

# SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: Communications and Public Utilities Committee

BILL: CS/SB 2070

SPONSOR: Communications & Public Utilities and Senator Constantine

SUBJECT: Tax/Substitute Communications Systems

DATE: April 12, 2005                      REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Halloran/Wiehle	Caldwell	CU	<b>Fav/CS</b>
2.	_____	_____	CA	_____
3.	_____	_____	GE	_____
4.	_____	_____	WM	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

**I. Summary:**

The bill provides that taxes on substitute communications systems are not to be levied or assessed during specified time periods; creates a task force to study the implications of emerging technologies on Florida’s communication service tax; and provides for access by the Department of Revenue to communications services companies’ books and records to properly assess taxes.

The bill substantially amends sections 202.11, 202.26, 212.02, and 212.13 of the Florida Statutes.

**II. Present Situation:**

In 1985, the Legislature added a substitute telephone or telecommunication system to the list of services subject to gross receipts and sales tax. At that time, most of the communications services available today did not exist. Ch. 85-174, Laws of Florida, provided:

Any person who purchases, installs, rents, or leases a telephone system or telecommunications system for his own use to provide himself with telephone service or telecommunication service which is wholly or partially independent of any local telephone system or any intrastate or interstate interexchange network or which is a substitute for any telephone company switched service or a substitute for any dedicated facility by which a telephone company provides a communications path is exercising a taxable privilege. . . .

The Legislature substantially rewrote Florida’s communications tax law in the 2000 Regular Session. Chapter 202, Florida Statutes, creates the Communications Services Tax Simplification Law (CST) which became effective January 1, 2002. The new CST was meant to replace the old tax structure with a simplified and revenue-neutral new tax statute. Communications services are

now subject to a uniform statewide tax rate and a local tax administered by the Department of Revenue (DOR).

Since the rewrite was so substantial, many of the details were not discussed individually in committee or in floor debate. The language in chapter 202, F.S., concerning substitute communications services was among the details not discussed, except in regards to changing the term “telephone service or telecommunication service” to the conforming term “communications service.” Presently, the term “substitute communications system” is defined in s. 202.11(16), F.S., to mean:

Any telephone system, or other system capable of providing communications services, which a person purchases, installs, rents or leases for his or her own use to provide himself or herself with services used as a substitute for any switched service or dedicated facility by which a dealer of communications services provides a communication path.

The original intent of taxing substitute telephone service or telecommunications services was to provide equal tax treatment on an in-house telephone system and telephone service purchased from a commercial provider. Prior to 2002, communications services were subject to the following taxes: gross receipts tax, state sales and use tax, local sales and use tax, and municipal utility tax. Each of these taxes had a different base, and the revenue raised by each tax was used for different purposes. Today, there is uncertainty as to the proper interpretation of a “substitute communications system.”

To address that uncertainty, the DOR issued a draft rule, 12A-19.036 on substitute communications systems to initiate discussion of this issue. A public workshop was held on August 1, 2003. At the workshop, many members of the business community expressed concern that the DOR’s interpretation of the term was too broad. Of particular concern was an example in the proposed rule that found that a taxpayer operating a local area network (LAN) to connect multiple computers was operating a substitute communications system. The department has not taken further steps in the rulemaking process for this rule. Examples of taxable substitute communications services from the DOR’s draft rule include:

- A telephone system with switching and routing capabilities allowing for intercom and other self-contained communications at the taxpayer’s facility.
- A computer local area network (LAN) system that uses a router to provide switching capabilities necessary to connect the multiple computers used by the taxpayer’s employees.
- A wireless dispatch system that transmits and switches voice or data signals to provide a communications path between and among remote receivers and a central base station.
- Telephone transmission and receiving equipment located at various sites where the owner does business which include a tower for the purpose of providing communications services between those sites in lieu of using a local exchange provider and long distance provider.
- A system to transmit, route, and switch data to permit monitoring the activities and operations of manufacturing equipment, pipelines, rail systems, or utilities.
- A small business with five computers each connected to a central router that allows the computers to share printers, files and documents, and other business related activities.

- A two-way mobile radio system that includes a base station, central tower used for signal switching, and several mobile radio units and for which the company does not buy airtime or switching services from a provider.

DOR states that each of these examples fit the definition of a substitute communications system. (Home users of local area networks would not be taxable since the tax liability is based on depreciation and allocation of other business costs not typically incurred in residential households.)

Generally, both the sales tax and the communications services tax attempt to create an equal tax situation between businesses that buy its goods or services from another and businesses that create the goods or services in-house. Taxing substitutes is generally viewed as a tax fairness issue rather than simply a way to raise additional revenue. According to the DOR, however, defining and valuing a substitute communications service is more difficult than defining and valuing a service that is purchased from another entity.

The substitute communications concept has been in statute since 1985, but has not been defined or examined in light of the switch to a tax on communications services. DOR reports that less than five companies presently pay taxes on substitute communications systems. DOR states it has not actively enforced the measure, but at the request of local governments, it will ultimately have to implement and enforce taxation of substitute communications systems.

### **III. Effect of Proposed Changes:**

Section 1 of the bill provides that the taxes on a substitute communications system that are provided for in ss. 202.12(1) (sales of communications services), 202.19(7) (local communications services tax), 202.15 (purchase, installation, rental, or lease of a substitute communications system), or 203.01 (gross receipts tax), F.S., are not to be levied during the period of from the bill's effective date (upon becoming law) through October 31, 2007. Additionally, the Department of Revenue is not to assess a tax on a substitute communications system for the period October 1, 2001, through the bill's effective date.

Section 2 creates a task force to review and evaluate existing national and state regulatory and tax policies relating to the communications industry and make recommendations to the Legislature concerning the scope of communications services that should be subject to the communications service tax.

The task force is to consist of nine members, three appointed by the Governor, three appointed by the Senate President, and three appointed by the Speaker of the House. Any non-legislative member is to have expertise in state or national telecommunications policy, taxation, law, or technology. Members serve at the pleasure of the appointing official and any vacancy is to be filled in the same manner as the original appointment. Members serve without compensation but are entitled to per diem and travel.

The task force is to be housed for administrative purposes within the Department of Revenue. The department is to provide staff for tax issues and the Public Service Commission is to provide staff for technical and regulatory issues.

The task force is to hold its organizational meeting by July 15, 2005. It is to report its findings to the Governor, the Senate President, and the Speaker of the House by January 15, 2006. It is to dissolve by June 30, 2007.

Section 3-6 provide for access by the Department of Revenue to communications services companies' books and records to properly assess taxes.

Section 7 provides that the bill takes effect upon becoming law.

#### **IV. Constitutional Issues:**

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

#### **V. Economic Impact and Fiscal Note:**

A. Tax/Fee Issues:

According to DOR, approximately \$300,000 of revenue is currently collected annually from the tax on substitute communication systems, which will not be collected if this bill passes. The loss will be split among PECO, General Revenue, and local revenue.

B. Private Sector Impact:

Less than five businesses will not be required to pay approximately \$300,000 annually in substitute communications systems taxes.

Taxpayers who may be subject to the tax, but who have never remitted the tax, will be relieved of any past and future liability for the tax.

C. Government Sector Impact:

According to the Revenue Estimating Conference, there would be a decrease in state revenues of at least \$300,000 and a decrease in local revenues of at least \$100,000.

#### **VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

None.

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This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.

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## **VIII. Summary of Amendments:**

None.

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