



Understanding and navigating your telecommunications tax and regulatory requirements

Tax and regulatory compliance can be a complex and daunting task for any business, but some of the most difficult to understand are the telecom and VoIP industries. There are various taxes and regulatory fees including communication services taxes, utility users' tax, E911 fees, Federal Excise Tax, right of way fees, USF, and more. Oh, and don't forget that each state has its own rules, definitions and interpretation of how each tax is applied. One of the first things anyone has to do in the telecom industry is to understand the Acronyms.....CLEC, ILEC, WAN, LAN, DSL, VoIP, IPTV, ISP, MVNO just to name a few. It's difficult to even know where to start.

While this guide is not intended to be all-encompassing, it does provide baseline information and the framework for establishing a process to ensure tax and regulatory compliance for your telecommunications and certain types of VoIP services. Keep reading for the top ten steps to telecom and VoIP sales tax compliance.

1. Identify the Federal Regulatory Requirements

Telecommunications services are regulated to varying degrees by the Federal authorities and as a result, various regulatory fees are assessed on the carrier. The most common regulatory fee is the USF (Universal Service

Fund) which is administered by USAC (Universal Service Administrative Company). The USF fee is calculated by applying a contribution factor to the assessable revenue. This contribution factor changes quarterly and has been ranging between 18% and 22% over the most recent quarters. This contribution factor should be charged against assessable revenue only. Several other



federal programs are funded through contributions assessed against certain revenue. An experienced telecommunications consultant can help identify which of your revenues are subject to Federal USF and other FCC funds and fees.



2. Identify the State and Local Regulatory Requirements

In addition to the Federal regulatory requirements, there could be additional state level regulatory requirements. Within each state, there is a Public Utility Commission or a Public Service Commission that is responsible for regulating telecommunications services. Take note that if your service is regulated at the Federal level, that does not mean your service will also be regulated at the state level. If you are providing service in a state that regulates your service, then you will be responsible for paying additional state level regulatory fees that you may be allowed to recover from your customers. A telecommunications consultant can help identify which of your revenues are subject to state level USF and other fees.

3. Determine the State and Local Transactions Tax Applicability

Telecommunications services will be taxed, to some extent, in almost every state. These taxes may include sales tax, communications services tax, gross receipts tax, business + occupation tax, and utility users tax. Each service you provide may have a different tax treatment in each state. It would be a poor assumption that a service which is taxable in one state is also taxable in another state. Making this assumption could put you at a competitive disadvantage if you are charging taxes when your competitor is not. A telecommunications tax advisor can help you identify which taxes apply to your services.





4. Determine How You Will Invoice Your Customers

The application of taxes and fees to an invoice requires three items:

- (1) Knowledge as to the applicability rules for both taxes and regulatory fees that is, do the taxes and fees apply to my service;
- (2) Knowledge of the current tax rates and regulatory fee contribution factors in the jurisdictions where I plan to provide service; and
- (3) A process to calculate the taxes and fees and apply those to your invoices. This third piece generally occurs within a billing, or invoicing, or ERP system. The complexity of the application of these taxes and fees grows exponentially as you span multiple states. As an example, a manual process can be very effective, both from a cost and accuracy perspective, if your service is limited to a specific geographic area. However, this manual process will not work effectively if you are providing service in numerous states. Your options for invoicing are:
 - a. Select a billing system where you can configure the taxability and tax rates in a manual fashion. If you provide service in a specific, isolated geography, and you know the applicability of taxes and fees to your services and you know the tax rates, many invoicing systems have the ability for you to manually configure these rules in their system. As noted before, this can be effective but if there are changes to the applicability rules or tax rates, you will have to update the billing system proactively yourself. As a result, this option should only be used when you have few customers in an isolated geographic area.
- b. Select a billing system with an existing integrated tax and regulatory calculation engine. Some billing systems are designed specifically to serve the telecommunications industry. These billing systems may include a tax and regulatory fee calculation module as part of the overall system. This tax and fee calculation module will contain the current applicability rules and current tax rates. Based on your specific service and where you are providing the service, the tax and fee calculation module will automatically calculate the applicable taxes and fees and add these to your invoices. The tax and fee calculation module should be constantly updated by the software provider so if



- an applicability rule or tax rate changes then the update should happen automatically within the software. This type of system becomes helpful as you expand into multiple jurisdictions and need an automated process for calculating the taxes and fees.
- c. Select a billing system and subscribe to a separate, third party tax and regulatory calculation solution which can be integrated with the billing system. This is similar to option "b" in that it leverages a tax and fee calculation solution but in this option the tax and fee calculation solution may not be provided or sold as part of the overall billing solution. As in option "b", this type of system becomes helpful as you expand into multiple jurisdictions and need an automated process for calculating the taxes and fees.



5. Apply for the Applicable Federal License(s)

The most common registration requirement at the Federal level is with USAC, the administrator of the USF and data collection agent for other programs. USAC is a private corporation operating under the oversight of the FCC (Federal Communications Commission). When you register with USAC you will receive a Form 499 filer id and will be designated as either a direct contributor to the USF or not. This direct contributor status means that you, as the carrier, are paying USF fees directly to the regulatory body. In this case, the FCC. However, if you are just starting your business and/or



have minimal assessable revenue, there is a de minimis threshold whereby you are not required to contribute directly to the fund. In this case, your upstream carrier will charge you the USF fee and they will contribute (or pay) the fee directly to USAC. Even de minimis providers, however, must register with USAC and obtain a filer id.

Providers of international telecommunications services offered generally to the public are also required to obtain FCC Section 214 Authorization (commonly referred to as a "214 License").

6. Apply for the Applicable State and Local Regulatory License(s)

If your service is regulated by the states where you anticipate providing



service, then you will need to either register with or obtain an appropriate license from the respective Public Utility or Public Service Commissions. Most states require local exchange providers to obtain a license, just over half the states require in-state long distance to seek licensure, and roughly half the states now require VoIP and Wireless providers to register.

7. Register with the Applicable State and Local Tax Authorities

Registrations for transactions tax purposes at the state level are generally via the state Departments of Revenue. Certain cities and counties may also require local registrations as well. Registering with the tax authorities can be done both proactively and reactively depending on the risk tolerance of your business. Most companies register proactively in states where they anticipate revenue. This might include their home state and other states where they expect significant revenue. Companies will then monitor the collection of tax, and based on where they collect, they will then register reactively and immediately start remitting.



8. Implement a Compliance Reporting Solution

Once you have determined the applicable taxes and fees, registered with the appropriate taxing and regulatory authorities, and are now invoicing and collecting taxes and fees, you must remit these taxes and fees to their respective authorities. There are two options available –

- perform the work
 in-house; or
 outsource the compliance process. Either option should include the following:
 - a. Return preparation and filing
 - b. Payment processing and remittance
 - c. Notice/jurisdictional communication and resolution
 - d. Ongoing renewals of registrations



Unfortunately, commercially available software packages that facilitate the compliance process are few and far between. As a result, an in-house process can become cumbersome as it is mostly manual. In-house processes can work well in situations where you are in very few jurisdictions. As an alternative, outsourcing leverages the experience, technology, and processes of a dedicated company. When evaluating outsourcing service providers, they should have expertise in the telecommunications industry. The reporting requirements for the telecommunications industry are very different and distinct from traditional sales tax oriented businesses.

9. Submit the Appropriate Exemption Documentation to Upstream Carrier(s)

Most taxes and fees qualify as exempt when telecommunications services are sold to a reseller. The taxes and fees are generally imposed upon the retail sale of telecommunications services only. The carriers



leave it up to the individual reseller to understand the requirements to achieve exempt status and to identify and prepare applicable forms. Generally, each state prescribes the form and/or content of information required to exempt a transaction from taxes and fees. Some of the larger carriers, Level3, AT&T, etc. have customized



their process for qualifying a reseller as exempt from various taxes and fees. The carriers generally have an exemption packet that could be as many as 50 or more pages in length. A tax and/or regulatory advisor can help you prepare the necessary forms including:

a. Federal Regulatory Exemption Certificates. In order for a carrier to exempt you from Federal USF fees, you must be registered as a direct contributor. Earlier, we referenced a de minimis threshold whereby you are not required to contribute directly to the USF rather you simply pay your carrier who remits the USF fee to USAC. Nonetheless, there are many situations where you can pass through this fee to your customers. Once you are over the de minimis threshold, then you are required to contribute directly to USAC. At this point, you will require that your upstream carrier exempt your services from the Federal USF. The de minimis threshold currently sits at \$10,000 in annual contributions.

b. State and Local Tax Exemption Certificates. If you are registered with the State Department of Revenue and have received a sales tax id or equivalent, then you are qualified to execute an exemption certificate as a reseller. As a reseller, you are requesting that the carrier exempt sales to your company from taxes. You are further stating that you will be responsible for collecting and remitting the



taxes from your customers. This is a fairly easy exemption to achieve; however, you must be registered with the State Departments of Revenue to achieve it.

10. Calculate, Bill, Collect, and Remit Your Taxes and Fees

Once you have implemented the steps above, the tendency is to become complacent. It's similar to the "set it and forget it" mentality. Even if you have a telecommunications specific billing system and a tax and fee calculation solution in place, you should periodically review your tax and regulatory foot print. The concern would be that as you expand your business into new jurisdictions, you will inevitably open yourself up to additional tax and regulatory compliance obligations.

Conclusion

A tax professional must have a solid grasp on the products and services their business sells as the tax base and implications are quite different from product to product and state to state.

The various indirect taxes often hover below the radar of many CEO's, CFO's and in some situations even the Tax Department. Sales, use and telecom



taxes should not be a financial issue when they are billed, calculated, reported and paid timely. Unfortunately, many companies may not realize they have nexus in a particular jurisdiction or perhaps they believe a product or service is not subject to tax until they are audited. If a company is not registered and filing, there is no statute of limitations. As a result, these taxes that should not be a financial issue (because they are a pass through) can become very costly, including penalties and interest.

For anyone with questions, don't be afraid to ask for help. Relying on a sales tax expert to manage the complexities of sales tax could relieve a lot of stress, time and liability from your shoulders. Consider working with **TaxConnex** to take the burden of sales tax off your plate.



About the Author

Brian Greer, Partner & CRO, TaxConnex

A graduate of Purdue University, Brian has a rich background in serving the Technology and Accounting industries, while leading successful sales and marketing teams. Brian joined TaxConnex as a partner in 2010, guiding the sales and marketing activity and giving TaxConnex a uniquely talented technology and sales tax professional.



About TaxConnex[™]

TaxConnex ™ is how businesses finally get sales tax off their plate – no matter how many states they're in or how often regulations change. Sales tax is more complicated than ever, especially in a post-Wayfair world. Yet the providers who claim to simplify sales tax often still leave the hardest parts – and the liability – up to you. When you work with TaxConnex, it's all on us. This means you get all the know-how, all the backup, and none of the risk. It's only possible because of our proprietary platform and network of sales tax experts. That's why large to mid-sized corporations, including accounting firms, turn to TaxConnex. Now it's all on us.™







