BELLSOUTH

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June 15, 2007

Ms. Beth O'Donnell
Executive Director
Public Service Commission
211 Sower Boulevard
P.O. Box 615
Frankfort, KY 40602

Re: Dialog Telecommunications, Inc., Complainant v. BellSouth Telecommunications, Inc., Defendant
KPSC 2005-00095

Dear Ms. O'Donnell:

Enclosed for filing in the above-referenced matter are the original and ten (10) copies of AT&T Kentucky's Supplemental Brief.

Sincerely,

Mary K. Keyer/bf
Mary K. Keyer

cc: Parties of Record

681578

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

DIALOG TELECOMMUNICATIONS, INC.	)	
	)	
v.	)	CASE NO. 2005-00095
	)	
BELLSOUTH TELECOMMUNICATIONS, INC.	)	

SUPPLEMENTAL BRIEF OF AT&T KENTUCKY

In accordance with the Commission's Order dated May 30, 2007, BellSouth Telecommunications, Inc., d/b/a AT&T Kentucky ("AT&T Kentucky"),[1] respectfully supplements its prior response to the arguments raised by Dialog Telecommunications, Inc. ("Dialog") in its the Motion for Reconsideration or, in the Alternative, to Reopen and Modify Order to Conform to Applicable Law ("Motion to Reopen").[2] As explained herein, under the plain terms of the parties' interconnection agreement ("ICA" or "contract") regarding payment of taxes, Dialog has a contractual obligation to pay the amounts it has refused to pay. Further, sound policy considerations and fundamental fairness – both of which are completely consistent with the parties' contract --- require Dialog to pay the amounts it has wrongfully withheld based on Dialog's unsupported belief that it should not be obligated to pay Kentucky sales tax on unbundled network elements ("UNEs") bought from AT&T Kentucky.

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[1] BellSouth Telecommunications, Inc. is now doing business in the Commonwealth of Kentucky as AT&T Kentucky and will be referred to herein as "AT&T Kentucky" rather than "BellSouth."

[2] AT&T Kentucky incorporates by reference its prior response Dialog's Motion to Reopen, including its motion to strike the affidavit of Steven L. Lenarz, which was attached to the Motion to Reopen. Given the Commission's desire to fully and fairly resolve all issues raised by the parties, *see* ¶¶ 13-18 of the Commission's Motion to Remand filed with the Franklin Circuit Court, AT&T Kentucky will address the substance and relevance of the Lenarz Affidavit, notwithstanding its pending motion to strike the same.

BACKGROUND

As the Commission is aware, in its Order dated March 23, 2007 ("*Recon Order*"), the Commission noted that Dialog did not dispute that it had withheld payment of over $530,000 in an attempt to effectively avoid paying Kentucky sales taxes which it contends it should not be obligated to pay.[3] Reluctantly and belatedly, Dialog has conceded that it has not paid such amount.[4] Based on certain language in the parties' ICA regarding the payment of taxes,[5] and the uncontested fact that Dialog had withheld payment of the tax in question (a point Dialog now concedes), the Commission concluded that "Dialog must pay the tax in question."[6]

Thereafter, Dialog moved to reopen the *Recon Order.* In its Motion to Reopen, Dialog submitted the Lenarz Affidavit to support its contention that the Commission's interpretation of the parties' contract (specifically, General Terms & Conditions "GTCs" Section 11.4.4) was "based upon fundamental errors of *tax* law"[7] and that AT&T Kentucky can seek a tax refund – *under Kentucky tax law* – notwithstanding the fact that Dialog has refused to pay the tax in question.[8] As discussed below, even if true, the

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3 *See Recon Order* at 2-3 and AT&T Kentucky's Motion for Reconsideration.

4 *See* Reply of Dialog Telecommunications, Inc. to BellSouth Response and Motion to Strike at 4. In an example of "double-speak" that defies description, Dialog makes the incredulous claim that its **May 2006** representation to Commission it had paid the taxes in full was accurate, *Id.* at 3-4. Dialog makes this claim, despite the fact that Dialog does not dispute that **prior to making such representation, Dialog had withheld from payment hundreds of thousand of dollars** based upon its contention that it should not be obligated to pay sales tax on UNEs. *See* Affidavit of Roger Edmonds, attached as Exhibit 1 to AT&T Kentucky's Motion for Rehearing and/or Reconsideration. In short, Dialog's claim that it has not misrepresented the facts is completely devoid of any semblance of merit and is ample reason to question any assertion made by Dialog.

5 Section 11.4.4 of the General Terms and Conditions ("GTCs") portion of the ICA.

6 *Recon Order* at 3.

7 Motion to Reopen (pages are not numbered).

8 Motion to Reopen (pages are not numbered).

Lenarz Affidavit does not negate the fact that Dialog has a contractual obligation to pay the tax in question. Accordingly, the Commission should reaffirm its *Recon Order.*

DIALOG HAS A CONTRACUAL OBLIGATION TO PAY THE AMOUNTS IT HAS REFUSED TO PAY

In the Commission's motion to remand – a motion that AT&T Kentucky did not oppose -- the Commission made clear that "[n]o question should be left unresolved"[9] in its desire to fully, fairly, and correctly resolve the sole issue in this case – i.e. whether Dialog has a ***contractual obligation*** to pay AT&T Kentucky the amount it has steadfastly refused to pay based on Dialog's contention that it should not be required to pay Kentucky sales tax on UNEs purchased from AT&T Kentucky.[10]

To assist the Commission in its endeavor to correctly interpret and enforce the tax provisions that are contained in the parties' ICA, the ICA's entire tax section is attached hereto as Exhibit "A".[11] A review of sections 11.4.3 and 11.4.4 demonstrates that Dialog has an unquestioned contractual obligation to pay the amounts it has refused to pay.

In concluding that Dialog has an obligation to pay the amounts it has refused to pay, the Commission relied upon the following contract language:

> In the event that all or any portion of an amount sought to be collected must be paid in order to contest the imposition of any such tax or fee, or to avoid the existence of a lien on the assets of the providing Party [AT&T Kentucky] during the pendency of such contest, the purchasing Party

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9 Motion to Remand, at ¶ 15.

10 *See* Motion to Remand, at ¶ 12 ("The question is whether, in issuing the March 23 Order, the Commission incorrectly interpreted the Interconnection Agreement by ordering Dialog to pay the unbundled network elements sales tax to BellSouth before requiring BellSouth to seek a refund through the Department of Revenue.")

11 Exhibit "A" is an excerpt from the parties' prior contract (executed in November 2001). This contract was in effect when Dialog first raised the tax issue and when Dialog filed this complaint (Dialog executed its current ICA in March 2006).

> [Dialog] shall be responsible for payment and shall be entitled to any refund or recovery.[12]

While the Commission has reached the correct decision, it is not necessary to rely exclusively on this provision of the contract. Indeed, AT&T Kentucky has never taken the position that the tax was required to be paid *to the Commonwealth* in order to contest its imposition.[13] Rather, AT&T Kentucky has consistently maintained that, under the ICA, it has the right to require Dialog to pay the tax as a condition of contesting its imposition with the Commonwealth. This right to payment arises under GTCs Section 11.4.3.

Exclusively focusing on GTCs Section 11.4.4 – in the manner suggested by Dialog --- while ignoring other relevant tax provisions, renders GTCs Section 11.4.3 meaningless. Under black letter contract law, a contract must be construed as a whole. Cantrell Supply, Inc. v. Liberty Mutual Ins., 94 S.W.3d 381, 384-385 (KY Ct. App. 2002) ("Any contract or agreement must be construed as a whole, giving effect to all parts and every word in it if possible.") (quoting City of Louisa v. Newland, 705 S.W.2d 916, 919 (KY 1986). Accordingly, black letter contract law requires the Commission to give effect to GTCs Section 11.4.3. In so doing, the Commission must necessarily reaffirm its prior conclusion. That is, Dialog has a contractual obligation to pay the amounts it has refused to pay.

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[12] ICA, GTCs Section 11.4.4.

[13] On several occasions, AT&T Kentucky has made the common sense observation that AT&T Kentucky cannot seek a refund *on Dialog's behalf* of amounts Dialog has not paid. AT&T Kentucky stands by this factually correct statement. More importantly, this statement should not be incorrectly construed as an assertion that *under Kentucky sales tax law,* a sales tax must be paid or must be collected from the customer before its imposition can be contested.

As noted in its Motion to Reopen, AT&T Kentucky has paid the tax amounts Dialog has refused to pay.[14] Accordingly, it is AT&T Kentucky that has suffered harm by paying taxes that Dialog has unreasonably refused to pay. Moreover, it is Dialog that has gained an unfair and improper competitive advantage over all contract-abiding (i.e. tax paying) competitive local exchange carriers ("CLECs") operating in Kentucky that buy UNEs from AT&T Kentucky because such CLECs have paid the amounts that Dialog has refused to pay. Since the taxes in question have been paid, the Lenarz Affidavit is effectively irrelevant (or moot) as it focuses on whether a Kentucky retailer -- under Kentucky tax law – can challenge a sales tax without paying it. Here, the taxes have been paid and AT&T Kentucky wishes to exercise its contractual right to be reimbursed amounts that it is out-of-pocket. Indeed, taken to its logical conclusion, the Lenarz Affidavit squarely supports the position that GTCs Section 11.4.4 is not applicable in a state like Kentucky (since a Kentucky tax payer does not have to pay a tax in order to challenge it). As such, the Lenarz Affidavit is irrelevant.

Moreover, and more importantly, even if relevant, the Lenarz Affidavit does not negate the fact that Dialog has a ***contractual obligation*** under GTCs Section 11.4.3 to pay the amounts it has refused to pay. In short, under GTCs Section 11.4.3, when the Purchasing Party (in this case, Dialog) disputes the application of a tax to products or services purchased under the ICA, the Purchasing Party (Dialog) can be required to bear the burden of the tax while it is being challenged by the Providing Party (here, AT&T Kentucky) . GTCs Section 11.4.3 provides that:

> If the purchasing Party [Dialog] disagrees with the providing Party's [AT&T Kentucky] determination as to the application or basis for any such tax or fee, the Parties shall consult with respect to the imposition and billing of

[14] Motion to Reopen (pages are not numbered).

such tax or fee. Notwithstanding the foregoing, ***the providing Party [AT&T Kentucky] shall retain ultimate responsibility for determining whether and to what extent any such taxes or fees are applicable, and the purchasing Party [Dialog] shall abide by such determination and pay such taxes or fees to the providing Party [AT&T Kentucky].*** The providing Party [AT&T Kentucky] shall further retain ultimate responsibility for determining whether and how to contest the imposition of such taxes and fees; provided however, that any such contest undertaken at the request of the purchasing Party [Dialog] shall be at the purchasing Party's [Dialog] expense.[15]

Under Section 11.4.3, AT&T Kentucky "retains ultimate responsibility for determining whether and to what extent any such taxes or fees are applicable," and Dialog has a contractual obligation to "abide by such determination and pay such taxes or fees" to AT&T Kentucky. In addition, GTCs Section 11.4.3 expressly reserves to the Providing Party (AT&T Kentucky) the responsibility for determining "whether and how to contest the imposition of [the tax]." In this case, AT&T has exercised its right under GTCs Section 11.4.3 by agreeing to contest the tax through the filing of a refund claim *after payment of the tax by Dialog.* Given the stated position of the Kentucky Revenue Cabinet – Division of Tax Policy that UNEs are subject to tax,[16] AT&T Kentucky's decision in this respect is entirely reasonable. As authorized by GTCs Section 11.4.3, AT&T Kentucky has repeatedly advised that upon Dialog's payment of the amount that has been withheld, AT&T Kentucky will seek a tax refund in accordance with the parties' ICA.

AT&T Kentucky's position is reasonable for at least five reasons. First, requiring payment ensures that AT&T Kentucky treats CLECs in a non-discriminatory manner

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15 ICA, GTCs Section 11.4.3.

16 In its letter to Dialog addressing the taxability of the sale of UNEs, the Division of Tax Policy concluded that UNEs were taxable as telecommunications services, notwithstanding their characterization for regulatory purposes. In addition, however, the Division of Tax Policy concluded that, even if they were not considered communications services but rather a lease of facilities as Dialog had asserted, "this lease would be subject to sales tax as a lease of tangible personal property." *See* October 31, 2003 Letter from Richard Dobson to Edward Depp, a copy of which is attached hereto as Exhibit "B".

since other CLECs operating in Kentucky have paid the tax that Dialog refuses to pay. Second (and again from a non-discrimination perspective), requiring payment ensures that AT&T Kentucky does not impermissibly favor Dialog by allowing Dialog to materially breach the parties' contract regarding payment of taxes. Third, requiring payment is prudent given the fact that Dialog's "no sales tax on UNEs" position was squarely and unequivocally rejected by the Kentucky Revenue Cabinet – Division of Tax Policy (see Exhibit "B"). Fourth, under Kentucky law (KRS 139.260), the gross receipts of a seller (here, the receipts from the sale of UNEs to Dialog) are presumed to be taxable. Fifth, as set forth below, requiring payment makes good business sense for a number of reasons.

Requiring payment helps minimize AT&T Kentucky's financial exposure associated with pursuing tax claims on behalf of non-paying CLECs that subsequently go out of business while such tax claims are pending. Additionally, the failure to require a customer to pay sales tax owed by it will have the unintended consequence of encouraging customers not to pay the sales tax and increase the likelihood of frivolous tax disputes. Businesses with even the slightest quarrel with the sales tax statutes may choose to require a seller to challenge a tax because the challenge will not "cost" the customer anything; that is, the customer gets to hold onto its own cash while the seller contests the tax.[17] Stated otherwise, there is no downside to the customer for failing to

[17] Obviously, if the seller has already paid the tax, it would have to contest it by filing a refund claim. However, under Dialog's position, as set forth in its Motion to Reopen and in the Lenarz affidavit, a seller need not pay the tax in order to contest it. While this statement is technically true as a matter of tax law, according to Dialog, a seller would be required simply to accept a purchaser's unsupported assertion that tax does not apply in a particular case, decline to pay it to the Commonwealth, wait to be audited by the Department of Revenue and have the tax assessed, and then contest it before payment. This position completely defies logic. If it were that simple for purchasers to avoid, or at least significantly defer paying sales tax, virtually every purchaser would simply instruct their seller not to charge tax and instead to dispute it if and when assessed. This would wreak havoc on the Commonwealth's tax revenue stream and essentially defeat the General Assembly's purpose in enacting the sales tax.

pay the tax, and no incentive for the customer to carefully consider and analyze the merits of any refund claim.

Furthermore, AT&T Kentucky's reliance on GTCs Section 11.4.3 to require payment of disputed taxes is entirely consistent with the outcome that would apply generally in commercial contexts absent a contractual agreement: The seller of a good or service makes the initial determination as to whether the sale of that good or service is subject to sales tax, and the buyer has no right to require the seller to contest the taxability prior to payment. GTCs Section 11.4.3, however, also contemplates that the parties may disagree as to the taxability of a particular transaction, as is the case here. The section further recognizes that a decision regarding taxability must be made and explicitly states that the seller (AT&T Kentucky) is responsible for making that decision and that the purchaser (Dialog) must abide by that decision.

In sum, the Lenarz Affidavit does not implicate, undermine, or otherwise impact Dialog's contractual obligation to pay AT&T Kentucky the amounts it has refused to pay as required by GTCs Section 11.4.3. To the contrary, reliance on the Lenarz Affidavit in the manner suggested by Dialog eviscerates GTCs Section 11.4.3 and absolves Dialog of its contractual obligation to pay the disputed tax. The Commission should flatly reject Dialog's pleas for it to impermissibly "re-write" the parties' contract. It is well established under Kentucky law that "[t]he intention of the parties to a written instrument must be gathered from the four corners of the instrument." *See* Hoheimer v. Hoheimer, 30 S.W.3d 176, 178 (KY 2000) The contract's "four corners" make crystal clear that AT&T Kentucky has the contractual right to demand payment before pursuing a tax refund.

In any event, the Lenarz Affidavit is remarkable not so much for the points it makes but for the point it omits; that is, the sales tax statutes create the same sharing of

burdens and responsibilities between the seller and its customers as is created by the ICA between AT&T Kentucky and Dialog. Mr. Lenarz correctly states that Kentucky law places the legal incidence of the sales tax on the seller.[18] Ignored by Mr. Lenarz and Dialog is the consequence of this legal obligation --- that the **seller** must determine the applicability of the tax to the transactions in which it enters into with its customers. Moreover, **under KRS 139.260, the gross receipts of a seller are presumed to be taxable.**

Next, the sales tax statutes require AT&T Kentucky to **collect** the tax from its customers. KRS 139.210 provides, in relevant part, that "the tax **shall be required to be collected** by the retailer from the purchaser." (Emphasis added.) Thus it is mandatory—not discretionary—that the seller (AT&T Kentucky) collect the tax from the purchaser (Dialog).[19] In fact, a failure to do so can subject the seller (AT&T Kentucky) to penalties under KRS 131.180(2). Finally, Kentucky law contemplates (although admittedly does not require) that refund claims will be filed after the tax has been collected by the seller from the purchaser, as KRS 139.770(3) specifically requires amounts collected be refunded to the purchaser before the seller is entitled to any refund.

The Lenarz affidavit also correctly states that, under Kentucky law, a seller may contest the imposition of a sales tax before payment. In other words, if the Department of Revenue audits a seller and determines that the seller has underpaid sales tax, then the seller has the right under Kentucky law to contest that determination prior to

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[18] KRS 139.200 provides that "a tax is **imposed** upon all **retailers**." (Emphasis added.)

[19] Prior to 1990, KRS §139.210 had permissive rather than mandatory language. In other words, the statute provided "[T]he taxes herein imposed **may** be collected by the retailer from the consumer." (*See*, 1990 Ky. Acts Ch. 137, §1, emphasis added.) However, the change in the statute evidences the General Assembly's intent that customers pay sales tax to the seller and that the seller then forward the tax to the Commonwealth.

payment, i.e. a "pre-deprivation remedy." However, that does not mean, and the tax provisions of the ICA do not require, that the seller (AT&T Kentucky) simply accept a purchaser's (Dialog) position that the tax does not apply. This is especially relevant here, given the fact that Dialog's position has been previously rejected by the Department of Revenue's Division of Tax Policy, see Exhibit B.

Dialog's position in this matter is nothing more than an attempt to "game the system" by using the dispute resolution process of the ICA in order to avoid paying a tax that is due and to circumvent the procedures that it would otherwise be required to follow to contest the application of the tax. A ruling by the Commission adopting Dialog's position would lead to absurd and untenable results. As stated above, any purchaser of any product or service could require the seller to bear the economic burden of the sales tax simply by disputing the tax and forcing the seller to challenge it before the purchaser can be required to pay it. Under Dialog's interpretation of the ICA, it makes no difference whether the purchaser's position is well-founded or completely spurious. This is not what is contemplated by the sales tax law and certainly not what was intended by the tax provisions of the ICA.

CONCLUSION

Dialog has a contractual obligation to pay the substantial amount (over $530,000) that it has refused to pay AT&T Kentucky. The Lenarz Affidavit does not negate the fact that Dialog has a contractual obligation to pay the amounts it has refused to pay. Moreover, the parties' contractual provisions concerning payment of taxes (specifically, GTCs Section 11.4.3) is completely consistent with Kentucky law. Accordingly, the Commission should deny Dialog's Motion to Reopen and issue an Order that supplements and reaffirms the *Recon Order* by making clear that Dialog has a

contractual obligation under Section 11.4.3 to pay AT&T Kentucky the amounts that have been withheld.

Respectfully submitted,

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CERTIFICATE OF SERVICE – KPSC 2005-00095

It is hereby certified that a true and correct copy of the foregoing was served on the following individuals by mailing a copy thereof, this 15th day of June, 2007.

Jim Bellina
Dialog Telecommunications, Inc.
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Mary K. Keyer

Mary K. Keyer

EXHIBIT A

Customer Name: Choice Telephone Company Inc.

AGREEMENT
GENERAL TERMS AND CONDITIONS

THIS AGREEMENT is made by and between BellSouth Telecommunications, Inc., ("BellSouth"), a Georgia corporation, and Choice Telephone Company, a North Carolina corporation, and shall be deemed effective ten calendar days following the date of the last signature of both Parties ("Effective Date"). This Agreement may refer to either BellSouth or Choice Telephone Company or both as a "Party" or "Parties."

W I T N E S S E T H

WHEREAS, BellSouth is a local exchange telecommunications company authorized to provide telecommunications services in the states of Alabama, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina and Tennessee; and

WHEREAS, Choice Telephone Company is or seeks to become a CLEC authorized to provide telecommunications services in the states of Alabama, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina, and Tennessee; and

WHEREAS, Choice Telephone Company wishes to resell BellSouth's telecommunications services and purchase network elements and other services, and, solely in connection therewith, may wish to utilize Collocation Space or space available pursuant to Adjacent Arrangement (all as defined in Attachment 4 of this Agreement); and

WHEREAS, the Parties wish to interconnect their facilities and exchange traffic pursuant to Sections 251 and 252 of the Act.

NOW THEREFORE, in consideration of the mutual agreements contained herein, BellSouth and Choice Telephone Company agree as follows:

Definitions

Affiliate is defined as a person that (directly or indirectly) owns or controls, is owned or controlled by, or is under common ownership or control with, another person. For purposes of this paragraph, the term "own" means to own an equity interest (or equivalent thereof) of more than 10 percent.

Commission is defined as the appropriate regulatory agency in each of BellSouth's nine-state region, Alabama, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina, and Tennessee.

Competitive Local Exchange Carrier (CLEC) means a telephone company certificated by the Commission to provide local exchange service within BellSouth's franchised area.

however, that the assigning Party shall notify the other Party in writing of such assignment thirty (30) days prior to the Effective Date thereof and, provided further, if the assignee is an assignee of Choice Telephone Company, the assignee must provide evidence of Commission CLEC certification. The Parties shall amend this Agreement to reflect such assignments and shall work cooperatively to implement any changes required due to such assignment. All obligations and duties of any Party under this Agreement shall be binding on all successors in interest and assigns of such Party. No assignment or delegation hereof shall relieve the assignor of its obligations under this Agreement in the event that the assignee fails to perform such obligations.

10. Resolution of Disputes

Except as otherwise stated in this Agreement, if any dispute arises as to the interpretation of any provision of this Agreement or as to the proper implementation of this Agreement, the aggrieved Party shall petition the Commission for a resolution of the dispute. However, each Party reserves any rights it may have to seek judicial review of any ruling made by the Commission concerning this Agreement.

11. Taxes

11.1 Definition. For purposes of this Section, the terms "taxes" and "fees" shall include but not be limited to federal, state or local sales, use, excise, gross receipts or other taxes or tax-like fees of whatever nature and however designated (including tariff surcharges and any fees, charges or other payments, contractual or otherwise, for the use of public streets or rights of way, whether designated as franchise fees or otherwise) imposed, or sought to be imposed, on or with respect to the services furnished hereunder or measured by the charges or payments therefore, excluding any taxes levied on income.

11.2 Taxes and Fees Imposed Directly On Either Providing Party or Purchasing Party.

11.2.1 Taxes and fees imposed on the providing Party, which are not permitted or required to be passed on by the providing Party to its customer, shall be borne and paid by the providing Party.

11.2.2 Taxes and fees imposed on the purchasing Party, which are not required to be collected and/or remitted by the providing Party, shall be borne and paid by the purchasing Party.

11.3 Taxes and Fees Imposed on Purchasing Party But Collected And Remitted By Providing Party.

11.3.1 Taxes and fees imposed on the purchasing Party shall be borne by the purchasing Party, even if the obligation to collect and/or remit such taxes or fees is placed on the providing Party.

11.3.2 To the extent permitted by applicable law, any such taxes and/or fees shall be shown as separate items on applicable billing documents between the Parties. Notwithstanding the foregoing, the purchasing Party shall remain liable for any such taxes and fees regardless of whether they are actually billed by the providing Party at the time that the respective service is billed.

11.3.3 If the purchasing Party determines that in its opinion any such taxes or fees are not payable, the providing Party shall not bill such taxes or fees to the purchasing Party if the purchasing Party provides written certification, reasonably satisfactory to the providing Party, stating that it is exempt or otherwise not subject to the tax or fee, setting forth the basis therefor, and satisfying any other requirements under applicable law. If any authority seeks to collect any such tax or fee that the purchasing Party has determined and certified not to be payable, or any such tax or fee that was not billed by the providing Party, the purchasing Party may contest the same in good faith, at its own expense. In any such contest, the purchasing Party shall promptly furnish the providing Party with copies of all filings in any proceeding, protest, or legal challenge, all rulings issued in connection therewith, and all correspondence between the purchasing Party and the taxing authority.

11.3.4 In the event that all or any portion of an amount sought to be collected must be paid in order to contest the imposition of any such tax or fee, or to avoid the existence of a lien on the assets of the providing Party during the pendency of such contest, the purchasing Party shall be responsible for such payment and shall be entitled to the benefit of any refund or recovery.

11.3.5 If it is ultimately determined that any additional amount of such a tax or fee is due to the imposing authority, the purchasing Party shall pay such additional amount, including any interest and penalties thereon.

11.3.6 Notwithstanding any provision to the contrary, the purchasing Party shall protect, indemnify and hold harmless (and defend at the purchasing Party's expense) the providing Party from and against any such tax or fee, interest or penalties thereon, or other charges or payable expenses (including reasonable attorney fees) with respect thereto, which are incurred by the providing Party in connection with any claim for or contest of any such tax or fee.

11.3.7 Each Party shall notify the other Party in writing of any assessment, proposed assessment or other claim for any additional amount of such a tax or fee by a taxing authority; such notice to be provided, if possible, at least ten (10) days prior to the date by which a response, protest or other appeal must be filed, but in no event later than thirty (30) days after receipt of such assessment, proposed assessment or claim.

11.4 Taxes and Fees Imposed on Providing Party But Passed On To Purchasing Party.

11.4.1 Taxes and fees imposed on the providing Party, which are permitted or required to be passed on by the providing Party to its customer, shall be borne by the purchasing Party.

11.4.2 To the extent permitted by applicable law, any such taxes and/or fees shall be shown as separate items on applicable billing documents between the Parties. Notwithstanding the foregoing, the purchasing Party shall remain liable for any such taxes and fees regardless of whether they are actually billed by the providing Party at the time that the respective service is billed.

11.4.3 If the purchasing Party disagrees with the providing Party's determination as to the application or basis for any such tax or fee, the Parties shall consult with respect to the imposition and billing of such tax or fee. Notwithstanding the foregoing, the providing Party shall retain ultimate responsibility for determining whether and to what extent any such taxes or fees are applicable, and the purchasing Party shall abide by such determination and pay such taxes or fees to the providing Party. The providing Party shall further retain ultimate responsibility for determining whether and how to contest the imposition of such taxes and fees; provided, however, that any such contest undertaken at the request of the purchasing Party shall be at the purchasing Party's expense.

11.4.4 In the event that all or any portion of an amount sought to be collected must be paid in order to contest the imposition of any such tax or fee, or to avoid the existence of a lien on the assets of the providing Party during the pendency of such contest, the purchasing Party shall be responsible for such payment and shall be entitled to the benefit of any refund or recovery.

11.4.5 If it is ultimately determined that any additional amount of such a tax or fee is due to the imposing authority, the purchasing Party shall pay such additional amount, including any interest and penalties thereon.

11.4.6 Notwithstanding any provision to the contrary, the purchasing Party shall protect, indemnify and hold harmless (and defend at the purchasing Party's expense) the providing Party from and against any such tax or fee, interest or penalties thereon, or other reasonable charges or payable expenses (including reasonable attorneys' fees) with respect thereto, which are incurred by the providing Party in connection with any claim for or contest of any such tax or fee.

11.4.7 Each Party shall notify the other Party in writing of any assessment, proposed assessment or other claim for any additional amount of such a tax or fee by a taxing authority; such notice to be provided, if possible, at least ten (10) days prior to the date by which a response, protest or other appeal must be filed, but in no event later than thirty (30) days after receipt of such assessment, proposed assessment or claim.

11.5 Mutual Cooperation. In any contest of a tax or fee by one Party, the other Party shall cooperate fully by providing records, testimony and such additional information or assistance as may reasonably be necessary to pursue the contest.

Further, the other Party shall be reimbursed for any reasonable and necessary out-of-pocket copying and travel expenses incurred in assisting in such contest.

12. Force Majeure

In the event performance of this Agreement, or any obligation hereunder, is either directly or indirectly prevented, restricted, or interfered with by reason of fire, flood, earthquake or like acts of God, wars, revolution, civil commotion, explosion, acts of public enemy, embargo, acts of the government in its sovereign capacity, labor difficulties, including without limitation, strikes, slowdowns, picketing, or boycotts, unavailability of equipment from vendor, changes requested by Customer, or any other circumstances beyond the reasonable control and without the fault or negligence of the Party affected, the Party affected, upon giving prompt notice to the other Party, shall be excused from such performance on a day-to-day basis to the extent of such prevention, restriction, or interference (and the other Party shall likewise be excused from performance of its obligations on a day-to-day basis until the delay, restriction or interference has ceased); provided however, that the Party so affected shall use diligent efforts to avoid or remove such causes of non-performance and both Parties shall proceed whenever such causes are removed or cease.

13. Adoption of Agreements

BellSouth shall make available, pursuant to 47 USC § 252 and the FCC rules and regulations regarding such availability, to Choice Telephone Company any interconnection, service, or network element provided under any other agreement filed and approved pursuant to 47 USC § 252, provided a minimum of six months remains on the term of such agreement. The Parties shall adopt all rates, terms and conditions concerning such other interconnection, service or network element and any other rates, terms and conditions that are legitimately related to or were negotiated in exchange for or in conjunction with the interconnection, service or network element being adopted. The adopted interconnection, service, or network element and agreement shall apply to the same states as such other agreement. The term of the adopted agreement or provisions shall expire on the same date as set forth in the agreement that was adopted.

14. Modification of Agreement

14.1 If Choice Telephone Company changes its name or makes changes to its company structure or identity due to a merger, acquisition, transfer or any other reason, it is the responsibility of Choice Telephone Company to notify BellSouth of said change and request that an amendment to this Agreement, if necessary, be executed to reflect said change.

14.2 No modification, amendment, supplement to, or waiver of the Agreement or any of its provisions shall be effective and binding upon the Parties unless it is made in writing and duly signed by the Parties.

14.3 In the event that any effective legislative, regulatory, judicial or other legal action materially affects any material terms of this Agreement, or the ability of Choice

promise other than as expressly stated in this Agreement or as is contemporaneously or subsequently set forth in writing and executed by a duly authorized officer or representative of the Party to be bound thereby.

33.2 This Agreement includes Attachments with provisions for the following:

Resale
Network Elements and Other Services
Network Interconnection
Collocation
Access to Numbers and Number Portability
Pre-Ordering, Ordering and Provisioning, Maintenance and Repair
Billing and Billing Accuracy Certification
Rights-of-Way, Conduits and Pole Attachments
Performance Measurements
BellSouth Disaster Recovery Plan
Bona Fide Request/New Business Request Process

33.3 The following services are included as options for purchase by Choice Telephone Company pursuant to the terms and conditions set forth in this Agreement. Choice Telephone Company may elect to purchase said services by written request to its Account Manager if applicable:

Optional Daily Usage File (ODUF)
Enhanced Optional Daily Usage File (EODUF)
Access Daily Usage File (ADUF)
Line Information Database (LIDB) Storage
Centralized Message Distribution Service (CMDS)
Calling Name (CNAM)
LNP Data Base Query Service

IN WITNESS WHEREOF, the Parties have executed this Agreement the day and year written below.

BellSouth Telecommunications, Inc.	**Choice Telephone Company**
By: Signature on File	By: Signature on File
Name: C. W. Boltz	Name: Patrick L. Eudy
Title: Managing Director	Title: Chairman
Date: 11/13/01	Date: November 9, 2001

EXHIBIT B

KENTUCKY REVENUE CABINET
DIVISION OF TAX POLICY
200 FAIR OAKS LANE
FRANKFORT, KENTUCKY 40620
PHONE 502-564-6843
FAX 502-564-9565

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October 31, 2003

Edward T Depp
Dinsmore & Shohl LLP
1400 PNC Plaza
500 West Jefferson Street
Louisville, KY 40202

Dear Mr. Depp:

Your correspondence addressed to Mr. Kevin West of the Sales and Use Tax Branch has been forwarded to the Division of Tax Policy for review and response. You are requesting information regarding the application of sales tax on purchases made by your client, Dialog Telecommunications, Inc. (Dialog).

Dialog is a competitive local exchange carrier (CLEC) under the Telecommunications Act of 1996 (the Act). According to the provisions of the Act, Dialog is purchasing unbundled network elements (UNE's) from BellSouth at wholesale rates. These elements include 2-wire loop, a switch port, installation and repair services, switch processing, network transport, and voice mail services, etc. Your letter characterizes these elements as "pieces of the entire telecommunications system that are necessary to provide telecommunications services." By virtue of these wholesale purchases, Dialog is able to provide local exchange service to its own retail end-user customers.

The 1996 Telecommunications Act was to encourage greater competition by requiring the incumbent local exchange carriers (ILEC's) to give competitors access to their networks. Section 251(c)(4) of the Act characterizes this access as the resale at wholesale rates of any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers. In Section 5 of your ruling request, Overarching Concerns Regarding KRS 139.200, you also describe the transactions in question as the wholesale purchase of communications services. BellSouth is providing the pieces of communications service that Dialog packages into local exchange service and sells to its own customers.

The argument that Dialog's purchase of telecommunications elements such as the 2-Wire Loop and the switch port are a lease of "facilities" rather than communications service is not persuasive. BellSouth is clearly providing Dialog with a communications service that enables it to provide local telephone service to its own clients. However, for the sake of argument, even if the purchase of access to the phone line or switch port were characterized as a lease of facilities or communications equipment, this lease would be subject to sales tax as a lease of tangible personal property. Dialog's purchase of taxable services or property is no different than the hotel operator who pays sales tax on beds, linens, and other items for use in providing taxable accommodations services. The hotel

operator then collects sales tax from customers who pay for the hotel accommodations. The Court of Appeals held in *Kentucky Board of Tax Appeals v. Brown Hotel Co.*, 528 S.W.2d 715 (1975) that a service provider could not purchase tangible personal property exempt from tax based upon the theory that the hotel acquired the property for resale to its customers who are the ultimate users of the property when paying for the accommodations service.

According to the provisions of Kentucky Regulation 103 KAR 28:140, Section 2, "communications service providers that purchase communications services from facilities-based carriers to resell to their own customer base shall not claim the communications services purchased are exempt as being transactions for resale." Furthermore, BellSouth is properly following Section 3 of the Regulation in refusing to accept Dialog's issuance of a resale certificate for the communications services in question. Dialog is the consumer of the communications services purchased in these transactions as stated in Section 1 of the Regulation. The resale exclusion from the definition of retail sale in KRS 139.100 applies only to the sale of tangible personal property for resale.

You have also asserted that the Act prohibits Kentucky from imposing sales tax on your client's wholesale purchase of UNE's. Upon review, it is the Cabinet's position that the Act does not prohibit the statutes in question. There is no evidence that this so-called "collection scheme" is a barrier to the wholesale purchase of UNE's. In fact, the use of the UNE platform is being utilized by CLEC's now more than ever. Furthermore, it is the Cabinet's responsibility to administer the current language of the law as it applies to companies such as Dialog until such time as an appropriate legislative or judicial body determines otherwise.

If you should have any further questions regarding this matter, please do not hesitate to contact my office at (502) 564-6843, ext. 4442.

Sincerely,

Richard Dobson

Richard Dobson
Tax Consultant
Division of Tax Policy

C: Kevin West