The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

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

Prepared By: The Professional Staff of the Appropriations Subcommittee on Finance and Tax

BILL: SB 712

INTRODUCER: Senator Galvano and others

SUBJECT: Taxes on Prepaid Calling Arrangements

DATE: April 2, 2014 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Wiehle	Caldwell	CU	**Favorable**
2.	Cote	Diez-Arguelles	AFT	**Favorable**
3.			AP	

I. Summary:

SB 712 revises the definition of "prepaid calling arrangement" in chapter 202, F.S., relating to the Communication Services Tax and chapter 212. F.S., relating to the sales tax, to include mobile communications services that meet specified conditions. The bill expands the definition of "prepaid calling arrangement" to include prepaid communication services other than those that consist exclusively of telephone calls, and provides that the purchaser of prepaid units may use the units to purchase communication services other than mobile communication services, if the other services are provided to or through the same handset or other electronic device the purchaser uses to access mobile communication services.

The changes made by the bill are intended to be remedial in nature and apply retroactively, but do not provide a basis for an assessment of any tax not paid or create a right to a refund or credit of any tax paid before the effective date, July 1, 2014.

The Revenue Estimating Conference estimated that this bill will have a zero cash impact in Fiscal Year 2014-2015, with the following recurring, negative impacts: General Revenue Fund ($1.4 million), Public Education Capital Outlay Trust Fund ($5.7 million), and local governments ($11.2 million). Additional losses of an indeterminate amount may occur due to the purchase, on a prepaid basis, of other communication services through the same handset or other electronic device that is used by the purchaser to access mobile communication services. See Section V. of this analysis for additional information regarding the fiscal impact of the bill.

The mandates constitutional provision may apply to this bill, requiring a two-thirds vote of the membership of each house for passage. See Section IV.A. of the analysis.

II. Present Situation:

Communications Services Tax

Chapter 202, F.S., provides for a tax on communication services, including telecommunications, cable, direct-to-home satellite and related services. The communications services tax includes a state tax rate of 6.65 percent and a state gross receipts tax rate of 2.52 percent for a combined rate of 9.17 percent.[1] In addition, local governments may impose a local tax rate of up to 7.12 percent.[2] The statewide, total average tax rate is approximately 14.21 percent.

A portion of the state taxes collected – including taxes collected on direct-to-home satellite service – are deposited into the General Revenue Fund and a portion is distributed to local governments.[3] Gross receipts tax collections are deposited into the Public Education Capital Outlay and Debt Service Trust Fund and are used to fund public schools', community colleges', and universities' capital projects.

Prepaid Calling Arrangement

The communication services tax (CST) is applied to the sales price of each communications service which originates and terminates in this state, or originates or terminates in this state and is charged to a service address in this state.[4] However, the definition of the term "sales price" expressly excludes the "sale or recharge of a prepaid calling arrangement," so CST is not collected on the sale of a prepaid calling arrangement. [5]

The term "prepaid calling arrangement" is defined to mean "the separately stated retail sale by advance payment of communications services that consist exclusively of telephone calls originated by using an access number, authorization code, or other means that may be manually, electronically, or otherwise entered and that are sold in predetermined units or dollars of which the number declines with use in a known amount."[6]

Chapter 212, F.S., provides for the application of the sales tax to the sale of tangible personal property and some services. The sales tax rate of 6 percent is applicable to charges for prepaid calling arrangements.[7] The term "prepaid calling arrangement" as defined in ch. 212, F.S., means "the separately stated retail sale by advance payment of communications services that consist exclusively of telephone calls originated by using an access number, authorization code, or other means that may be manually, electronically, or otherwise entered and that are sold in predetermined units or dollars whose number declines with use in a known amount."[8] The

[1] See ss. 202.12(1)(a) and 203.01(1)(b), F.S. The gross receipts tax is 2.37 percent, plus an additional 0.15 percent for certain services. Direct-to-home satellite is taxed at a rate of 10.8 percent and is also subject to the 2.37 percent gross receipts tax. The local tax does not apply to these services.
[2] Section 202.19, F.S.
[3] Section 202.18, F.S.
[4] Section 202.12, F.S.
[5] Section 202.11(13)(b)4., F.S.
[6] Section 202.11(9), F.S.
[7] Section 212.05(1)(e)1., F.S.
[8] *Id*.

definition of “prepaid calling arrangement” in ch. 202, F.S. is virtually identical to the definition in ch. 212, F.S.

When the definition of prepaid calling arrangement was placed in the statute[9], prepaid calling arrangements typically consisted of prepaid calling cards purchased in advance and limited to telephone calls. However, since then the telecommunications industry has developed to offer more prepaid plans compatible with the texting, data, video, and other capabilities of today’s modern smartphones. This has led to increased utilization of prepaid mobile services. As markets and technology have evolved, the statutory definition has become increasingly incompatible and inconsistent with industry practice and the ability to collect communication services taxes.

As technology evolved, most communications service providers and other prepaid phone retailers continued to apply the sales tax to all prepaid mobile phone plans, even though the plans did not meet the strict definition of a “prepaid calling arrangement.” This practice continues today for all prepaid plans.

DOR Tax Information Publication on Prepaid Communications Services

In March of 2012, DOR issued Tax Information Publication (TIP) No. 12ADM-02 to provide clarification regarding the application of Florida taxes to sales of certain prepaid communications plans and services.[10] The TIP stated that certain prepaid communications plans or services are not "prepaid calling arrangements." It continued:

> Examples of such plans that do not fall under this definition include, but are not limited to:
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> - service that includes text messaging, multimedia messaging, web, e-mail, etc.;
> - unlimited calling plans that do *not* decline with usage;
> - services or plans that are *not* sold in predetermined units or dollars; or
> - services or plans that are *not* originated using an access number or authorization code.[11]

The TIP concluded that a “sale of a prepaid card or prepaid arrangement that does not fall under the strict definition of a "prepaid calling arrangement" is not subject to sales tax. Instead, sales of such plans are subject to CST.[12]

The TIP was retracted on July 29, 2013, after DOR received a notice contesting the TIP as an un-promulgated rule. Currently, DOR is in the rule development process.

In summary, the current statutory provisions seem to require the conclusion that sales of prepaid calling plans or services that meet the **strict** definition of a “prepaid calling arrangement” are

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[9] Chapter 2000-260, Laws of Florida.
[10] Florida Department of Revenue, *Prepaid Communications Services,* TIP No. 12ADM-02 (March 27,2012) *available at* http://dor.myflorida.com/dor/tips/tip12adm-02.html.
[11] *Id*. Emphasis in the original.
[12] *Id.*

subject to the state sales tax (6 percent) and local discretionary sales surtaxes, and that sales of plans that do not meet the strict definition are subject to the state CST (6.65 percent), gross receipts tax (2.52) and the local CST (variable rate) applicable to other communication services.

Communications service providers do not agree with this conclusion and argue that the prepaid mobile phone plans being sold today are subject only to the state sales tax and local discretionary sales surtaxes.

III. Effect of Proposed Changes:

Section 1 amends subsection 202.11(9), F.S., to revise the definition of the term “prepaid calling arrangement.” For other than mobile communications services, the term includes a right to use communications services “for which a separately stated price must be paid in advance, which is sold at retail in predetermined units that decline in number with use on a predetermined basis, and which consists exclusively of telephone calls originated by using an access number, authorization code, or other means that may be manually, electronically, or otherwise entered.”

For mobile communications services, the term includes “a right to use mobile communications services that must be paid for in advance and is sold at retail in predetermined units that expire or decline in number on a predetermined basis if:

1. The purchaser’s right to use mobile communications services terminates upon all purchased units expiring or being exhausted unless the purchaser pays for additional units;
2. The purchaser is not required to purchase additional units; and
3. Any right of the purchaser to use units to obtain communications services other than mobile communications services is limited to services that are provided to or through the same handset or other electronic device that is used by the purchaser to access mobile communications services.”

Predetermined units may be quantified as amounts of usage, time, money, or a combination of these or other means of measurement.

The bill expands the definition of “prepaid calling arrangement” to include prepaid communication services other than those that consist exclusively of telephone calls. The changes recognize that under current industry practices prepaid services may include services other than telephone calls, such as text messaging, web access, and email.

In addition, the bill provides that the purchaser of prepaid units may use the units to purchase other communication services other than mobile communication services if the other services are provided to or through the same handset or other electronic device the purchaser uses to access mobile communication services. This provision may result in communication services currently subject to CST tax rates being subject to only sales tax in the future if they are sold as part of a prepaid calling arrangement.

Section 2 amends paragraph 212.05(1)(e), F.S., to define the term “prepaid calling arrangement” to have the same meaning as provided for in s. 202.11, F.S.

The bill also provides that if a purchaser of a prepaid calling arrangement has paid sales tax on the sale or recharge of such arrangement, no additional sales tax or CST tax is due or payable if the purchaser applies one or more units of the prepaid calling arrangement to obtain communications services that are provided to or through the same handset or other electronic device that is used by the purchaser to access mobile communications services, other services that are not communications services, or products.

Section 3 provides that the amendments made by the bill are intended to be remedial in nature and apply retroactively, but do not provide a basis for an assessment of any tax not paid or create a right to a refund or credit of any tax paid before the effective date of this act.

Section 4 provides that, except as otherwise expressly provided in section 3, the bill takes effect July 1, 2014.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

Subsection (b) of s. 18, Art. VII, State Constitution, provides that except upon approval of each house of the Legislature by two-thirds vote of the membership, the Legislature may not enact, amend or repeal any general law if the anticipated effect of doing so would be to reduce the authority that municipalities or counties have to raise revenue in the aggregate, as such authority existed on February 1, 1989.

The mandates provision may apply because the bill redefines the types of services to which local Communication Services tax rates apply, thereby potentially reducing the authority of municipalities to raise revenue.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

The Revenue Estimating Conference estimated that SB 712 will have a zero cash impact in Fiscal Year 2014-2015, with the following recurring, negative impacts: General Revenue ($1.4 million), PECO Trust ($5.7 million), and Local ($11.2 million). Additional losses of an indeterminate amount may occur due to the purchase, on a prepaid basis, of other communication services through the same handset or other electronic device that is used by the purchaser to access mobile communication services.

In addition, a loss of up to $600 million in audit recoveries may occur if the Department of Revenue were to successfully enforce the strict definition of “prepaid calling arrangement,” with a potential loss of up to $200 million annually on a going-forward basis. These amounts reflect the estimate of what CST tax collections would have been in the past and would be in the future if CST tax, instead of sales tax, were collected on prepaid calling arrangements. However, because current industry practice is to collect sales tax on prepaid mobile communications services, and the timing of any successful Department of Revenue action is unknown, it is uncertain if and when these losses would be realized.

B. Private Sector Impact:

Communications service providers can continue to offer a prepaid plan consisting of a flat-rate charge for a predetermined number of units that can be used to purchase mobile communications services, including services such as texting, without the sale being subject to the higher CST rate. Purchasers of these plans will continue to pay the sales tax rate instead of the higher CST tax rate.

C. Government Sector Impact:

The bill may require that the Department of Revenue (DOR) notify all businesses that sell prepaid wireless telecommunication services of the changes made by the bill. This would require mailing a Tax Information Publication to 262,200 businesses. The estimated nonrecurring cost to DOR is $125,646.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 202.11 and 212.05.

IX. Additional Information:

A. Committee Substitute – Statement of Changes:

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.