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**SUPREME COURT BY RONALD R. CARPENTER
OF THE STATE OF WASHINGTON**

**Community Telecable of Seattle, Inc., Comcast of Washington I, Inc.,
and Comcast of Washington IV, Inc.,**

Petitioners

v.

City of Seattle,

Respondent

Brief of Amicus Curiae Qwest Corporation

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I. INTRODUCTION

The decision of the court of appeals contains several errors, one of which this Court recognized four months ago in *Qwest Corporation v. City of Bellevue*, 161 Wn.2d 353, 368, 166 P.3d 667 (2007) (disapproving the court of appeals' interpretation of state law precluding city taxation of charges for interstate access as well as interstate service).

The court of appeal's most fundamental error is misunderstanding and ignoring the definitions of the Internet and Internet access contained in state and federal law. This failure results in misapplication of the Internet Tax Freedom Act ("ITFA"), Pub. L. 105-277, 112 Stat. 2681-719 (1998), and the state Internet tax moratorium, Laws of 1997, ch. 304.

Second, the court of appeals erroneously concluded that Seattle's imposition of utility tax on Internet access was protected by the ITFA's grandfather clause. The ITFA grandfather clause does not protect Seattle's tax because it was not imposed on Internet access prior to October 1, 1998. The decision of the court of appeals is dependent upon reading RCW 82.04.065(2) as classifying all data transmissions as "network telephone services." This reading of RCW 82.04.065 both (a) ignores the exclusion of "internet service" from the definition of "network telephone service" in RCW 82.04.065(2) and (b) conflicts with RCW 35.21.714, which expressly limits city taxation of both interstate data transmission services and access to such services. Seattle did not impose-and was

barred by state law from imposing-tax on interstate services or access to interstate services, whether those were voice or data services.

Third, the court of appeals erroneously concluded that Seattle's imposition of tax on Comcast's Internet access was not a discriminatory tax on electronic commerce under the ITFA because Seattle was taxing all telephone companies similarly. In addition to the reasons cited in Comcast's Supplemental Brief, this is incorrect because the City did not impose utility tax on other taxpayers who provided interstate service or access to interstate service. By singling out Comcast's provision of access to the Internet-the quintessential interstate service-for taxation, the City is discriminating against electronic commerce in violation of the ITFA.

II. IDENTITY AND INTEREST OF AMICUS

Qwest is one of the largest providers of telecommunications services in the City of Seattle and the State of Washington. In addition to local network telephone service and access to interstate network telephone service, Qwest provides high speed Digital Subscriber Line ("DSL") Internet access service in competition with petitioners Community Telecable of Seattle, Inc., Comcast of Washington I, Inc., and Comcast of Washington IV, Inc. (collectively, "Comcast"). Qwest has a direct interest as a taxpayer, competitor, and service provider in the authority of Seattle and other cities to impose telephone utility tax on Internet access service.

III. STATEMENT OF THE CASE

Qwest adopts the Statement of the Case set forth by Comcast in its Petition for Review and its Brief of Respondents filed with the court of appeals. Pet. for Review at 4 - 5; Br. of Respondents at 2 - 13.

IV. ARGUMENT

A. **The Court of Appeals' Decision Ignores the Definition of the Internet and, as a Result, Permits the Taxation of Internet Access in Violation of Federal and State Law.**

The court of appeals' analysis focuses on the literal inclusion of "data transmission" within the definition of "network telephone service" under RCW 82.04.065(2). However, the court's analysis ignores the critical definitions of the "Internet," "Internet service," and "Internet access," which both qualify the definition of "network telephone service" and limit the ability of cities to tax data transmissions that are part of Internet access and service.

1. **What Is the "Internet"?**

Congress defined the "Internet" in the ITFA as follows:

The term "Internet" means collectively the myriad of computer and telecommunication 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.

Pub. L. 105-277, 112 Stat. 2681-719, § 1104(4). The Washington Legislature adopted a similar definition:

"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.

RCW 82.04.297(2).

The Internet is not a fixed destination or facility. Rather, it is that collection of linked computer networks using certain defined common protocols—a network of networks. Computer networks and the Internet exist solely by reason of data transmission between computers. *See* P. Gralia, *How the Internet Works* (8th ed. 2007). The connection of Comcast's coaxial cable to its customer's home or business is the location where the customer plugs into and becomes a part of the Internet within the meaning of the ITFA and RCW 82.04.297. The City's claim to be able to carve out and tax Internet data transmission strikes at the core of the Internet, which Congress and the Legislature sought to protect against city taxation.

2. The City Is Attempting to Tax "Internet Access."

The ITFA limits city taxation of "Internet access," which was defined:

The term "Internet access" means a service that enables users to access content, information, electronic mail, or other services offered over the Internet, and may also include access to proprietary content, information, and other services as part of a package of services offered to users. Such term does not include telecommunication services.

Pub. L. 105-277, 112 Stat. 2681-719, § 1104(5). The definition of "Internet access" explicitly excludes "telecommunications services" (as specifically defined therein), which remains subject to local taxation.

For purposes of the ITFA, the term "telecommunications services" means telecommunications services as defined in Section 3(46) of the Communications Act of 1934, 47 U.S.C. § 153(46). Pub. L. 105-277, 112 Stat. 2681-719, Section 1104(9). The ITFA thus expressly incorporates a regulatory standard. The Federal Communications Commission ("FCC"), the federal agency charged with interpreting and administering this regulatory standard, has ruled that cable modem Internet access services are not "telecommunications services" under the Section 3(46) of the Communications Act. *In re Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities*, 17 FCC Rcd. 4798 (2002). The FCC's determination was specifically upheld by the United States Supreme Court in *Nat'l Cable & Telecommun. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 125 S. Ct. 2688, 162 L.Ed. 2d 820 (2005). Accordingly, there is no open argument that cable modem Internet access service is not "Internet access" under the ITFA by reason of the exception for "telecommunications services."

The court of appeals concluded that *Brand X* is not binding in this case because "it did not consider whether data transmission was inseparable from Internet service under Washington law" and "did not address whether, under federal law, states and local governments can tax revenue from cable modem service as a network telephone service."

Community Telecable of Seattle, Inc. v. City of Seattle (Comcast), 136 Wn.App. 169, 181, 149 P.3d 380 (2006). However, in *Brand X* the United States Supreme Court held that cable modem Internet access service is not a "telecommunications service" within Section 3(46) of the Communications Act of 1934 (47 U.S.C. § 153(46)). Because the ITFA incorporates the same definition of "telecommunications service" construed in *Brand X*, cable modem Internet access service is "Internet access" protected from state and local taxation by the ITFA.

3. The City Is Attempting to Tax "Internet Service" Contrary to State Law.

State law prevents cities from taxing "Internet service" at a rate higher than the rate applied to the general service classification.

RCW 35.21.717. The Legislature defined "Internet service" as follows:

"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.

RCW 82.04.297(3) (emphasis added). The definition includes communications within those networks comprising the Internet as well as the act of gaining initial access to that network.

The court of appeals concluded that Seattle could bifurcate Internet access service and tax a portion as data transmission (network telephone

services). However, RCW 82.04.065(2) explicitly provides that "the provision of internet service as defined in RCW 82.04.297" is not a "network telephone service." The key to distinguishing "network telephone service" from "Internet service," which inherently includes various data transmission including "access to the Internet," is to identify the function of the data transmission network.

Part of the confusion in the present case may arise out of the fact that changes in the underlying technology allow a single physical network structure to be used for more than one type of transmission. A telephone network historically was a closed system, allowing for voice and data transmission only on that network. However, developments in technology coupled with regulatory changes and interconnections with other networks now allow a variety of different physical network structures to be interconnected to form connecting computer networks. These include telephone networks, cable networks, and electrical networks (via DSL over power lined) as well as dedicated computer networks (both hardwired and Wi-Fi).

For example, for many years residential consumers accessed the Internet through "dial-up" connections provided over the public switched telephone network. *See National Cable & Telecommunications Ass'n v. Brand X*, 545 U.S. 967, 974, 125 S.Ct. 2688 (2005). A consumer with a basic telephone connection could, though the use of a modem to transform

¹ *See In the Matter of United Power Line Council's Petition for Declaratory Ruling Regarding the Classification of Broadband over Power Line Internet Access Service as an Information Service*, 21 FCC Red 13281, 2006 FCC LEXIS 5966.

the format of the signal, dial a number on the public switched telephone network to reach an Internet service provider. However, that consumer's telephone connection remained a basic telephone connection able to make and receive traditional telephone calls.²

There are two principal broadband, high-speed services that allow residential consumers to access the Internet: cable modem service and Digital Subscriber Line ("DSL") service. *Brand X* at 975. Cable modem Internet access service is linked to a specific Internet service provider (in this case, Comcast) and there is no alternative connection for the cable modem Internet access. Pursuant to the Supreme Court's decision in *Brand X*, the cable system operator providing cable modem Internet access service does not have to allow other Internet service providers access to its network. Unlike a traditional telephone line, which can be used to access the Internet and, for other functions, Comcast's cable modem Internet access service represents dedicated Internet access provided at the customer's home or business on one unified and exclusive system.

Until September of 2005, DSL service offered by local telephone companies such as Qwest was classified as a "telecommunications service" under Section 3(46) of the Communications Act. As such, telephone companies were required to allow other Internet service providers to interconnect to the telephone company's data switch to receive connections from consumers. *In re Deployment of Wireline*

² The Washington Legislature specifically preserved taxation of a customer's use of a public switched network to transmit to the site of an Internet service provider. RCW 82.04.065(2).

Services Offering Advanced Telecommunications Capability, 13 FCC Red. 24011, 24030-24031, ¶ 36-37 (1998). For that reason, a DSL connection by itself was historically nothing more than a data transmission line-the functional equivalent of other private data transmission lines, such as ISDN data transmission lines or a T-1 or larger capacity line supporting a greater capacity of voice and/or data transmission. While a DSL line would have no functional use except to connect to an Internet service provider, the consumer was engaged in making two purchases-one of a data transmission line and a second purchase of Internet access-for the simple reason that the consumer had a choice in selecting Internet service providers.

Following the *Brand X* decision, the FCC reclassified DSL service to allow local telephone service providers to offer a unified Internet access service, i.e., dedicated Internet access based on DSL, and discontinued the regulatory requirement that such DSL line be offered for connection to other Internet service providers. *In the Matters of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities, et. al*, 20 FCC Red. 14853, 2005 FCC LEXIS 5257 (2005).

The issue in the present case is whether the customer is purchasing Internet access or making two purchases-one for Internet access and one for data transmission. Although the court of appeals dismisses *Brand X* as not controlling on Washington law, the case is, at a minimum, very instructive because the FCC and the U.S. Supreme court were faced with the same fundamental issue: is cable modem Internet access a single

integrated information service or separate telecommunications service and information service. The U.S. Supreme Court described the issue and the FCC's conclusions:

The issue before the Commission was whether cable companies providing cable modem service are providing a "telecommunications service" in addition to an "information service."

* * *

[T]he Commission concluded that cable modem service was not "telecommunications service." "Telecommunications service" is "the offering of telecommunications for a fee directly to the public." 47 U.S.C. §153(46). ... The Commission conceded that, *like all information-service providers, cable companies use "telecommunications" to provide consumers with Internet service*; cable companies provide such service via the high-speed wire that transmits signals to and from an end user's computer. *Declaratory Ruling 4823, P40*. For the Commission, however, the question whether cable broadband Internet providers "offer" telecommunications involved more than whether telecommunications was one necessary component of cable modem service. . . .

Seen from the consumer's point of view, the Commission concluded, *cable modem service is not a telecommunications offering because the consumer uses the high-speed wire always in connection with the information-processing capabilities provided by Internet access*, and because the transmission is a necessary component of Internet access. . . . The wire is used, in other words, to access the World Wide Web, newsgroups, and so forth, rather than "transparently" to transmit and receive ordinary-language messages without computer processing or storage of the message. See *supra*, at 4 (noting the *Computer II* notion of "transparent" transmission). *The integrated character of this offering led the Commission to conclude that cable modem service*

is not a "stand-alone," transparent offering of telecommunications.

Brand X, 545 U.S. 967, 986-988 (emphasis added).

Like the cable modem Internet access provider in *Brand X*, Comcast is offering Seattle consumers integrated Internet access. While the Internet and access to the Internet inherently involve data transmission, RCW 82.04.065(2) explicitly provides that "Internet services," including Internet access are not taxable as network telephone services.

The court of appeals relies heavily on the Washington Department of Revenue's Excise Tax Advisory 2029.04.245. ETA 2029.04.245 confirmed the exclusion for "telecommunication services" from the definition of "Internet access" as contained in the ITFA. Thus, the ETA concluded that a party purchasing stand-alone data transmission services to support Internet access services could not claim that the services were converted into Internet access based on their intended use. However, the ETA did not say that sales tax extended to Internet access. The court of appeals improperly expanded the ETA to include Comcast's provision of Internet access.

The Department's ETA also has limited value in analyzing city taxation because the State of Washington taxes interstate telecommunications services and access. In contrast, the Legislature has expressly prohibited cities from taxing interstate telecommunications services and access. RCW 35.21.714; *Qwest Corporation v. City of Bellevue*, 166 P.3d 667, 676 (2007).

B. The ITFA Grandfather Clause Does Not Save Seattle's Tax Because Seattle Did Not-And Could Not-Impose or Enforce Tax on Interstate Service or Access to Interstate Service.

The court of appeals concluded that the City's tax was exempt from federal preemption under the ITFA's grandfather clause because "it was authorized by the State before October 1, 1998, the City notified taxpayers of the tax before October 1, 1998, and the city generally collected the tax prior to October 1, 1998." *Comcast*, 136 Wn.App. at 387. The court's decision is wrong for at least two reasons.

First, the City's utility tax has never been applied to "Internet access" as defined in the ITFA. The City's prior administrative rule (repealed during the middle of the audit in this case) imposed utility tax only on transmission activities that were not Internet access under the ITFA. To give Seattle Business Rule 5-44-155(6) the reading given by the court of appeals and now argued by the City would make all Internet access taxable under the City's utility tax. The City's prior enforcement practice was that dial-up Internet access services were taxable under the service classification of the City's B&O tax, not the utility tax. The court of appeals was wrong when it concluded that the City notified taxpayers that they were subject to utility tax on Internet access before October 1, 1998.

Second, even accepting the court of appeal's reading of repealed Seattle Rule 5-44-155, the City did not have the power to tax the services at issue as "network telephone services." State law-before and after

October 1, 1998-barred the City from imposing tax "for access to, or charges for, interstate services." RCW 35.21.714, as amended by Laws of 1983, 2nd ex. sess., ch. 3, § 37. This Court recently rejected the court of appeal's erroneous limitation of RCW 35.21.714 in deciding *Qwest Corporation v. City of Bellevue*, 161 Wn.2d 353, 368, 166 P.3d 667, 676 (2007).⁴

The City argues that this Court's decision in *Qwest* should not affect this case because Comcast failed to assert that it was exempt from tax under RCW 35.21.714. However, Comcast pleaded in its Complaint that the FCC determined that cable modem service is an interstate service and that, pursuant to RCW 35.21.714, among other laws, Comcast's Internet service revenues should not be subject to telephone utility tax. CP 5, 7 (Comcast Complaint, ¶¶ 12, 24). Moreover, there is no dispute that Comcast did argue that the City's tax was preempted by the IFTA and was not protected by the ITFA grandfather clause. The court of appeal's conclusion that Seattle's tax on data transmissions providing Internet access was validly levied before October 1, 1998 and thus grandfathered for the ITFA is both directly in issue and erroneous. Seattle's imposition of tax on interstate service and access was barred by RCW 35.21.714 prior to October 1, 1998. Seattle also gave no indication before October 1, 1998-or until this case-that it intended to impose tax on interstate service or access. Accordingly, Seattle's imposition of utility tax on

⁴ *Qwest* dealt with the restrictions on code cities under RCW 35A.82.060, the language of which is identical to RCW 35.21.714 applicable to non-code cities. *Qwest* at 363 (n. 12).

Internet access violates the ITFA and is not saved by the grandfather clause.

C. Seattle's Tax Is a Discriminatory Tax on Electronic Commerce Under the ITFA Because It Is Imposed on Comcast But Not Other Providers of Interstate Service and Access.

The court of appeals decision concludes that Seattle's tax does not violate the ITFA's moratorium on "discriminatory taxes on electronic commerce" because "[t]he City's telephone utility tax applies uniformly to companies engaged in the telephone business." *Comcast*, 136 Wn.App. at 189. In addition to the reasons outlined in Comcast's Supplemental Brief, this is wrong because the City does not and cannot tax interstate telecommunications service or access to such service. Thus, even if Comcast's Internet access could be bifurcated to separate out a network telephone service component, Seattle is not taxing Comcast uniformly with other providers of interstate service or access.

In *Qwest v. Bellevue*, this Court held that the City of Bellevue could not, as a matter of state law limitation on municipal taxing authority, impose city telephone utility tax on charges imposed to access interstate telecommunications service. In doing so, the Court explicitly disapproved of court of appeals conclusion in this case that RCW 35.21.714 prohibited city tax on charges for interstate services or access only when the charges were to another telecommunications company. *Qwest* at 368.

This Court's decision in *Qwest* confirms Seattle's general practice of not taxing interstate network telephone service or access to such

service. It also highlights Seattle's current discrimination when it taxes Comcast's provision of Internet access. Like Washington's limitation on the ability of cities to tax interstate telecommunications service or access, New York State does not tax "interstate and international telephony and telegraphy and telephone and telegraph service." N.Y. Tax Law § 1105(b)(1)(B). The New York Board of Tax Appeals concluded that telecommunication services purchased by Internet service providers were nontaxable interstate services:

It would be hard to imagine a communications activity more imbued with interstate and international characteristics than the use of the internet. Subscribers to the services of an internet service provider like petitioner may use the internet for a wide range of activities including sending and receiving electronic mail messages, visiting web sites for recreational, commercial, or academic information, and ordering goods and services which may be delivered through the mail or downloaded directly to the user's computer. *In conducting these activities, it is impossible to avoid interstate communications.* A subscriber in Albany, New York is as likely to have an electronic mail box maintained on a computer in Virginia as in his home state. If he sends an e-mail message to his grandmother who lives in Buffalo, it might be received in her mail box maintained on a computer in California. She might read the message on a hand held wireless device while visiting Chicago or at an internet cafe in Istanbul. A message to a cousin in California might end up in an electronic mail box on a computer in New York State. If the subscriber goes to the world wide web site of a local newspaper to check the latest high school basketball scores, he might be surprised to be told that he is communicating with the computer of a web hosting business thousands of miles away. *It seems that any intrastate aspect of access*

to the internet is merely random and incidental to an interstate and international service.

In re Petition of Concentric Network Corporation, 2006 WL 776279

(*N.Y. Tax. App. Trib.*), Dkt. No. 819533 (March 16, 2006) at *12

(emphasis added). The Board also addressed the fact that some lines at issue in the case carried communications between in-state subscribers and the Internet service provider's in-state point of presence:

It is artificial ... to treat the point of presence as the destination of these communications in the sense that a voice call to a telephone number at a residence in Buffalo has a destination in Buffalo. . . . The data originating in the key strokes on the subscriber's computer flow out to the internet through petitioner's point-of-presence facilities and data flows back in a continuous process that has no geographical reference that is perceptible to the subscriber or his interlocutors. Accordingly, the link in question seems is merely "an intrastate strand of an interstate service."

Id.

Thus, while Seattle properly refrains from taxing most taxpayers' provision of interstate service and access, it taxes Comcast's provision of such service. The City argues that it is not taxing access to interstate service. However, its argument depends on the City's ability to arbitrarily divide Comcast's Internet service into components, one of which it characterizes as intrastate telephone service. This ignores *Qwest*, which rejected a similar attempt by the City of Bellevue to mischaracterize the interstate access limitation based on a geographic test. The test under

RCW 35.21.714 is based on the function of the service and not the geographic scope.

Comcast customers are not paying Comcast to get communication between their homes and Burien. Customers are paying a single monthly fee for access to the Internet. The facts are undisputed that Comcast's customers connect with the Internet at their homes and businesses. Customers do not purchase Comcast transmission services to access another Internet service provider (as is the case with dial up service using a traditional telephone line). As the New York Tax Tribunal noted that "[i]t would be hard to imagine a communications activity more imbued with interstate ... characteristics than the use of the internet" and that any intrastate communication is "random and incidental" to interstate service. *In re Petition of Concentric Network Corporation*, 2006 WL 776279 (N.Y. Tax. App. Trib.), Dkt. No. 819533 (March 16, 2006) at *12.

The City argues that this Court's decision in *Qwest* should not affect this case. However, there is no dispute that Comcast argued that the City's tax was a discriminatory tax on electronic commerce under the IFTA. The court of appeal's decision that Seattle was treating all telecommunications companies similarly was based on a misunderstanding that Seattle was taxing all companies on the provision of interstate services and access. It was not. Seattle was imposing tax on Comcast's interstate Internet access service while not taxing most other interstate data service and access. Seattle's discriminatory administration

violates the ITFA independently of whether Comcast is exempt from tax under RCW 35.21.714.

V. CONCLUSION

For the foregoing reasons, Qwest respectfully urges the Court to reverse the decision of the court of appeals.

DATED: December 20, 2007.

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to be served by legal messenger a true and correct copy 9 Br efiof iirctas ENTER

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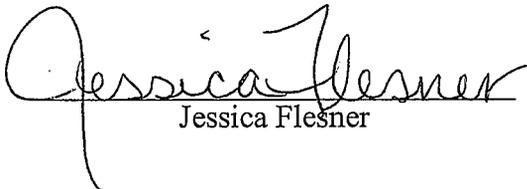
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I further certify that on this 21st day of December, 2007, I caused
to be served by U.S. Mail, postage prepaid, a true and correct copy of
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Signed at Seattle, Washington, this 21st day of December, 2007.


Jessica Flesner

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