunications purchased at retail from retailers by such persons. 35 ILCS 636/5-10 and 5-15. The incidence of the tax is on the person who originates or terminates intrastate or interstate telecommunications, and the tax is collected and remitted to the Department by the retailer of the telecommunications.

“Telecommunications,” in addition to the meaning ordinarily and popularly ascribed to it, includes, without limitation, messages or information transmitted through use of local, toll and wide area telephone service; private line services; channel services; telegraph services; teletypewriter; computer exchange services; cellular mobile telecommunications service; specialized mobile radio; stationary two way radio; paging service; or any other form of mobile and portable one-way or two-way communications; or any other transmission of messages or information by electronic or similar means, between or among points by wire, cable, fiber-optics, laser, microwave, radio, satellite or similar facilities. “Telecommunications” do not include “value added services in which computer processing applications are used to act on the form, content, code and protocol of the information for purposes other than transmission.” See 35 ILCS 630/2(a) and 2(c). If telecommunications retailers provide these services, the charges for each service must be disaggregated and separately stated from telecommunications charges in the books and records of the retailers. If these charges are not thus disaggregated, the entire charge is taxable as a sale of telecommunications.

“Gross charges” means the amount paid for the act or privilege of originating or receiving telecommunications in this State and for all services and equipment provided in connection therewith by a retailer, valued in money whether paid in money or otherwise, including cash, credits, services and property of every kind or nature, and shall be determined without any deduction on account of the cost of such telecommunications, the cost of materials used, labor or service costs or any other expense whatsoever. “Gross charges” do not include “charges for the storage of data or information for subsequent retrieval or the processing of data or information intended to change its form or content.” See 86 Ill. Adm. Code 495.100(c).

The Internet Tax Freedom Act imposes a federal moratorium on state or municipal taxes on Internet access until November 1, 2014. 47 USCA § 151 note; § 1101. “Internet access”:

(A) means a service that enables users to connect to the Internet to access content, information, or other services offered over the Internet;

(B) includes the purchase, use or sale of telecommunications by a provider of a service described in subparagraph (A) to the extent such telecommunications are purchased, used or sold-

(i) to provide such service; or

(ii) to otherwise enable users to access content, information or other services offered over the Internet;

(C) includes services that are incidental to the provision of the service described in subparagraph (A) when furnished to users as part of such service, such as a home page, electronic mail and instant messaging (including voice and video-capable electronic mail and instant messaging), video clips, and personal electronic storage capacity;

(D) does not include voice, audio or video programming, or other products and services (except services described in subparagraph (A), (B), (C), or (E)) that utilize Internet protocol or any successor protocol and for which there is a charge, regardless of whether such charge is separately stated or aggregated with the charge for services described in subparagraph (A), (B), (C), or (E); and

(E) includes a homepage, electronic mail and instant messaging (including voice and video-capable electronic mail and instant messaging), video clips, and personal electronic storage capacity, that are provided independently or not packaged with Internet access.

Telecommunications that are purchased, used or sold by a provider to enable users to connect to the Internet or to otherwise enable users to access content, information or other services offered over the Internet are subject to the federal moratorium. There are services that are not subject to the moratorium. Paragraph D of the definition of "Internet access" excludes "voice, audio or video programming, or other products and services (except services described in subparagraph (A), (B), (C), or (E)) that utilize Internet protocol or any successor protocol and for which there is a charge, regardless of whether such charge is separately stated or aggregated with the charge for services described in subparagraph (A), (B), (C), or (E)." Therefore, telecommunications, including for example Voice over Internet Protocol (VoIP), that are not purchased, used or sold to a provider to enable users to connect to the Internet or to otherwise enable users to access content, information or other services offered over the Internet, are not subject to the federal moratorium and are subject to the Telecommunications Excise Tax.

Generally, Internet access purchased by COMPANY's clients is subject to the federal moratorium under the Internet Tax Freedom Act and is not subject to Telecommunications Excise Tax during the moratorium. However, as explained above, not all services qualify as Internet access. The client may use the Internet access to originate or terminate telecommunications that are not subject to the moratorium and are subject to Telecommunications Excise Tax. Section 1106 of the Internet Tax Freedom Act states:

"If charges for Internet access are aggregated with and not separately stated from charges for telecommunications or other charges that are subject to taxation, then the charges for Internet access may be subject to taxation unless the Internet access provider can reasonably identify the charges for Internet access from its books and records kept in the regular course of business."

Under the Department's regulations, non-taxable services are not subject to Telecommunications Excise Tax provided that the charges for such services are disaggregated and separately identified from other charges in the books and records of the telecommunications retailer. See 86 Ill. Adm. Code 495.100.

Generally, lit fiber strands sold to Internet Service Providers, or ISPs, who use the lit fibers to provide Internet access service to their customers are subject to federal moratorium under the Internet Tax Freedom Act and are not subject to Telecommunications Excise Tax during the moratorium.

Generally, dark fiber strands provided on a long-term lease basis pursuant to an Irrevocable Right to Use, or IRU, are not subject to Telecommunications Excise Tax.

I hope this information is helpful. If you have further questions, you may contact me at 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters
Associate Counsel

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