



STOLL
KEENON
OGDEN

STATE & FEDERAL TAX PRACTICE

Timothy Eifler
Louisville
502.568.4208
Timothy.Eifler@skofirm.com

Jennifer S. Smart
Lexington
859.231.3619
Jennifer.Smart@skofirm.com

Erica L. Horn
Lexington
859.231.3037
Erica.Horn@skofirm.com

Jackson White
Lexington
859.231.3617
Jackson.White@skofirm.com

Kentucky Court of Appeals Rules Prepaid Wireless Provider Subject To Commercial Mobile Radio Service Charge

Jennifer S. Smart

In *Virgin Mobile USA, LP v. Commonwealth of Kentucky on behalf of the Commercial Mobile Radio Service Telecommunications Bd.*, Ky. Ct. of Appeals, Docket. No. 2010-CA-001185-MR and No. 2010-CA-001266 (June 29, 2012), the Kentucky Court of Appeals (“Court”) held that Virgin Mobile USA, LP (“Virgin Mobile”) was subject to the Commercial Mobile Radio Service (“CMRS”) “service charge” imposed under KRS 65.7629 prior to amendments in July 2006 specifically imposing the charge on prepaid wireless connections.

The Court examined the background and history of KRS 65.7621-65.7643, the CMRS Act, which was enacted in 1998 in response to a mandate from the Federal Communications Commission requiring all emergency 911 systems to service wireless callers. Virgin Mobile was a reseller of wireless services over the Sprint Network during the periods at issue, 2002 through 2005. Its customers prepaid for their service and did not receive phone bills.

Virgin Mobile remitted the CMRS service charge to the Commercial Mobile Radio Service Telecommunications Board (“Board”) from 2002 through 2005. However, rather than collecting the tax from its customers, Virgin Mobile remitted the tax from its general revenues. Virgin Mobile stopped remitting the tax in June 2005 and requested refunds of all prior payments after learning that several national tax reporting agencies had determined the service charge did not apply to prepaid wireless services. The Board refused to issue the refunds.

After the statutes were amended in July 2006 to clearly apply to prepaid wireless connections, Virgin Mobile began crediting its prior payments against the services charges. Virgin Mobile began remitting tax in November 2008 after exhausting its credit.

The Board filed suit against Virgin Mobile in Jefferson Circuit Court (“Circuit Court”) which held for the Board, awarding it the service charges, as well as additional amounts, that Virgin Mobile did not remit between 2005 and 2007. The Circuit Court also awarded the Board post-judgment interest, but denied its request for prejudgment interest. The Board filed a motion requesting prejudgment interest and attorney’s fees. The Circuit Court again denied the Board’s request for prejudgment interest, but granted its request for attorney’s fees.

The Court first noted that the issues before it were disputed questions of law, so that it was not bound by the Circuit Court’s decision, but would review the decision *de novo*. The Court indicated that Virgin Mobile raised three issues on appeal: (1) the Circuit Court erred in holding

that the CMRS service charge applied to it prior to the July 2006 amendments; (2) Virgin Mobile was entitled to a refund of amounts mistakenly paid or a credit for such amounts against post-July 2006 charges; and (3) the Circuit Court erred in requiring Virgin Mobile to pay the Board's attorney's fees. In response, the Board argued: (1) the Circuit Court correctly held that the statutes in effect prior to 2006 applied to prepaid wireless customers and providers; (2) Virgin Mobile was not entitled to a refund or credit for the taxes it had remitted; and (3) the Circuit Court correctly awarded the Board its attorney's fees pursuant to KRS 65.7635(5). Further, in its cross-appeal the Board argued that it was entitled to prejudgment interest.

The Court held that a plain reading of KRS 65.7629 left no question but that the tax applied to CMRS providers, defined in the statute as "a person or entity who provides CMRS to an end user, including resellers." The Court determined that Virgin Mobile was a CMRS provider because it clearly provided mobile phone services to its customers, whether those services were purchased directly from Virgin Mobile or through a third-party retailer and subsequently activated by Virgin Mobile. The Court determined that the 2006 amendments changed only the permissible methods of collection and not the duty to collect.

The Court next held that because it affirmed the Circuit Court in finding that the pre-2006 statute applied to Virgin Mobile and it was required to collect the charges in question, the issue of whether it was entitled to a refund or credit was moot and it declined to address the issue further.

The Court noted that KRS 65.7635(5) authorizes an award of attorney's fees to the prevailing party in litigation. The Court determined that the statute was "somewhat unclear" and recognized that national tax services had opined that prepaid wireless providers were not subject to the taxes. Accordingly, the Court held that Virgin Mobile disputed payment of the charges in good faith and held that the Circuit Court exceeded its discretion in ordering Virgin Mobile to pay the Board's attorney's fees. It therefore reversed the Circuit Court's award of attorney's fees.

The Court next addressed the Board's cross-appeal, where it argued that it was entitled to prejudgment interest because: (1) the CMRS service charge was not a tax; (2) if the CMRS service charge were a tax, KRS 131.183 allows prejudgment interest; and (3) the CMRS Board was entitled to prejudgment interest on a liquidated sum. The Court indicated that Virgin Mobile argued in response: (1) the fee was indeed a tax; (2) interest on taxes is not authorized unless specifically provided by statute; (3) KRS 131.183 does not provide for prejudgment interest; and (4) Kentucky law is clear that prejudgment interest shall not be awarded where there is a good faith dispute as to whether the amount was actually due and owing.

The Court first opined that a trial court's decision to deny prejudgment interest must be reviewed under an abuse of discretion standard. The Court reviewed the language of KRS 131.183, and held that because it only authorized interest on taxes administered by the Department of Revenue and did not extend to taxes administered by the Board, it excluded other taxes, including those administered by the Board. The Court also held that Virgin Mobile disputed the CMRS tax in good faith in reliance upon national tax and business law information services as well as its own accountants and tax advisors. It therefore affirmed the Circuit Court's decision holding that prejudgment interest was improper.

On July 19, 2012, Virgin Mobile filed a Petition for Modification or Extension of Opinion with the Court, first indicating that it agreed with the Court's conclusion regarding prejudgment interest and attorney's fees, but that it disagreed with its determinations on all other issues, which it reserved for discretionary review by the Kentucky Supreme Court. Virgin Mobile then requested that the Court modify or extend the Opinion to hold that the Opinion applies only prospectively from the effective date of the CMRS Act's 2006 amendments specifically referencing prepaid services.

The author's law firm represents Virgin Mobile in this case.