

Communications Services Tax Working Group

Options and Written Comments

Received as of October 1, 2012

Submissions by:

- Charles Dudley
- Sharon Fox
- Gary Lindsey
- Mayor Gary Resnick
- Brian Smith
- Marshall Stranburg
- Florida Retail Federation
- AT&T, CenturyLink, Sprint, T-Mobile, and Verizon

Communications Services Tax Working Group

Options for Consideration

Submitted by Working Group Member:

Charles Dudley

CST Task Force Options and Background
Submitted by Task Force Member Charles Dudley
September 14, 2012

- I. Findings - based on testimony and written materials presented to the Task Force. The following are my interpretation/observations for suggested Findings:
- A. CST state and local revenues have been and are projected to continue to decline. Several reasons for this were presented by DOR staff and others:
1. Substitution of "non-taxable" services, mostly delivered over the Internet (i.e., over the top services), for taxable services - video and voice examples were provided and demonstrated (*August 21, 2012 Agenda, Tabs 5 & 6*)
 2. While there is a "use tax" component of the CST, the same administrative and enforcement problems that DOR faces in regard to the sales and use tax on the on-line sale of goods and services negatively impacts CST receipts (*August 21, 2012 Agenda, Tabs 5 & 7*).
 3. The growth of "pre-paid" wireless, as a substitute for more traditional, post-pay plans, has impacted CST receipts. There is a dispute over the statutory interpretation of the application of the CST to pre-paid wireless, but the DOR has issued a formal opinion saying pre-paid is taxable under CST. Retailers testified that they are NOT dealers of communications services. Providers of pre-paid wireless services and retailers presented legal counter arguments to the DOR interpretation and several administrative issues that make collection/enforcement of the CST on pre-paid very difficult and some would say impossible, especially since 72% of these pre-paid services are sold by non-dealer third parties and 17% via remote sales (*July 25, 2012 Agenda, Tab 7, Slide 4*).
- According to the DOR survey, nearly every other state subjects pre-paid to sales tax only. (*June 11, 2012 Agenda, Tab 4, Slides 33 and 40*) The pre-paid/CST issue is one that may require more time, study and review - similar to the approach taken regarding the application of Florida's 911 fee to pre-paid wireless. Interestingly, the title of one of our pre-paid presentations—"31 Flavors of Pay Go, Pay-as-you-Go, Pay in Advance, Pay & 60, Pre-Pay..."-- illustrates many of the difficulties in defining and implementing changes to the taxation of pre-paid. (*July 25, 2012 Agenda, Tab 7*)
4. While the use of wireless services has clearly increased dramatically, prices have fallen, impacting CST receipts, while the growth of internet access services which are exempt under federal and state law from taxation has

resulted in reduced CST receipts. *(Several DOR presentations to date and EDR)*

- B. DOR audits over the last 12 years have resulted in the additional collection of revenues that represent **less than 1%** of total CST collections, while costing the DOR auditors over 60,000 hours (nearly 50% of total = 121,336). DOR testified and presented data that over 50% of its CST audit staff's time and energy was spent on "situsing" issues, but the resolution of those issues only resulted in "around 20%" of the total additional revenues collected. *(August 21, 2012 Agenda, Tab 7)*
- C. As wireless devices and services have grown exponentially, landline service has correspondingly decreased. *(June 11, 2012 Agenda, Tab 5, Slide 16)* All wireless accounts are determined to be "non-residential" under the CST and so customers who use their wireless phones as their primary phone or as a substitute for their former landline phone, do not receive the benefits of the partial residential exemption to the state sales tax component of the CST *(June 11, 2012 Agenda, Tab 8)*. The residential exemption in 2012-13 has a value of \$124m. If repealed, and the state sales tax component of the state CST was reduced in a revenue neutral manner, the current 6.65% sales tax rate component would become 5.95%, resulting in an overall rate of 8.47% on all communications services subject to the State CST. *(July 25, 2012 Agenda, Tab 6, Slide 11 and phone call with B. McKee)*
- D. Florida has the highest state CST taxes in the country and the second largest variance of local CST tax rates according to the DOR survey. *(June 11, 2012 Agenda, Tab 4, Slides 24 and 25)*
- E. Local governments rely on their CST revenues as a source of general operating revenue as well one of their more reliable sources of revenues to pledge in cases of bond financing. Any changes to the CST law that impact the amount of local CST revenues need to take into account these factors *(July 25, 2012 Agenda, Tab 5)*, and, according to our Mission, our options should not "unduly" reduce local CST revenues *(August 21, 2012 Agenda, Tab 1)*.
- F. The revenues generated by the State gross receipts portion of the CST have similarly decreased over the last several years - and when combined with falling utility gross receipts - has limited the state's ability to issue new bonds for school construction. There was no option or other ideas presented for how to address this issue in terms of changes to the CST, but any changes should take into account their impact on these receipts. *(June 25, 2012 Agenda, Tab 8)*

II. Options

At the July 25, 2012 Agenda, DOR put forth at Tab 4, Slide 6, Guiding Principles for how a tax structure would ideally function: Reliable, Simple, Neutral, Transparent,

Fair, and Modern. Clearly, Florida's CST needs significant reform in nearly every one of these areas, especially given the pace of technological change over the last 11 years since the CST's effective date.

In reviewing the materials and testimony presented to the Task Force to date, these suggested Guiding Principles, and the statutory "Mission" of the Task Force, I would offer the following options for consideration:

Option A - eliminate the partial residential exemption for voice services from the state sales tax component of the CST and suggest a corresponding revenue neutral reduction in that tax rate.

Option B - eliminate the situsing requirements for the local CST component and move to a single statewide CST rate as is currently done for DBS service, the rate of which is 13.17%. DOR and interested parties would work to develop a distribution mechanism similar to what is currently done with 4% of the DBS tax to cities/counties. There may need to be a phase-in moving to the 13.17% unified tax rate (or lower upon adoption of Option A and reduction of the state sales tax component of the state CST) in which the impact on each city and county could be minimized by guaranteeing certain revenue amounts; additional state CST revenues could be added to the distribution pool for sharing; or other methods consistent with the Guiding Principles and Mission.

While many details would remain for further review and discussion, I submit that these options would meet the criteria set out in the suggested Guiding Principles and the Mission of the Task Force.

Communications Services Tax Working Group

Options for Consideration

Submitted by Working Group Member:

Sharon Fox

Introduction:

The development of the CST was a consensus effort of the state, communications service providers, and local governments, intended to simplify the administrative burden of the seven different state and local taxes and fees for both the communications industry and local governments, by employing the Florida Department of Revenue (DOR) to receive, track, and distribute the resulting tax revenues and audit any discrepancies, as they already did for the state's sales and gross receipts taxes.

The CST was initially implemented to cover the broad spectrum of communications services, such that all communications services were taxed, giving no one service provider or communications service delivery method benefit over another, no matter the technology used. Additionally, the taxable base was broadened, such that the seven different state and local taxes and fees, when bundled into a single tax on the larger base, provided revenue neutrality and a stable, bondable revenue source to each of the governmental entities, a single entity for the communications industry to be accountable to for reporting and collection purposes, and a reduced cumulative tax rate on communication services for taxpayers.

Legislative and technological changes which have occurred over the past several years have resulted in a diminution of CST revenues to the state and to local governments, diminishing the reliability of this revenue stream for future bonding needs. These changes have additionally resulted in like services being taxed differently depending on the service provider or method of sale, causing the very discrimination that the Communications Services Tax Simplification Law was intended to prevent and confusing taxpayers in the process.

We have heard industry members' concerns regarding the difficulty in situsing services to the appropriate local jurisdiction, particularly regarding the taxable prepaid market; and the complexity and time-consuming nature of CST audits, given the number of jurisdictions involved, the available records, and the limited resources available to DOR.

In this light, municipal governments propose a number of options which, while individually not sufficient to address all noted concerns, when taken in combination with others may provide assistance in stabilizing the revenue stream for state and local governments, address concerns voiced by DOR regarding the complexity of administration, and provide the communications industry with relief regarding the prepaid service market and removing competitive advantages within the industry.

Option #1: Further broaden the taxable base, including all like services without exemption, no matter the technology or service provider used. (a) Eliminate the prepaid calling arrangement tax exemption in its entirety, and establish a methodology to assess a tiered surcharge, based upon the amount of the sale and sitused to the place of purchase. Industry presentations indicated that the bulk of the retail prepaid sales is repeat walk-in business, which leads one to conclude that the location of the sale is in the vicinity of its use. Given the lack of personal data collected, the place of a prepaid cash sale is a reasonable location for situsing for CST purposes. The retail presenters seemed to indicate that taxation in this situation was do-able through a surcharge at the point of sale, while they were averse to a different tax rate for prepaid sales, as vending machines and small retail establishments could accommodate a surcharge better than a varying tax rate. Tiering would prevent a customer from paying

the same amount of surcharge on a \$20 basic prepaid calling plan as would be paid on a \$120 enhanced prepaid calling plan, while further stabilizing the revenues currently being lost for lack of situsing ability.

(b) If prepaid calling plans and arrangements cannot be taxed or surcharged at the point of sale, tax each minute of use using the 9-1-1 location from which the minutes are sent to situs the tax.

(c) Eliminate the state residential tax exemption on communication services, which would make the administration and audit of the CST less burdensome, by further homogenizing the base for both the local and state components of the base.

Option #2: Unbundle franchise fees from the Communications Services Tax and return franchise fees and the administration of franchise agreements to local government. Franchise fees have traditionally been seen as license to do business within a specific jurisdiction for the privilege of providing services for profit for the company using the rights-of-way, and rent for the use of the jurisdiction's rights-of-way, in lieu of the need to contract with each parcel owner along the route where facilities have been placed (be they for electric, gas, communications, chilled water, etc.) Local franchise fees on gross revenues generated through the use of local rights-of-way is a nationwide method of providing a stable revenue stream for use for debt service or other local purpose, and most states other than Florida continue to allow franchise fees for use of rights-of-way by communications service providers, in addition to any other state and local taxes and fees. Franchise fees are simply another expense associated with a particular business model, i.e. the cost of renting rights-of-way for the physical placement of facilities. It is not a cost that satellite providers incur, but neither do cable operators have the same cost structure for technology that satellite providers have. Consequently, returning to the local collection of franchise fees is not violative of the goal of tax neutrality within the industry.

Option #3: Substitute an alternate, stable and revenue-neutral combination of revenue sources to replace the utility tax, franchise fee and permit fee components of the original CST bundle of seven taxes and fees. The alternate revenue stream should be able to be used for any public purpose, from continuing local government operations to public safety expenditures to debt service payments on infrastructure improvements, etc.

Option #4: Provide additional resources for DOR to increase audit capacity, given the complex and time-consuming nature of CST audits. (a) DOR currently has the authority to assess up to 1% of the total revenue generated for all taxing jurisdictions, and the total administrative costs must be prorated among those taxing jurisdictions on the basis of the amount collected for a particular jurisdiction to the total amount collected for all jurisdictions. However, the full assessment is not being spent to support audits for local government CST components. Municipal governments believe that adequate resources should be made available to the Department of Revenue such that they are able to perform the audit functions necessary to maximize revenues and minimize non-compliance. Additionally, if an increase in the 1% allowed by statute is necessary in order to justify additional audit coverage and audit manpower, then we support the 1% be increased.

(b) **Municipal government believes that the definition of "additional resources" should include financial sanctions (such as loss of collection allowance) for communications service dealers who do not comply with due diligence requirements in the assignment and maintenance of customers to local taxing jurisdictions.** Simplification should not mean that communications services providers are allowed to disregard the situsing provisions of Chapter 202, as such tactics merely punish the taxpayers who do not receive the benefit of their taxes, add additional burden to DOR to determine where the

communications service providers customers are located, and relieve service providers of the accountability for the task for which they are paid with collection allowances. Consequently, recent changes made to Chapter 202.22 (5) and (6) should be reversed.

Option #5: Reverse 2012 statutory changes to Chapter 202.11(13) allowing books and records to be used when determining sales price for other than internet access services when non-taxable property or other services are bundled as part of the sale and for which the charge is not separately itemized on a customer's bill. This provision is contrary to how Florida Sales and Use Tax is administered in Chapter 212, thereby increasing the complexity and administrative burden on the Department of Revenue, while adding yet another loophole to diminish the stability of the CST. Communications service providers previously had the option of separately stating charges for taxable and non-taxable items, and could revert back to that ability.

Option #6: Unbundle permit fees from the Communications Services Tax and return permit fees and the administration of permit fees to local government. If franchise fees are unbundled from the CST for local administration, then rights-of-way construction permit fees might also be considered to be unbundled for local administration. The local governments have the responsibility of making sure that construction in the local rights-of-way is done properly and that the construction site is restored to its original condition, for the safety of the traveling public. Permit fees cover the costs to review plans and inspect the work sites. Providers sometimes forget the purpose of construction permits when there is no direct cost associated with them.

Option #7: Municipal government recommends that a working group chaired by the Department of Revenue be convened to draft legislation to implement consensus recommendations. The options above are offered in the spirit of beginning a meaningful dialogue on the difficult issues before the CST Working Group. They are not meant to be exclusive and it is certain that additional new ideas will be identified as the Working Group continues its work. But we believe it is incumbent on all to begin to discuss solutions to the various problems that have been identified to date, and these options are offered to begin the discussion.

Communications Services Tax Working Group

Options for Consideration

Submitted by Working Group Member:

Gary Lindsey

Florida Communications Services Tax Working Group
Submittal of Options for Consideration
Gary S. Lindsey

Introduction

Florida law Section 12 of Chapter 2012-70 charges the Communications Services Tax (CST) Working Group with the responsibility to review data and information about the current Florida CST obtained from the Working Group meetings and material presented by stakeholders and to then identify options for 1) streamlining the administrative system and 2) to identify options that remove competitive advantages within the industry as it relates to the state's tax structure without unduly reducing revenue to local governments. It was decided in the August 21st Working Group meeting that each member of the Working Group would submit his/her own list of options to the Working Group Chair by September 14, 2012. I am therefore submitting my list of options by way of this document.

Summary of Options

I have compiled the following options based on information and ideas from the Working Group meetings, from industry input and from my knowledge and experience in the area of tax policy. These options are listed below and discussed briefly in my analysis that follows.

- Maintain CST "As Is"
- Eliminate CST and Go Back to Traditional State/Local Taxes and Fees
- Eliminate CST and Apply Florida Sales and Use Tax
- Develop a Statewide CST That Applies To All Communications Service
- Address Issue Regarding the Application of CST to Prepaid Communications Services

Communications Services Tax Background and Current Industry Perspective

The 2001 adoption of Florida's CST represented forward looking reform that considered the rapid technological changes, growth, and increased competition that was taking place in the communications arena. This reform removed a myriad of taxes and fees that were linked to the rate based monopoly era in which local governments assessed taxes and fees, and regulated providers were able to recover the cost of local fees that were assessed directly on them through the ratemaking process. As unregulated providers entered the marketplace and as the industry shifted to a competitive model, the monopoly era tax and fee structure that still applied to certain communications services and not to others became highly discriminatory and unfair to customers and providers.

The 2001 CST represented a significant step forward; however the new structure effectively spread the old monopoly era taxes and fees over a broader base of communications services including satellite and wireless. The CST provided a much simpler structure than before for most providers, however there are still many complexities including those related to administering the local component of the tax. The CST was designed to encompass a broader base of services, however many traditional revenue streams that were perhaps considered a given in 2001 are diminishing, while new types of services are introduced constantly that may not necessarily fit into the CST taxation model. The rapid technological changes, growth, and increased competition that was evident in 2001 has only accelerated since that time.

As I consider these issues and ongoing changes, I am hopeful that my submission and analysis will contribute to the Working Group effort to collectively generate new ideas that address these ongoing changes and that can lead to options that are administrable, that can generate adequate governmental revenues and that are fair to the Florida taxpayer.

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(Gary Lindsey – AT&T – 9/14/2012)

Methods of Analysis

It is my opinion that as the Working Group proceeds, each of the options submitted must be evaluated through application of certain assumptions and generally accepted benchmark measures which I list below. Many of these are complimentary to or overlap one another; therefore I am not suggesting a strict “checklist” but instead as items to consider holistically when the Working Group reviews each option.

Functionality – This is an understanding of the particular option’s working characteristics including but not limited to implementation, jurisdictional sourcing, ability to apply the tax to the array of communications services sold by CST providers, compliance (i.e., reporting and remittance by providers), and audit considerations.

Viability – This is an overall assessment of whether the option would have a reasonable chance of succeeding if adopted, including an assessment of attributes and potential problems for the particular option.

Tax Policy – the AICPA provides time-tested benchmarks to evaluate each option by reference to the AICPA’s “Ten Principles of Good Tax Policy” and the AICPA’s “Guiding Principles for Tax Equity and Fairness” Both of these references are listed below.

AICPA Ten Principles of Good Tax Policy:

(http://www.aicpa.org/InterestAreas/Tax/Resources/TaxLegislationPolicy/Advocacy/DownloadableDocuments/Tax_Policy_Concept_Statement_No.1.doc)

1. Equity and Fairness - Similarly situated taxpayers should be taxed similarly.
2. Certainty - The tax rules should clearly specify when the tax is to be paid, how it is to be paid, and how the amount to be paid is to be determined.
3. Convenience of Payment - A tax should be due at a time or in a manner that is most likely to be convenient for the taxpayer.
4. Economy in Collection - The costs to collect a tax should be kept to a minimum for both the government and taxpayers.
5. Simplicity - The tax law should be simple so that taxpayers understand the rules and can comply with them correctly and in a cost-efficient manner.
6. Neutrality - The effect of the tax law on a taxpayer’s decisions as to how to carry out a particular transaction or whether to engage in a transaction should be kept to a minimum.
7. Economic Growth and Efficiency - The tax system should not impede or reduce the productive capacity of the economy.
8. Transparency and Visibility - Taxpayers should know that a tax exists and how and when it is imposed upon them and others.
9. Minimum Tax Gap - A tax should be structured to minimize noncompliance.

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10. Appropriate Government Revenues - The tax system should enable the government to determine how much tax revenue will likely be collected and when.

Streamlining of the Administrative System – options for streamlining should be considered in light of the AICPA’s “Guiding Principles for Tax Simplification”.

AICPA Principles:

(<http://www.aicpa.org/InterestAreas/Tax/Resources/TaxLegislationPolicy/Advocacy/DownloadableDocuments/TPCS%20-%20-%20principles%20for%20tax%20simplification.pdf>)

- Make Simplification a Priority
- Seek Simplest Approaches
- Minimize Compliance Burdens
- Reduce Frequency of Tax Law Change
- Use Consistent Concepts and Definitions
- Consider Administrative Burdens
- Avoid Limited Applicability

Competitive Advantage – I consider this to be any aspect of the taxation that would in and of itself influence or compel a consumer to make a particular purchasing decision. This could be related to the applicability of the tax itself or related to the ability of a provider to administer a characteristic of the tax structure.

Revenue Neutrality – The Working Group Study requires options that do not unduly reduce existing tax revenues to local governments. There may be some options that generate sufficient revenue on a stand-alone basis and there may be options that may require some additional means to hold each local government relatively harmless with regard to revenue impact.

Other Comments

There are certain issues that should also be considered and addressed in any of the options listed above. Some of these issues may be touched upon in my discussion of particular options or may reside within the tax policy benchmarks. I will list these issues below, at the risk of some redundancy, to help ensure that these are considered by the Working Group.

Sourcing/Audit issues - one of the primary challenges of the current CST is to correctly and consistently associate a customer’s address to the appropriate jurisdiction. Providers spend millions of dollars and human resources to have systems in place to accomplish this, and are yet still subjected to detailed audits that require further expenditure of dollars, time and effort of providers as well as the Department of Revenue. Providers are motivated by their taxpayer role and also of equal importance by the need to satisfy their customers by taxing them correctly. This task becomes increasingly complex with annexations, new subdivisions and the mobility of customers. A number of states have moved to a statewide tax in recognition of this growing complexity.

Nexus Issues – there are a growing number of entrants to the Florida marketplace that may have no physical presence in the state and are therefore not required to collect and remit the CST.

Internet Tax Freedom Act (“ITFA”) – may cause issues with taxing of package/bundled marketing plans that include internet service and other services. This may also cause limitations in the ability to tax certain new service offerings that are emerging in the marketplace.

List of CST Options and Comments

Maintain CST “As Is”

This option preserves the status quo. Growth in wireless may offset future landline cord cutting, and local governments may adopt some level of future rate increases to help preserve their tax revenue stream. This option does nothing to eliminate competitive issues or to enhance streamlining of administrative processes. This option also would do nothing with regard to considering the ability to address new and emerging services that may be offered by providers.

Eliminate CST and Go Back to Legacy Taxes and Fees

A question was raised during one of the recent meetings about the possibility of restoring right of way fees or other usage or licensing fees. I cannot envision the viability or the necessity of adding such fees to the existing CST. Such fees would theoretically be applied to services that have some presence in the right of way and would therefore apply to some providers and not others. Therefore I am assuming that this option would also entail disbanding the CST and reverting back to the old tax regime. This would be an unjustifiable step backward that would exacerbate competitive issues, would reintroduce the same complexities that existed prior to 2001, and would most likely not generate any additional tax or fee revenues but would likely result in declining revenues instead. I do not believe this would be a viable option that warrants much, if any consideration. Also, it is important - when reviewing other states that may have a sales tax and local franchise, right of way or other local fees - to note whether these fees apply in addition to the sales tax or in lieu of the sales tax (e.g., a state may apply sales or other communications tax to wireless, and may apply local franchise taxes to landline and/or video programming in lieu of the sales tax).

Eliminate CST and Apply Florida Sales and Use Tax

The 2011 CST is a discriminatory tax on communications services customers when compared to the sales tax that applies to the purchase of other goods and services in Florida. Therefore shifting from the higher CST to the sales tax would create a mathematical challenge to the requirement that local government revenues are not to be unduly impaired. Consideration would therefore have to be given to expanding the sales tax base to additional services outside of the communications services arena. Applying the state and local sales tax would still require local sourcing of communications services, and a statewide DBS tax would also still be required. Despite the challenges noted, this option presents a progressive and direct move from the legacy CST structure to one is fair to Florida taxpayers when compared to the tax that they pay on other goods and services, and that would meet the “Good Tax Policy” criteria presented earlier.

Develop a Statewide CST That Applies To All Communications Service

This option would adopt a statewide CST that would apply to all communications services. The key to this option would be the elimination of any requirement for local sourcing or any local reporting by communications providers when remitting the tax. This would greatly simplify administration and audits and may ultimately allow the Florida address database to be eliminated.

This option would require development of an appropriate state-wide tax that would maintain the existing total tax revenue. It could also include a “hold-harmless” distribution methodology so that local governments would continue to receive their proportionate share of the tax going forward. Consideration could also be given to developing another distribution methodology that would be acceptable to the local governments (e.g., based on population, etc) for further transition and streamlining in the future. This statewide CST platform would result in a uniform communications services tax that would be the same for all Florida communications services consumers. This option would still preserve a higher tax rate on Florida taxpayers than they pay on other goods and service in the state, however one that could be

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(Gary Lindsey – AT&T – 9/14/2012)

reviewed periodically by legislators should they want to consider a path to a more equitable tax rate for consumers of Florida communications services in the future.

Issue – Application of the CST to Prepaid Communications Services

The prepaid product is a retail product that has historically been subjected to the general sales tax in Florida. Failure to update the definition of prepaid communications service has generated an assertion that there is a perceived CST tax gap and therefore would not technically be defined as a tax increase. Florida taxpayers would however ultimately perceive this as a tax increase. The survey information that the DOR has provided to the Working Group indicated that all other states that tax prepaid communications service use the sales tax or other general tax (e.g., Hawaii, etc) that applies to general goods and services. Options for this area are as follows:

A - The option exists for Florida to be an outlier and to assert the CST and to develop further legislation that would explicitly apply the CST to prepaid communications services. Pursuit of this option would result in a higher tax burden on prepaid communications services customers than they currently pay. This burden would be particularly impactful on those prepaid communications services customers who are in lower income levels. This option would also explicitly require retailers to collect the tax, and the Working Group has already received input from the retail industry regarding the issues that they would have in trying to collect a separate tax at the retail point of sale.

B - Another option was mentioned that would create a single statewide flat tax that would apply to prepaid communications services in lieu of the CST, effectively placing the same level of higher tax on this service through the use of a flat dollar amount instead of a percentage. Comments received by the Working Group from retail representatives indicated that large retailers with robust systems might be able to administer such a fee structure however many other retailers may have difficulty in administering a separate fee of this nature. Consideration would have to be given to deciding on the appropriate amount of the fee to meet the objectives of the various stakeholders (e.g., state, local governments, taxpayers, etc). This option would also position Florida as a tax policy “outlier” throughout the U.S. for taxation of this service, and would also place a regressive burden on low income prepaid communications services consumers.

C - Another viable option is to recommend adoption of an updated definition of prepaid communications services (e.g., the Streamlined Sales Tax definition, etc) so that these services would continue to be subject to (only) the state and local sales tax. Consistent with comments that I made earlier with regard to the sales tax, this option would ensure that Florida communications services consumers are not burdened with a higher tax than they pay on other goods and services in Florida. This option requires no change in methodology for retailers or providers and it maintains the existing actual revenue stream that Florida receives through the state and local sales tax.

Conclusion/Summary

This completes my review and comments regarding options for this phase of the Working Group effort. I am hopeful that the options and guidelines that I have provided will be helpful to the overall effort as the Working Group considers all of the options submitted by Working Group members and other stakeholders.

Communications Services Tax Working Group

Options for Consideration

Submitted by Working Group Member:

Mayor Gary Resnick



City of Wilton Manors

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Gary Resnick
Mayor

Tom Green
Vice Mayor

Julie A. Carson
Commissioner

Ted Galatis
Commissioner

Scott Newton
Commissioner

Joseph L. Gallegos
City Manager

Kerry Ezrol
City Attorney

September 14, 2012

Via Electronic Mail

Andrea J. Moreland
Director, Legislative and Cabinet Services
Florida Department of Revenue
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Re: Request for Options

Dear Ms. Moreland:

This is in response to Chair Stranburg's request that members of the Communications Services Tax (CST) Workgroup submit options for the Workgroup to include for Legislative consideration by September 14. The options listed below follow the Workgroup's tasks as set forth in the Statute.

Sections 12(4)(a) and (b) of the Statute provide for the Workgroup to review national and state policies relating to communications taxes and to review the effects of Florida law on the decline in CST revenues, respectively. As information provided to the Workgroup has revealed, every state other than Florida allows local governments to charge users of the rights-of-way reasonable fees to support local governments' costs associated with management of their public rights-of-way. The federal government also charges fees for using its rights-of-way. We have not had information presented to us as to whether the State of Florida charges fees for use of the State's rights-of-way. One of the replaced revenue sources that the local CST was supposed to be sufficient to cover was franchise fees for use of public rights-of-way by communications providers. As we learned, CST revenues to local governments have declined sharply. Accordingly, the Workgroup should include as one of the options for the Legislature to consider, reinstating local governments' ability to charge franchise fees to communications providers that use their public rights-of-way. Even states that have adopted state-wide franchising of cable services, similar to Florida, allow local governments to charge cable franchise fees and to collect such fees directly for use of their rights-of-way. Such fees would be easy to administer by providers as well as governments, easily understood by consumers and would not require any involvement of DOR or create further administrative issues. DOR should be able to estimate based on historic data the amount of revenue this would generate for local governments. Similarly, the Workgroup should also include

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Director, Legislative and Cabinet Services
Florida Department of Revenue
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that the Legislature should consider restoring local governments' ability to charge permit fees, without reducing CST rates, to communications providers that apply for permits to perform work in the rights-of-way. Permitting functions often involve complicated and costly reviews by local governments and the local CST structure, as it currently exists, is not sufficient to cover such permitting costs.

Section 12(4)(c) of the Statute provides for the Workgroup to review the extent local governments have bonded CST revenues. As presentations to the Workgroup have revealed, most local governments have bonded their CST revenues. Going forward, significant infrastructure and capital projects that will be vital for Florida's economic recovery require that local governments retain their full bonding capacity with CST revenues, which is one of very few unrestricted sources of revenues for any public purpose. Accordingly, the Workgroup should include as an option for the Legislature's consideration that it adopt a policy expressly preserving that local CST revenue may be used by local governments for any public purpose and that any revisions to the CST Statute must ensure that there are no negative financial impacts to local governments.

Section 12(4)(d) of the Statute provides for the Workgroup to review the fairness and administrative burdens of the CST, and the extent the CST is reasonably clear to stakeholders and (e) provides for the workgroup to provide options for streamlining administrative burdens. Based on the presentations to the Workgroup, it does not appear that the CST creates any unfairness or that providers, retailers, consumers, governments and DOR do not have a reasonably clear understanding of the CST. It may be helpful for the Legislature to consider requiring that certain charges by providers on various bills must be clarified as to whether they are a government-imposed fee or tax or not. Further, based on information presented to the Workgroup, the Workgroup should include as one of its options for the Legislature's consideration that the Legislature adopt more strict and definite laws regarding auditing of the CST. DOR presented information that it has the capability of auditing only a small percentage of communications providers, that it does not use contract auditors, and that the vast majority of audits – over 75% -- result in recovery of revenues. Further, DOR did not provide information to the Workgroup as to how it addresses communications providers that should be filing returns and paying CST but do not. Prior to the replaced revenue sources being centrally administered by DOR, local governments were very effective at conducting audits, often utilizing outside auditors with expertise in the industry, with the costs of such audits being borne by the provider if underpayments exceeded a certain percentage. Accordingly, the Workgroup should include that the Legislature should consider mandating

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more audits, requiring DOR to contract for external auditing services, allowing local governments to conduct and to contract for external audits, and requiring that providers pay for the cost of the audit if underpayments exceed a certain percentage. Such policies will not only lead to increased revenues for the State and local governments by ensuring more accurate reporting and collection of CST revenue, they will also reduce the burden and cost of administering the CST.

Section 12(4)(f) of the Statute provides for the Workgroup to identify options that remove competitive advantages within the industry as to the state's tax structure without unduly reducing revenue to local governments. We have had much discussion about the intent of this subsection without reaching any consensus. We discussed to some extent advantages that Internet retailers enjoy over brick and mortar retailers with respect to sales taxes. Consumers alter buying decisions and make purchases over the Internet solely to avoid state sales taxes. Accordingly, to address competitive advantages enjoyed by Internet retailers, the Workgroup should include as an option that the Legislature consider revising the state's tax structure and impose sales taxes on Internet retailers. We have had no presentations that particular segments of the communications industry enjoy a competitive advantage over others by virtue of the state's tax structure. Information provided to the Workgroup indicates that by far, the fastest growing segments of the industry are wireless services generally and in particular prepaid wireless services. The information provided to us indicates that consumers are abandoning landline telephones and utilizing wireless services. Accordingly, options the Workgroup should propose for the Legislature are: 1) eliminate the residential exception from CST and 2) impose a surcharge on prepaid wireless services to add to the state's tax structure. In addition, so as not to reduce unduly CST to local governments from such services, the Workgroup should include that the Legislature should consider requiring consumers of prepaid services, at the time of purchase, to identify the user and address where such services will be used to allow providers to properly and to determine easily the situs of such local CST. Given the importance of knowing who is utilizing communications services and where, there are numerous other public policy benefits of having such information apart from the state's tax policies.

In addition to the options for the Legislature's consideration as outlined above, it is important to note issues with our process for producing a report to the Legislature. It is troubling that after several meetings, the Workgroup has not established a process for producing a report to the Legislature. The Statute clearly provides for the Workgroup to prepare and to submit a report; it does not provide for DOR to do so. Further, the Statute clearly contemplates the Workgroup

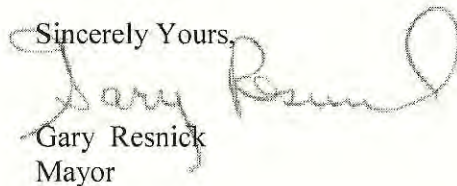
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voting. Having every Workgroup member's options included in a report prepared by DOR would not be consistent with the Statute and may also be a violation of the Sunshine Law, particularly if members of the Workgroup engage in communications with DOR staff. For example, it would be a violation of the Sunshine Law for the Interim Executive Director of DOR to instruct DOR staff on how to prepare a report or what content to include in any report since, as a member of the Workgroup, such person is bound by the Sunshine Law, unless of course such communications occurred during one of our noticed meetings. The better process would be for the Workgroup to debate information to be included in a report, and ultimately to vote on how to prepare a report and what to include in a report to be issued by the Workgroup. A member of the Workgroup may volunteer to compile such report or alternatively, we could vote on what to instruct DOR to prepare. To do otherwise, would be a disservice to the State's taxpayers.

Thank you for providing this to members of the Workgroup. As always, I appreciate your assistance.

Sincerely Yours,



Gary Resnick
Mayor

Communications Services Tax Working Group

Options for Consideration

Submitted by Working Group Member:

Brian Smith

DIRECTV's Comments to the Communications Services Tax Force

As you are aware, the task force's mission includes the following:

- a) review of national and state tax policies relating to the communications industry;
- b) review the historical amount of tax revenue that has been generated by the state and local communications services taxes imposed or administered pursuant to Chapter 202, Florida Statutes, for the purposes of determining the effect that laws passed in the past 5 years have had on declining revenues;
- c) review the extent to which this revenue has been relied on to secure bonded indebtedness;
- d) review the fairness of the state's communications tax laws and the administrative burdens it contains, including whether the applicability of the tax laws is reasonably clear to communications services providers, retailers, customers, local government entities and state administrators;
- e) identify options for streamlining the administrative system; and
- f) identify options that remove competitive advantages within the industry as it relates to the state's tax structure without unduly reducing revenue to local governments.

With this in mind, the goals of any reform should be revenue neutrality and creating a favorable business climate.

The current differences in taxation based on method of content delivery has resulted in uncertain revenues for the State. This uncertainty is due, in large part to;

- (1) changing customer patterns with respect to the consumption of media and the use of communications services, and
- (2) the increasing use of business strategies to minimize the tax burden.

Any reform should start with an expansion of the tax base and the creation of a level playing field for all communication providers. This will ensure that the tax burden imposed on the customer will remain the same regardless of the manner in which content is consumed. By way of example, a family in Gainesville should be subject to the same exact tax burden when it watches a TV show or movie on DIRECTV or DISH as a family in Jacksonville who watches the same TV show on Comcast, BrightHouse, or Cox. And both families should be subject to the same tax burden as a family who watches the same show or movie via the Internet, whether it's through Netflix, Amazon, or Apple TV. Similarly, an expansion of the tax base should result in no differentiation between bundled and unbundled services (separately stated movie rentals should be taxed the same as flat-fee rentals).

To the extent the tax base is expanded, there should be an offsetting reduction to the state tax rate in order to achieve revenue neutrality and restore competitive balance between cable and satellite TV providers. As an initial matter, the rates applicable to communications services should be uniform at the state and local level, regardless of technology. We recommend setting the local rate at the highest current local rate to address the needs of the local government for revenue. This would also promote simplicity in compliance since there would only be one local rate for all localities in the state. Furthermore, the Task Force should consider whether the localities should be entitled to payment for the actual and direct use of their right of ways. The uniform rates would provide simplification for retailers (selling prepaid and other taxable items), local governments estimating revenue streams, persons estimating revenue streams for bonding, certainty of collecting and remitting and ease of audit and administration for the Department.

These suggestions will have the additional impact of achieving a favorable business climate. Any uncertainty regarding the taxation of different types of communications services would be removed. Furthermore, a single tax base and single rate would ensure ease of administration and that the tax base was not subject to manipulation (creating competitive advantages amongst industry members).

Communications Services Tax Working Group

Options for Consideration

Submitted by Working Group Member:

Marshall Stranburg

Florida Department of Revenue

Options Submitted to Communications Services Tax Working Group

A. Options to Streamline the Administrative System

1. Rate Structure Changes
 - a. Create a statewide Local Communications Services Tax rate and distribute the tax to local governments via a formula. In addition, consideration may wish to be given to restructuring the collection allowance since administrative burdens will be reduced.
 - b. Create one Local Communications Services Tax rate per county and distribute the tax to the local governments via a formula. In addition, consideration may wish to be given to restructuring the collection allowance since administrative burdens will be reduced.
2. Records
 - a. Clarify the definition of records and which records must be kept by providers.
 - b. Facilitate the audit process for both providers and the Department by requiring that records be provided in a format that is capable of being exported to the Department as a searchable file.
3. Transparency
 - a. Specify the consequences that will result when customers are not provided with a breakdown of the Florida Communications Services Tax (combined state and gross receipts tax) and Local Communications Services Tax.
 - b. Allow providers to further breakdown the Florida Communications Services Tax into state and gross receipts tax, if desired, on customer bills.
 - c. Allow the Department to release the provider's contact person's name and contact information and/or managerial representative's name and contact information to its customers who have tax questions or complaints, including jurisdictional situsing issues.
 - d. Create a requirement that, when requested by customers or the Department, providers must provide a breakdown of bundled services including a description of the service, amount taxed, tax rate applied, and the period of time the rate applies. Provide a penalty for non-compliance.
 - e. If a breakdown of bundled services is not given to the customer, use tax on the entire amount will be due from the customer as provided by current law. Clarify use tax provision such that customers who request unbundling breakdown in writing from provider, but do not receive it within 30 days may use their own reasonable breakdown in order to calculate use tax.
 - f. Create an incentive for providers to notify customers and the Department of the breakdown of bundled services. For companies that provide advance notice of their unbundling practices to the Department, allow them to use a managed compliance agreement for an agreed upon time period.
4. Refunds
 - a. Amend the refund statute (s. 202.23, F.S.) to allow the local component of the Communications Services Tax that exceeds 90% of the local jurisdiction's average monthly distribution to be refunded to the dealer and recaptured from the local government on a pro-rated basis over a time period that equals the period covered by the refund.

B. Options to Remove Competitive Advantages within the Industry as it relates to the State's Tax Structure without Unduly Reducing Revenue to Local Governments

1. Tax Base
 - a. Revise the sales tax base to include a definition for digital goods. These goods and associated services have historically been sold in tangible form, but in recent years are increasingly migrating to electronic delivery. Examples of such products are music, videos, and books.
 - b. Clarify that the definition of video service includes payments for licensure of content.
 - c. Clarify that the residential exemption only applies to landline telephone service.

2. Prepaid Wireless Services
 - a. Create a flat Communications Services Tax rate and distribute to local governments via a formula.
 - b. Apply sales and use tax and a fee for gross receipts tax. The gross receipts tax fee could be a flat fee by dollar amount or a percentage, or a tiered amount based on dollars or time.
 - c. Consider a gross receipts tax on the provider of prepaid calling arrangements that can be offset with a dollar-for-dollar credit, if communications services tax is collected from the purchaser of the prepaid calling arrangement.

Communications Services Tax Working Group

Written Comments

Submitted by: Florida Retail Federation



September 17, 2012

Marshall Stranburg
Interim Executive Director
Florida Department of Revenue
5050 West Tennessee Street
Tallahassee, FL 32399-0100

Dear Mr. Stranburg:

On behalf of the 8,000 members of the Florida Retail Federation, we appreciate the opportunity to provide written comments to the Communications Service Tax Work Group regarding the imposition and collection of the Communications Service Tax on certain prepaid calling arrangements that the Department of Revenue has indicated may not be entitled to the exemption from the collection of Communications Service Tax contained in Sec. 202.11(9), FS.

As you are aware, prepaid calling arrangements are very popular with a large segment of the public at large and are sold at thousands of locations throughout Florida. Currently, retailers are collecting the state and local sales taxes on the sale of these products at the point of sale, as required by Chapter 212, FS. Any determination by the Department that certain prepaid calling arrangements are not included in the exemption referenced above will cause extreme confusion among retailers and result in possible disruption in the sales of these products in the future because the Communications Service Tax, with its complicated provisions, cannot be applied at the point of sale by any retailer in this state.

We encourage the work group to continue with its work and would hope that during the deliberations other collection methodologies would be discussed, since the "Point of Sale" methodology will not work with a tax that is as complicated as the Communications Service Tax. The Florida Retail Federation stands ready to assist in vetting any proposals that may evolve from the work of the work group.

Sincerely,

Randy Miller
Executive Vice President

RM/sw

Communications Services Tax Working Group

Written Comments

Submitted by:

AT&T, CenturyLink, Sprint, T-Mobile, and Verizon

Telecommunications Industry Proposal to the Florida Communications Services Tax Working Group

Submitted by: AT&T, CenturyLink, Sprint, T-Mobile, and Verizon

Overview

The average Florida Communications Services Tax (CST) rates on consumers are more than twice as high as the sales tax imposed on other taxable goods and services sold in Florida. At the same time, changes in technology are providing consumers with alternatives to traditional communications services that allow consumers to avoid paying the CST.

This system is not sustainable. Under the status quo, state and local governments will experience revenue declines as discriminatory tax policy, technological change, and consumer preferences continue to undermine the CST base by shifting consumer purchases to services not subject to the CST.

The telecommunications providers listed above recommend that the state repeal the CST and bring all communications services under the state and local sales tax. This proposal would promote competitive neutrality between communications providers, resolve the current dispute over the taxation of prepaid wireless service, and reduce excessive tax burdens on consumers.

The Problem

The Florida CST was enacted to simplify and reduce the number of state and local taxes on communications providers and consumers. However, technological changes and limitations imposed by federal law continue to undermine the CST base. As the presentation by AT&T at the August 21st commission meeting explained in great detail, many services are increasingly being provided as applications that “ride” over a high-speed Internet connection. As communications providers upgrade their landline and wireless networks to accommodate higher speeds and higher volumes of data, the capability to provide these enhanced communications services via Internet protocol will grow dramatically.

Instead of purchasing a monthly calling plan, consumers will purchase a fast Internet connection and install applications that provide voice, video, and other services. This will occur in both the wireless and wireline environment. Widespread availability of these “over the top” Internet-enabled services will undermine the CST base in two ways: 1) consumers will continue to drop services subject to CST altogether and install communications applications instead; and 2) competitive pressures from these Internet-based applications will force traditional

communications services providers to lower prices, reducing revenues from percentage-based taxes.

Additionally, federal law prohibits state and local governments from imposing taxes on charges for Internet access service. Therefore, state and local governments will not be able to capture revenues from this shift in technology and consumer preferences. Compounding this problem is the current CST rate structure. All else being equal, a customer switching to an Internet-protocol based communications application will save an average of 14% simply by avoiding services subject to the CST. The existence of the CST will reinforce and exacerbate market forces leading consumers to adopt new technology.

The Solution: Repeal the CST and Impose the Sales and Use Tax on Communications

The industry recommends that the CST be repealed and the sales and use tax base be broadened to include a broad range of communications services that would be subject to the same state and local tax rates as other taxable goods and services. This proposal would solve many of the problems inherent with the current CST structure and position Florida to fairly capture revenue from a broad base of communications services today and in the future.

First of all, this proposal would significantly reduce or eliminate the tax differential between different types of communications services. It would bring taxation of contract wireless plans in line with the current taxation of prepaid calling arrangements under the sales tax at the point-of-sale. Additionally, when Congress passes the Main Street Fairness Act or other similar legislation to permit states to require non-nexus providers to collect sales taxes, Florida would be positioned to collect sales tax equitably. This would place all providers on a level playing field, an important benefit of eliminating the CST in favor of the sales tax. All of the bills currently being considered by Congress to grant state the power to enforce collection on non-nexus sellers would only apply that power to the sales tax, not to other taxes like the Florida CST.

Second, this proposal would dramatically reduce administrative costs for the Florida Department of Revenue and local governments. Instead of an entire structure necessary to administer the CST as a stand-alone tax, our proposal would allow the department to administer the tax under the existing sales and use tax administrative structure.

Finally, the proposal brings fairness and relief to Florida consumers. Federal and state policies have long sought to make sure that all Americans are connected, first through basic telephone service and now through high speed Internet connections (wireline and wireless). Numerous studies show that low- and moderate-income Americans increasingly rely on their

Internet connections to successfully participate in the American economy, whether on the job or even to search for a job. Tax policies that impose excessive tax burdens on communications services work at cross purposes with federal, state, and local economic development goals. Repealing the regressive CST will most benefit low- and moderate-income Floridians.

Prepaid Wireless Telecommunications Services

The industry proposal to eliminate the CST would render moot the current effort by the Department of Revenue to assert that most current prepaid service offerings, including prepaid wireless service offerings, are subject to the CST. Regardless of what the Communications Services Tax Working Group recommends for long term changes to the CST, it is imperative that the current dispute over the status of prepaid wireless service be resolved immediately.

In excluding prepaid calling arrangements from the CST and making such services subject to the sales tax at the point of sale, the Legislature has long recognized that it is simply not feasible to impose the CST on services that are not billed to customers. There is no workable method to situs prepaid transactions to a customer address because address information is not collected in the majority of prepaid transactions. If the State were to require that retailers collect the CST at the point of sale, all Florida retailers that sell prepaid service would be required to collect customer address information and install a parallel CST point-of-sale tax system with hundreds of local CST tax rates alongside their current sales tax systems. This would be a significant expense for retailers and would require additional CST audits on thousands of retail establishments.

Thus, if CST is not eliminated, the industry recommends that the Legislature modernize the definition of "Prepaid Calling Arrangement" to accommodate technological changes that have occurred over the last decade, and encompass current prepaid service offerings. Such a change would conform the Florida Statutes to the original legislative intent of limiting the CST to billed services -- for which it is feasible to collect local CST based on customer addresses.