



COLORADO
Department of Revenue
Taxation Division

Office of Tax Policy
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DOR_TaxPolicy@state.co.us

PLR-15-001

XXXXXXXXXXXXX
Attn: XXXXXXXXX
XXXXXXXXXXXXX
XXXXXXXXXXXXX

Re: Electronic Messaging Services

Dear XXXXXXXXXXX,

You submitted on behalf of XXXXXXXXXXXX ("Company") a request for a private letter ruling to the Colorado Department of Revenue ("Department") pursuant to Department Rule 24-35-103.5. This letter is the Department's private letter ruling.

Issues

- 1) Are the services subject to Colorado sales and use tax as a "telephone and telegraph service" or any statutorily enumerated service?
- 2) If Company's services could be deemed taxable as a "telephone and telegraph service" or other type of taxable service under Colorado's taxing statutes, is the state prohibited from imposing the tax under the federal Internet Tax Freedom Act?
- 3) If any of Company's services are considered taxable, how should the receipts be sourced?
- 4) If any of Company's services are considered taxable, is Company entitled to purchase "telephone and telegraph services" for resale if the services are used in carrying out Company's own services?

Conclusion

- 1) The services described in the request are not subject to Colorado sales and use tax as a "telephone and telegraph service" or any other statutorily enumerated service.
- 2) Even if production email is a telegraph service subject to tax, the Internet Tax Freedom Act prohibits Colorado from levying the tax on such service.
- 3) Because Company's services are not taxable, sourcing is not an issue that requires a ruling.
- 4) Company is the consumer of the telephone and telegraph services used in provide Company's services.

Background¹

Company is engaged in providing computer based electronic messaging services to business enterprises, utilizing their customers' own networks of computer servers and the public internet. Company is not regulated as a provider of telecommunications by the Federal Communications Commission. Company's servers are located outside of Colorado. Company offers the following services:

- 1) Integrated desktop messaging (IDM)
- 2) Electronic data interchange (EDI) value added network (VAN) service
- 3) Broadcast fax
- 4) Notifications email
- 5) Production email

1. *Integrated Desktop Messaging (IDM)*

IDM service enables businesses to send and receive traditional facsimile documents in digital form, directly from (or to) their desktop computer applications, utilizing email and electronic mailboxes. The IDM service replaces a business' entire fax infrastructure (i.e. traditional fax machines, networking hardware and software, telecommunications lines, and maintenance contracts) with a cloud-based service that utilizes the business's existing computer applications.

The IDM system provides the data processing and conversion functions necessary to both: accept a customer's documents and data in email format (i.e. an email with attachments from a word processing application) and convert such data into the necessary format for delivery to a traditional paper fax machine; and to receive a fax transmission from a traditional fax machine and convert that data into email format that is then sent as an email and stored in the customer's electronic mailbox. A customer can track messages, receive delivery confirmations, and run analytical reports. Customers also have access to web-based "dashboard" where they can customize, set preferences and otherwise manage the service. IDM customers can contract with Company for inbound service, outbound service, or both. Although some customers establish (and pay a third-party telecommunications provider for) a dedicated link to Company's servers, such as a secure Virtual Private Network (VPN) or other method (e.g., File Transfer Protocol (FTP)), most users simply utilize their existing email client to send and receive messages utilizing the IDM service. Transmissions of data onto Company's servers are typically made in Simple Mail Transfer Protocol (SMTP), a standard data format for messaging over the internet. Once on Company's servers, customers' emailed data and attachments are converted by Company's proprietary software into a TIFF image capable of being processed by a traditional paper fax machine. If the customer's recipient also utilized IDM or similar service offered by a competitor, the transmission would ultimately be delivered from one electronic mailbox to another entirely without a fax machine. Once processed, the converted message is delivered from Company's servers to the recipient via third-party telecommunications carriers. Company pays for such transmission services, including any taxes charged by the provider, and

¹ The facts set forth in the Background are provided by Company and the Department assumes that they are correct and complete for the purpose of providing this ruling.

absorbs the cost. Company does not claim a resale exemption on the taxes charged, nor does it separately bill customers for this telecommunications expense.

Company assigns to customers who receive inbound messaging services through IDM service an "e-fax" phone number that is linked to that user's email address. Company obtains such numbers from a third-party telecommunications carrier, the cost of which is borne by Company and not separately billed to customers. Customers also have the option to port/ transfer their existing traditional fax number to the IDM service. A fax document sent to an IDM customer's e-fax number is delivered (via the sender's own telecommunications carrier) to Company's servers, where it is converted into either a TIFF or PDF format and delivered (as an email with a file attachment) to the email address associated with the e-fax number. An optional PDF editor feature allows incoming faxes to be converted to a PDF format capable of being edited. The transmission of the email from Company's servers to the customer is carried out by a third-party telecommunications carrier, the cost of which is borne by Company, including any taxes. Company does not claim a resale exemption on these charges, nor does Company separately bill customers for this telecommunications expense.

A customers' systems administrator has the ability to manage and set preferences for the service, including creating customized cover pages, determining send and receive settings and setting preferences for signatures. All such customizations and preferences are stored by Company and applied to the customer's inbound and/or outbound messages.

Company charges a one-time fee for IDM service and a monthly subscription fee, plus a usage fee based on the volume of transactions processed on Company's network (measured by number of pages processed). However, Company does not bill customers for its telecommunications costs in providing this service.

2. Electronic Data Interchange (EDI) Value Added Network (VAN) Services

EDI is a form of business-to-business messaging that allows businesses to exchange electronically routine business documents, such as purchase orders invoices, shipping confirmations and invoices, utilizing industry standard data formats. The structured formats allow these documents to be processed automatically by the business' computer systems without manual intervention.

Although EDI, in its simplest form, can operate as computer-to-computer exchange over a real-time telecommunications channel, such a link is impossible for many large businesses that need to process hundreds of transactions per day with numerous trading partners. Through the use of the Company's EDI VAN service, a customer can send transactions to the VAN and have the transaction converted into the necessary format for processing by the recipient. This eliminates the need for the customer to establish and manage individual interconnects with trading partners, and ensures EDI transactions are exchanged and processed regardless of whether the recipient's data standards or computer systems are compatible. Rather than the unstructured text contained in an ordinary email message, an EDI formatted transaction places all necessary information into an industry-standard structure so each data field is recognized and processed automatically.

The VAN also acts as a virtual post office that provides customers with electronic mailboxes and the capability to manage their inboxes and outboxes, as well as, store, track, search, and archive all of their EDI transactions.

The VAN utilizes Company's network of computer servers, the internet, and interconnects with competing value-added EDI networks. A customer who wants to send an electronic EDI transaction to a trading partner uploads the data onto one of Company's servers. Transmission of the customers' uploaded data, either between Company' servers or onto the internet, is accomplished by third-party telecommunications providers. Company does not provide a communications channel for customers to access the network. The customer is responsible for maintaining a telecommunication line to access Company's servers.

Once the customer has sent its data to Company's servers, proprietary software processes, translates, and converts the data based on the EDI standard necessary for the recipient to process the transaction (e.g., as an automated purchase order). EDI standards specify how data and data fields necessary to complete particular transactions are formatted. Once processed, the transaction is delivered to an electronic mailbox maintained by the recipient. The email is stored until the recipient contacts the VAN to retrieve the transaction for processing. Transactions processed by the VAN operate exclusively by way of email delivered (once converted into EDI format) to electronic mailboxes. If a customer's recipient is also a subscriber to Company's service, the converted data is placed into a mailbox on Company's VAN. If the recipient uses a competitor's service, the converted data is "handed off" to the competing VAN for delivery to the recipient's mailbox on that VAN. The cost of such transmission, including any sales tax, is paid by Company. Company neither claims a resale exemption on the cost of the transmission, nor are customers separately billed for these costs.

VAN customers are provided with an electronic mailbox, which is hosted on the Company's servers. Customers log into a web-based portal to access their mailbox. An online dashboard allows customers to store, archive, search, and track transactions in their inbox and outboxes and queue transactions for processing. The service provides detailed transaction reporting for the purposes of monitoring, auditing, and tracking. Some customers can upload files that are already in standard EDI formats. These customers benefit primarily from the VAN's electronic mailbox capability, including the ability to actively manage their inboxes and outboxes and track transactions. Other customers have the ability to upload data in virtually any format (e.g. traditional email, unstructured text files or faxes) and have that data translated and converted into the necessary standard capable of being recognized and processed by the recipient as an EDI transaction. The EDI VAN service supports all current EDI data standards, as well as proprietary standards, the XML standard, financial industry standards and others depending on which is employed by the customer or its recipient.

Customers are charged a monthly usage fee based on the volume of both incoming and outgoing transactions. The charge is calculated on total kilocharacters per message. If both the sender and recipient of a transaction are customers, both are charged for the transaction. If only the sender is a customer, then only the sender is charged. The service agreement between Company and the customer provides that

both parties are responsible for paying their own telecommunications line(s) and usage fees to their respective telecommunications provider pursuant to their own agreements. No tangible personal property is transferred to the customer under the service.

3. *Broadcast Fax*

The broadcast fax service automates the creation and distribution of high-volume fax-based messages. Examples of typical applications of the service include an electric utility needing to issue warnings of power outages or service interruptions, and travel companies needing to send promotional offers—all of which must be output to a large volume of recipients. Customers are able to upload a single message containing the data specific for that communication, and the message is merged with other text files (i.e. mailing lists and stored formats) to create multiple messages personalized and delivered to multiple recipients. Company's servers accept various forms of uploaded data from customers' systems, including files transferred via SMTP, FTP, and application programming interface. Customers can access the broadcast fax service via a web-based portal.

Customers use their own third-party telecommunications carrier or internet access provider to access the service and to upload data. In addition, customers can access the service either over the internet, via a virtual private network (VPN) or other methods such as FTP or message queue (MQ).

Customers wishing to initiate a broadcast fax message typically upload a digital file containing the general content of the message, accompanied by other unstructured text files such as recipient fax lists and/or additional content to be inserted into the fax message. Customers can also set preferences and store data on Company's servers by using the web portal. This includes storing recipient lists, business rules and preferences, in addition to customized logos and cover pages applicable to all messages. The broadcast fax service parses and combines the customer's message with any stored or attached text files, applies any stored business rules or preferences, and creates a personalized fax message for each intended recipient. The merged and processed data is then converted into "TIFF" format for delivery to recipients either via internet/ digital connectivity or via third-party telephony lines.

Charges for third-party telecommunications services to deliver processed fax messages from Company's servers are borne by Company, including any taxes. Company neither claims a resale exemption, nor is the charge for the transmission services separately billed to Company's customers.

The broadcast fax service provides customers with detailed delivery and attempted delivery reports for all recipients as well as management reports allowing customers to monitor the service and provide a complete audit trail for all transactions.

Broadcast fax customers are charged a single, per-page fee for processing a transaction; the cost per page varies based on the global location of the recipients. The customer is not separately billed for the transmission of processed messages.

4. *Production Messaging (Notifications Email/Production Email)*

This service enables customers to automate the creation and delivery of high volumes of outbound electronic messages that require customization for each recipient.

The Production email service allows the same message uploaded by the customer to be delivered to multiple addresses, or allows customized messages to be created and delivered to each individual recipient. The message is almost always personalized and unique for each recipient. Typical applications for production email include customer billing statements, letters of credit, and trade confirmations.

The service allows customers to upload a single message common for all recipients, along with unstructured text files containing specific data necessary for each intended recipient. The message is then personalized according to the business rules and other information supplied by the customer. Data fields can be merged, logos can be added, and other customizations can be performed before messages are delivered to individual recipients.

The service also allows file attachments, trackable web links to other websites (notifications email), and/ or recipient-specific data not included in an attachment or in the message itself (both services) to be added to the message. The data can be stored on Company's servers for retrieval by message recipients.

Once the data is uploaded, Company's proprietary software processes the customer's message, along with any accompanying text files, stored business preferences, logos and / or other customizations to create individual messages addressed to each intended recipient. The service provides customers with the ability to store business rules and customizations on Company's servers for application to all outbound messages.

Company's servers accept various data formats from customers' systems, including SMTP, FTP, API, and data entered through web-based portal accessible by customers of both services. Customers utilize their own third-party telecommunications or internet access provider to transmit the data onto Company' servers. Any costs for this transmission/connectivity are borne by the customer.

Customers may receive detailed reports of attempted, successful, and unsuccessful deliveries. Additionally, customers can access other management reports allowing them to monitor usage of the service and provide a complete audit trail for all transactions.

The service is billed on a per-transaction basis (i.e. per email). Customers are charged both for successful deliveries and attempted and reattempted deliveries. Company optionally receives additional revenue when a customer's recipient clicks a link to retrieve any stored files or data intended for them. Company and their customers are responsible for paying their own telecommunications access and usage fees to their respective telecommunications providers, along with any applicable taxes. Company does not separately bill customers for its telecommunications costs.

Discussion

1) *Integrated Desktop Messaging*

Colorado imposes a sales tax on the sale of intrastate telephone and telegraph services.² This tax is levied on "telephone and telegraph services, whether furnished by public or private corporations or enterprises for all intrastate telephone and telegraph... service." Department Regulation (39)26-104.1(c)(l)(a) defines telephone and telegraph services to include, but not limited to:

On or after August 1, 2002, all telephone and telegraph services except those services defined as mobile telecommunications services under 4 United States Code section 124(7), which are intrastate telephone and telegraph service are subject to the tax imposed by C.R.S. 39-26-106, whether furnished by public, private, mutual, cooperative, or governmental corporations or agencies. The term "service" includes but is not limited to additional listings, joint-user service, non-talking circuits, leased circuits and facilities, local exchange service (whether on a flat or measured basis), information charges, service connection charges, and any other charges assessed or passed on to the consumer with the exception of charges for installation or repair which are taxed according to the Special Regulation on Contractors. Telephone service is taxable whether either local or toll calls are made or telegrams are sent from telephone pay stations.

Whether fax services constitute a telephone service or telegraph service is a difficult and close question. On the one hand, the terms "telephone" and "telegraph" services are broadly construed for sales and use tax purposes.³ In *AT&T Communications of the Mountain States v. Charnes*, 78 P2d 677 (Colo. 1989), the Court concluded that this statute should not be interpreted as applying only to the technology that existed when the statute was first enacted but, rather, should be broadly interpreted to apply to telephone and telegraph service as the technology underlying the services evolves. Fax services are neither defined in statute nor in Department regulation. However, fax is commonly understood to mean "a system for sending and receiving printed materials (such as documents and drawings) and photographs using telephone lines."⁴ The Department has traditionally viewed telephone services as, fundamentally, an open communication line and any related services required for two or more parties to communicate instantaneously in a two-way communication. In contrast, a fax service is viewed as a one way, closed communication. That is, the party receiving the fax does not have the ability to instantaneously respond.⁵ Therefore, we conclude that fax service is not a telephone service subject to sales or use tax.

² §39-26-104(c)(l), C.R.S.

³ *AT&T Communications of the Mountain States, INC v. Alan Charnes*, 78 P2d 677 (Colo. 1989). See, also, §39-26-104(c)(l), C.R.S., which states that it applies to "all" intrastate telephone and telegraph services.

⁴ "Fax" 2014. In *Merriam-Webster.com*. Retrieved October 28, 2014 from <http://www.merriam-webster.com/dictionary/fax>

⁵ We understand that the process of faxing initially requires the interactive transmission of signals by both parties (a.k.a. a "handshake") to create the communication link and to terminate the link, but the actual faxing is generally a one-way communication.

Telegraph service is commonly defined as a system for electronically transmitting messages over a distance by creating signals by making and breaking an electrical connection.⁶ The Department has viewed this communication as limited to text communications. When someone sends a fax, they are essentially transmitting an object, in this case an electronic image. That is, a fax is the transmission of an image and the fax, itself, is not a text message that can be reconstituted into text. We acknowledge the obvious that a fax also serves as a means of sending printed communications (e.g., faxing a letter to the recipient). However, and on balance, we conclude that this image is the true object of the transaction and, therefore, fax service is not a telegraph service subject to sales and use tax.

Company's IDM service allows customers to replace a traditional facsimile infrastructure with an electronic based platform for sending and receiving documents. Company, in essence, is providing a service similar to a traditional fax service. If a customer took a desired communication to an office supply store who uses traditional fax services and had the store format it and send the fax to its desired party, the charges for those services would not be subject to tax. Therefore, we do not believe Company's IDM services are subject to tax.

Traditional telephone and telegraph lines must be utilized for fax and facsimile services. Those telephone and telegraph lines are subject to tax, and the fax or facsimile service providers are considered to be the consumers of the telephone and telegraph lines, and, therefore, must pay tax on the purchase of those lines.

2) *Electronic Data Interchange (EDI) Value Added Network (VAN) Services*

EDI VAN is a form of business to business communication that allows routine business documents, such as purchase orders invoices, shipping confirmations, and other invoices, to be exchanged electronically among trading partners and others utilizing industry-standard data formats. The structured formats allow such documents to be processed automatically by the partners' computer systems without the need for manual intervention. As previously noted in the background, Company's EDI VAN service eliminates the need for a customer to establish and manage individual interconnects with trading partners, and it ensures EDI transactions can be exchanged and processed regardless of whether the recipient's data standards or computer systems are otherwise compatible.

The Department believes customers utilize the EDI VAN services in order to access Company's proprietary software that formats their communications accordingly, and that the transmission portion of the service is incidental to the entire service. In essence, the true object of the transaction is the data conversion service, not the data transmission service. Therefore, we rule that Company's EDI VAN services are not subject to sales and use tax.⁷ Finally, Company is considered to be the

⁶ "Telegraph" 2014. In *oxforddictionaries.com*. Retrieved October 28, 2014 from http://www.oxforddictionaries.com/us/definition/american_english/telegraph

⁷ EDI VAN services are not commonly viewed as traditional telephone and telegraph services. See the *Streamlined Sales and Use Tax Agreement, Amended October 8, 2014* in part: "Telecommunications service" does not include:

- a. Data processing and information services that allow data to be generated, acquired, stored, processed, or retrieved and delivered by an electronic transmission to a purchaser where

consumer of the telephone and telegraph services it uses in the provision of the EDI VAN service and is, therefore, required to pay tax on such purchases.

3) *Broadcast Fax*

Broadcast fax services replace the need for a traditional fax infrastructure. A customer has the ability to utilize Company's proprietary software to send out mass faxes instead of sending out faxes to desired parties one at a time. Had a customer employed the services of a traditional fax or facsimile service provider, and sent each communication one at a time, those service charges would not be subject to taxation. This service is similar to IDM, and, therefore, conclude that charges for the broadcast fax service are not subject to taxation. Finally, and as the case with IDM, Company is considered to be the consumer of the telephone and telegraph services utilized in the provision of the broadcast fax service.

4) *Production Messaging (Production Email)*

As with the other services addressed in this ruling, it is a close question whether or not an email could be considered a telegraph service. As previously noted, the Department considers text communications to be a form of telegraph service subject to tax. When a person sends an email, he or she inputs and sends a text communication together with any attachments or images. By definition, email services could fall within the purview of telegraph services.

However, the Internet Tax Freedom Act ("ITFA") prevents state taxation of email services. Therefore, we do not need to reach a conclusion on this issue in this ruling. ITFA has preempted state taxation of "internet access" services since its original enactment in 1998.⁸ The original definition of "internet access" applied only to services that actually provided a connection to the internet (i.e. "a service that enables users to connect to the internet to access content, information or other services offered over the internet").⁹ In other words, the prior definition applied only to internet service providers ("ISPs").

In 2007, Congress significantly expanded the scope of what was intended to be covered by the tax moratorium. First, the definition of "internet access" was expanded to include services deemed "incidental to" providing an internet connection, including a "home page, electronic mail and instant messaging *including voice- and video-capable electronic mail and instant messaging*, video clips, and personal electronic storage capacity."¹⁰ More importantly, the 2007 act also provided that these types of "incidental" services were exempt from state taxation whether provided in connection with internet access services or not.

The essence of this service is very similar to the ubiquitous email services of Google, Yahoo, and many other web-based providers. Users of such systems send data, including documents and image files, to recipients via the internet. If a customer were to customize each email and sent it individually to each desired recipient, any charges for those communications would not be subject to tax.

such purchaser's primary purpose for the underlying transaction is the processed data or information;"

⁸ See Internet Tax Freedom Act, Pub. L. No. 105-277 (1998). Codified at 47 U.S.C. § 151.

⁹ Pub. L. No. 105-277 former § 1104(5).

¹⁰ Pub. L. No. 105-277, as amended by Pub. L. 110-108 (2007), § 1105(5)(E) (*emphasis added*).

Therefore, we conclude that Company's charges for production email are not subject to tax.

Miscellaneous

This ruling applies only to sales and use taxes administered by the Department. Please note that the Department administers state and state-collected city and county sales taxes and special district sales and use taxes, but does not administer sales and use taxes for self-collected home rule cities and counties. You may wish to consult with local governments which administer their own sales or use taxes about the applicability of those taxes. Visit our web site at www.colorado.gov/revenue/tax for more information about state and local sales taxes.

This ruling is premised on the assumption that Company has completely and accurately disclosed all material facts. The Department reserves the right, among others, to independently evaluate Company's representations. This ruling is null and void if any such representation is incorrect and has a material bearing on the conclusions reached in this ruling. This ruling is subject to modification or revocation in accordance to Department Regulation 24-35-103.5.

Enclosed is a redacted version of this ruling. Pursuant to statute and regulation, this redacted version of the ruling will be made public within 60 days of the date of this letter. Please let me know in writing within that 60 day period whether you have any suggestions or concerns about this redacted version of the ruling.

Sincerely,

Office of Tax Policy
Colorado Department of Revenue