ALABAMA TAX TRIBUNAL

CELLULAR EXPRESS, INC.,	§	
	§	
Taxpayer,	§	DOCKET NO. S. 14-320-JP
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

OPINION AND FINAL ORDER

The Alabama Department of Revenue entered final assessments of state and local sales tax against Cellular Express, Inc. (Taxpayer), concerning prepaid wireless service. The assessment for state sales tax totaled $363,416.16 and the assessment for local sales tax totaled $181,654.98. Each assessment included tax and interest only, with no penalties being assessed, and each assessment covered the periods of April 2009 through March 2012. The Taxpayer timely appealed.

In its Answer, the Revenue Department asked that the appeal be held in abeyance pending the outcome of a similar case involving Beauty & More, LLC, that had been appealed from the Revenue Department's Administrative Law Division to the Montgomery Circuit Court. Shortly after the filing of the Answer, Act 2014-336 was signed into law. The Act's stated purpose was "to clarify that prepaid wireless service that is evidenced by a physical card and prepaid wireless service that is not evidenced by a physical card, are subject to sales and use tax." The Revenue Department then amended its Answer to assert that the Act resolved the dispute in the tax agency's favor and, thus, that there was no need to hold the appeal in abeyance pending the outcome in *Beauty & More, LLC*.

Subsequently, the Taxpayer raised a constitutional challenge to the Act by claiming

that the Act violated the Taxpayer's right to due process. The Taxpayer's appeal then was held in abeyance for a lengthy period while two other, separate cases – *Atheer Wireless, LLC v. State Department of Revenue* and *Alabama Department of Revenue v. Downing* – made their way through Alabama's trial and appellate courts.

After *Atheer Wireless* and *Downing* were concluded, the Taxpayer supplemented its previous filings with the Tax Tribunal to state a total of five reasons why the final assessments should be voided, three of which constitute facial constitutional challenges. Because the Tax Tribunal has no authority to declare an act of the legislature void on its face, the constitutional challenges are preserved for the trial court. *See* Ala. Code § 40-2B-2(g)(6). A hearing was conducted in 2019, followed by the submission of briefs.

Questions Presented

Alabama law subjects the sale of prepaid telephone calling cards and prepaid authorization numbers to sales tax. And the sale of prepaid wireless service that is not evidenced by a physical card constitutes the sale of an authorization number. Here, the Taxpayer accepted payments from customers that replenished the customers' monthly cellular-service plans. The Taxpayer did not provide a card to its customers upon payment, and it contends that it did not provide an authorization number, either. Additionally, the Taxpayer sold phones and accessories. It collected and remitted sales tax on its sales of those items, but not on the amounts that were prepaid to replenish monthly service plans. The questions presented are:

1) Whether the Taxpayer was merely facilitating customer payments to Boost Mobile, so as to be similarly situated with the online travel companies in *City of Birmingham v. Orbitz, LLC*?

2) Whether Alabama law required the Taxpayer to actually provide an authorization number to its customers for those transactions to be subject to sales tax?

3) Whether the Taxpayer proved that the Revenue Department violated the Alabama Administrative Procedure Act or the Taxpayers' Bill of Rights in its audit and assessment of the Taxpayer?

Facts

Mr. Suhail Assad, who is the owner of the Taxpayer, testified that the Taxpayer was an authorized dealer for Boost Mobile during the audit period. The Taxpayer's three stores bore Boost Mobile branding and sold Boost phones and accessories. Mr. Assad described Boost Mobile as "a monthly plan company" that offered differing packages at varying prices, in addition to phones and accessories, without the need to perform credit checks on customers. As an authorized dealer, Mr. Assad stated that he had to abide by Boost Mobile's corporate policies and had to sign a personal guarantee for the Taxpayer's financial dealings with Boost. Also, the Taxpayer was required to provide Boost with access to the Taxpayer's bank account, with authorization to withdraw funds.

Boost also required the Taxpayer to accept customer payments for the monthly cell-phone service plans offered by Boost. For that purpose, Boost programmed certain computers within the Taxpayer's stores to provide the Taxpayer with a customer's account information, including the amount the customer had to pay to replenish their monthly plan. That activity was referred to as "real-time replenishment" and, of course, was done in advance of replenishing the plan for another month. Mr. Assad stated that, generally, there were three plans offered, although Boost changed the plans from time to time. One monthly plan cost $35 and provided 1,000 minutes of talk time and 10 gigabits of data usage. A $45 plan offered 2,000 minutes and 15 gigabits of data. And a third plan, for $50

per month, offered unlimited minutes and data. Under the first two plans, if a customer used all of the minutes before the end of the month, the customer had to wait until the end of the month to renew.

When a customer replenished their plan, the customer provided the Taxpayer with their phone number, and the Taxpayer entered the number into the terminal dedicated to replenishments. The display showed the amount due, and the Taxpayer collected that amount. Once the payment was approved, the Taxpayer provided the customer with a receipt that showed a reference number pertaining to that transaction. The monthly plan then was reloaded onto the customer's phone automatically. Within a day or two of the customer's payment being deposited into the Taxpayer's account, Boost withdrew the payment and later paid the Taxpayer a 5% commission.

Mr. Assad testified that all three plans were sold by the Taxpayer during the audit period and that no sales tax was collected on any of those transactions. According to Mr. Assad, Boost's computer system did not allow for the collection of sales tax on replenishment payments. He also stated that the Taxpayer did not provide those customers with a card, which is not disputed by the Revenue Department, nor did the Taxpayer provide customers with an authorization number, which is disputed by the Revenue Department. The Taxpayer collected and remitted sales tax on its sales of phones and accessories, and those transactions are not in issue here.

When the Taxpayer filed its sales-tax returns during the audit period, it reported all gross receipts that it received each month, including the receipts from customer payments that were made to replenish their monthly service plans. On those returns, however, the

Taxpayer then deducted the replenishment payments and calculated tax due on the net amounts.

Concerning the audit, Mr. Assad testified that he and the Taxpayer's accountant met with the auditor at the accountant's office, but that the meeting lasted only about ten minutes even though Mr. Assad brought all of the Taxpayer's records for the auditor to review. According to Mr. Assad, the records were left in the accountant's office in anticipation of another meeting with the auditor. Instead, the auditor phoned the accountant and requested only the front page of the Taxpayer's monthly bank statements that showed total deposits. The auditor did not review the records in the accountant's office and did not meet with Mr. Assad or the accountant again. The auditor disallowed the deductions taken by the Taxpayer on its returns and the Revenue Department entered the final assessments that are at issue.

Law and Analysis

Alabama's sales tax applies to the retail sale of tangible personal property. Ala. Code § 40-23-2(1). In 1997, Alabama adopted Act 97-867 concerning the tax treatment of the sale of prepaid telephone calling cards and prepaid authorization numbers, both of which related to the use of cellular phone service. The Act addressed certain public-utilities taxes (in Title 40, Chapter 21) and sales and use taxes (in Title 40, Chapter 23).

First, the 1997 Act excluded from the utility gross receipts tax "all revenues derived from... [t]he furnishing of utility services through the use of a prepaid telephone calling card." Act 97-867, § 1 (amending Ala. Code § 40-21-83). Likewise, the Act excluded from the utility service use tax "[t]he storage, use, or other consumption of utility services ...

[w]henever utility services are furnished through the use of a prepaid telephone calling card." Act 97-867, § 2 (amending Ala. Code § 40-21-103). And the Act excluded from the cellular telecommunication services tax and mobile telecommunications services tax "[t]he furnishing of Cellular Radio Telecommunications Service through the use of a prepaid telephone calling card, a prepaid authorization number, or both." Act 97-867, § 3 (amending Ala. Code § 40-21-122). Second, the Act stated that the "sale of a prepaid telephone calling card or a prepaid authorization number, or both, shall be deemed the sale of tangible personal property subject to" Alabama's sales and use taxes. Act 97-867 §§ 4 and 5 (amending Ala. Code §§ 40-23-1 and 40-23-60, respectively).

Subsequently, the Revenue Department's Administrative Law Division issued an opinion in a sales-tax case in which the taxpayer, a beauty supply store, also sold prepaid cellular phone minutes and other cellular services such as texting and internet access. *See Beauty & More, Inc. v. Alabama Dep't. of Revenue, Admin. Law Div.*, No. S. 12-336 (Opinion and Preliminary Order, June 10, 2013). Beauty & More argued that the cellular minutes and services that it sold were not prepaid calling cards or authorization numbers within the scope of the 1997 Act. The Administrative Law Division agreed, ruling that the taxpayer's transactions were not taxable because the minutes and services sold by the taxpayer did not exist when the 1997 Act was passed. "Rather, in 1997, when Act 97-867 was enacted, the only type of prepaid telephone calling card that was available for purchase was a physical card that contained an authorization number." *Id.* at 4.

In response, Act 2014-336 was adopted, which amended Ala. Code. §§ 40-23-1 and 40-23-60 (Alabama's sales and use tax definitional sections). The stated purpose of the

Act was "to clarify that prepaid wireless service that is evidenced by a physical card and prepaid wireless service that is not evidenced by a physical card, are subject to sales and use tax." To accomplish its purpose, the 2014 Act added the following to the sales and use tax definitions of "prepaid telephone calling card:"

> For purposes of this subdivision (13), the sale of prepaid wireless service that is evidenced by a physical card constitutes the sale of a prepaid telephone calling card, and the sale of prepaid wireless service that is not evidenced by a physical card constitutes the sale of a prepaid authorization number.

In Section 6, the 2014 Act addressed transactions that already had occurred:

> For transactions that occurred prior to the effective date of this act in which the consumer did not receive from the retailer either an authorization number or a physical card, neither the Department of Revenue nor local tax officials may seek payment for sales tax not collected. This limitation on the authority of the department or local officials shall not apply to audits that began or assessments that were entered prior to the effective date of this act. With regard to such transactions in which sales tax was collected and remitted, neither the taxpayer nor the entity remitting sales tax shall have the right to seek refund of such tax.

These matters made their way to one of Alabama's appellate courts. First, in *Atheer Wireless, LLC v. State Dep't of Revenue*, 228 So.3d 464 (Ala. Civ. App. 2017) (on rehearing), the Court of Civil Appeals reviewed the circuit court's grant of summary judgment to the Revenue Department concerning an assessment of sales tax on the sales of prepaid wireless services. The tax periods in issue occurred after the effective date of the 1997 Act but prior to the passage of the 2014 Act. However, the 2014 Act became law while the initial appeal was pending in the Revenue Department's Administrative Law Division. The Revenue Department amended its answer in the administrative proceeding to assert that the 2014 Act clarified the taxability of Atheer's sales. In addition to its initial argument that its sales were not subject to the 1997 Act, Atheer then supplemented its

argument to challenge the constitutionality of the 2014 Act. The administrative appeal was decided in the Revenue Department's favor based on the 2014 Act, without consideration of the Act's constitutionality. On appeal to circuit court, Atheer again challenged the constitutionality of the 2014 Act, and both parties requested summary judgment. The Revenue Department's request was granted. The Court of Civil Appeals affirmed, stating that "Atheer cannot obtain relief by proving that the Department could not have assessed Atheer under its allegedly unlawful or unauthorized interpretation of the previous version of § 40-23-1(a)(13) [the 1997 Act]. The assessment would still stand under the 2014 Act." *Id.* at 469.

A year later, in *Alabama Dep't of Revenue v. Downing*, 272 So.3d 184 (Ala. Civ. App. 2018), the Court of Civil Appeals held that Downing's sales of prepaid authorization numbers for use with wireless services on cellular telephones were subject to Alabama's sales tax. In doing so, the court acknowledged that the 1997 Act included such sales in the sales-tax levy while excluding such sales from the cellular telecommunication services tax levy, as noted by the Revenue Department. Specifically, the court stated that "wireless service on a cellular telephone does not appear to be distinguishable from 'cellular telecommunications service' for the purpose of assessing taxation pursuant to § 40-23-1(a)(13)." *Id.* at 193. The court did not express any reliance on the 2014 Act.

Here, the Taxpayer argues that it was merely facilitating customer payments to Boost Mobile instead of making retail sales, citing *City of Birmingham v. Orbitz, LLC*, 93 So.3d 932 (Ala. 2012). In that case, several municipalities requested declaratory judgment from the Jefferson Circuit Court that Orbitz and other online travel companies were liable

for municipal lodgings tax because the companies were engaged in the business of renting hotel rooms. The undisputed facts showed that the companies facilitated the making of hotel (as well as airline and car-rental) reservations using the internet, for which they received from customers an amount for occupying a hotel room, a lodgings-tax recovery charge, and an additional amount which was retained by the companies as compensation. The room-occupancy amount and the lodgings-tax charge were remitted to the hotel, and the hotel paid the lodgings-tax charge to the appropriate government agencies. The municipalities contended that lodgings tax also should have been remitted by the companies on their compensation. The circuit court disagreed, however, ruling that the companies were not engaged in the business of renting rooms and, thus, did not owe lodgings tax. The court relied primarily upon an administrative rule of the Revenue Department that stated "that only 'persons who operate [a] hotel' are persons who rent or furnish rooms." *Id.* at 935, citing Ala. Admin. Code r. 810-6-5-.13(5).

> The DOR has also determined that online travel service providers are not engaged in the business of renting or furnishing hotel rooms. Therefore, they are not hotel operators and are not obligated to collect and remit the lodgings tax on what they charge for their online services. While the opinion of the DOR is not binding on this court, it is persuasive.

Id. at 935. The Alabama Supreme Court affirmed, adopting the circuit court opinion in its entirety.

Here, though, there is no administrative rule that addresses the Taxpayer's situation. In fact, the Revenue Department stated in brief that it has not adopted any rule regarding Ala. Code § 40-23-1(a)(13), either before or after the audit of the Taxpayer. Instead, the relevant acts of our legislature address the taxability of the Taxpayer's transactions.

As noted, the 1997 Act subjected the sales of prepaid calling cards and authorization numbers to sales and use taxes and excluded transactions involving those items from utility and telecommunications services taxes. The 2014 Act clarified that "prepaid wireless service that is evidenced by a physical card and prepaid wireless service that is not evidenced by a physical card, are subject to sales and use tax." Further, the 2014 Act added that "the sale of prepaid wireless service that is not evidenced by a physical card constitutes the sale of a prepaid authorization number."

"Prepaid wireless service" was defined in the 2014 Act as "[t]he right to use mobile telecommunications service, which must be paid for in advance and that is sold in predetermined units or dollars of which the number declines with use in a known amount..."

The phrase "mobile telecommunications service" appears to be indistinguishable from "cellular telecommunications service." *See* Act 2001-1090, which substituted one phrase for the other. And in *Downing*, the court stated that wireless service on a cellular phone was indistinguishable from cellular telecommunications service for purposes of Ala. Code § 40-23-1(a)(13). *Id.* at 193. Therefore, the Taxpayer sold wireless service, and the facts show that the service was prepaid because customers could not continue utilizing their monthly plans until they had paid the Taxpayer. Also, Mr. Assad testified that three plans were offered by the Taxpayer, two of which provided a specified – or predetermined – number of minutes and gigabits that a customer could use during the month. The third plan, which offered unlimited minutes and gigabits, nevertheless was limited to a period of one month. The Revenue Department argues that the specified period of one month, or thirty days, also fit within the definition of "prepaid," because that time period was a

predetermined unit. The Tax Tribunal agrees. And the number of predetermined units – whether minutes or gigabits or days – declines with use in a known amount.

The Taxpayer also argues that it did not provide authorization numbers to its customers. But the 2014 Act negates the Taxpayer's argument by stating that "the sale of prepaid wireless service that is not evidenced by a physical card constitutes the sale of a prepaid authorization number." It is undisputed that the Taxpayer did not provide its customers with physical cards when the customers renewed their monthly plans. But that fact, by default, constituted "the sale of a prepaid authorization number" which, according to Ala. Code § 40-23-1(a)(13), was deemed to be the sale of tangible personal property subject to sales tax.

Finally, the Taxpayer argues that the assessments should be voided because the Revenue Department failed to execute its responsibilities pursuant to the Alabama Taxpayers' Bill of Rights (TBOR) in Ala. Code § 40-2A-1, *et seq.*, and the Alabama Administrative Procedure Act (AAPA) in Ala. Code § 41-22-1, *et seq*. Concerning the TBOR, the Taxpayer argues that the auditor had no training in the sales-tax auditing of cellular wireless companies; had no recollection at the hearing of various aspects of the audit meeting with Mr. Assad and the Taxpayer's accountant, which lasted less than 10 minutes; did not schedule a subsequent audit meeting with the Taxpayer, as promised; did not maintain audit notes or workpapers; and had been instructed by her supervisor prior to the audit that the transactions in question were taxable.

The Tax Tribunal takes the Taxpayer's claims seriously, especially as to the alleged predetermination that tax was due. However, during the hearing, the Tax Tribunal

specifically questioned the auditor about that claim and the auditor stated that she was not instructed concerning the Taxpayer in particular. Rather, she was instructed that authorization numbers and physical cards were to be treated the same. The Tax Tribunal also is concerned about the auditor assuming that the numbers at the bottom of customer receipts were authorization numbers that provided minutes on customer phones. Such a conclusion could have proved decisive and should not have been presumed. Nevertheless, these claims of the Taxpayer do not rise to the level of voiding the assessments, especially in light of the Tax Tribunal's ruling that the Taxpayer's transactions were subject to sales tax.

Concerning the AAPA, the Taxpayer argues that the Revenue Department "utilized a new interpretation of 40-23-1(a)(13), and the applicable regulations, without following the proper procedures for new rules set forth in the [AAPA]. The new interpretation was including the processing of payments for sales of cellular air time minutes within the definition of taxable sales…" But the Taxpayer's argument begs the question of what the transactions involved – the processing or facilitating of payments versus the sale of prepaid wireless service. And the Tax Tribunal disagrees with the Taxpayer's characterization of the transactions, as discussed. The Taxpayer did not show that the Revenue Department violated the AAPA.

Conclusion

Based on the foregoing, the final assessment of state sales tax is upheld in the amount of $363,416.16, plus additional interest, and the final assessment of local sales tax is upheld in the amount of $181,654.98, plus additional interest. Judgment in favor of the

Revenue Department is entered accordingly. The Taxpayer's constitutional claims are preserved for circuit court.

This Opinion and Final Order may be appealed to circuit court within 30 days, pursuant to Ala. Code § 40-2B-2(m).

Entered January 21, 2021.

/s/ *Jeff Patterson*
JEFF PATTERSON
Chief Judge
Alabama Tax Tribunal

jp:cm
cc: Russell M. Cunningham, IV, Esq.
Steve Schniper
Mary Martin Mitchell, Esq.