

MAINE STATE LEGISLATURE

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Inter-Departmental Memorandum Date July 28, 1977

To Ralph H. Gelder, Chairman Dept. Public Utilities Commission
From Stephen C. Clarkin, Asst. Atty. Gen. Dept. Bureau of Taxation
Subject Federal Communications Tax

FACTS:

In your opinion request you have stated that the Internal Revenue Service has ordered the New England Telephone & Telegraph Company to revise its procedure for calculating the Federal Communications Tax on charges for telephone service in the State of Maine. Presently, the Company excludes charges for Maine Sales Tax on telephone bills from the tax base when computing the Federal Communications Tax. Effective August 1, 1977, the I.R.S. has ordered the Company to include all Sales Tax charges in the tax base for purposes of calculating the Federal tax.

QUESTION PRESENTED:

Whether the Maine Sales Tax constitutes a part of the charges for telephone services under 26 U.S.C.A. Sec. 4251 and is thereby properly includible in the tax base utilized for calculating the Federal Communications Tax.

ANSWER:

The Maine Sales Tax does constitute a part of the charges for telephone services under 26 U.S.C.A. Sec. 4251 and is thereby required to be included in the tax base utilized for calculating the Federal Communications Tax.

REASONING:

26 U.S.C.A. Sec. 4251 imposes a tax on amounts paid for certain "communications services," including local telephone service and toll telephone service and requires that the tax be paid ". . . by the person paying for the services." Pursuant to this section, therefore, the legal incidence of the tax is upon the consumer. Treas. Reg. Sec. 49.4251-2(c). Under 26 U.S.C.A. 4291, the telephone company providing the service is charged with the responsibility of collecting the tax from its customers on behalf of the Federal government. 26 U.S.C.A. Sec. 4251 prescribes the method of computation of the federal tax as follows:

"(a) General rule. - If a bill is rendered the taxpayer for local telephone service or toll telephone service -

(1) the amount on which the tax with respect to such services shall be based shall be the sum of all charges for such services included in the bill. . ."

[Emphasis Added]

The position of the I.R.S. is apparently predicated primarily upon its prior decision in Revenue Ruling 69-151, 1961-1 C.B. 288. In that ruling, the Service considered the question of whether certain amounts attributable to state and local taxes, including gross receipts or sales taxes, and separately stated on customers' telephone bills, were properly includible in determining the amount upon which the Federal Communications Tax is imposed. In resolving the issue, the I.R.S. observed:

"Unlike the Federal communications tax, which is imposed on the person paying for the service, the State and local taxes under consideration are imposed on the companies engaged in the business of providing the service. Since these taxes are directly attributable to the telephone services provided, they constitute an element of the cost of providing the services along with costs attributable to labor and equipment. The fact that amounts attributable to such taxes are passed on and are separately stated on bills sent to customers does not change the legal incidence of the taxes."

Accordingly, the Service maintained that as the state and local taxes in question were imposed upon the companies, they were not excludible in determining the amount upon which the federal tax is based.

Although the Maine Sales Tax Law is somewhat contradictory with regard to the incidence of the sales tax, two decisions of the Law Court have foreclosed the possibility of any doubt on this issue. W. S. Libby Co. v Johnson, 148 Me. 411 (1953); Harvey F. Gamage, Shipbuilder, Inc. v Halperin, Me. 359 A2d 72 (1976) In both decisions, the court construed the sales tax statute as imposing tax liability upon the retailer for the privilege of making retail sales within the state and specifically rejected contentions that the legal incidence of the tax was upon the consumer, rather than upon the retailer.

Consequently, the Maine Sales Tax falls squarely within the ambit of Revenue Ruling 69-151, supra.

The only remaining question, therefore, is whether the conclusion expressed in that ruling is correct.

A nearly identical issue was presented in Agron v Illinois Bell Telephone Company, 449 F.2d 906 (7th Cir. 1971), cert. denied 92 S.Ct. 1171, 405 U.S. 954, 31 L.Ed. 2d 231. In that case, the plaintiff, a telephone subscriber, challenged the company's procedure for computing the Federal Communications Tax. The Illinois Bell Telephone Company (IBT) had computed the federal tax on a base which included not only the company's service charges but also charges for state and local "Messages Taxes" which were stated

separately in each customer's bill. As in Revenue Ruling 69-151, supra, the court regarded the determinative issue to be the legal incidence of the state and local taxes. After construing the statutes involved, the court concluded that the taxes were imposed upon the company for the privilege of doing business within the state, rather than upon the consumer. Accordingly, although the taxes were separately stated and identified as such on each bill, the court held that they were properly includible in the federal tax base as "amounts paid for. . .communication services" within the meaning of 26 U.S.C.A. Sec. 4251(c). In so holding, the court explained:

"All costs incurred in making a product or service available - including the cost of federal, state and local taxes - are ultimately borne by consumers. That the cost of taxes imposed on manufacturers and retailers is added into the price at which goods are sold, even if such taxes are itemized and specifically identified, simply increases the price the consumers must pay to receive the goods and services." Id., pg. 912

"[The] amounts IBT demands. . .as reimbursement for taxes it pays are as much a part of the price for its services as amounts reimbursing it for labor and equipment costs." Id., note 13

In Apostolou v United States, 347 F. Supp. 1264 (1972), an analagous problem was considered. There, the question was whether amounts attributable to a state amusement tax on ticket prices were required to be included by the seller in computing the tax base upon which the federal admissions tax, a consumer tax, was imposed. Like the communications tax, the federal admissions tax statute charged the seller of admissions tickets with the responsibility of collecting the tax from his customers.

Relying, in part, on Agron, supra, the court determined that the legal incidence of the state tax was dispositive of the question. After construing the state statute as imposing tax liability upon the seller of the tickets, the court concluded that the tax constituted part of the "amount. . .paid for admission. . ." within the meaning of the federal statute. Consequently, the tax was properly includible in the tax base upon which the federal tax was required to be calculated.

The validity of the legal incidence approach is further illustrated by several decisions which have considered the converse problem, i.e., whether amounts attributable to certain state or federal taxes are properly includible as part of gross sales or receipts for the purposes of computing state sales tax or gross receipts tax liability. Gurley v Rhoden, 421 US 200, 95 S. Ct. 1605, 44 L.Ed. 2d 110, (1975); Ferrara v Director, Division of Taxation, N.J., 317 A.2d 80 (1974); Martin Oil Service, Inc. v

Department of Revenue, Ill., 273 N.E.2d 823 (1971); American Oil Company v. Mahin, Ill., 273 N.E.2d 818 (1971); State v. Thoni Oil Magic Benzol Gas Stations, Inc., Ga., 174 S.E.2d 224 (1970); Tax Review Board v Esso Standard Division of Humble Oil and Refining Co., Pa., 227 A.2d 657 (1967). In each opinion, the decision was predicated upon a determination of the legal incidence of the tax. In each case, moreover, where the tax in question was construed as imposing liability upon the seller, it was held properly includible in the tax base used for calculating the sales tax or gross receipts tax.

In view of the foregoing, therefore, it is evident that the Maine Sales Tax constitutes a part of the charges for telephone services under 26 U.S.C.A. Sec. 4251 and that it should be included in determining the amount upon which the Federal Communications Tax is imposed.


Assistant Attorney General

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