

NO. 39872-9-II

**COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON**

PUGET SOUND ENERGY, INC.,

Appellant,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

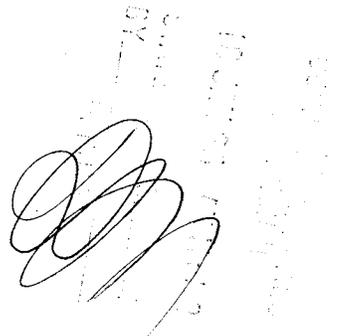
Respondent.

BRIEF OF RESPONDENT

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I. INTRODUCTION

This is a public utility tax case. The sole issue is whether Puget Sound Energy (“Puget”) was entitled to deduct amounts paid to Northwest Pipeline GP (“Northwest”) for natural gas transportation services that Northwest provided to Puget under a written contract. The tax deduction Puget is claiming is codified at RCW 82.16.050(3) and provides that a taxpayer subject to the public utility tax may deduct “[a]mounts actually paid by a taxpayer to another person taxable under this chapter as the latter’s portion of the consideration due for services furnished jointly by both, if the total amount has been credited to and appears in the gross income reported for tax by the [taxpayer].”

Puget is not entitled to the deduction. Unlike Northwest, Puget was not engaged in the transport of natural gas for hire. Rather, Puget sold natural gas to its nearly 750,000 residential, commercial, and industrial customers as part of its regulated local natural gas distribution business. While Puget was permitted to charge its customers a regulated rate for the natural gas it sold, that rate did not include a charge for transporting natural gas. Thus, the service Northwest furnished to Puget—transportation of natural gas—was not the same service Puget provided its customers—retail sale of natural gas. Consequently, none of the amounts Puget paid to

Northwest were Northwest’s “portion of the consideration due for services furnished **jointly by both.**”

Puget simply misreads and misapplies the plain and unambiguous language of the statute. When read as a whole, the statute requires that the “amounts actually paid” to the other person must be “the latter’s portion of the consideration due for services furnished jointly by both.” Here, the amounts Puget paid Northwest were the entire amount of the consideration due for services Northwest provided to Puget, not a portion of the consideration due for services furnished jointly by both. Because Puget did not meet the statutory requirements for the deduction, the superior court correctly denied Puget’s refund claim.

II. RESTATEMENT OF THE ISSUE

The sole issue in this appeal is whether Puget was entitled under RCW 82.16.050(3) to deduct amounts it paid to Northwest for transporting natural gas to Puget as Northwest’s “portion of the consideration due for services furnished jointly by both” Puget and Northwest.

III. STATEMENT OF THE CASE

A. Overview of Puget Sound Energy.

Puget is Washington’s oldest and largest energy utility, and provides natural gas to nearly 750,000 residential, commercial, and industrial consumers situated within the Puget Sound region of Western

Washington. CP 32-33 (Stip. of Facts, ¶¶ 1, 4); CP 40.¹ Puget’s natural gas operations are regulated by the Washington Utilities and Transportation Commission, and the company qualifies as a “gas distribution business” under the Washington public utility tax. CP 33 (Stip., ¶ 4). Within the natural gas industry, Puget is a “local distribution company.” CP 33 (Stip., ¶ 7); CP 46 (“Shipper [Puget] is a local distribution company for natural gas.”).

The amount Puget is allowed to charge its customers is regulated by the Washington Utilities and Transportation Commission and is listed in various tariff schedules. CP 170-209. For residential customers, Puget is authorized to impose a “customer charge,” a “delivery charge,” and a charge for the cost of the gas. CP 175 (tariff for general residential service). Puget is authorized to impose the same general charges for commercial and industrial service. CP 180 (tariff for general commercial and industrial service). Puget explains these charges in brochures provided to its customers. CP 213-225. None of the charges are for the transportation of natural gas. *Id.*

¹ In addition to its natural gas segment, Puget also provides electricity to customers in the Puget Sound region. CP 32 (Stip., ¶ 2). Only the natural gas segment is at issue in this case. CP 33 (Stip., ¶ 3).

B. Natural Gas Industry.

Natural gas is a fossil fuel that is found in deposits around the world. CP 33 (Stip., ¶ 5). Raw natural gas is a mixture of methane, ethane, propane, butane, and other hydrocarbons, along with various contaminants. *Id.* Processed natural gas is mainly methane, with a small amount of ethane and other components. *Id.*

Once extracted from the ground, raw natural gas is piped to a processing plant to be refined to a suitable level of purity. CP 33 (Stip., ¶ 6). From there, the natural gas is piped to various trading hubs or market centers where it is sold as a commodity. *Id.*

A local distribution company, such as Puget, buys natural gas directly from the producer or from a gas marketer at a market center and then contracts with one or more large-diameter, high-pressure pipeline companies to move the gas to the local distribution company's service area. CP 33 (Stip., ¶ 7). The local distribution company then distributes the natural gas to its customers via its smaller-diameter, low-pressure pipeline or stores the natural gas for later distribution. *Id.*

C. Puget's Natural Gas Supply Source.

Puget purchases 100% of its natural gas from a diverse group of major and independent natural gas producers and marketers. CP 33 (Stip., ¶ 8). Just over half of the natural gas purchased by Puget originates from

British Columbia and Alberta, Canada, with the remainder originating from the western United States. CP 33 (Stip., ¶ 8); CP 41.

Natural gas purchased by Puget must be transported to Puget's local distribution area. Puget contracts with several "upstream" pipeline companies in Canada and the United States to transport the gas from the production region to the Northwest pipeline interconnection. CP 34 (Stip., ¶ 11).² From there, the natural gas is transported by Northwest to Puget's service area. CP 34 (Stip., ¶¶ 9, 12). This transportation service is performed pursuant to written contracts, the most significant of which is the Replacement Firm Transportation Agreement entered into between Puget and Northwest in July 1991. CP 34 (Stip., ¶ 12); CP 46-53. Under the terms of that Transportation Agreement, Puget pays a fee for the transportation service provided by Northwest. The amount Northwest is permitted to charge for this service is regulated by the Federal Energy Regulatory Commission ("FERC") and is set out in Rate Schedule TF-1 that is filed with the FERC. CP 34 (Stip., ¶ 13); CP 55-59.

During the periods January 1999 through December 2003 (the "Refund Period"), Puget paid a total of \$264,945,212.75 to Northwest for

² The natural gas pipeline operated by Northwest is roughly 3,900 miles long. CP 34 (Stip., ¶ 10). It extends from the San Juan Basin area of northwest New Mexico and southwest Colorado to a point of termination at the Canadian border near Sumas, Washington. *Id.* The Northwest pipeline also connects up with other natural gas pipelines, allowing for the transfer of natural gas into and out of Northwest's natural gas pipeline. *Id.*

the transportation of natural gas from the Northwest interconnect to the Puget service area. CP 34 (Stip., ¶ 14). As a result of taxpayer confidentiality constraints, the Department is unable to disclose whether Northwest paid public utility tax on any of the amounts it received from Puget for the transportation service. CP 35 (Stip., ¶ 16). *See generally* RCW 82.32.330 (taxpayer confidentiality statute).

Natural gas transported by Northwest is received by Puget at various meter points connecting the Puget local distribution system with the Northwest transmission pipeline. CP 35 (Stip., ¶ 17). There are currently 40 such meter points within Puget's local distribution system. *Id.* These meter points (also known generally within the natural gas industry as "gate stations") serve three primary functions. CP 35 (Stip., ¶ 18). First, they reduce the pressure in the line from the higher levels used by Northwest in transporting the gas to the lower levels used by Puget in distributing the gas to its customers. *Id.* Second, they serve as the point at which odorant is added to the otherwise odorless gas. *Id.* Third, the Puget gate stations measure the flow rate of the gas to determine the amount being received. *Id.*

D. Audit Assessment And Refund Claim.

In February 2005 the Department of Revenue's Audit Division ("Audit Division") completed an excise tax audit of Puget covering the

January 1999 through June 2003 reporting periods. During the audit, Puget requested a credit for public utility tax it had paid on amounts it asserts were deductible under RCW 82.16.050(3). CP 36 (Stip., ¶ 21); CP 232-33. RCW 82.16.050(3) sets out what is commonly referred to as the deduction for “jointly furnished services.” According to Puget, during the January 1999 through June 2003 audit period it had erroneously paid \$9,247,042 in public utility tax on amounts received from customers for natural gas “service” that had been jointly furnished by Puget and Northwest. CP 36 (Stip., ¶ 21).

The Audit Division denied Puget’s refund claim. CP 36 (Stip., ¶ 22); CP 245-46 (audit narrative discussing “Credit Request”). Puget timely appealed the denial of its refund claim to the Department’s Appeals Division. CP 36 (Stip., ¶ 22); CP 297-300. The Appeals Division upheld the denial of the refund claim in Determination No. 07-0338. CP 36 (Stip., ¶ 22); CP 302-13. While Determination No. 07-0338 addressed three issues, the “jointly furnished services” refund claim is the sole issue remaining in this case. CP 36 (Stip., ¶ 22).

E. Proceedings Below.

Pursuant to RCW 82.32.180, Puget filed a de novo refund action in Thurston County Superior Court. CP 4-9. In its complaint, Puget requested a \$10,205,690 refund of public utility tax it claims it overpaid

during 1999 through 2003 on amounts paid to Northwest for transporting natural gas to Puget's gate stations. CP 5-7 (Petition, ¶¶ 4, 5, and 13).³ The parties filed cross-motions for summary judgment on stipulated facts. The superior court granted the Department's motion and denied Puget's cross-motion. CP 376-77. This appeal followed.

IV. ARGUMENT

A. Standard Of Review.

This appeal stems from the grant of summary judgment in favor of the Department of Revenue. The Court of Appeals reviews a grant of summary judgment de novo, using the same standard used by the lower court in ruling on the motion. *Seiber v. Poulsbo Marine Center, Inc.*, 136 Wn. App. 731, 736, 150 P.3d 633 (2007).

Summary judgment is appropriate when no genuine issue of material fact exists and the moving party is entitled to judgment as a matter of law. CR 56. A "material fact" is one upon which the outcome of the litigation depends, in whole or in part. *Barrie v. Hosts of Am., Inc.*, 94 Wn.2d 640, 642, 618 P.2d 96 (1980). The material facts supporting the Department's motion for summary judgment were not disputed. When the material facts in an excise tax refund action are undisputed, and the only issues to be resolved are legal in nature, the appellate court reviews the

³ Puget also sought a refund of sales tax relating to the construction of a natural gas storage facility. CP 7-8. That issue was resolved by settlement. CP 35 (Stip., ¶ 20).

legal conclusions de novo. *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 148, 3 P.3d 741 (2000).

B. Puget Is Not Entitled To Deduct Amounts Paid To Northwest For Transporting Natural Gas To Puget's Gate Stations.

The public utility tax, chapter 82.16 RCW, is imposed for the act or privilege of engaging within this state in any of the public service or transportation businesses listed in RCW 82.16.020, including a “gas distribution business.” RCW 82.16.020(1)(c). A “gas distribution business” is defined as “the business of operating a plant or system for the production or distribution for hire or sale of gas, whether manufactured or natural.” RCW 82.16.010(7). There is no dispute that Puget is a “gas distribution business” subject to the public utility tax. CP 33 (Stip., ¶ 4).

The public utility tax is computed by multiplying the “gross income of the business” by the rate specified for the particular type of business being taxed. The term “gross income” is defined in RCW 82.16.010(12):

“Gross income” means the value proceeding or accruing from the performance of the particular public service or transportation business involved, including operations incidental thereto, but **without any deduction on account of the cost of the commodity furnished or sold**, the cost of materials used, labor costs, interest, discount, **delivery costs**, taxes, **or any other expense whatsoever paid or accrued** and without any deduction on account of losses.

(Emphasis added).

While the Washington Legislature has clearly stated that costs of doing business are generally not deductible in computing the gross income of a public utility business, there are several deductions that are permitted. *See* RCW 82.16.050. This case involves a dispute over the deduction codified at RCW 82.16.050(3). That section provides:

82.16.050 Deductions in computing tax. In computing tax there may be deducted from the gross income . . .

(3) Amounts actually paid by a taxpayer to another person taxable under this chapter as the latter's portion of the consideration due for services furnished jointly by both, if the total amount has been credited to and appears in the gross income reported for tax by the [taxpayer].

To qualify for the deduction, the taxpayer must have paid an amount to a vendor subject to the public utility tax as that vendor's portion of the consideration due for services furnished jointly by both the taxpayer and the vendor, and the total amount paid for the jointly furnished service must be included in the gross income reported by the taxpayer. The primary example is where a customer hires and pays a motor carrier to haul goods from point "A" to point "B" and a portion of the transportation service is performed by a subcontractor. *See* WAC 458-20-179(9)(c)(ii). In that situation the object of the service transaction—the transport of goods for the end consumer—is performed by both the taxpayer and the subcontractor. Moreover, the amount paid by the motor carrier to the

subcontractor represents “the latter’s portion of the consideration due” for the transport services furnished jointly by both.

During the periods at issue, Puget did not meet the requirements for the deduction. More specifically, Puget was not hired by its customers to transport natural gas. While Puget sold natural gas at regulated rates, the object of the transaction was the purchase and sale of the gas, not the transport of the gas from the production site to the customers’ homes and businesses. Stated another way, Puget was selling a commodity (natural gas), not transportation services. As a result, there was no “service furnished jointly by both” Puget and Northwest.

It is clear from the stipulated record that Puget and Northwest provided no joint transportation service to Puget’s customers. This can be verified from a review of the Washington Utilities and Transportation Commission tariff schedules that established the rates Puget could charge its customers, and from the “glossary of charges” that Puget provided to its customers to explain how the rates were determined. CP 170-209, 214, 219.

In general, Puget charged its customers a “customer charge,” a “delivery charge,” and a charge for the cost of the natural gas. CP 174,

180.⁴ The “customer charge” was a fixed amount per month and applied “regardless of the amount of gas used and cover[ed] a portion of the costs of meter reading, billing and other related fixed costs.” CP 214. The “delivery charge” was for “construction, operation and maintenance of pipes, gate stations, pressure regulators and other equipment necessary for the delivery of natural gas” to the customer. *Id.* The charge imposed for the cost of gas “reflect[ed] the actual market cost of natural gas” and was made up of a demand cost and a commodity cost. CP 214, 202.

Notably absent from the amounts Puget was allowed to charge its customers is a charge for transporting natural gas from the point of purchase to the customers’ homes or businesses. While this transportation cost may have been included in the “cost of gas” (i.e., as part of the amount charged for the sale of the commodity), it clearly was not identified in the Washington Utilities and Transportation Commission tariff schedules as a service Puget’s customers were responsible for paying. Since Puget’s customers did not pay a specified amount for the transportation of natural gas, the amount Puget paid Northwest did not, and could not, qualify as Northwest’s “**portion of the consideration due for services furnished jointly by both**” Puget and Northwest.

⁴ In addition to these general charges, the Washington Utilities and Transportation Commission allowed Puget to impose a gas conservation charge, a local or city tax charge, and a line extension charge. *See* CP 211 (representative example customer bill), 214 (glossary of charges).

RCW 82.16.050(3), when construed as a whole, simply does not apply to the natural gas transportation services Northwest provided to Puget under the terms of the Replacement Firm Transportation Agreement entered into between the two companies. The Transportation Agreement required Northwest to deliver natural gas belonging to Puget to Puget's gate stations. CP 34-35 (Stip., ¶¶ 14 & 17); CP 46-52. This was a service that Northwest furnished to Puget, not jointly with Puget. Moreover, the consideration paid to Northwest for this transportation service was not a portion of any identifiable amount Puget charged its customers. If this qualified as Northwest's "portion of the consideration due for services furnished jointly by both," then the phrase has no real meaning and is effectively removed from the statute.

C. The Deduction Is Not Ambiguous. But Even If It Were, Rules Of Statutory Interpretation Do Not Support Puget's Argument.

1. The deduction is not ambiguous.

RCW 82.16.050(3) is not ambiguous. The statute clearly states that to qualify for the deduction the amount paid by the taxpayer to another person taxable under the public utility tax chapter must be a portion of the consideration due for services furnished jointly by both the taxpayer and the other entity. When, as here, the language of the statute is plain and unambiguous, the meaning is derived from the wording of the

statute itself. *POWER v. Utilities & Transp. Comm'n.*, 101 Wn.2d 425, 429-30, 679 P.2d 922 (1984). In deriving the meaning of an unambiguous statute, the reviewing court may consider “the context of the statute in which the provision is found, related provisions, and the statutory scheme as a whole.” *State v. Jacobs*, 154 Wn. 2d 596, 600, 115 P.3d 281 (2005). The court may not, however, add words to an unambiguous statute or change the meaning of key terms. *State v. J.P.*, 149 Wn.2d 444, 450, 69 P.3d 318 (2003).

Puget seems to concede that the statute is not ambiguous. Br. of App., pp. 7-8. However, Puget goes on to suggest that the term “jointly” should be replaced with “work together.” Br. of App., p. 8. *See also Id.* at p. 1 (issue statement). From this seemingly innocuous change in the statutory language, Puget argues that it qualifies for the deduction because, according to Puget, it is “working together” with Northwest to distribute natural gas to Puget’s customers. *Id.* at p. 8.⁵

Puget’s “jointly furnished = working together” analysis is based on a logical fallacy. Puget argues that since Northwest provided natural gas

⁵ Under Puget’s proposed interpretation, the deduction would be allowed for amounts Puget pays to Northwest as Northwest’s “portion of the consideration due for services furnished [working together] by both.” Thus, replacing “jointly” with “working together” not only changes the meaning of the statutory language, it creates a grammatically awkward sentence. Moreover, there is no reason to conclude that the phrase “working together” is more certain in its meaning than “jointly.” The Legislature chose the word “jointly,” not the phrase “working together.” The statute should be read and applied as written.

transportation services to Puget, and Puget provided natural gas distribution “service” to its customers, it follows that both companies were “working together” to distribute natural gas to Puget’s customers. Br. of App., p. 8. There are two fundamental problems with this logic. First, the transportation services Northwest provided to Puget are not the same as the “distribution services” Puget provided its customers. Northwest was hired by Puget to transport natural gas belonging to Puget to Puget’s gate stations. CP 35 (Stip., ¶ 17). Northwest performed this activity alone, not jointly with Puget. From there, Puget sold and distributed the natural gas to its customers. CP 33 (Stip., ¶ 4). Puget performed this activity alone, not jointly with Northwest. Puget’s analysis, whereby these transactionally distinct activities somehow qualify as “services jointly furnished by both,” requires a very broad reading of the deduction statute that effectively equates “jointly furnished” with any activity that does not undercut or sabotage the final distribution of natural gas to Puget’s customers. Nothing in the plain language of the statute supports such a broad interpretation.

Second, Puget is ignoring or changing key words in the statute. “Working together” for some common goal is not equivalent to furnishing services “jointly.” Had the Legislature intended the deduction to apply

when two entities subject to the tax “work together,” it would have expressly said so.

Simply purchasing transportation services offered by another person subject to the public utility tax does not qualify for the deduction. Otherwise, the phrase “portion of the consideration due for services furnished jointly by both” would be rendered meaningless. As the Court is aware, statutes should be construed “so that all the language is given effect and no portion is rendered meaningless or superfluous.” *Kilian v. Atkinson*, 147 Wn.2d 16, 21, 50 P.3d 638 (2002). This is particularly true for tax deductions, which are construed strictly, though fairly, against the taxpayer. *Group Health Coop. v. Wash. State Tax Comm’n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967). There is no basis in the law to ignore key language or to otherwise overlook the statutory requirement that the amount paid by the taxpayer to another person subject to the tax must be the “latter’s portion of the consideration due for services furnished jointly by both.” To do so would expand the deduction far beyond what the plain language allows.

2. The legislative purpose and structure of the deduction does not support Puget’s claim for refund.

The public utility tax is a gross receipts tax similar to the Washington B&O tax. However, unlike the B&O tax, the public utility

tax allows a deduction for “[a]mounts derived from the sale of commodities to persons in the same public service business as the seller, for resale as such within this state.” RCW 82.16.050(2). This deduction—commonly referred to as the “sale of commodities” deduction—effectively prevents the pyramiding of the public utility tax as it relates to the wholesale sale of commodities such as water or natural gas. *Public Utility District No. 2 of Grant County v. State*, 82 Wn.2d 232, 241, 510 P.2d 206 (1973).⁶

Puget argues that the deduction for “services furnished jointly by both” is also designed to prevent the pyramiding of the public utility tax. Br. of App., pp. 10-11. Puget cites no actual legislative history or statement of purpose to support this claim. The “services furnished jointly by both” deduction was part of the 1935 act that created the public utility tax. *See* Laws of 1935, ch. 180, § 40(c). As far as the Department is aware, there is no legislative history describing the purpose for the deduction. In addition, the public utility tax chapter contains no statement of purpose or similar pronouncement by the Legislature stating that the deduction is designed to prevent pyramiding of the tax. *Compare* chapter 82.16 RCW (public utility tax), *with* RCW 82.24.080(1) (express statement of legislative intent that cigarette tax is to be imposed only on

⁶ The term “pyramiding” refers to the imposition of the tax at each stage of the transfer of goods or services.

first possession or sale within the state) *and* RCW 82.26.030 (express statement of legislative intent that tobacco products tax is to be imposed “once, and only once.”) Thus, Puget’s claim that the deduction is designed to prevent pyramiding is mere speculation.

In addition, Puget’s contention that the “purpose and structure” of the public utility tax supports its broad reading of the “services furnished jointly by both” deduction is undercut by the language of RCW 82.16.050(2). As noted above, that subsection sets out the “sale of commodities” deduction and provides that in computing the public utility tax a taxpayer may deduct

[a]mounts derived from the sale of commodities to persons in the same public service business as the seller, for resale as such within this state. **This deduction is allowed only with respect to water distribution, gas distribution or other public service business which furnish water, gas or any other commodity in the performance of public services businesses.**

(Emphasis added).

Puget is a gas distribution business that furnishes gas to its customers in the performance of its public service business. Thus, Puget is selling a commodity within the meaning of RCW 82.16.050(2). If Puget sold natural gas to a person in the same public service business for resale within the state, Puget would be allowed the deduction under RCW 82.16.050(2). However, the “sale of commodities” deduction does not

apply to retail sales or to sales to persons who are not in the same public service business. For this reason, Puget is not entitled to claim the deduction for the retail sale of natural gas to its 750,000 customers.

The fact that Puget is selling a commodity of the type described in the “sale of commodities” deduction undermines its claim that it is entitled to the “services furnished jointly by both” deduction. Had the Legislature intended the retail sale of a commodity such as natural gas to be deductible, it would have clearly said so. In effect, Puget is attempting to defeat the general “purpose and structure” of the tax by claiming that a portion of its gross income from the retail sale of natural gas is deductible under the “services furnished jointly by both” deduction even though Puget is selling a commodity, not furnishing a service. In short, not only is Puget’s refund claim inconsistent with the plain language of the statute, it is inconsistent with the general policy of taxing gross income derived from the retail sale of natural gas.

In any event, even if Puget’s understanding of the legislative purpose of the “services furnished jointly by both” deduction is correct, it does not follow that the deduction should be allowed in all cases where pyramiding of the tax would result. *Cf. Mayflower Park Hotel, Inc. v. State, Dep’t of Revenue*, 123 Wn. App. 628, 633-34, 98 P.3d 534 (2004) (general non-pyramiding nature of the retail sales tax does not compel a

broad reading of the “purchase for purpose of resale” exclusion in order to alleviate possible double taxation). To do so would permit the (unstated and presumed) legislative purpose for the deduction to control over the plain and unambiguous language used in the statute.

In the present case, Puget has not met the requirements for the “services furnished jointly by both” deduction. As a result, the deduction was properly denied. *In re Sehome Park Care Ctr., Inc.*, 127 Wn.2d 774, 778, 903 P.3d 443 (1995) (taxpayer must clearly establish its eligibility for a tax deduction or tax exemption); *Corporation of Catholic Archbishop of Seattle v. Johnston*, 89 Wn.2d 505, 510, 573 P.2d 793 (1978) (same). The general purpose for the deduction, whatever that purpose might be, does not compel a different result. Many, if not all, tax deductions and tax exemptions are premised on some legislative policy choice. But the underlying policy does not control over the language used. *See, e.g., Overton v. Economic Assistance Authority*, 96 Wn.2d 552, 555, 637 P.2d 652 (1981) (taxpayer did not qualify for tax deferral under Economic Assistance Act of 1972 even though it was conceded that “[a]s a policy argument there is considerable merit” to taxpayer’s claim). Rather, courts have consistently held that tax deductions and exemptions are construed “strictly, though fairly and in keeping with the ordinary meaning of their

language, against the taxpayer.” See, e.g., *Group Health Coop.*, 72 Wn.2d at 429.

3. The 1974 case involving Puget Sound Power & Light does not support Puget’s claim for refund.

Puget argues that the holding in a 1974 Thurston County Superior Court case involving Puget Sound Power & Light Company (“Puget Sound Power”) supports Puget’s broad reading of the “services furnished jointly by both” deduction. Br. of App., pp. 10-11. While the 1974 decision is obviously not controlling authority, Puget seems to suggest that since Puget Sound Power was held to be entitled to the deduction under the facts of the 1974 case, Puget must likewise be entitled to the deduction under the facts of this case. However, assuming *arguendo* that the 1974 case was correctly decided, the two cases are distinguishable, and each case must be evaluated on its specific facts.

In that 1974 case two local electric utilities (Puget Sound Power and Clallam County PUD) provided electrical service to their respective customers. From time to time electricity belonging to Puget Sound Power had to be “wheeled” across power lines owned by Clallam County PUD.⁷ Puget Sound Power paid Clallam County PUD for this wheeling service. Summarizing the pertinent facts, the trial court explained:

⁷ Wheeling means “the activity of delivering or distributing electricity owned by others using power lines and equipment of the person doing the wheeling.” WAC 458-20-179(3)(a).

Basically, we have a situation where Puget [Sound Power] receives consideration from its customers to provide electrical services which may have to be 'wheeled' to that customer for Puget. In essence, the two utilities are providing a joint service to the customer who pays the consideration for movement of the electricity from point 'A' to point 'B'.

CP 332.

We do not have the stipulated facts upon which the 1974 case was decided. As a result, it is not known with any degree of certainty what facts the trial court relied on in granting the deduction. On its face, the holding is questionable. The Memorandum Opinion does not describe any bona fide service that was furnished jointly by both Puget Sound Power and Clallam County PUD. Rather, the superior court seemed to equate "services furnished jointly by both" with "joint effort of the interconnected power companies of the Northwest" to provide electricity to consumers. CP 333. In this respect, the superior court's analysis in the 1974 case suffers from the same difficulty as Puget's argument that "jointly furnished" means "working together." Had the Legislature intended "services furnished jointly by both" to mean "joint effort of interconnected power companies" it would have said so. At most, the 1974 superior court decision establishes the furthest extent to which the "services furnished jointly by both" deduction has ever been extended.

Puget's attempt to use this 1974 decision to extend the deduction even further should be rejected.

In any event, there were facts discussed in the superior court's 1974 Memorandum Opinion that distinguish the facts of that case from the facts in the present case. For example, both Puget Sound Power and Clallam County PUD were local distribution companies engaged in the sale and distribution of electricity to consumers. Thus, both companies were selling the same "service." In addition, the Memorandum Opinion states that Clallam County PUD was wheeling electricity to Puget Sound Power's customers "who [pay] the consideration for movement of the electricity from point 'A' to point 'B'." CP 332. Thus, it appears that the electric power was being wheeled to the customer who paid for that wheeling service.

By contrast, the undisputed facts in the present case do not support Puget's refund claim. First, unlike the facts in the 1974 case, Northwest is not engaged in the same type of activity as Puget (i.e., sale and distribution of energy). Second, the record in this case clearly demonstrates that Northwest does not transport natural gas to Puget's customers. Rather, Northwest transports natural gas to Puget at the Puget gate stations. CP 35 (Stip., ¶ 17). From there, Puget either sells and distributes the natural gas to its customers (without any intervening effort from Northwest) or stores

the natural gas for future sale. Moreover, Puget does not charge its customers for natural gas transportation service. CP 174, 180. Thus, unlike the 1974 case, Puget's customers do not pay "consideration for the movement of the [natural gas] from point 'A' to point 'B'."

The fact that Puget Sound Power prevailed in the superior court in 1974 based on the stipulated facts in that case does not mean Puget is entitled to the deduction some thirty-five years later based on different facts. Instead, Puget must prove its entitlement to the deduction in its own right and upon the undisputed facts presented in this case. Puget has not done so. As a result, the superior court below correctly denied Puget's refund claim.

4. The Department's administrative rule does not support Puget's claim for refund.

In support of its claim for refund, Puget next argues that examples provided in WAC 458-20-179(9)(c) support its broad reading of the "services furnished jointly by both" deduction. Br. of App., pp. 11-14.⁸

Puget has misread the administrative rule.

Rule 179(9)(c) provides:

(9) Specific deductions. Amounts derived from the following sources may be deducted from the gross income under the public utility tax if included in the gross amount reported:

⁸ A copy of WAC 458-20-179 is attached as Appendix A.

....

(c) Amounts actually paid by a taxpayer to another person taxable under chapter 82.16 RCW as the latter's portion of the consideration due for services jointly furnished by both. This includes the amount paid to a ferry company for the transportation of a vehicle and its contents (but not amounts paid to state-owned or operated ferries) when such vehicle is carrying freight or passengers for hire and is being operated by a person engaged in the business of urban transportation or motor transportation. It does not include amounts paid for the privilege of moving such vehicles over toll bridges. However, this deduction applies only to the purchases of services and does not include the purchase of commodities. The following examples show how this deduction and the deduction for sales of commodities would apply:

(i) CITY Water Department purchases water from Neighboring City Water Department. CITY sells the water to its customers. Neighboring City Water Department may take a deduction for its sales of water to CITY since this is a sale of water (commodities) to a person in the same public service business. CITY may not take a deduction for its payment to Neighboring City Water as "services jointly furnished." The service or sale of water to the end consumer was made solely by CITY and was not a jointly furnished service.

(ii) Customer A hires ABC Transport to haul goods from Tacoma, Washington to a manufacturing facility at Bellingham. ABC Transport subcontracts part of the haul to XYZ Transport and has XYZ haul the goods from Tacoma to Everett where the goods are loaded into ABC's truck. ABC may deduct the payments it makes to XYZ as a "jointly furnished service."

The ferry example in Rule 179(9)(c) is not very helpful. The example does not set out the underlying facts in sufficient detail to determine if or why the payment is deductible under RCW 82.16.050(3) as

a service furnished jointly by both. At most, the ferry example confirms that if the requirements of the deduction are met, the deduction is not denied simply because a portion of the jointly furnished service was provided by a ferry company as opposed to another motor carrier.

While the ferry example is not helpful, the other two examples in Rule 179(9)(c) provide more factual detail and, therefore, are much more illuminating. In the CITY Water example, CITY Water Department purchases water from Neighboring City Water Department and resells the water to its end customers. The example explains that “CITY may not take a deduction for its payment to Neighboring City Water as ‘services jointly furnished.’ **The service or sale of water to the end consumer was made solely by CITY and was not jointly furnished.**” (Emphasis added). This example confirms that in order to deduct the payment made to another entity taxable under the public utility tax there must be a bona fide service that is actually furnished jointly by both entities. While it could be argued that CITY Water and Neighboring City were “working together” to distribute the water to CITY’s customers, there was no actual service being furnished jointly by both. Therefore, CITY Water did not qualify for the deduction. Similarly, Puget’s sale of natural gas to its end customers is an activity conducted solely by Puget and is not a service

furnished jointly by Puget and Northwest. Therefore, Puget does not qualify for the deduction.

The example in Rule 179(9)(c)(ii) is also inconsistent with Puget's broad reading of the "jointly furnished service" deduction. In that example, the end consumer (Customer A) hires ABC Transport to haul goods from Tacoma to Bellingham. ABC Transport subcontracts part of the haul to XYZ Transport. In effect, XYZ Transport is hired to fulfill a portion of an existing contract between ABC Transport and Customer A.

The purchase of natural gas transportation service by Puget is fundamentally different from the ABC Transport example provided in Rule 179(9)(c)(ii). Northwest is not a subcontractor performing a portion of an existing contract between Puget and its customers.⁹ Rather, the Transportation Agreement is between Puget and Northwest only and contains no express or implied suggestion that Northwest is acting as a subcontractor or that the agreement is designed to fulfill part of some natural gas transportation contract between Puget and its customers. *See* CP 46-53. This is consistent with admissions Puget made in discovery.

⁹ A "subcontract" is "a contract subordinate to another contract" and made for the purpose of carrying out the other contract or part of it. Black's Law Dictionary, 324 (6th ed. 1990). The stipulated record in this case reveals no contract between Puget and its 750,000 customers for the transportation of natural gas from the production site to the customers' homes or businesses. Since there is no transportation contract between Puget and its customers, there can be no subcontract between Puget and Northwest calling for Northwest to fulfill a part of that contract.

When asked to identify “any tariffs on file with the Washington Utilities and Transportation Commission that show the amount Puget . . . could charge its customers for the transmission of natural gas from the point of purchase to the point where the natural gas entered Puget[’s] natural gas distribution facilities,” Puget answered as follows:

[Puget] does not have WUTC tariffs that specifically identify or segregate the charge for the transportation of natural gas from the point of purchase to the point where the natural gas enters PSE’s system. All transportation charges are included in tariffs identified in Interrogatory No. 18 and produced in response to Request for Production No. 23.

CP 321 (Answer to Interrogatory No. 19). None of the tariffs provided by Puget describe any “transportation” contract between Puget and its customers, and none of the tariffs identify any transportation charge. *See* CP 171-209.

It is evident from the record that Puget did not hire Northwest as a subcontractor to fulfill a portion of an existing contract between Puget and its customers. Therefore, the example in Rule 179(9)(c)(ii) does not apply.

When considered as a whole, Rule 179(9)(c) correctly points out that not all services purchased from another person taxable under the public utility tax will qualify for the “services furnished jointly by both” deduction. To qualify, the two entities must actually act in concert to

jointly furnish the service contracted for by the end consumer. Puget's purchase of natural gas transportation service from Northwest does not meet this basic requirement. As a result, Puget is not entitled to the deduction.

Additionally, even if the examples in Rule 179(9)(c) could be construed as supporting Puget's claim that simply purchasing a service offered by another person subject to the public utility tax is sufficient to qualify for the deduction, that construction of the Rule would be contrary to the plain language of RCW 82.16.050(3) which requires the services to be "furnished jointly by both." In that case, "the statute would trump the [Rule]." *Mayflower Park Hotel v. Dep't of Revenue*, 123 Wn. App. 628, 633, 98 P.3d 534 (2004).

In the final analysis, accepting Puget's broad construction of Rule 179(9)(c) would make it very difficult to draw any principled line in a chain of contracting parties that result, to some extent, in providing public services or commodities to the end consumer. The "services furnished jointly by both" deduction would be available to contracting parties in virtually all situations involving public service businesses subject to the public utility tax. There is simply no legal or logical support for such a broad reading of the statute or the Department's administrative rule.

5. Puget has not met its burden of proving it is entitled to the deduction.

Finally, if any lingering doubt remains, it is important to note that Puget bears the burden of proving that it is entitled to the deduction. *In re Sehome Park Care Ctr., Inc.*, 127 Wn.2d 774, 778, 903 P.3d 443 (1995) (citing *Group Health Coop v. Wash. State Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967)). Tax deductions and exemptions are to be construed “strictly, though fairly and in keeping with the ordinary meaning of their language, against the taxpayer.” *Group Health*, 72 Wn.2d at 429. In *Corporation of Catholic Archbishop of Seattle v. Johnston*, 89 Wn.2d 505, 510, 573 P.2d 793 (1978), the Washington Supreme Court applied the rule this way:

Appellant’s qualification under [the statute] is at best uncertain and ambiguous, and ambiguities must be construed against the person claiming the exemption. Given a choice between broad construction and narrow construction of the exemption, we construe [it] narrowly. Because there is no provision explicitly and clearly authorizing this exemption, it must be denied.

In other words, “to doubt an exemption is to deny it.” *Chesapeake & Potomac Tel. Co. v. Comptroller*, 561 A.2d 1034, 1038 (Md. 1989) (quoting *Perdue, Inc. v. Department of Assess.*, 286 A.2d 165, 167 (Md. 1972)).

Because Puget is not clearly and unambiguously entitled to the deduction under the undisputed facts of this case, the superior court

correctly denied Puget's refund claim. To the extent Puget believes the statutory language should be amended to exclude the "furnished jointly by both" requirement, the remedy lies with the Washington Legislature, not the Courts.

V. CONCLUSION

For the reasons set forth above, the Department respectfully requests that the Court affirm the trial court's order granting the Department of Revenue's motion for summary judgment. The trial court correctly concluded that Puget was not entitled to deduct amounts it paid to Northwest Pipeline for natural gas transportation services Northwest provided to Puget.

RESPECTFULLY SUBMITTED this 25th day of January, 2010.

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WAC 458-20-179

Public utility tax.

(1) **Introduction.** Persons engaged in certain public service businesses are taxable under the public utility tax. (See chapter 82.16 RCW.) These businesses are exempt from the business and occupation tax on the gross receipts which are subject to the public utility tax. (See RCW 82.04.310.) However, many persons taxable under the public utility tax are also engaged in some other business activity which is taxable under the business and occupation (B&O) tax. For example, a gas distribution company engaged in operating a plant or system for distribution of natural gas for sale, may also be engaged in selling at retail various gas appliances. Such a company would be taxable under the public utility tax with respect to its distribution of natural gas to consumers, and also taxable under the business and occupation tax with respect to its sale of gas appliances. It should also be noted that some services which generally are taxable under the public utility tax are taxable under the B&O tax if the service is performed for a new customer, prior to receipt of regular utility services by the customer.

(2) **Definitions.** The following definitions apply to this section:

(a) The term "gross income" means the value proceeding or accruing from the performance of the particular public service or transportation businesses involved. It includes operations incidental to the public utility activity, but without any deduction on account of the cost of the commodity furnished or sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

(b) The term "service charge" means those specific charges made to a customer for providing a specific service. The term includes the actual charge to a customer for the sale or distribution of water, gas, or electricity. This term does not include utility local improvement district assessments (ULID) or local improvement district assessments (LID).

(c) The term "subject to control by the state" means control by the utilities and transportation commission or any other state department required by law to exercise control of a business of a public service nature as to rates charged or services rendered.

(3) **Persons taxable under the public utility tax.** The term "public service businesses" includes any of the businesses defined in RCW 82.16.010 (1) through (9), and (11). It also includes any business subject to control by the state, or having the powers of eminent domain, or any business declared by the legislature to be of a public service nature, irrespective of whether the business has the powers of eminent domain or the state exercises its control over the business. It includes, among others, without limiting the scope thereof: Railroad, express, railroad car, water distribution, sewerage collection, light and power, telegraph, gas distribution, urban transportation and common carrier vessels under sixty-five feet in length, motor transportation, tugboat businesses, certain airplane transportation, boom, dock, ferry, pipe line, toll bridge, toll logging road, and wharf businesses. (See WAC 458-20-251 for sewerage collection.) Persons engaged in these business activities are subject to the public utility tax even if they are not publicly recognized as providing that type of service or the amount of income from these activities is not substantial.

(a) "Light and power business" includes charges made for the "wheeling" of electricity for others. "Wheeling" is the activity of delivering or distributing electricity owned by others using power lines and equipment of the person doing the wheeling.

(b) Persons engaged in hauling for hire by motor vehicle should also refer to WAC 458-20-180.

(c) Persons hauling property, other than U.S. mail, by air transportation equipment are taxable under the other public service public utility tax. Income from the hauling of U.S. mail or passengers is not subject to the public utility tax because of specific federal law. (See 49 U.S.C. section 1301 and section 1513(a).)

(d) Persons engaged in hauling persons or property for hire by watercraft between points in Washington are taxable under the public utility tax. Income from operating tugboats of any size and income from the sale of transportation services by vessels over sixty-five feet is taxable under the public service utility tax classification. Income from the sale of transportation services using vessels under sixty-five feet, other than tugboats, is taxable under "vessels under sixty-five feet" public utility tax classification. These classifications include businesses engaged in chartering or transporting persons by water from one location in Washington to another location within this state. This does not include sightseeing tours or activities which are in the nature of guided tours where the tour may include some water transportation. Persons engaged in providing tours should refer to WAC 458-20-258.

(e) Income from activities which are incidental to a public utility activity are generally taxable under the public utility tax when performed for an existing customer. This includes charges for line extensions, connection fees, line drop charges, start up fees, pole replacements, testing, replacing meters, line repairs, line raisings, pole contact charges, load factor charges, meter reading fees, etc. However, if any of these services are performed for a customer prior to sale of a public utility service to the customer, the income is taxable under the business and occupation tax. (See subsection (4) of this section.)

(4) **Business and occupation tax.** As indicated above, services which are incidental to a public utility activity are generally subject to the public utility tax. However, these types of charges are taxable under the service and other business activities B&O tax classification if performed for a customer prior to receipt of the utility services (gas, water, electricity) by a new customer. A "new customer" is a customer who previously has not received utility services, such as water, gas, or electricity, at the location where the charge for a specific service was provided. For example, a customer of a water supplier who currently

receives water at a residence constructs a new residence a short distance from the first location. This customer will be considered a "new customer" with respect to any charges for services performed at the new location until the customer actually receives water at the new location, even though this customer may be receiving services at a different location. The charge for installing a meter or a connection charge for this customer at the new location would be taxable under the service and other activities B&O tax classification.

Amounts charged to customers as interest or penalties are generally taxable under the service and other business activities B&O tax classification. This includes interest charged for failure to timely pay for utility services or for special services which were performed prior to the customer receiving services, such as connection charges. However, any interest and/or penalty charged because of the failure to timely pay a LID or ULID assessment will not be taxable for the public utility tax or the B&O tax.

(5) **Tax rates.** The rates of tax for each business activity are imposed under RCW 82.16.020 and set forth on appropriate lines of the combined excise tax return forms.

(6) **Uniform system of accounts.** In distinguishing gross income taxable under the public utility tax from gross income taxable under the business and occupation tax, the department of revenue will be guided by the uniform system of accounts established for the specific type of utility concerned. However, because of differences in the uniform systems of accounts established for various types of utility businesses, such guides will not be deemed controlling for the purposes of classifying revenue under the Revenue Act.

(7) **Volume exemption.** Persons subject to the public utility tax are exempt from the payment of this tax if the taxable income from utility activities does not meet a minimum threshold. Prior to July 1, 1994, there was a similar exemption for the business and occupation tax with different threshold amounts. Beginning July 1, 1994, the law provides for a B&O tax credit for taxpayers who have a minimal B&O tax liability. (See WAC 458-20-104.) The volume exemption for the public utility tax applies independently of the business and occupation tax credit or exemption. The volume exemption for the public utility tax applies for any reporting period in which taxable income reported under the combined total of all public utility tax classifications does not equal or exceed the minimum taxable amount for the reporting periods assigned to such persons according to the following schedule:

| | |
|-------------------------------------|--------------------|
| Monthly reporting basis | \$500 per month |
| ... | |
| Quarterly reporting basis | \$1500 per quarter |
| | |
| Annual reporting basis | \$6000 per annum |
| .. | |

(8) **Exemption of amounts or value paid or contributed to any county, city, town, political subdivision, or municipal corporation for capital facilities.** RCW 82.04.417 previously provided an exemption from the public utility tax and the business and occupation tax for amounts received by cities, counties, towns, political subdivisions, or municipal corporations representing contributions for capital facilities. These contributions are often referred to as "contributions in aid of construction." This law was repealed effective July 1, 1993, and this exemption is no longer available after that date. (See chapter 25, Laws of 1993 sp.s.) However, contributions in the form of equipment or facilities will not be considered as taxable income. For example, if an industrial customer purchases and installs transformers which it donates to a public utility district as a condition of receiving future service, the public utility district will not be subject to the public utility tax or B&O tax on the receipt of the donated transformers. For a water or sewerage collection business, the value of pipe, valves, pumps, or similar items donated by a developer to the utility business would not be taxable income to the utility business. Monetary payments are considered to be payments for installation of facilities so that a customer may receive the public utility commodity or service. When the facilities are installed or constructed by the customer and subsequently given to the utility business, there is no payment for installation of the facilities.

(9) **Specific deductions.** Amounts derived from the following sources may be deducted from the gross income under the public utility tax if included in the gross amounts reported:

(a) Amounts derived by municipally owned or operated public services businesses directly from taxes levied for the support thereof, but not including service charges which are spread on the property tax rolls and collected as taxes. LID and ULID assessments, including interest and penalties on such assessments, will not be considered part of the taxable income because they are exercises of the jurisdiction's taxing authority. These assessments may be composed of a share of the costs of capital facilities, installation labor, connection fees, etc. A deduction may be taken for these amounts if they are included in the LID or ULID assessments.

(b) Amounts derived from the sale of commodities to persons in the same public service business as the seller, for resale as such within this state. This deduction is allowed only with respect to water distribution, light and power, gas distribution or

other public service businesses which furnish water, electrical energy, gas or any other commodity in the performance of a public service business.

(c) Amounts actually paid by a taxpayer to another person taxable under chapter 82.16 RCW as the latter's portion of the consideration due for services jointly furnished by both. This includes the amount paid to a ferry company for the transportation of a vehicle and its contents (but not amounts paid to state-owned or operated ferries) when such vehicle is carrying freight or passengers for hire and is being operated by a person engaged in the business of urban transportation or motor transportation. It does not include amounts paid for the privilege of moving such vehicles over toll bridges. However, this deduction applies only to the purchases of services and does not include the purchase of commodities. The following examples show how this deduction and the deduction for sales of commodities would apply:

(i) CITY Water Department purchases water from Neighboring City Water Department. CITY sells the water to its customers. Neighboring City Water Department may take a deduction for its sales of water to CITY since this is a sale of water (commodities) to a person in the same public service business. CITY may not take a deduction for its payment to Neighboring City Water as "services jointly furnished." The service or sale of water to the end consumers was made solely by CITY and was not a jointly furnished service.

(ii) Customer A hires ABC Transport to haul goods from Tacoma, Washington to a manufacturing facility at Bellingham. ABC Transport subcontracts part of the haul to XYZ Transport and has XYZ haul the goods from Tacoma to Everett where the goods are loaded into ABC's truck. ABC may deduct the payments it makes to XYZ as a "jointly furnished service."

(d) Amounts derived from the distribution of water through an irrigation system, solely for irrigation purposes.

(e) Amounts derived from the transportation of commodities from points of origin in this state to final destination outside this state, or from points of origin outside this state to final destination in this state with respect to which the carrier grants to the shipper the privilege of stopping the shipment in transit at some point in this state for the purpose of storing, manufacturing, milling, or other processing, and thereafter forwards the same commodity, or its equivalent, in the same or converted form, under a through freight rate from point of origin to final destination.

(f) Amounts derived from the transportation of commodities from points of origin in the state to an export elevator, wharf, dock or shipside on tidewater or navigable tributaries thereto from which such commodities are forwarded, without intervening transportation, by vessel, in their original form, to an interstate or foreign destination: Provided, That no deduction will be allowed when the point of origin and the point of delivery to such export elevator, wharf, dock, or shipside are located within the corporate limits of the same city or town. The following examples show how this deduction applies:

(i) ABC Trucking delivers logs to a storage area which is adjacent to the dock from where shipments are made by vessel to a foreign country. The logs go through a peeling process at the storage area prior to being placed on the vessel. The peeling process changes the form of the original log. Because the form of the log is changed, ABC Trucking may not take a deduction for the haul to the storage area. It is immaterial that the trucker may be paid based on an "export" rate.

(ii) ABC Trucking hauls logs from the woods to a log storage area which is adjacent to the dock. The logs will be sorted prior to being placed in the hold of the vessel, but no further processing will be performed. The storage area is quite large and the logs will be moved by log stacker and will be placed alongside the ship. The logs are loaded using the ship's tackle and then transported to a foreign country. ABC Trucking may take a deduction for the amounts received for transporting the logs from the woods to the log storage area. The movement of the logs within the log storage area is not considered to be "intervening transportation," but is part of the stevedoring activity.

(iii) ABC Trucking hauls logs from the woods to a "staging area" where the logs are sorted. After sorting, XY Hauling will transport some of the logs from the staging area to local mills for lumber manufacturing and other logs to the dock which is located approximately five miles from the staging area where the logs immediately are loaded on a vessel for shipment to Japan. The dock and staging area are not within the corporate city limits of the same city. ABC Trucking may not take a deduction for amounts received for hauling logs to the staging area. Even though some of these logs ultimately will be exported, ABC Trucking is not delivering the logs directly to the dock where the logs will be loaded on a vessel.

However, XY Hauling may take a deduction for the income from hauls to the dock. Its haul was the final transportation prior to the logs being placed on the vessel for shipment to Japan. The logs remained in their original form with no additional processing. The haul also did not originate or terminate within the corporate city limits of the same city or town. All the conditions were met for XY Hauling to claim the deduction.

(g) Amounts derived from the distribution of water by a nonprofit water association which are used for capital improvements by that association.

(h) Amounts received from sales of power which is delivered by the seller out-of-state. A deduction may also be taken for the sale of power to a person who will resell the power outside Washington where the power is delivered in Washington. These sales of power are also not subject to the manufacturing B&O tax.

(i) Amounts received for providing commuter share riding or ride sharing for the elderly and the handicapped in accordance with RCW 46.74.010.

(j) Amounts expended to improve consumers' efficiency of energy end use or to otherwise reduce the use of electrical energy or gas by the consumer. (For details see WAC 458-20-17901.)

(k) Income from transporting persons or property by air, rail, water, or by motor transportation equipment where either the origin or destination of the haul is outside the state of Washington.

(10) **Other deductions.** In addition to the deductions discussed above there also may be deducted from the reported gross income (if included within the gross), the following:

- (a) The amount of cash discount actually taken by the purchaser or customer.
- (b) The amount of credit losses actually sustained.
- (c) Amounts received from insurance companies in payment of losses.
- (d) Amounts received from individuals and others in payment of damages caused by them to the utility's plant or equipment.

(11) **Exchanges by light and power businesses.** There is no specific exemption which applies to an "exchange" of electrical energy or the rights thereto. However, exchanges of electrical energy between light and power businesses do qualify for deduction in computing the public utility tax as being sales of power to another light and power business for resale. An exchange is a transaction which is considered to be a sale and involves a delivery or transfer of energy or the rights thereto by one party to another for which the second party agrees, subject to the terms and conditions of the agreement, to deliver electrical energy at the same or another time. Examples of deductible exchange transactions include, but are not limited to, the following:

(a) The exchange of electric power for electric power between one light and power business and another light and power business;

(b) The transmission or transfer of electric power by one light and power business to another light and power business pursuant to the agreement for coordination of operations among power systems of the pacific northwest executed as of September 15, 1964;

(c) The Bonneville Power Administration's acquisition of electric power for resale to its Washington customers in the light and power business;

(d) The residential exchange of electric power entered into between a light and power business and the administrator of the Bonneville Power Administration (BPA) pursuant to the Pacific Northwest Electric Power Planning and Conservation Act, P.L. 96-501, Sec. 5(c), 16 U.S.C. 839(c) (Supp. 1982). In some cases, power is not physically transferred, but the purpose of the residential exchange is for BPA to pay a "subsidy" to the exchanging utilities. For public utility tax reporting purposes, these subsidies will be treated as a nontaxable adjustment (rebate or discount) for purchases of power from BPA.

(12) **Customer billing information.** RCW 82.16.090 requires that customer billings issued by light or power businesses or gas distribution businesses serving more than twenty thousand customers shall include the following information:

(a) The rates and amounts of taxes paid directly by the customer upon products or services rendered by such businesses; and

(b) The rate, origin and approximate amount of each tax levied upon the revenue of such businesses which has been added as a component of the amount charged to the customer. This does not include taxes levied by the federal government or taxes levied under chapters 54.28, 80.24, or 82.04 RCW.

(13) **Motor or urban transportation.** For specific rules pertaining to the classifications of "urban transportation" and "motor transportation," see WAC 458-20-180.

[Statutory Authority: RCW 82.32.300, 94-13-034, § 458-20-179, filed 6/6/94, effective 7/7/94; 86-18-069 (Order 86-16), § 458-20-179, filed 9/3/86; 85-22-041 (Order 85-6), § 458-20-179, filed 11/1/85; 83-01-059 (Order ET 82-13), § 458-20-179, filed 12/15/82; Order ET 71-1, § 458-20-179, filed 7/22/71; Order ET 70-3, § 458-20-179 (Rule 179), filed 5/29/70, effective 7/1/70.]

NO. 39872-9-II

**COURT OF APPEALS FOR DIVISION II
STATE OF WASHINGTON**

PUGET SOUND ENERGY, INC.,

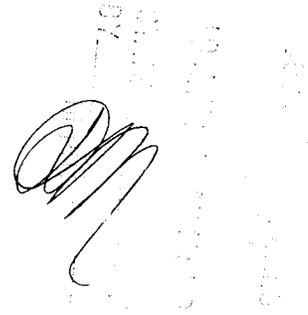
Appellant,

v.

STATE OF WASHINGTON
DEPARTMENT OF REVENUE,

Respondents.

CERTIFICATE OF
SERVICE

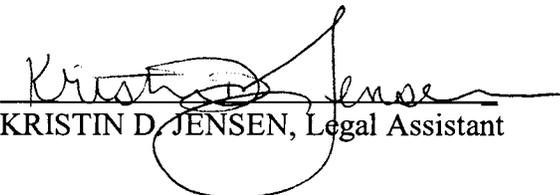


I certify that on January 25, 2010, I served a true and correct copy of the Brief of Respondent, via via U.S. Mail, postage prepaid, through Consolidated Mail Services, on the following:

Robert Mahon
Perkins Coie LLP
1201 Third Avenue, Suite 4800
Seattle, WA 98101-3099
RMahon@perkinscoie.com

I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED this 25th day of January, 2010, at Tumwater, WA.


KRISTIN D. JENSEN, Legal Assistant