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## I. Introduction

Washington imposes B&O tax at different rates, depending upon the business classification of the taxpayer. The tax on persons engaged in the business of making “sales at retail” is 0.471% of the gross proceeds of sales of the business. RCW 82.04.250(1). In addition, buyers are required to pay, and sellers are required to collect (RCW 82.08.050), the sales tax on each “retail sale” in the state, (RCW 82.08.020(1)), as that term is defined in RCW 82.08.010(4).

As a consequence of legislation enacted during 1981 and 1983, RCW 82.08.050 provides that the term “retail sale” “shall also include the providing of telephone service, as defined in RCW 82.04.065, to consumers.” During the audit period, RCW 82.04.065 defined “telephone service” to include the sale or lease of “competitive telephone service” and “network telephone service”.

This case arises from the Department of Revenue’s attempt to classify sophisticated data networks as a pure transmission services and thus subject them to the retail sales tax. Sprint’s Telenet (SprintNet) “X.25” data network was part of a worldwide network of packet switched data networks. These advanced networks could “talk” to each other (interoperate) via gateways based on the “X.75” internetworking protocol. Interoperable networks of networks are generally termed “internets.”

The Federal Communications Commission (“FCC”) classified SprintNet as an unregulated value added network (“VAN”) rather than a regulated transmission network under its rules, because SprintNet served users with distributed computer communications processing applications—called enhanced services—that would otherwise need to be performed by centralized large scale mainframe computers. The Washington Utilities and Transportation Commission (“WUTC”) has adopted the same FCC rules.

The Washington Legislature has never classified an enhanced distributed computer service as network telephone service, and has specifically excluded computer, data processing, information, internet, and value added non-voice data services from the retailing (network telephone service) classification. Therefore, SprintNet X.25 data network service is a service business as a matter of law.

Sprint’s Frame Relay network service was a basic transmission service during the audit period, and not an enhanced service, but it is properly classified as service business because private line service is not included in the statutory definition of network telephone service.

## **II. Assignments of Error**

- A. The trial court erred in granting DOR's motion for summary judgment and denying Sprint's motion, thereby ruling that Sprint provided network telephone service via its X.25 data network.
- B. The trial court erred in granting DOR's motion for summary judgment and denying Sprint's motion, thereby ruling that Sprint provided network telephone service via its Frame Relay network.
- C. The trial court erred in granting DOR's motion for summary judgment and denying Sprint's motion, thereby ruling Sprint was not denied equal protection of the laws.

## **III. Issues Pertaining to Assignments of Error**

- A. If the undisputed facts show that Sprint's X.25 data network is an enhanced (computer) service, must it be classified as a general service business rather than network telephone service?
- B. If the undisputed facts show that Sprint's Frame Relay data network offers private line service, must it be classified as service business rather than network telephone service?
- C. If the undisputed facts show that services functionally equivalent to Sprint's X.25 data network services are classified as service business, must Sprint's X.25 network be classified as service business?

#### IV. Statement of the Case

##### A. Statement of Procedure and Standard of Review

The defendant/respondent Washington State Department of Revenue (“DOR”) audited plaintiff/appellant Sprint International Communications Corporation (“Sprint”) for the period January 1, 1989 through December 31, 1993 (the “audit period”). DOR determined that data network services sold by Sprint were “network telephone service” as it is defined by RCW 82.04.065(2) and assessed Sprint sales and B&O tax under the retailing classification rather than the general services or selected business services classifications. RCW 82.04.065(3). *Determination No. 00-159E*, 20 WTD 372 (2001) CP 484, *revised*, *Determination No. 00-159ER* (2001).

Sprint paid the assessment and filed an action for refund in the superior court, where Sprint and DOR filed cross-motions for summary judgment. CP 55-311 (Sprint); CP 10-54 (DOR). Summary judgment is appropriate if there are no genuine issues of material fact, and the moving party is entitled to judgment as a matter of law. CR 56(c). The superior court granted DOR’s motion. CP 610-612.

The appellate court reviews the trial court’s decision de novo. *See Qwest Corp. v. City of Bellevue*, 161 Wash.2d 353,358, 166 P.3d 667 (2007).

## **B. Statement of Facts**

### **1. Packet Switched Network Technology**

With packet switched data networks, each user's data is split up into small discrete "packets" or "frames." CP 355, ¶ 19; CP 314, ¶ 16. Each packet has attached to it binary address information indicating its destination. *Id.* This is also referred to as "encapsulation" of data within a packet. Parties' Stipulation of Agreed Facts and Exhibits ("Stip. Ex.") 27, 79:14-16.<sup>1</sup> This encapsulation does not change the content of the message or "payload" of the packet. Stip. Ex. 27, 26:16-17; 77:23-78:4. The packets are sent through the network separately, then reassembled at their destination. CP 355, ¶ 19. During transmission, packets belonging to one user can be interspersed among packets belonging to other users, allowing the channel to be more fully occupied than it would be if it were dedicated to a single user. CP 355, ¶ 19; CP 314, ¶¶ 18-19. With packet switched data networks, many users can share a single digital transmission channel. CP 355, ¶ 19.

### **2. Sprint's Packet Switched Networks**

Throughout the audit period, Sprint sold data communication services that used its predecessor Telenet's X.25 packet switched network,

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<sup>1</sup> The exhibits to the stipulation were inadvertently omitted from the original Clerk's Papers. They were subsequently designated, and all of the documents referred to herein as Stipulated Exhibits will be found in the supplemental designation, beginning with CP 617.

which became known as SprintNet.<sup>2</sup> CP 315, ¶¶ 21 and 22. The X.25 network's public-facing interfaces, which are known as "ports", complied with the internationally recognized X.25 standard protocol. CP 354, ¶¶ 11 and 15; CP 355, ¶ 21; CP 312-322, Stip. Ex. 26, 19:5-24, 73:19-23. Internally, Sprint's network used a proprietary protocol, but it was nonetheless generally referred to as an "**X.25 network**."<sup>3</sup> Stip. Ex. 26, 19:19-24; S ¶ 26.

Around 1994,<sup>4</sup> Sprint Communications Company L.P. began offering its "SprintLink" data communications service. Stip. Ex. 24, 8:20-21; Stip. Ex. 26, 77:3-6. SprintLink service was also known as "IP service", and it ran over Sprint's separate Internet Protocol ("**IP network**"). Stip. Ex. 26, 34:22-35:2; 150:15-18 and 153:11-23. Sprint's IP service became a commercial success by 1996. Stip. Ex. 26, 149:21-150:1. The IP network was "all IP" protocol, Stip. Ex. 26, 150:15-18, meaning its public-facing interfaces and its internal network all used the IP protocol. Sprint's IP network is one of the networks comprising the network of networks known as the Internet. Stip. Ex. 26, 150:19-151:1.

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<sup>2</sup> Unless otherwise noted, all references herein to "the X.25 network" refer to the Telenet/SprintNet X.25 packet switched network.

<sup>3</sup> Unless otherwise noted, all references herein to "the X.25 network" refer to the Telenet/SprintNet X.25 packet switched network.

<sup>4</sup> Sprint's IP services were not provided during the audit period, however they are relevant because they are functionally equivalent to SprintNet service and are a type of service the Washington Legislature has classified as general service rather than network telephone service.

Beginning in 1992, Sprint Communications Company L.P. sold data communication services running over its new “**Frame Relay**” network. CP 315, ¶ 22. Like X.25 and IP, Frame Relay refers to the customer-facing and internal network protocol standards. See, Stip. Ex. 26, 67:18-19.<sup>5</sup> The primary reason customers subscribed to frame relay services was to obtain a virtual private line for host-to-host data transmission. CP 321, ¶ 66, Ex. 26 at 57:6-11. (“Host-to-host” refers to communications between two or more mainframe computers. Stip. Ex. 26, 52:5-7.)

### 3. **Methods of Accessing Sprint’s Packet Switched Networks**

The two primary ways to access a packet switched network are known as “dial” access and “dedicated” access. CP 317 (X.25), ¶ 42; CP 317 ¶ 68 (Frame Relay); Stip. Ex. 26, 7:4-8; 146:24-147:2, 159:1-4; 161:8-13 (IP). In most cases, dial access occurs at the terminal or personal computer (“PC”) side of the connection, and the dedicated access occurs at the host or mainframe computer side. CP 317, ¶ 42 (X.25); Stip. Ex. 26, 161:12-14 (IP); Exhibit No. 6, II.B.1 and 3 (Generic IP).

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<sup>5</sup> Sprint also provided a data communications service known as “ATM” (Asynchronous Transfer Mode), which had its own ATM protocol. Stip. Ex. 26, 67:8-23. The ATM network provided mainframe-to-mainframe connectivity, and in that respect was more similar to the Frame Relay network than the X.25 network. *Id.*, 67:24-68:5. The taxation of ATM service is not an issue in this case.

**a. Dial Access**

Sprint's X.25 service was more of a dial-in service than a dedicated service. Stip. Ex. 26, 60:20-25. In fact, the main asset the X.25 network provided customers was its national footprint of dial-up numbers, which provided users remote access to mainframe host computers from multiple locations. Stip. Ex. 26 at 60:20-61:8; Stip Ex. 27, 19:18-25. Sprint's X.25 and IP networks provided remote users with the connectivity they needed to log in and do work on computer processing applications hosted on mainframe computers and servers across the data network. Stip. Ex. 26, 63:20-22, 82:16-17, 194:8-22 (X.25); Exhibit No. 6, II.B.1 and 3 (Generic IP). By March 1994, Sprint's X.25 network had over 30,000 public dial ports. Stip. Ex. 5-24.

Dial access, as its name suggests, is a temporary connection made via the public telephone network between the user's terminal or personal computer side of the connection and an X.25 port on a nearby Sprint X.25 network switch or an IP port on a nearby IP network router. CP 318, ¶¶ 46-48 (X.25); Exhibit No. 6, II.B.1 and 3 (Generic IP). Dial access was not used to connect to the Frame Relay network. CP 321, ¶¶ 66 and 68.

Dial access was usually accomplished by typing a command to a modem connected to the terminal or personal computer to dial a local telephone number. Stip. Ex. 26, 63:13-19. The local telephone company

would carry the call over the public switched [voice] telephone network (“PSTN”) to the telephone number of the nearest Telenet Access Center (“TAC”)<sup>6</sup>, which was also known as a Point of Presence (“POP”), where there would be a modem to make the computer signal intelligible to the network. CP 318, ¶ 46; Stip. Ex. 26, 72:11-16 (X.25). A personal computer would connect to the IP network POP in the same manner. Exhibit No. 6, II.B.1 and 3 (Generic IP). In both cases, the user would be billed for the call by his or her telephone company. CP 318, ¶¶ 46-48 (X.25); Exhibit No. 6, II.B.1 and 3 (Generic IP).

Sprint also provided toll free X.25 network access and paid all sales tax assessed by the long distance telephone companies with respect to its purchases of toll free long distance services used for 800/888 number dial access. CP 318, ¶ 48.

**i. Technical Aspects of Dial Access:  
Asynchronous to X.25 protocol  
conversion.**

Data terminals and personal computers typically use an “asynchronous” protocol to transmit information. CP 319, ¶ 54. They are frequently described as “ASCII terminals” because they combine a

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<sup>6</sup> The Telenet Access Center for the X.25 network was typically located near a local telephone company central office, since Sprint needed to purchase private line service connecting the TAC to the telephone company office. Stip. Ex. 26, 43:21-44:4. The TAC was also referred to as a Point of Presence (“POP”). Id. The Point of Presence for the IP network was typically co-located with Sprint Communications Company L.P.’s voice network switches. Stip. Ex. 26, 38:15-20.

character coding method known as ASCII coding<sup>7</sup> with other transmission attributes, i.e., serial ASCII coding in asynchronous format, and use of the RS-232C<sup>8</sup> standard for access and transmission control. CP 354, ¶ 13. An “asynchronous” format, or protocol, distinguishes between pieces of information (characters) based on specific flag signals (i.e., start and stop bits) and not timing. CP 319, ¶ 55.

X.25 is a synchronous protocol in that it uses timing to structure the information, not flags. CP 319, ¶ 56. With the majority of terminals and computers using the asynchronous interface, not the synchronous X.25 interface, it became necessary to build into the network packet assembler/disassembler devices (“PADs”) with inherent asynchronous/X.25 conversion capabilities, that form the signals from asynchronous terminals into X.25 packets. CP 355, ¶ 21; CP 319, ¶¶ 57 and 58. The PAD’s internal software runs the PAD processor to perform the conversion. Stip. Ex. 27, 80:1-8, 19-21. This conversion by a PAD from asynchronous protocol to synchronous protocol changes the protocol of the data sent. CP 320, ¶ 58.

Sprint’s DataCall product permitted remote users to access the X.25 network via a dial-in connection that was mainly used to provide

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<sup>7</sup> ASCII refers to the American Standard Code for Information Interchange. CP 354, ¶ 14.

<sup>8</sup> EIA Standard RS 232C, Interface between Data Terminal Equipment and Data Communications Equipment Employing Serial Binary Data Interexchange. CP 380, fn. 15.

access to the Sprint customer's host computers. CP 319, ¶ 49 and 50.

DataCall users dialed into the X.25 network, where a PAD would receive the signal and put it into an X.25 packet. CP 319, ¶ 53.

**ii. Technical Aspects of Dial Access:  
Synchronous X.25 Dial.**

Sprint's X.25 Dial Service operated in similar fashion for those users whose terminals, PC's or minicomputers were equipped with an X.25 interface, but instead of traversing asynchronous local telephone lines, they reached the X.25 network over synchronous X.25 dial lines. Stip. Ex. 1, 1-2. X.25 Dial was always a minor part of Sprint's revenue stream due to its additional complexity. Stip. Ex. 25-9:1-3. In a typical city before 1994 Sprint would have between 20-30 dial up asynchronous lines versus 2 or 3 synchronous X.25 dial up lines. Stip. Ex. 25-9:3-4. In other words, only 10% of Sprint's dial up access capacity was dedicated to X.25 dial, while 90% was dedicated to asynchronous dial. X.25 PADs were connected to asynchronous dial up lines, Stip. Ex. 25, 9:1-4, and 85 percent of the data entering the Sprint network at a Sprint PAD was converted from asynchronous to synchronous, Id., at 7:4-5.

Sprint's Dial IP product was similar to its X.25 dial in DataCall service, Stip. Ex. 26, 162:2-4, 22-25 (SprintLink), although the X.25 service was slower, Stip. Ex. 27, 24:16-19, and more reliable, Stip. Ex. 27,

23:10-15. The types of customers subscribing to X.25 services were the same types that subscribe to IP services. Stip. Ex. 27, 35:3-8.

**b. Dedicated Access**

Sprint's X.25 and IP networks could also be accessed via dedicated access. CP 317, ¶¶ 43-45 (X.25); Stip. Ex. 26, 155:1-3 (IP). Dedicated access is a permanent, "always on" connection, made via private lines provisioned by a Local Exchange Carrier ("LEC"), between a port on the Sprint network switch (X.25) or network router (IP), and the mainframe host (X.25) or server (IP) on the customer side of the connection. CP 317, ¶ 43 (X.25); Stip. Ex. 26, 162:12-13 (IP); Exhibit No. 6, II.B.1 and 3 (Generic IP).<sup>9</sup> Modems were placed at either end of the private line.<sup>10</sup> Stip. Ex. 75:5-11.

Sprint purchased the private lines used for dedicated access and paid all sales taxes assessed by the telephone companies with respect to those purchases. CP 318, ¶ 48 (X.25; Exhibit No. 6, II.B.1 and 3 (Generic IP).

All remote dial "DataCalls" were terminated at the host via a Global Data Connection, (Stip. Ex. 26, 69:22-23), and all Global Data

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<sup>9</sup> The network to which the naming convention applies is indicated in parentheses.

<sup>10</sup> The private line, switch port, modem, and associated equipment was termed a Dedicated Access Facility ("DAF"). CP 317, ¶ 43. The DAF provided the host an "always on" connection to the X.25 network, enabling the host to remain in a constant state of readiness to engage in interactive data sessions with the Dial access terminals. Id.

Connections were made via an X.25 interface at the host computer. Stip. Ex. 5-47. A customer could convert the X.25 protocol to another protocol, but Sprint's X.25 network handed off the data at the customer-facing interface in X.25 protocol format.

The product name given by SprintNet to the dedicated sides of a host-to-host connection is Custom Link. For a flat monthly rate, a Custom Link connection allows unlimited data transfers between host computers. Stip. Ex. 5-48, 49. Custom Link services do not convert the signal from asynchronous to synchronous or vice versa. *Id.* However, asynchronous dial in users could be redirected from the first host to a second host over a Customer Link connection if the requested application resided on the second host. Stip. Ex. 26, 87:12-88:5. In that case, both hosts would be participating in an asynchronous / X.25 dial in data session.

#### **4. The X.25 Network Was Part of a Worldwide Network of Networks.**

Like the Internet, the reach of the X.25 network was global. Stip. Ex. 26, 194:8. Sprint's X.25 network was interconnected to at least 100 foreign packet switched public data networks via X.75 interconnection. Stip. Ex. 2-136, 2-149; Stip. Ex. 3-4. The X.25 network was part of a worldwide set of networks that needed to talk to each other. Stip. Ex. 26, 20:6-8. The X.75 gateway protocol allowed dissimilar network switches

to talk to each other. Stip. Ex. 26, 20:3-6. The X.25 network provided like service to the Internet given the technology that was available at the time. Stip. Ex. 26, 193:14-15.

### **5. Applications Hosted by Sprint's X.25 Network**

The X.25 network hosted an electronic mail service that was first known as Telemail, then Sprintmail. Stip. CP 41; Ex. 27, 75:21-77:10; Ex. 2-283. The Sprintmail offering was the predecessor of Internet email. Stip. Ex. 26, 193:24-194:1. It was a public electronic messaging service offered as a host-based application on the SprintNet X.25 Public Data Network. Stip. Ex. 2-285.

Sprintmail included a "Bulletin Boards" application. A bulletin board is a catalog of messages that can be read by a group of users; they are suitable for information that is of interest to a large number of people.. Stip. Ex. 2-288

## **V. Argument**

### **A. SprintNet's X.25 Data Network Services Are "Value Added" "Enhanced" (Computer) Services Under the FCC's and WUTC's Rule.**

#### **1. The Historical Development of the FCC/WUTC Rule and Its Application by the FCC to SprintNet and the Other Value Added Networks ("VANs")**

The regulatory history of X.25 service distinguishes it from normal telephone service. The FCC began an inquiry during the 1960s, known as

its First Computer Inquiry, to address the regulatory and policy problems raised by the interdependence of computer technology, its market applications, and communications common carrier services. *See In the Matter of Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry)*, Final Decision, 77 F.C.C. 2d 384, 389 (1980) ("Computer II Order") CP 174, ¶ 14 and fn. 1. The FCC struggled with the problem of distinguishing regulated communication services from unregulated data processing services, and in 1971 adopted a rule for doing so, but that rule that was ultimately rewritten by the FCC in its Computer II Order. *Id.*, at 77 F.C.C. 2d at 390, CP 175, ¶ 17.

In the interim, the FCC used the terms "value added" and "augmented" interchangeably to describe Telenet's (later SprintNet) services. *In the Matter of Application of G.T.E. to Acquire Telenet*, Memo Op. & Order, 72 FCC 2d 111, 120 (1979) ("*Telenet Merger Order*") CP 84 at CP 93, ¶ 25. The FCC described these "augmented data transmission" services as follows:

Telenet participates in two markets. It primarily provides value added service, which for clarity we will call augmented data transmission. To some degree, it also provides basic transmission service.

*Id.*, 72 FCC 2d at 112, CP 85, ¶ 4.

Augmented data transmission services provide users with protocol conversion, speed matching, time sequencing,

message preparation, and other useful features. These services allow otherwise incompatible computers and terminals to communicate without the user providing specialized software and equipment.

*Id.*, 72 FCC 2d at 120, CP 93, ¶ 25.

Transmission economies are not the salient feature of Telenet's service. ...[C]ustomers with both very high and very low volume data communications requirements are attracted to Telenet's service because of the augmented data features. These are features which a customer using basic transmission service, such as MTS [Message Telephone Service] or Private Line, can only obtain by adding their own special purpose equipment and programming.

*Id.*, 72 FCC 2d at 121, CP 94, ¶ 29. Although the FCC then favored the term "augmented", Telenet (and Tymnet<sup>11</sup>) were still generally known as value added networks, or "VANs". *Petition for Waiver of Rules*, Memo. Op. & Order, 100 F.C.C. 2d 1057 (1985) ("*Waiver Order*") CP 379, fn 2.

Concluding Telenet provided augmented "data transmission" service, the FCC continued to regulate the Telenet (and Tymnet) VANs until it revisited the treatment of VANs in its 1980 Computer II Order. *Waiver Order, supra*, 100 F.C.C. 2d 1057, CP 379, fn 2.

As the *Telenet Merger Order* illustrates, by the late 1970's, hardware and software advances were resulting in the removal of data processing and communications control applications from centralized

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<sup>11</sup> Tymnet was Telenet's biggest competitor. Stip. Ex. 26, 100:3-7; Stip. Ex. 27, 72:22-73:10.

large scale general-purpose computers to applications within data networks and at customers' premises. Computer II Order, *supra*, 77 F.C.C. 2d 384, 381, CP 174, ¶ 19. New devices ranging from "smart" remote access devices to "distributed" data processing devices and systems were capable of executing local processing operations, thus easing the processing burden for a remote host computer that would otherwise perform the task in its central processing unit (CPU). *In the Matter of the Amendment of Section 64.702 of the Commission's Rules and Regulations*, Supplemental Notice of Inquiry and Enlargement of Proposed Rulemaking, 64 F.C.C. 2d 771, 772 (1977) CP 520, ¶ 4. These devices were also capable of message addressing and routing operations, which, again, would otherwise be implemented in a host CPU. *Id.*

## 2. The FCC's Rule

Reversing its practice of classifying VANs as regulated transmission services, the FCC in its Computer II Order adopted a rule containing three independent criteria for establishing a service as an unregulated "enhanced" (computer) service. Computer II Order, *supra*, 77 F.C.C. 2d 384, 498, CP 218, ¶ 287; 47 C.F.R. § 64.702(a). The FCC rule, which is in force today in its original form, states:

For the purpose of this subpart, the term *enhanced service* shall refer to services, offered over common carrier transmission facilities used in interstate communications,

which employ computer processing applications that [1] act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information; [2] provide the subscriber additional, different, or restructured information; or [3] involve subscriber interaction with stored information. Enhanced services are not regulated under title II of the Act.

47 C.F.R. § 64.702(a), (italics in original text). The WUTC adopted this FCC rule. WAC 480-120-999(4) (FCC rules adopted by reference).

The FCC rule's second and third clauses classify as enhanced (computer) services those data processing and storage and retrieval services that are generally thought of as computer services.

The first clause of the FCC rule classifies as enhanced services communications control applications of the sort that were migrating from centralized computer CPUs to the VANs and customer sites, specifically "*services [which employ] computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information.*" 47 C.F.R. § 64.702(a), italics added. These first-clause services may be unfamiliar to the public at large, but their importance is well recognized by computer engineers.

With regard to "first-clause" services, the FCC observed that the VANs and other enhanced service vendors provide asynchronous /X.25 conversion, as well as other protocol conversions, (*Waiver Order* 100 F.C.C. 2d 1057 at CP 352, ¶ 3, and deregulated them in its Computer II

Order, thereafter using the terms “VAN” and “enhanced service provider” interchangeably. *Id.*, CP 379, fn. 2.

The FCC also began to use the “enhanced service” terminology from its rule when referring to the SprintNet (Telenet) X.25 network:

[W]hile a number of entities have offered digital transmission services in the past using packet switching technology (e.g. Telenet and Tymnet), their offerings have often been enhanced offerings, in that they support communications among incompatible terminals (and perform code, format, and protocol conversion to support this service within their facilities). [AT&T’s] BPSS [basic packet switching service] as proposed does not do so.

*Application of American Telephone and Telegraph for Authority to Offer Basic Packet Switching Service*, Memorandum Opinion, 94 FCC 2d 48, 54, CP 251, ¶ 13 (1983).

The FCC rejected arguments that first-class communications processing functions could be practically distinguished between “communications” and “data processing”:

We conclude that the public interest would not be served by any classification scheme that attempts to distinguish enhanced services based on the communications or data processing nature of the computer processing activity performed. Accordingly, we conclude that all enhanced computer services should be accorded the same regulatory scheme and that no regulatory scheme could be adopted which would rationally distinguish and classify enhanced services as either communications or data processing.

Computer II Order, *supra*, 77 F.C.C. 2d 384, 428, CP 194, ¶ 113, emphasis added.

**3. SprintNet Services Were Enhanced Services Within the First-Clause of the FCC Rule.**

The Statement of Facts explains that the SprintNet X.25 network was primarily a dial in service. IV.C.3.a., *supra*. Roughly 85 or 90 percent of the dial in services involved asynchronous / X.25 protocol conversions by Sprint's PADs, IV.C.3.a.i., which allowed ASCII terminal and PC users to terminate their data sessions at a Global Data Connection X.25 host interface, IV.C.3.b. These protocol conversions were enhanced services under the FCC and WUTC rule.

For example, an attorney needing access to Westlaw service could dial up a local access number given to Westlaw by SprintNet and engage in an interactive data session with a Westlaw host computer. The attorney is not aware that Westlaw has subscribed to DataCall Plus – Asynchronous Dial service, which enables the attorney to dial a local number from his asynchronous PC. The attorney is not aware that Westlaw has subscribed to a synchronous X.25 Global Data Connection so that its host applications and databases will be accessible when the attorney initiates the data session. Nor is the attorney aware that a net protocol conversion from asynchronous to synchronous X.25 (and vice

versa for received data) is occurring in order for the interactive data session to occur. But the Information Technology officers of Westlaw likely would not have subscribed to SprintNet services if net protocol conversion was absent from the service.

Custom Link was an X.25 host-to-host synchronous protocol service that did not require net protocol conversion. However, Custom Link might be used if Westlaw decided to disperse its databases across multiple host computers in different locations. The hosts could be communicating in the background, unbeknownst to the attorney, to deliver the response to his or her data inquiry. Thus, although Custom Link is a synchronous connection, the data exchanged can be part of an asynchronous data session. *See*, Statement of Facts, IV.C.3.b.i., *supra*.

In fact, the term X.25 has come to represent a common reference point by which mainframe computers, mini-computers, VDUs [Visual Display Units], microcomputers and a wide variety of specialized terminal equipment from many manufacturers can be made to work together over a type of data communications network called a packet switched network. Newton, *Newton's Telecom Dictionary*, Telecom Books, 14<sup>th</sup> ed. 1998, at 856, CP 81.

**4. SprintNet Provided Services Within the Second and Third Clauses of the FCC's Rule.**

SprintNet's electronic mail and bulletin board applications, offered over the X.25 network, were enhanced services under the second and third clauses of the FCC rule. *See*, Statement of Facts, IV.C.5, *supra*.

**B. The Legislature Has Always Classified Enhanced Services as General Services, Rather Than Network Telephone Service.**

Washington's legislative scheme parallels the federal regulations in this area. Under Washington's statutory B&O tax scheme, any business activity that is not specifically described by statute falls under the general category set forth in RCW 82.04.290 (1992):

Upon every person engaging within this state in any business activity other than or in addition to those enumerated in RCW 82.04.230, 82.04.240, 82.04.250 . . . as to such persons the amount of tax on account of such activities shall be equal to the gross income of the business multiplied by the rate of 1.50 percent. This section includes, among others, and without limiting the scope hereof . . . persons rendering any type of service which does not constitute a "sale at retail" or a "sale at wholesale."

If no statute describes a business activity with sufficient particularity, it falls under the category of "service and other" for B&O purposes.

"Network telephone service" is expressly taxed as a "sale at retail." RCW 82.04.050(5) (1992). Hence, if SprintNet's enhanced services are outside

the definition of network telephone service, they should be taxed as a service under this statute and not as a retail activity.

When the Legislature has dealt with computer-related services, it has categorized them as general services. ESSB 5967, Laws 1993, ch. 25 selected certain business services, including computer-related services, and raised the B & O tax rate from 1.5 percent to 2.5 percent. *See* Final Bill Report, 1993 ESSB 5967, CP 418. Definitions were assigned to the computer-related services—data processing services, computer services, and information service—in RCW 82.04.055 (1993), which was repealed in 1998 when the rate was lowered to the 1.5 percent rate applicable to all services. EHB 1821, Laws of 1997, ch. 7, § 5, eff. July 1, 1998; *See* Final Bill Report, 1997 EHB 1821. CP 418-419.

Internet service was added to the definition of information services immediately prior to its repeal. SSB 5763, Laws 1997, ch. 304, § 3, eff. May 9, 1997. The Legislature enacted the following definitions of internet service, which it intended as a clarification that Internet service was to be taxed as a selected business service and as a general service if the former classification was repealed. House Bill Report, SSB 5763, April 10, 1997, CP 421 at 423. The Legislature also clarified that the provision of Internet service was not network telephone service. *Id.* *See* SSB 5763 Laws 1997, ch. 304, § 5, App. 1 at 6.

(1) The provision of internet services is a selected business service activity and subject to tax under RCW 82.04.290(1), but if RCW 82.04.055 is repealed then the provision of internet services is taxable under the general service business and occupation tax classification of RCW 82.04.290.

(2) "Internet" means the international computer network of both federal and nonfederal interoperable packet switched data networks, including the graphical subnetwork called the world wide web.

(3) "Internet service" means a service that includes computer processing applications, provides the user with additional or restructured information, or permits the user to interact with stored information through the internet or a proprietary subscriber network. "Internet service" includes provision of internet electronic mail, access to the internet for information retrieval, and hosting of information for retrieval over the internet or the graphical subnetwork called the world wide web.

Laws 1997, ch. 304, § 4, App. 1, at 5, RCW 82.04.297.<sup>12</sup> As a clarification of existing law, Laws 1997, ch. 304, relates back to the audit period. Thus, when the Legislature chose to enumerate these enhanced services, it did not classify them as telephone services.

**C. In 2007 the Legislature Excluded “Value-Added Nonvoice Data Service” From “Telecommunications Service” in Clarification of Existing Law.**

SSB 5089, Wash. Laws 2007, ch. 6, confirms value-added nonvoice data services are excluded from the definition of “network

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<sup>12</sup> The first subparagraph of RCW 82.04.297 was later amended to read “(1) The provision of internet services is subject to tax under RCW 82.04.290(2).” Laws 2000, ch. 103, § 5.

telephone service” prevailing during the audit period.<sup>13</sup> The Legislature amended RCW 82.04.050(5) to replace the term “network telephone service” with “telecommunications service,” and “ancillary services,” as those terms are defined in RCW 82.04.065, to consumers. Wash. Laws 2007, Ch. 6 § 1004. “Telecommunications service” is defined, in part, as follows:

(8) “Telecommunications service” means the electronic transmission, conveyance, or routing of voice, data, audio, video, or any other information or signals to a point, or between or among points. “Telecommunications service” includes such transmission, conveyance, or routing in which computer processing applications are used to act on the form, code, or protocol of the content for purposes of transmission, conveyance, or routing without regard to whether such service is referred to as voice over internet protocol services or is classified by the federal communications commission as enhanced or value added.

\* \* \*

CP 289-290. The new legislation, however, carves out “Value-added nonvoice data service”, which is defined in a separate subsection, RCW 82.04.065(17), and is not enumerated in RCW 82.04.050(5) as a subject of the retail sales tax:

(17) “Value-added nonvoice data service” means a service that otherwise meets the definition of telecommunications services in which computer processing applications are used to act on the form, content, code, or protocol of the information or data primarily for a purpose other than transmission, conveyance, or routing.

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<sup>13</sup> Part 10 of SB 5089 (Wash. Laws 2007, ch. 6) CP 284-304 and the Senate Final Bill Report, CP 279-283.

CP. 292. The Final Bill Report states: “Several telecommunication definitions recently incorporated into the SSUTA [Streamlined Sales and Use Tax Act] are adopted. These are changes to terminology in current law, but do not change current law regarding taxability and exemptions. Final Bill Report, SSB 5089, Ch. 6 Laws 2007, CP 282, bracketed material added.

Thus, a service is neither “network telephone service” or “telecommunications service” if it uses code or protocol conversion for a purpose other than transmission, conveyance, or routing.

**D. Washington Statutes Failed to Clearly Classify SprintNet’s Services as Telephone Services, and Must Be Construed to Classify Them as General Services.**

In the 1997 legislation that defined internet service, the Legislature found that a clear statutory definition had been lacking up till then. SSB 5763, Laws 1997, ch. 304, § 1, Appendix 1 at 1. As is explained *infra*, V.E., SprintNet’s value added network (VAN) services were internet services to other internet services and are functionally equivalent.

If there is doubt as to the meaning of a taxing statute, it is to be construed in favor of the taxpayer and against the taxing body. *Paccar, Inc. v. Washington Department of Revenue*, 85 Wn.App.48, 930 P.2d 954 (1997) (citations omitted). Pro-taxpayer construction of tax statutes protects citizens “by informing [them] in unambiguous terms as to the

amount and nature of [their] duty to pay taxes. Singer, *Sutherland Stat. Const.* § 66.1. Strict construction is also desirable as a way to secure equality and uniformity in the imposition of tax burdens. *Id.* (citing, among other authority, *State v. Lawton*, 25 Wn.2d 750, 172 P.2d 465 (1946); Blum, *State and Local Taxing Authorities Taking More Than Their Fair Share of the Electronic Information Age*, 14 J. MARSHALL J. COMPUTER & INFO. L. 493 (1996)).

As the Legislature found, the classification of internet services, and, by logical extension VAN services, was ambiguous and the classification should therefore be construed as general service since this is the most favorable classification for Sprint.

**E. SprintNet's Services Were Internet Services and Thus Taxed at the General Services Rate.**

**1. SprintNet Provided Internet Services Because It Met the RCW 82.04.297 Definition of Internet Service, Which Relates Back to the Audit Period.**

SprintNet was part of the international X.25 computer network of federal and nonfederal interoperable packet switched data networks. It connected to other domestic and foreign packet switched networks, including networks owned by the Postal Telephone and Telegraphs of other countries, via X.75 gateway protocols that allowed the networks to

talk to each other, or “interoperate.” Like the Internet, SprintNet’s reach was global. Stip. Ex. 26, 194:8. *See*, Statement of Facts, IV.C.4., *supra*.

SprintNet service includes computer communications processing applications permitting users to interact with stored information through the X.25 internet, including SprintNet’s proprietary subscriber network. SprintNet also provides Sprintmail and Bulletin Board applications that provide users with additional or restructured information.

SprintNet’s service was thus plainly included in the definition of internet service at RCW 82.04.297, a conclusion that has been reinforced by Congress’ enactment of the Internet Tax Freedom Act (“ITFA”) in 1998. 47 U.S.C. 151 (Note). The ITFA imposes a moratorium on state and local taxes on Internet access. ITFA § 1101(a)(1). The ITFA defines the Internet as follows:

Internet.—The term “Internet” means collectively the myriad of computer and telecommunications facilities, including equipment and operating software, which comprise the interconnected world-wide network of networks that employ the Transmission Control Protocol/Internet Protocol, or any predecessor or successor protocols to such protocol, to communicate information of all kinds by wire or radio.

ITFA § 1105(5). SprintNet was part of a worldwide network of networks that employed the X.25 protocol, and the X.25 protocol was a predecessor of the IP protocol. Stip. Ex. 26, 193:14-18. (X.25 provides like service to

the Internet.) Therefore, the ITFA definition confirms SprintNet was plainly within the definition of internet service at RCW 82.04.297.

**2. RCW 82.04.297 Applies to All Internet Service Providers.**

The RCW 82.04.297 definitions of the “Internet” and “Internet service” plainly are not limited to capital “I” internet service.

When it was first enacted in 1997, RCW 82.04.297(1) classified lower case “i” internet service as selected or general services. SSB 5763 Laws 1997, ch. 304, § 4, App. 1 at 5. The Legislature’s preamble twice referred to lower case “i” internet service. *Id.* at 1. And when RCW 82.04.297(1) was amended in 2000, the lower case “i” in subsection (1) was not changed to a capital “I”. Laws 2000, ch. 103, § 5.

The use of capital “I”s in subsections (2) and (3) can be explained as grammatical in nature rather than substantive in nature, because every instance of capital “I” Internet appears at the beginning of a sentence, and every other appearance of the word throughout SSB 5763, Laws 1997, ch. 304, employs the lower case “i”. SprintNet service falls within the plain meaning of “internet service” and must accordingly be classified as a general service.

**3. As an Internet Service Provider, SprintNet Was Not Subject to the Retailing Classification With Respect to Any Basic Transmission Included in Its Service.**

In *Community Telecable of Seattle, Inc. v. City of Seattle*, (“*Telecable*”) 163 Wash.2d 35, 186 P.3d 1032 (2008), the court rejected the City’s attempt to tax a cable internet service provider as a network telephone service provider with respect to cable data transmission from the customer’s premise to the cable “head end, where it was handed off to an internet service provider for connection to the Internet. The court held that although RCW 82.04.065(2) encompasses transmission services to the site of an internet service provider, the Legislature’s plain intent in enacting Laws of 1997, ch. 304 was “to prohibit the taxation of Internet service providers as network telephone service providers.” *Id.*, 163 Wash.2d at 43. The court observed that the provision of data via cable *is* cable “Internet services” as defined by RCW 82.04.297(3). *Id.*, 163 Wash.2d at 44.

Similarly, any packet switched or other transmission services provided by an internet service provider such as SprintNet incidental to its overall enhanced service would be classified as general service rather than retailing.

**4. Sprint Was Prohibited From Charging Retail Sales Tax to Its Internet Service Provider Customers.**

SprintNet's X.25 network was utilized by numerous other internet service providers such as AOL and MSN beginning around 1994, and, during the audit period, CompuServe, Dow Jones, Westlaw and Earthlink. Stip. Ex. 26, 91:6-16 (AOL); 107:20-23 (MSN); 108:5-13 (CompuServe, Dow Jones, Westlaw, Earthlink).

In *Telecable*, the court held that a data transmission link to an internet access portal *is* internet access. *Telecable, supra*, 163 Wash.2d 35, 44. Therefore, when an internet access provider purchases dial up access services from SprintNet permitting users to access the internet, that dial up access *is* internet access. As purchaser of the dial up access, the internet service provider would be liable for the sales tax if it applied, RCW 82.08.020(1), but since the internet access provider is *not* subject to the sales tax under RCW 82.04.297, Sprint is not liable for it either.

**5. SprintNet Service Is Functionally Equivalent to Other Internet Services.**

**a. The Networks Are Functionally Equivalent.**

Like the other internets, the SprintNet X.25 network is part of a worldwide internetwork. *See*, Statement of Facts, IV.C.4., and Argument, V.D.1., *supra*. Basic packet switched data transmission is inherent in all

internets, but it is the interoperability of the networks and the attached devices that defines the service, because the fundamental purpose of any computer network is to allow users interactive access to network-attached computers, providing the opportunity to run hosted electronic mail applications, data processing applications, and information retrieval applications. RCW 82.04.297. Both Internet access services and SprintNet services are a functionally integrated combination of data transmission and computer processing to provide interactive access to network-attached computers.

**b. The Access Methods Are the Same.**

The dial up and dedicated access methods for "IP" Internet access are remarkably similar to the local and 800 dial up access methods for SprintNet access. *See*, Statement of Facts, IV.C.3.

SprintNet charges its customers fees for interactive access to host computers connected to the global X.25 network. Internet access providers charge their customers fees for interactive access to servers connected to the global Internet. In that respect, the charging scheme is identical.

For example, the same attorney that previously accessed Westlaw using SprintNet's DataCall Service, today accesses Westlaw using Internet access service. In both cases, the attorney's personal computer is

connected to the sign-in page hosted on the Westlaw server. And in both cases, the information is sold by Westlaw. The purchase of Internet access service does not give the Internet access subscriber access to cases or statutes. For that, a separate subscription to Westlaw service is required. Thus, there is no functional difference between Internet access service and SprintNet service in the Westlaw example, because both services give the users an interactive portal to the Westlaw host or server, but neither give the user access to Westlaw's databases of cases and statutes.

More telling, an Internet access service is considered an information service even when there is not a separate charge for the information retrieved:

Some information on the Internet is available at no charge, while other information is available only if the user pays a subscription or use fee.

House Bill Report, 1997 SSB 5763, CP 422. There is no meaningful difference between the charging models for SprintNet service and Internet access service. In each case, someone pays for the interactive connection, and the host may or may not charge that person for the information retrieved.

**c. SprintNet and Other Internet Access Services Process Protocols and Are Information Services Under Federal Law.**

There is a significant functional difference between SprintNet service and Internet access service which only serves to reinforce the conclusion that SprintNet should be classified as a service activity rather than network telephone service.

SprintNet insured interoperability among dissimilar devices by providing protocol processing that primarily resulted in net “protocol conversion”. Internet access service providers (ISPs) provide protocol processing that does not result in net protocol conversion. Nevertheless, the Federal Communications Commission classifies both services as information services rather than telecommunications services under the provisions of the 1996 Telecommunications Act:<sup>14</sup>

104. We further conclude that, subject to the exceptions discussed below, protocol processing services constitute information services under the 1996 Act. We reject Bell Atlantic's argument that "information services" only refers to services that transform or process the content of information transmitted by an end-user, because we agree with Sprint that the statutory definition makes no reference

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<sup>14</sup> The 1996 Telecommunications Act, Pub. L. 104-104, 110 Stat. 56, defines “telecommunications” as: “the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received.” 47 U.S.C. § 153(43). “Information service” is defined as: “the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications, and includes electronic publishing, but does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service.” 47 U.S.C. § 153(20).

to the term "content," but requires only that an information service transform or process "information." We also agree with ITI and ITAA that an end-to-end protocol conversion service that enables an end-user to send information into a network in one protocol and have it exit the network in a different protocol clearly "transforms" user information. We further find that other types of protocol processing services that interpret and react to protocol information associated with the transmission of end-user content clearly "process" such information. Therefore, we conclude that both protocol conversion and protocol processing services are information services under the 1996 Act.

105. This interpretation is consistent with the Commission's existing practice of treating end-to-end protocol processing services as enhanced services. We find no reason to depart from this practice, particularly in light of Congress's deregulatory intent in enacting the 1996 Act. Treating protocol processing services as telecommunications services might make them subject to Title II regulation. Because the market for protocol processing services is highly competitive, such regulation is unnecessary to promote competition, and would likely result in a significant burden to small independent ISPs that provide protocol processing services. Thus, policy considerations support our conclusion that end-to-end protocol processing services are information services.

*In the Matter of the Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as Amended,*  
First Report and Order, Docket 96-149, 11 FCC Rcd 21905, ¶¶ 104-105  
(1996) CP 426, 448-449.

**d. SprintNet Provides Applications Similar to Those of Other Internet Access Service Providers.**

SprintNet provided like service to the Internet given the technology that was available at the time. Stip. Ex. 26, 193:14-15. Included within the Sprint offering was email, which was the predecessor of Internet email. Id. 193:24-194:1. SprintNet also provided electronic bulletin boards, which were much like internet blogs. *See*, Statement of Facts, III.C.5. SprintNet was just like the Internet in that it provided the connectivity to get to the application. Id. 194:12-22.

**F. Frame Relay Service Is Not “Network Telephone Service” Because It Is a “Private Line” Service.**

The definition of “network telephone service” is largely the product of the 1981 legislature and a response to the impending breakup of the Bell System.<sup>15</sup> At that time the regulated utilities—Pacific Northwest Bell and General Telephone—paid the utility tax rather than the B&O tax paid by non-regulated companies. *See* 1981 SHB 61. Non-regulated companies could not offer local telephone service at that time, but they had begun offering telephone equipment and were planning to move into long-distance service.

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<sup>15</sup> The breakup was the result of an antitrust action filed by the Department of Justice in 1974, which ended in a settlement in January 1982.

When 1981 SHB 61 and later 1983 SB 3909 were enacted, the definitions of “Telephone business” and “Network telephone service” plainly included coin service, local telephone service, and toll telephone service, including data and other communications via local and toll communications pathways that comprise the worldwide *public* telecommunications network. Private line services that are not part of the public telecommunications network were plainly excluded from “Network telephone service” as a result of their omission from the definition.

The legal standard for reviewing the definition of “Network telephone service” is set forth in *Tingey v. Haisch*, 159 Wn.2d 652, 657, ¶ 8, ¶ 10, 152 P.3d 1020 (2007) (citations omitted):

[I]f the statute’s meaning is plain on its face, then the court must give effect to that plain meaning as an expression of legislative intent.” A statutory provision’s plain meaning is to be discerned from the ordinary meaning of the language at issue, the context of the statute in which that provision is found, related provisions, and the statutory scheme as a whole. . . .

When a term has a well-accepted, ordinary meaning, a regular dictionary may be consulted to ascertain the term’s definition. When a technical term is used in its technical field, the term should be given its technical meaning by using a “technical rather than a general purpose dictionary” to resolve the term’s definition.

In this case, the ordinary, technical, and contextual meanings of the terms used in the definition of “Network telephone service” are easily

ascertained, and refer to local and toll services used to transport voice and data communications. They do not include private line services.

**1. Regular Dictionary Definitions.**

The Merriam Webster Online Dictionary defines “local” in the telephone service context as “of or relating to telephone communication within a specified area”, while “toll” is defined as “a charge for a long-distance telephone call”. Merriam Webster Online Dictionary, <http://www.merriam-webster.com/dictionary/toll>.

**2. Tariff Definitions.**

The technical meaning of “network telephone service” may be found in Pacific Northwest Bell Telephone Company’s Tariff WN U-14, which is entitled “Exchange and Network Telephone Service.” CP 306. The tariff contained the following definitions immediately prior to the enactment of SHB 61:

Local Service – Exchange service available in a particular exchange area for communication throughout the exchange area.” Tariff WN U-14, Pacific Northwest Bell Telephone Company, Original Sheet D-4, Definitions, Issued January 16, 1981, Effective February 22, 1981. [CP 308]

Exchange – The telephone system, including plant and equipment, by means of which local or exchange service is furnished to patrons within a defined area, and which, in conjunction with interexchange plant and equipment, toll or long distance service is furnished.” Tariff WN U-14, Pacific Northwest Bell Telephone Company, Original

Sheet D-2, Definitions, Issued January 16, 1981, Effective February 22, 1981. [CP 307]

“Toll Service – Telephone service furnished between two exchange stations located in different local service areas, between two toll stations, or between a toll station and an exchange station.” Tariff WN U-14, Pacific Northwest Bell Telephone Company, Original Sheet D-7, Definitions, Issued January 16, 1981, Effective February 22, 1981. [CP 309]

“Toll Message – A completed call between two exchange stations located in different local service areas, between two toll stations, or between a toll station and exchange station.” Tariff WN U-14, Pacific Northwest Bell Telephone Company, Original Sheet D-7, Definitions, Issued January 16, 1981, Effective February 22, 1981. [CP 309]

Each of these definitions refers to the public telephone network.

There is no definition of private lines because private line service was separately tariffed. Contemporaneous with the enactment of SHB 61, Pacific Northwest Bell Telephone Company provided private line service in Washington pursuant to its Tariff WN U-10.

Tariff WN U-10 defined “Private line service” as follows:

Private line service is the furnishing of Company facilities, including channels and station equipment, for communication purposes of the customer and authorized users between specified locations. Service is furnished 7 days per week, 24 hours per day for a minimum period of one month.

CP 311. Tariff WN U-10, Pacific Northwest Bell Telephone Company, 3<sup>rd</sup> Revision of Sheet 5134, Regulations, Issued April 15, 1981, Effective

May 20, 1981. PNB clearly distinguished between “network telephone service” which was available to the public, and private lines, which were dedicated to the customer and authorized users. Had PNB meant to subject private lines to the retail sales tax, it clearly knew how to write a definition that included the private service. The fact that it was omitted is a clear indication that it was not intended to be covered by the term “network telephone service.”

### **3. Federal Law.**

The Communications Act of 1934, prior to its amendment by the Telecommunications Act of 1996, Public Law 104-104, provided the following definitions of exchange (local) and toll service:

Telephone exchange service” means service within a telephone exchange, or within a connected system of telephone exchanges within the same exchange area operated to furnish to subscribers intercommunicating service of the character ordinarily furnished by a single exchange, and which is covered by the exchange service charge. (47 U.S.C. § 153(r).)

Telephone toll service” means telephone service between stations in different exchange areas for which there is made a separate charge not included in contracts with subscribers for exchange service. (47 U.S.C. § 153(s).)

The United States Tax on Communication Services, (a.k.a. the “federal excise tax”), was in effect when SHB 61 and SB 3909 were enacted, and provided the following, more detailed, definitions of local and toll services, although the federal excise tax was limited to charges for

“telephonic quality communications” carried over the local and toll networks:

(a) Local telephone service.--For purposes of this subchapter, the term “local telephone service” means--

(1) the access to a local telephone system, and the privilege of telephonic quality communication with substantially all persons having telephone or radio telephone stations constituting a part of such local telephone system, and

(2) any facility or service provided in connection with a service described in paragraph (1).

The term “local telephone service” does not include any service which is a “toll telephone service” or a “private communication service” as defined in subsections (b) and (d).

(b) Toll telephone service.--For purposes of this subchapter, the term “toll telephone service” means--

(1) a telephonic quality communication for which (A) there is a toll charge which varies in amount with the distance and elapsed transmission time of each individual communication and (B) the charge is paid within the United States, and

(2) a service which entitles the subscriber, upon payment of a periodic charge (determined as a flat amount or upon the basis of total elapsed transmission time), to the privilege of an unlimited number of telephonic communications to or from all or a substantial portion of the persons having telephone or radio telephone stations in a specified area which is outside the local telephone system area in which the station provided with this service is located.

26 U.S.C. § 4252.

In contrast, the federal excise tax law, *supra*, provides the following definition of “private communications service”

(d) Private communication service.--For purposes of this subchapter, the term “private communication service” means--

(1) the communication service furnished to a subscriber which entitles the subscriber--

(A) to exclusive or priority use of any communication channel or groups of channels, or

(B) to the use of an intercommunication system for the subscriber’s stations, regardless of whether such channel, groups of channels, or intercommunication system may be connected through switching with a service described in subsection (a), (b), or (c),

(2) switching capacity, extension lines and stations, or other associated services which are provided in connection with, and are necessary or unique to the use of, channels or systems described in paragraph (1), and

(3) the channel mileage which connects a telephone station located outside a local telephone system area with a central office in such local telephone system, except that such term does not include any communication service unless a separate charge is made for such service.

26 U.S.C. § 4252.

The definitions contained in the PNB tariffs and federal tax statutes, strongly support Sprint’s contention that “private line service” is qualitatively different than local or toll service. Private line service is described as a fixed, station-to-station service for private use that does not provide inward or outward communication capability with other stations

on the public telephone networks. The titles and separation of Pacific Northwest Bell Telephone Company's "Private Line Services" (CP 310) and "Exchange and Network Telephone Services" tariffs lends further support for Sprint's contention that private line services would have been expressly mentioned in RCW 82.04.065(2) if they were included in the definition of "Network telephone service".

## VI. Conclusion

For the reasons set forth above, Sprint requests this court reverse the trial court and order that summary judgment be denied to DOR and granted to Sprint.

DATED this 8th day of December, 2008.

Davis Wright Tremaine LLP  
Attorneys for Sprint

By   
Michele Radosevich,  
WSBA #24282



# APPENDIX 1

CERTIFICATION OF ENROLLMENT

**SUBSTITUTE SENATE BILL 5763**

Chapter 304, Laws of 1997

55th Legislature  
1997 Regular Session

PROHIBITING TAXATION OF INTERNET SERVICE PROVIDERS AS TELEPHONE  
SERVICES PROVIDERS

EFFECTIVE DATE: 5/9/97

Passed by the Senate April 19, 1997  
YEAS 44 NAYS 0

BRAD OWEN

President of the Senate

Passed by the House April 10, 1997  
YEAS 97 NAYS 1

CLYDE BALLARD

Speaker of the  
House of Representatives

Approved May 9, 1997

CERTIFICATE

I, Mike O Connell, Secretary of the Senate of the State of Washington, do hereby certify that the attached is **SUBSTITUTE SENATE BILL 5763** as passed by the Senate and the House of Representatives on the dates hereon set forth.

MIKE O'CONNELL

Secretary

FILED

May 9, 1997 - 1:51 p.m.

GARY LOCKE

Governor of the State of Washington

Secretary of State  
State of Washington

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**SUBSTITUTE SENATE BILL 5763**

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AS AMENDED BY THE HOUSE

Passed Legislature - 1997 Regular Session

**State of Washington                      55th Legislature                      1997 Regular Session**

**By Senate Committee on Energy & Utilities (originally sponsored by Senators Finkbeiner, Brown, Rossi, McAuliffe, Roach, Kohl, Jacobsen, Hochstatter, Haugen, Goings and West)**

Read first time 02/27/97.

1            AN ACT Relating to prohibiting the taxation of internet service  
2 providers as network telephone services providers; amending RCW  
3 82.04.055 and 82.04.065; adding a new section to chapter 35.21 RCW;  
4 adding a new section to chapter 82.04 RCW; creating a new section; and  
5 declaring an emergency.

6 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

7            NEW SECTION.    **Sec. 1.**    The legislature finds that the newly  
8 emerging business of providing internet service is providing widespread  
9 benefits to all levels of society. The legislature further finds that  
10 this business is important to our state's continued growth in the high-  
11 technology sector of the economy and that, as this industry emerges, it  
12 should not be burdened by new taxes that might not be appropriate for  
13 the type of service being provided. The legislature further finds that  
14 there is no clear statutory guidance as to how internet services should  
15 be classified for tax purposes and intends to ratify the state's  
16 current treatment of such services.

17            NEW SECTION.    **Sec. 2.**    A new section is added to chapter 35.21 RCW  
18 to read as follows:

1       Until July 1, 1999, a city or town may not impose any new taxes or  
2 fees specific to internet service providers. A city or town may tax  
3 internet service providers under generally applicable business taxes or  
4 fees, at a rate not to exceed the rate applied to a general service  
5 classification. For the purposes of this section, "internet service"  
6 has the same meaning as in section 4 of this act.

7       **Sec. 3.** RCW 82.04.055 and 1993 sp.s. c 25 s 201 are each amended  
8 to read as follows:

9       (1) "Selected business services" means:

10       (a) Stenographic, secretarial, and clerical services.

11       (b) Computer services, including but not limited to computer  
12 programming, custom software modification, custom software  
13 installation, custom software maintenance, custom software repair,  
14 training in the use of custom software, computer systems design, and  
15 custom software update services.

16       (c) Data processing services, including but not limited to word  
17 processing, data entry, data retrieval, data search, information  
18 compilation, payroll processing, business accounts processing, data  
19 production, and other computerized data and information storage or  
20 manipulation. Data processing services also includes the use of a  
21 computer or computer time for data processing whether the processing is  
22 performed by the provider of the computer or by the purchaser or other  
23 beneficiary of the service.

24       (d) Information services, including but not limited to electronic  
25 data retrieval or research that entails furnishing financial or legal  
26 information, data or research, internet service as defined in section  
27 4 of this act, general or specialized news, or current information  
28 unless such news or current information is furnished to a newspaper  
29 publisher or to a radio or television station licensed by the federal  
30 communications commission.

31       (e) Legal, arbitration, and mediation services, including but not  
32 limited to paralegal services, legal research services, and court  
33 reporting services.

34       (f) Accounting, auditing, actuarial, bookkeeping, tax preparation,  
35 and similar services.

36       (g) Design services whether or not performed by persons licensed or  
37 certified, including but not limited to the following:

1 (i) Engineering services, including civil, electrical, mechanical,  
2 petroleum, marine, nuclear, and design engineering, machine designing,  
3 machine tool designing, and sewage disposal system designing;

4 (ii) Architectural services, including but not limited to:  
5 Structural or landscape design or architecture, interior design,  
6 building design, building program management, and space planning.

7 (h) Business consulting services. Business consulting services are  
8 those primarily providing operating counsel, advice, or assistance to  
9 the management or owner of any business, private, nonprofit, or public  
10 organization, including but not limited to those in the following  
11 areas: Administrative management consulting, general management  
12 consulting, human resource consulting or training, management  
13 engineering consulting, management information systems consulting,  
14 manufacturing management consulting, marketing consulting, operations  
15 research consulting, personnel management consulting, physical  
16 distribution consulting, site location consulting, economic consulting,  
17 motel, hotel, and resort consulting, restaurant consulting, government  
18 affairs consulting, and lobbying.

19 (i) Business management services, including but not limited to  
20 administrative management, business management, and office management,  
21 but not including property management or property leasing, motel,  
22 hotel, and resort management, or automobile parking management.

23 (j) Protective services, including but not limited to detective  
24 agency services and private investigating services, armored car  
25 services, guard or protective services, lie detection or polygraph  
26 services, and security system, burglar, or fire alarm monitoring and  
27 maintenance services.

28 (k) Public relations or advertising services, including but not  
29 limited to layout, art direction, graphic design, copy writing,  
30 mechanical preparation, opinion research, marketing research,  
31 marketing, or production supervision, but excluding services provided  
32 as part of broadcast or print advertising.

33 (1) Aerial and land surveying, geological consulting, and real  
34 estate appraising.

35 (2) Subsection (1) of this section notwithstanding, the term  
36 "selected business services" does not include:

37 (a) The provision of either permanent or temporary employees.

1 (b) Services provided by a public benefit nonprofit organization,  
2 as defined in RCW 82.04.366, to the state of Washington, its political  
3 subdivisions, municipal corporations, or quasi-municipal corporations.

4 (c) Services related to the identification, investigation, or  
5 cleanup arising out of the release or threatened release of hazardous  
6 substances when the services are remedial or response actions performed  
7 under federal or state law, or when the services are performed to  
8 determine if a release of hazardous substances has occurred or is  
9 likely to occur.

10 (d) Services provided to or performed for, on behalf of, or for the  
11 benefit of a collective investment fund such as: (i) A mutual fund or  
12 other regulated investment company as defined in section 851(a) of the  
13 Internal Revenue Code of 1986, as amended; (ii) an "investment company"  
14 as that term is used in section 3(a) of the Investment Company Act of  
15 1940 as well as an entity that would be an investment company under  
16 section 3(a) of the Investment Company Act of 1940 except for the  
17 section 3(c)(1) or (11) exemptions, or except that it is a foreign  
18 investment company organized under laws of a foreign country; (iii) an  
19 "employee benefit plan," which includes any plan, trust, commingled  
20 employee benefit trusts, or custodial arrangement that is subject to  
21 the Employee Retirement Income Security Act of 1974, as amended, 29  
22 U.S.C. Sec. 1001 et seq., or that is described in sections 125, 401,  
23 403, 408, 457, and 501(c)(9) and (17) through (23) of the Internal  
24 Revenue Code of 1986, as amended, or similar plan maintained by state  
25 or local governments, or plans, trusts, or custodial arrangements  
26 established to self-insure benefits required by federal, state, or  
27 local law; (iv) a fund maintained by a tax exempt organization as  
28 defined in section 501(c)(3) or 509(a) of the Internal Revenue Code of  
29 1986, as amended, for operating, quasi-endowment, or endowment  
30 purposes; or (v) funds that are established for the benefit of such tax  
31 exempt organization such as charitable remainder trusts, charitable  
32 lead trusts, charitable annuity trusts, or other similar trusts.

33 (e) Research or experimental services eligible for expense  
34 treatment under section 174 of the Internal Revenue Code of 1986, as  
35 amended.

36 (f) Financial services provided by a financial institution. The  
37 term "financial institution" means a corporation, partnership, or other  
38 business organization chartered under Title 30, 31, 32, or 33 RCW, or  
39 under the National Bank Act, as amended, the Homeowners Loan Act, as

1 amended, or the Federal Credit Union Act, as amended, or a holding  
2 company of any such business organization that is subject to the Bank  
3 Holding Company Act, as amended, or the Homeowners Loan Act, as  
4 amended, or a subsidiary or affiliate wholly owned or controlled by one  
5 or more financial institutions, as well as a lender approved by the  
6 United States secretary of housing and urban development for  
7 participation in any mortgage insurance program under the National  
8 Housing Act, as amended. The term "financial services" means those  
9 activities authorized by the laws cited in this subsection (2)(f) and  
10 includes services such as mortgage servicing, contract collection  
11 servicing, finance leasing, and services provided in a fiduciary  
12 capacity to a trust or estate.

13 NEW SECTION. **Sec. 4.** A new section is added to chapter 82.04 RCW  
14 to read as follows:

15 (1) The provision of internet services is a selected business  
16 service activity and subject to tax under RCW 82.04.290(1), but if RCW  
17 82.04.055 is repealed then the provision of internet services is  
18 taxable under the general service business and occupation tax  
19 classification of RCW 82.04.290.

20 (2) "Internet" means the international computer network of both  
21 federal and nonfederal interoperable packet switched data networks,  
22 including the graphical subnetwork called the world wide web.

23 (3) "Internet service" means a service that includes computer  
24 processing applications, provides the user with additional or  
25 restructured information, or permits the user to interact with stored  
26 information through the internet or a proprietary subscriber network.  
27 "Internet service" includes provision of internet electronic mail,  
28 access to the internet for information retrieval, and hosting of  
29 information for retrieval over the internet or the graphical subnetwork  
30 called the world wide web.

31 **Sec. 5.** RCW 82.04.065 and 1983 2nd ex.s. c 3 s 24 are each amended  
32 to read as follows:

33 (1) "Competitive telephone service" means the providing by any  
34 person of telecommunications equipment or apparatus, or service related  
35 to that equipment or apparatus such as repair or maintenance service,  
36 if the equipment or apparatus is of a type which can be provided by

1 persons that are not subject to regulation as telephone companies under  
2 Title 80 RCW and for which a separate charge is made.

3 (2) "Network telephone service" means the providing by any person  
4 of access to a local telephone network, local telephone network  
5 switching service, toll service, or coin telephone services, or the  
6 providing of telephonic, video, data, or similar communication or  
7 transmission for hire, via a local telephone network, toll line or  
8 channel, cable, microwave, or similar communication or transmission  
9 system. "Network telephone service" includes interstate service,  
10 including toll service, originating from or received on  
11 telecommunications equipment or apparatus in this state if the charge  
12 for the service is billed to a person in this state. "Network  
13 telephone service" includes the provision of transmission to and from  
14 the site of an internet provider via a local telephone network, toll  
15 line or channel, cable, microwave, or similar communication or  
16 transmission system. "Network telephone service" does not include the  
17 providing of competitive telephone service, the providing of cable  
18 television service, (~~nor~~) the providing of broadcast services by  
19 radio or television stations, nor the provision of internet service as  
20 defined in section 4 of this act, including the reception of dial-in  
21 connection, provided at the site of the internet service provider.

22 (3) "Telephone service" means competitive telephone service or  
23 network telephone service, or both, as defined in subsections (1) and  
24 (2) of this section.

25 (4) "Telephone business" means the business of providing network  
26 telephone service, as defined in subsection (2) of this section. It  
27 includes cooperative or farmer line telephone companies or associations  
28 operating an exchange.

29 NEW SECTION. **Sec. 6.** If any provision of this act or its  
30 application to any person or circumstance is held invalid, the  
31 remainder of the act or the application of the provision to other  
32 persons or circumstances is not affected.

33 NEW SECTION. **Sec. 7.** This act is necessary for the immediate  
34 preservation of the public peace, health, or safety, or support of the  
35 state government and its existing public institutions, and takes effect  
36 immediately.

Passed the Senate April 19, 1997.  
Passed the House April 10, 1997.  
Approved by the Governor May 9, 1997.  
Filed in Office of Secretary of State May 9, 1997.