

IN THE COURT OF APPEALS OF TENNESSEE
WESTERN SECTION AT NASHVILLE

MCI TELECOMMUNICATIONS)
CORPORATION,)

Plaintiff/Appellant,)

VS.)

JOE HUDDLESTON, COMMR.)
OF REVENUE OF THE STATE OF)
TENNESSEE and THE DEPT.)
OF REVENUE OF THE STATE)
OF TENNESSEE,)

Defendants/Appellees.)

Davidson Chancery No. 92-1907-III(I)

Appeal No. 01A01-9510-CH-00471

FILED

July 24, 1996

Cecil W. Crowson
Appellate Court Clerk

APPEAL FROM THE CHANCERY COURT OF DAVIDSON COUNTY
AT NASHVILLE, TENNESSEE
THE HONORABLE IRVIN H. KILCREASE, JR., CHANCELLOR

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AFFIRMED

ALAN E. HIGHERS, J.

CONCUR:

W. FRANK CRAWFORD, P.J., W.S.

DAVID R. FARMER, J.

MCI Telecommunications Corp. brought this suit challenging certain sales and use

taxes assessed against it by the Commissioner of Revenue of the State of Tennessee. The trial court upheld the Commissioner's assessment. MCI appealed and has raised the following issues for our consideration: (1) whether the trial court employed an improper standard of review and erroneously allocated the burden of proof, and (2) whether the trial court erred in interpreting and defining the term "conduit," as that term is used within the Tennessee sales and use tax statute. For the reasons stated below, we affirm the trial court's judgment.

The pertinent facts are undisputed. Between the years 1986 and 1989, MCI purchased and installed approximately \$13.5 million of fiber optic cable and fiber optic ground ("FOG") wire in Tennessee for use in its telecommunications network. Following an audit, the Tennessee Department of Revenue assessed a use tax against MCI in the amount of \$1,047,446.23, plus interest and applicable penalties. In 1992, MCI filed a complaint challenging the assessment on the basis that the fiber optic cable and FOG wire were not subject to Tennessee's sales and use tax because such items were not "tangible personal property," as defined by T.C.A. § 67-6-102.

T.C.A. § 67-6-201 imposes a sales and use tax on "tangible personal property."

Tangible personal property is defined as:

'Tangible personal property' means and includes personal property which may be seen, weighed, measured, felt, or touched, or is in any other manner perceptible to the sense. 'Tangible personal property' does not include stocks, bonds, notes, insurance or other obligations or securities. 'Tangible personal property' does not include utility poles, anchors, guys and conduits, and such facilities shall be deemed to be real property for the purposes of this chapter.

T.C.A. § 67-6-102(28) (Supp. 1995).

MCI contends that fiber optic cable and FOG wire are "conduit" within the meaning of the above provision and, therefore, are not subject to Tennessee's sales and use tax.

The trial court upheld the Commissioner's assessment, reasoning that MCI had

failed to prove by clear and convincing evidence that the Commissioner was in error. The trial court stated in its Memorandum Opinion as follows:

A taxpayer challenging a tax assessment has 'the heavy and exacting burden of proving error in the assessment.' Tennessee Farmers' Cooperative v. State Commissioner of Revenue, 736 S.W.2d 87, 90 (Tenn. 1987). The Commissioner is presumed to be correct, and unless error is shown by clear and convincing evidence, this Court will not disturb the Commissioner's assessment. (citations omitted)

* * * * *

The plaintiff has not carried its burden of proving error in the Commissioner's assessment by clear and convincing evidence.

* * * * *

While the plaintiff claims its definition of conduit is 'more appropriate,' it has not established by clear and convincing evidence that it was error for the Commissioner to adopt the definition found in the National Electric Safety Code. The plaintiff has therefore not met its burden of proof, and this Court will affirm the tax assessment together with applicable interest and penalties.

MCI's first contention on appeal is that the trial court employed an improper standard of review by presuming that the Commissioner's assessment was correct and by placing the burden upon MCI to prove otherwise by clear and convincing evidence. According to MCI, only factual determinations made by the Commissioner are entitled to a presumption of correctness. MCI argues that the Commissioner's conclusion that fiber optic cable and FOG wire are not "conduit" is a legal, rather than a factual determination.

In the present case, our task is to construe the subject statute and apply the law to the undisputed facts. We thus agree with MCI's assertion that our review of the trial court's judgment is *de novo*. Tibbals Flooring Co. V. Huddleston, 891 S.W.2d 196, 198 (Tenn. 1994); Beare Co. v. Tennessee Dept. Of Revenue, 858 S.W.2d 906, 907 (Tenn. 1993). Even assuming, without deciding, that the trial court erred regarding the burden of proof or the standard of review, it is nevertheless our opinion that any such error is harmless because we will conduct a *de novo* review of the record before us.

In a suit by a taxpayer claiming an exemption, the taxpayer bears the burden of proving entitlement to the exemption. Jersey Miniere Zinc Co. v. Jackson, 774 S.W.2d

928, 930 (Tenn. 1989); Silver Fleet Motor Exp. v. Carson, 219 S.W.2d 199, 200 (Tenn. 1949). In the recent case of Tibbals Flooring Co. v. Huddleston, 891 S.W.2d 196 (Tenn.1994), the Tennessee Supreme Court stated the applicable rules governing the construction and review of claimed exemptions from taxation:

First, our role in construing statutes is to ascertain and give effect to the legislative intent without unduly restricting or expanding a statute's coverage beyond its intended scope. State v. Sliger, 846 S.W.2d 262, 263 (Tenn. 1993). Next, we must determine the legislative intent, whenever possible, from the plain language of the statute, 'read in the context of the entire statute, without any forced or subtle construction which would extend or limit its meaning.' National Gas Distributors, Inc. v. State, 804 S.W.2d 66, 67 (Tenn. 1991). Since exemptions in tax statutes are strictly construed against the taxpayer, the burden is on the taxpayer to establish its exemption. Every presumption is against the exemption and a well-founded doubt is fatal to the claim. Kingsport Publishing Corp. v. Olsen, 667 S.W.2d 745 (Tenn. 1984); Shearin v. Woods, 597 S.W.2d 895 (Tenn.1980); Woods v. General Oils, Inc., 558 S.W.2d 433 (Tenn. 1977). Moreover, when, as here, there is no conflict in the evidence as to any material fact, the question on appeal is one of law, and our scope of review is *de novo* with no presumption of correctness accompanying the conclusions of law. Union Carbide Corp. v. Huddleston, 854 S.W.2d 87, 91 (Tenn. 1993).

Id. at 198.

The Court has also stated that "[t]echnical words in a statute are to be taken in their technical sense unless it is clear from the context that another sense was intended." Cordis Corp. v. Taylor, 762 S.W.2d 138, 139-40 (Tenn. 1988).

MCI argues that both fiber optic cable and FOG wire are "conduit," or, alternatively, that at least the outer shell of the FOG wire is "conduit." Conversely, the Commissioner's position is that fiber optic cable and FOG wire are cable, rather than "conduit," and are not exempt from sales and use tax.

At the outset of the trial, MCI and the Commissioner agreed that the term "conduit" as used in T.C.A. § 67-6-102(28) is a technical term and should be defined according to the telecommunications industry's standards. However, the parties disagreed as to the appropriate definition of the term "conduit."

Billy Stevenson, an expert in fiber optic cable, FOG wire, and telecommunications testified on behalf of MCI. Stevenson defined “conduit” as a “housing that contains and transmits a utility from Point A to Point B without impacting the environment on the outside of that particular conduit system.”

Dr. Francis Wells, a professor of electrical engineering, testified on behalf of the Commissioner. Wells based his definition of “conduit” upon the definition found in the National Electric Safety Code (“NESC”), which establishes guidelines applicable to the telecommunications industry and the electrical industry. The NESC defines “conduit” as “a structure containing one or more ducts.” A “duct” under the NESC is “a single enclosed raceway for conductors or cable.”

Fiber optic cables are bundles of hair-thin glass fibers through which laser light beams carry communications and other data at high speed. A cladding made of silica surrounds the bundled optic fibers in order to protect the fibers from the environment. FOG wire is more advanced than fiber optic cable. FOG is a composite product that consists of steel strands, which conduct electricity and prevent heat buildups, surrounding an aluminum pipe, which conducts electricity and protects the inner fibers from outer forces. Inside the pipe, tape and Kevlar surround the unit sheath, which contains the fiber optics.

Stevenson testified that both fiber optic cable and the outer portions of FOG wire are “conduit,” as that term is used within the telecommunications industry. Stevenson conceded, however, that to some extent, the NESC applies to the telecommunications industry.

In support of MCI’s position that the outer shell of the FOG wire is conduit, Pat Risen, a manager in the optical cable business, testified that it is possible to install the outer casing of the FOG wire into the ground and to subsequently pull fiber optics through it. Risen also stated, however, that FOG wire is manufactured as one unit and that installing the outer casing of FOG wire into the ground without fiber optics inside had never

been done and did not make business sense. Similarly, Stevenson testified that optic fibers are not placed into the outer casing once the casing has been laid in the ground because, as a practical matter, it is not economically feasible.

In contrast, Wells stated unequivocally that neither FOG wire nor fiber optic cable is “conduit.” Wells testified:

Q: Okay. Can you describe the roll [sic] of conduit and utility poles in a distribution network for a telephone company or electric utility?

A: Yes, sir.

Q: What would that be?

A: The poles, guide wires, conduits are pretty much permanent structures. They are installed essentially by mechanics, constructors. And after the poles and guide wires and conduits are in place, then the next crew comes in and installs cables and wires either in the ducts or on the poles.

* * * * *

Q: What is the relationship of cable to duct? How do those two things relate?

A: Cable is greased and pulled into a duct.

Q: Are those things distinguishable? Are they different?

A: Oh, yes. You can pull a cable back out of a duct if it hasn't welded itself in for some reason to pull it out and put it in another one. You can replace the cables in a duct, but the duct will be there.

* * * * *

Q: What is your opinion as to whether the fog wire is or is not a conduit?

A: My opinion is that there's no conduit here, this is a cable. We're looking at a sample of cable.

* * * * *

Q: With respect to the optical fiber that's inside the fog wire, do you have an opinion as to whether or not that is a conduit?

A: Yes, sir.

Q: What is your opinion?

A: It is not a conduit.

Q: What is the basis for your opinion?

A: Well, a conduit is a duct that you put things in, that you install cables in. And this is a solid material. It transmits light, but it functions in the same manner that a conductor functions [by delivering] electromagnetic energy from one point to another.

* * * * *

A: There's no element of [FOG wire] which is a duct through which wires or cables are pulled. There's no element of it which remains when the cables are pulled out. There's just no permanent structure here, its all just one cable.

The trial court held that the term “conduit” should be defined in accordance with the NESC as a structure containing one or more single enclosed raceways for conductors or

cable. The trial court explained in its Memorandum Opinion as follows:

While the plaintiff emphasizes many differences between fiber optics and conventional electrical currents, the plaintiff has not shown why the Electrical Safety Code definition is obsolete or in error. Nor has the plaintiff shown how the differences between electrical wires and fiber optic cable transform fiber optic cable into "conduit." While the use of fused silica within the fiber optic wire is a new innovation, the use of insulation to protect impulses traveling along cable is a time-tested technology. The fact that this cable carries light impulses along glass rather than electrical currents along wire does not automatically transform the cable into "conduit." (TR 47)

The trial court further held that the outer shell of the FOG wire was not conduit because the evidence presented at trial indicated that the optical fibers and the surrounding material were considered by the industry to constitute one unit in which the fiber optics are permanently enclosed in the outer casing.

After a thorough examination of the record, we conclude that MCI has not met its burden of proving its entitlement to an exemption. Although MCI has persuasively advanced a novel and cogent argument in support of its position, exemptions are to be strictly construed against the taxpayer and "any well-founded doubt is fatal to the claim." Tibbals, 891 S.W.2d at 198. The conflicting testimony from the parties' witnesses creates a "well-founded doubt" as to whether fiber optic cable and FOG wire constitute "conduit." It is our opinion that to construe "conduit" as including fiber optic cable or FOG wire would afford the term a forced construction that would extend its meaning beyond that which was intended by the legislature. Tibbals, 891 S.W.2d at 198. This we cannot do in light of the fact that exemptions must be strictly construed against the taxpayer. Id. We find no error in employing the definition of "conduit" found in the NESC because witnesses for both parties conceded that at least to some extent the NESC establishes guidelines for the telecommunications industry. We also agree with the trial court that the protective shell of the FOG wire is not exempt from taxation. The record reflects that according to industry standards, the optical fibers and surrounding material are considered to be a single unit.

Accordingly, the judgment of the trial court is affirmed. Costs on appeal are taxed to appellant.

HIGHERS, J.

CONCUR:

CRAWFORD, P.J., W.S.

FARMER, J.