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Supreme Court No. 79702-1

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COMMUNITY TELECABLE OF SEATTLE, INC.,  
COMCAST OF WASHINGTON I, INC., AND  
COMCAST OF WASHINGTON IV, INC.,

Petitioners,

v.

CITY OF SEATTLE,

Respondent.

Petitioners' Supplemental Brief

Randy Gainer, WSBA No. 11823  
Dirk Giseburt, WSBA No. 13949  
Davis Wright Tremaine LLP  
Attorneys for Petitioners

1201 Third Avenue, Suite 2200  
Seattle, Washington 98101-3045  
(206) 622-3150 Phone  
(206) 757-7700 Fax

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## I. Introduction

The decision below should be reversed for four reasons. *First*, the Court of Appeals' interpretation of the federal Internet Tax Freedom Act ("ITFA")<sup>1</sup> violates both the statute's plain language and the stated intent of Congress. The ITFA prohibits local governments from segregating data transmission from other aspects of Internet service and then taxing the alleged data transmission "component" of Internet service.

*Second*, the Court of Appeals misapplied the ITFA's grandfather and antidiscrimination clauses, applying them to the alleged data transport component of Internet access rather than to Internet access as a whole.

*Third*, the Courts of Appeals similarly misinterpreted the language and intent of Washington's 1997 statute, "Prohibiting Taxation of ISP's as Telephone Service Providers" ("1997 State act"), Laws of 1997, Ch. 304. The court misread the statute's exclusion of Internet services from "network telephone services" as an authorization to tax the supposed data transmission component of Internet services at the telephone tax rate.

*Fourth*, the court misconstrued RCW 35.21.714, holding that it authorizes cities to tax interstate network telephone service revenues.

*Cnty. Telecable of Seattle, Inc. v. City of Seattle*, 136 Wn. App. 169, 181-

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<sup>1</sup> The citation for the ITFA and excerpts from the versions adopted in 1998, 2004, and 2007 are included in Appendices A, B, and C, respectively. Other than extending the tax moratorium to 2014, the 2007 amendments did not alter the effect of the ITFA in this case. ITFA cites are to the 2004 version unless otherwise noted.

82 ¶¶ 24-25, 149 P.3d 380 (2006). This Court has since rejected such a reading of RCW 35.21.714, *Qwest Corp. v. City of Bellevue*, 161 Wn.2d 353, 368 ¶ 30, 166 P.3d 667, 676 (2007), thus confirming that the Court of Appeals' decision must be reversed.

## **II. Issues for Review**

1. Does the federal moratorium in the ITFA bar Seattle from imposing its telephone utility tax on Comcast's Internet access service?
2. Does the City violate the ITFA's antidiscrimination provision by taxing cable Internet access providers at a 6% rate while taxing other Internet access providers at a 0.415% tax rate?
3. May the City tax Internet services as "Network telephone service" even though the 1997 State act prohibits such taxes, especially where the Internet services are provided through interstate connections as a matter of law and fact?

## **III. Statement of the Case**

Comcast relies on the Statement of the Case in its Petition for Review, at 4-5, and in its Brief to the Court of Appeals, at 2-13.

## **IV. Argument**

### **A. Congress and the State Legislature Intended to Prevent Taxation of Internet Services as Telephone Services.**

In the late 1990s, several cities and states, including Tacoma, attempted to tax Internet service as a telephone service. This provoked a

strong, negative political reaction.<sup>2</sup> The Washington Legislature in 1997 and Congress in 1998 each passed statutes prohibiting new taxes on Internet service and limiting how existing taxes applied to Internet service.

These reactions occurred in part because of the overlap and integration of Internet features with telecommunications and the resulting potential for inconsistent tax treatment of Internet access providers.

Congress recognized that the states attempting to tax Internet access in 1998 were “do[ing] so in an inconsistent and potentially burdensome manner,” treating Internet access as data processing services in some places, information services in others, and telecommunications services in still others. H.R. Rep. No. 105-570, pt. 1, at 7 (1998).

Congress understood that Internet service represents a convergence of communications and computer-based services. Congress sought to confine state and local telephone taxes solely to recognized telecommunications services. “For more than 30 years, the FCC has been analyzing the nature of the convergence of communications and computer services. . . . For States now to start classifying computer-based services as ‘telecommunications services’ only creates confusion for the industry.” *Id.* at 10.

In 2004, Congress extended the ITFA moratorium from 2003 to

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<sup>2</sup> See, e.g., Washington Department of Revenue Determination No. 01-036, 21 Wash. Tax Dec. 13, 17 (2002), available at <http://taxpedia.dor.wa.gov/> (“[T]he legislature adopted RCW 82.04.297 in response to an attempt by the City of Tacoma to treat persons who provide access to the Internet as a utility.”).

2007, Pub. L. 108-435, 118 Stat. 2615, and reiterated that its protection of “Internet access” was intended to prevent states and local governments from segregating and taxing data transport used for Internet access:

*In practice, Internet access provided to the user may include a transmission component that is an integral part of the Internet access, as in the case of . . . cable modem Internet access, and certain wireless Internet access. In such cases, the transmission component is not a separate telecommunications service subject to taxation.*

H.R. Rep. 108-234, at 9 (2003), CP 699 (emphasis added).

Similarly, the Washington Legislature reacted to the action of Tacoma by enacting a bill entitled “Prohibiting Taxation of Internet Service Providers as Telephone Service Providers.” Laws of 1997, Ch. 304 (attached as Appendix D). Section 1 of that act found that “the newly emerging business of providing internet service is providing widespread benefits” and “should not be burdened by new taxes . . . .” But because “there [was] no clear statutory guidance as to how internet services should be classified for tax purposes,” *id.*, it was not clear whether Tacoma’s action was justified by the preexisting definition of “network telephone service.” The Legislature resolved this ambiguity by excluding “internet service” from “network telephone service,” *id.*, section 5,<sup>3</sup> so that neither cities nor the State could tax an Internet provider as a telephone business.

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<sup>3</sup> *Western Telepage, Inc. v. City of Tacoma*, 140 Wn.2d 599, 610, 998 P.2d 884, 891 (2000) (“The Legislature *expressly excluded* from RCW 82.04.065(4) various types of ‘network telephone service,’ such as competitive telephone services, cable television, radio, broadcast television, and the Internet.”) (italics in original; underlining added).

**B. The Court of Appeals Erred by Applying the ITFA's Grandfathering and Antidiscrimination Provisions to Taxes on Data Transport.**

1. In the ITFA, Congress prohibited (1) all state and local taxes on "Internet access" (unless grandfathered) and (2) all discriminatory taxes on "electronic commerce," including the provision of "Internet access." ITFA §§ 1101(a), 1105(3) (App. B-1, B-4).

Understanding the statutory definition of "Internet access" – which the Court of Appeals passed over – is crucial before applying the ITFA's protections. The definition of "Internet access," together with other statutory definitions, is what "defines the scope of the moratorium." H.R. Rep. No. 105-570, pt. 1, at 22 (1998) (emphasis added).

The ITFA originally defined "Internet access" as:

*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 telecommunications services.*

1998 ITFA § 1104(5) (emphasis added) (App. A-3). Congress created a protected zone of "Internet access" subject to the ITFA moratorium by defining "Internet access" to exclude "telecommunications services" but not all telecommunications. Only "telecommunications" that constituted "telecommunications services" under the Communications Act of 1934 were excluded from that zone. 1998 ITFA § 1104(9) (App. A-3); 2004

ITFA § 1105(9) (App. B-4). Data transport performed by a cable Internet provider is *not* a “telecommunications service” and therefore falls under the ITFA’s moratorium. *See infra*, pp. 9-10.

The ITFA definition of “Internet access” covers Comcast’s cable service. By subscribing to Comcast’s Internet service, Comcast’s customers obtain access to all the features and services “offered *over* the Internet.” The court below acknowledged this. 136 Wn. App. at 179 ¶ 20. Comcast provides a service that Congress sought to protect from all state and local taxes (unless grandfathered) and from discriminatory taxes.

2. The ITFA’s grandfather clause permits the survival of some state and local taxes on “Internet access,” ITFA § 1104(a) (App. B-1), but Seattle’s tax does not qualify. For a state or local tax to be grandfathered under the ITFA, the facts must show that either—

(i) a provider of Internet access services had a reasonable opportunity to know by virtue of a rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that *such agency has interpreted and applied such tax to Internet access services*; or

(ii) a State or political subdivision thereof generally collected such tax on *charges for Internet access*.

ITFA, § 1104(a)(1)(B) (emphasis added) (App. B-1-2).<sup>4</sup>

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<sup>4</sup> ITFA § 1104(a)(1)(A) (App. B-1) also requires that the tax be authorized by statute. As discussed above, page 4, below, pages 14-15, and in Respondent’s Br. to the Court of Appeals, at 13-21 and 38-39, statutory authority for the tax was withdrawn in 1997 when the Legislature excluded “internet service” from the definition of “network telephone

Seattle's argument for grandfathering fails because its telephone utility tax did not apply to the class of activities defined by Congress as "Internet access" – "a service that enables users to access content, information, electronic mail, or other services offered over the Internet" – but to only a subset of Internet access services, i.e., to data transmission. In other words, because the City never applied the telephone utility tax fully to "Internet access" – and, to this day, still claims that it is not taxing "Internet access" – the City cannot invoke the ITFA's grandfather clause.

The Court of Appeals made a similar mistake. Citing Seattle's Rule 155 (CP 439, quoted at 136 Wn. App. at 185 ¶ 31), the court stated that Seattle had applied the telephone utility tax to "companies transmitting data related to the Internet," 136 Wn. App. at 185-87 ¶¶ 31, 33-35, but this does not assert a tax on "Internet access" that otherwise might qualify under the ITFA grandfather clause.<sup>5</sup> By its own terms, Rule 155 did not purport to tax Internet access providers primarily under the telephone utility tax. Instead, Seattle purported to apply its *service B&O*

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service."

<sup>5</sup> Comcast also argued that Rule 155 was itself invalid and therefore could not provide effective "notice" under the ITFA. Respondents' Br. at 39-41. The court held that any invalidity did not undermine the notice, 136 Wn. App. at 186 ¶ 34, but this finding is inconsistent with the general rule that an invalid state action cannot satisfy a specific federal statutory requirement. See *Eastern Telecom Corp. v. Borough of E. Conemaugh*, 872 F.3d 30, 34 (3d Cir. 1989) (city's failure to comply with state law in commencing franchise renewal process voided subsequent procedures under Cable Act).

*tax* to Internet access providers. 136 Wn. App. at 175 ¶ 11, 190 ¶ 39.<sup>6</sup>

Moreover, the ITFA, the FCC, and the Supreme Court make clear that the data transmission aspect of cable Internet access may not be segregated and taxed. *See infra*, pp. 9-10. Because Seattle's claim of grandfathering depends on such segregation, it must be rejected.

The Court of Appeals' approach is emblematic of the problems that motivated Congress to clarify the ITFA in 2004 by expressly prohibiting states and cities from bifurcating DSL Internet service into "information" and "communication" components of Internet access.

[W]hile apparently no states tax the dial-up method of Internet access (with the exception of those subject to the grandfather clause), *some tax other technologies, such as DSL Internet services, thereby undermining the purpose of the ITFA*. In contrast, *other states have ruled that transmission and access together constitute "Internet access" and are included within the ITFA moratorium. The Committee believes that the latter interpretation more correctly conforms with Congressional intent*.

H.R. Rep. 108-234, at 9-10 (2003), CP 699-700 (emphasis added).

The Senate Commerce Committee agreed that separately taxing data transport used to provide "Internet access" was not intended:

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<sup>6</sup> The court below asserted that it could apply the grandfather and discrimination tests without deciding whether Comcast is providing Internet access. 136 Wn. App. at 182 ¶ 26. It drew support from the approach in *Concentric Network Corp. v. Commw.*, 897 A.2d 6, 15 (Pa. Commw. Ct. 2006) (*en banc*), *aff'd per curiam on other grounds*, 922 A.2d 883 (Pa. 2007). The Pennsylvania court's analysis was wrong in failing to apply the ITFA's terms, but it is distinguishable in any event because the issue involved sales tax on transmission services purchased by an ISP. The court recognized that, under the ITFA, an ISP would not have to pay sales and use taxes on telecommunications the ISP itself provides. *Id.* Because Comcast provides its own telecommunications, if the *Concentric* rationale were applied here, the City's telephone tax would not apply.

[T]he Committee believes that the current definition of Internet access under the Act requires clarification *to ensure that States and localities do not attempt to circumvent the moratorium on Internet access taxes by taxing individual components of access such as telecommunications services used to provide Internet access.* To date, some States have interpreted narrowly the definition of Internet access under the ITFA in order to impose taxes on certain types of Internet access or components thereof. . . .

S. Rep. No. 108-155, at 3 (2003) (emphasis added).

The 2004 amendments were intended to ensure that taxing agencies treat DSL service the same as cable Internet service. Indeed, Congress had already recognized that “cable modem Internet access services, *which are not telecommunications services*, are already subject to the moratorium.” H.R. Rep. 108-234, at 10, CP 700 (emphasis added).

The clinching fact is that the FCC has also ruled, and the U.S. Supreme Court has affirmed, that data transmission used in cable Internet service is not a “telecommunications service” as that phrase is used in the Communications Act but instead is an inseparable part of cable modem Internet service. *Declaratory Ruling*, 17 FCC Rcd. 4798, 4823 ¶ 39 (2002). The Supreme Court specifically affirmed the FCC’s holding on this point. *Nat’l Cable & Telecomm. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967, 987-88, 1000-02, 125 S. Ct. 2688, 2703-04, 2710-11, 162 L. Ed. 2d 820, 842-43, 850 (2005). The FCC’s and Supreme Court’s determination that the data transmission aspect of cable Internet service is

not a “telecommunications service” under the Communications Act must be applied in this case.<sup>7</sup> Accordingly, the data transmission aspect of cable Internet access may not be segregated and taxed, and Seattle’s argument for grandfathering under the ITFA should be rejected.

3. In addition to not qualifying for grandfather status, the City’s tax runs afoul of the ITFA prohibition of discriminatory taxes on electronic commerce, which the ITFA defines in part as a tax that:

establishes a classification of *Internet access service providers* . . . for purposes of establishing a higher tax rate to be imposed on such providers than the tax rate generally applied to providers of similar information services delivered through other means . . . .

ITFA § 1105(2)(A)(iv) (emphasis added) (App. B-3). The Court of Appeals, having held that State law established a clean division between Internet service and telephone service, found no discrimination because “[a]ll companies in Seattle that engage in the telephone business are subject to the telephone utility tax, and all companies that provide Internet services are subject to the B&O tax.” 136 Wn. App. at 190 ¶ 39. This position is demonstrably false under the undisputed facts.

First, the court upheld the assessment of telephone utility tax on 100% of Comcast’s cable modem service revenues despite having noted

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<sup>7</sup> The FCC has reiterated this 2002 finding in at least three other cases. See *In the Matter of Appropriate Regulatory Treatment for Broadband Access to the Internet Over Wireless Networks*, 22 FCC Rcd. 5901, 5903-04, 5913 (2007).

that “Comcast also provides ‘Internet services’ (as defined in RCW 82.04.297).” *Id.* at 179 ¶ 20. The court also noted that the other cable Internet provider in Seattle, Summit Communications, was subjected only to the telephone business tax. *Id.* at 187 ¶ 36. Because the City taxes cable Internet services at the telephone utility tax rate, the court’s claim that “all companies that provide Internet services are subject to the B&O tax,” 136 Wn. App. at 189-90 ¶ 39, does not survive scrutiny.

Second, Seattle does not tax all providers of transmission services equally under the telephone utility tax. Internet service, cable television service, and radio and television broadcasting all fall within the definition of “network telephone service,” *Western Telepage*, 140 Wn.2d at 610, 998 P.2d at 891, because they involve “the providing of telephonic, video, data, or similar communication or transmission for hire, via a telephone network, toll line or channel, cable, microwave, or similar communication or transmission system.” RCW 84.04.065(2). Though Seattle has no authority to tax cable TV, radio or TV broadcasting, or Internet service as a telephone business, RCW 84.04.065(2), it is only with Internet providers – not the others – that Seattle claims to bifurcate the income and treat part of the activity as telephone business.<sup>8</sup>

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<sup>8</sup> The City cannot arbitrarily apportion revenue from one of these four types of businesses, taxing the data transport portion of Internet service as a “telephone business,” and not apply the telephone utility tax rate to the data transport portion of cable television

Third, Seattle also discriminates between a class of Internet service providers (those who provide Internet service by cable) and providers of information services provided by other (non-Internet) means. The City's Rule 155 states that information service providers are subject to the service B&O tax, while the City has consistently asserted the telephone business tax (or the higher-rate cable tax) against cable Internet providers. This difference in treatment, too, discriminates against cable ISPs. Because Seattle imposes telephone tax on cable Internet providers and a B&O service tax on other Internet providers and on non-Internet information providers, the City's taxes are unlawfully discriminatory.

**C. The Court of Appeals Erred by Finding that Comcast's Internet Service Is Taxable as a Telephone Service.**

As discussed above, at 4, the Washington Legislature also acted to prevent the taxation of Internet services at telephone rates. To resolve the classification of Internet service, the 1997 State act specified that "network telephone service" "includes the provision of transmission to and from the site of an internet provider via a telephone network, toll line or channel, cable, microwave, or similar communication or transmission system," but *not* "the provision of internet service as defined in RCW 82.04.297, including the reception of dial-in connection, provided at the

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service, radio broadcasting, and television broadcasting. *Lone Star Cement Corp. v. City of Seattle*, 71 Wn.2d 564, 569-72, 429 P.2d 909, 912-14 (1967) (finding violation of equal application of privileges and immunities when revenues of one business were taxed and similar revenues of similarly situated taxpayers were not).

site of the internet service provider.” RCW 82.04.065(2) (App. D-4). The Court of Appeals found that, although Comcast provides Internet services, the services are also taxable as “network telephone service” based on its view that the services are data transmission and that Comcast’s services are “transmissions to and from the site of an internet provider.” 136 Wn. App. at 179 ¶ 19. The court was wrong on both counts.

First, undisputed facts show that Comcast does not passively “transmit Internet services” that are supplied by other companies.<sup>9</sup> Comcast’s email, domain name, and provisioning servers, and its CMTS equipment, which assigns Internet Protocol addresses to each data packet, all actively manipulate data and are necessary to provide Internet services to Comcast’s customers in Seattle. CP 32-33, ¶¶ 5, 8; CP 34-35, ¶¶ 3; 7.

Second, the Court of Appeals’ mischaracterization of Comcast’s services as “network telephone service” ignored the plain language and structure of the 1997 State act. The act adopted both the definition of “internet service” in section 4 (App. D-4) (now codified at RCW 82.04.297(3)) and the revised exclusions from the definition of “network

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<sup>9</sup> The Court of Appeals referred to Comcast’s activity as “transmitting Internet services,” 136 Wn. App. at 175 ¶ 11, 184 ¶ 30, apparently adopting the phrase from the City’s Opening Brief, 3. This nonstatutory language derives from the Ninth Circuit Court of Appeals’ discredited holding that “transmission of Internet service to subscribers over cable broadband facilities is a telecommunications service.” *AT&T Corp. v. City of Portland*, 216 F.3d 871, 880 (9th Cir. 2000). The *Portland* decision has no force after the Supreme Court’s decision in *Brand X*, 545 U.S. at 979-80.

telephone service” in section 5 (App. D-4) (now codified in RCW 82.04.065(2)). Section 4 of the act defined “internet service” broadly:

“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 services” 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 sub-network called the world wide web.

App. D-4 (emphasis added). If “internet service” did not include data transmission, it could not provide restructured information over the Internet, could not make it possible for users to interact with stored information over the Internet, could not provide Internet email, and could not give users the ability to make use of the Internet.

By defining “internet service” in terms that necessarily include data transmission, the Legislature knowingly created an overlap with the existing definition of “network telephone service.”<sup>10</sup> It resolved that issue by expressly *excluding* “internet service” from the definition of “network telephone service.” Nevertheless, the Court of Appeals erroneously interpreted the 1997 State act as “preserving the City’s ability to tax Comcast’s data transmission activities as telephone business.” 136 Wn.

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<sup>10</sup> The overlap is not unique to Washington law. See *Clark v. BellSouth Telecomm., Inc.*, 461 F. Supp. 2d 541, 545, 547 (D. Ky. 2006) (finding similar overlap in Kentucky tax code; holding DSL communications services used to provide Internet access to be an integral part of Internet access and therefore not taxable as a “communications service”).

App. at 178 ¶ 18. The court's assertion that the exclusion acts as an authorization renders the exclusion language superfluous.

Third, the Court of Appeals also erred by holding that Comcast's services were "transmissions to and from the site of an internet provider" and therefore "network telephone services" under RCW 82.04.065(2). 136 Wn. App. at 178 ¶ 19. The court based this finding on its conclusion that "Comcast provides a cable transmission system from its customers' homes and businesses to Comcast's facilities in Burien and then to the Westin Building." *Id.* This conclusion is wrong because it repeats the same error of bifurcating Comcast's Internet service.

In addition, the court ignored uncontested facts showing that the point of transfer of data from customers to Comcast is where data from the customers' computers leave cable modems and enter Comcast's coaxial cable at the customers' homes and offices. CP 34-35, ¶ 3. In this regard, cable Internet networks are unlike dial-up ISPs' networks; no phone company transmits data to and from a customer and a receiving site across town or across the country before they enter an ISP's network. CP 908-09, ¶¶ 8-9; *see also Brand X*, 545 U.S. at 974-75 (same) (citing cases). Rather, in cable Internet networks, the "site of an Internet provider" begins at the location of that data transfer. *See id.* at 975 (cable companies act as ISPs themselves unless they lease their cables to another ISP). Data

transmissions within Comcast's network from the customers to the Westin Building (CP 911-13, ¶¶ 16-22) are not "to and from the site of an Internet provider."

The City attached as an appendix to its reply brief in the Court of Appeals Excise Tax Advisory 2029.04.245 ("ETA") issued by the Washington Department of Revenue in 2006, after the trial court granted summary judgment to Comcast in November 2005. CP 765-66. The City cited and relied on the ETA in its reply at 4-5. The Court of Appeals held that the ETA supported its conclusion that "State law . . . allow[s] the City to tax Comcast's data transmission activities as a 'telephone business.'" 136 Wn. App. at 180 ¶¶ 20, 21.

The Court of Appeals misread the ETA. The issue the Department of Revenue addressed in the ETA was whether the 2004 amendment of the ITFA prohibited the State from continuing to tax services "used to connect an ISP to the Internet or to ISP customer locations" as the State had taxed those services in the past. ETA, 1. The ETA noted that "Washington has traditionally taxed the sale of these network telephone services to a consumer under the retailing classification of the business and occupation tax (B&O) tax and required the seller to collect retail sales tax."<sup>11</sup> *Id.* The

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<sup>11</sup> The State retail B&O tax rate is 0.471% and the State service B&O rate is 1.5%. *See* RCW 82.04.250(1), 82.04.290(2). If a sale is a retail sale, the seller must also charge the customer a retail sales tax. In Seattle, the combined retail sales tax rate is 8.9%. *See*

Department concluded that the State could apply retail B&O tax to telephone services under the ITFA grandfather clause because the subsection of RCW 84.04.065(2) that permitted the State to tax revenues from “the provision of transmission to and from the site of an internet provider via a local telephone network” at telephone tax rates was imposed and enforced prior to October 1, 1998. ETA, 2.

The ETA endorsed telephone tax rates *only* for services that amount to “the provision of transmission to and from the site of an internet provider.” *Id.* The Court of Appeals incorrectly read the ETA as supporting its view that the definition of “network telephone service” in the 1997 State act includes *all* of “Comcast’s data transmission activities.” 136 Wn. App. at 178 ¶ 19, 180 ¶¶ 20, 21.

As shown above, however, Comcast’s Internet services do not include “the provision of transmission to and from the site of an internet provider.” Nothing in the ETA says the State may collect *retail* B&O taxes on Comcast’s Internet service revenues. The Department of Revenue itself confirmed this when it issued audit reports in October 2007 regarding each of the petitioners. In those audit reports, the Department recognized that petitioners are “Internet service providers,” confirmed that

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[http://dor.wa.gov/Docs/Pubs/SpecialNotices/2007/sn\\_07\\_KingCoTransporationTax.pdf](http://dor.wa.gov/Docs/Pubs/SpecialNotices/2007/sn_07_KingCoTransporationTax.pdf). Thus if the *retail* B&O and retail sales taxes that the Department stated it “traditionally” imposed on “network telephone services” were also applied to revenues from cable Internet services rather than *service* B&O taxes, it would significantly increase the total taxes collected from consumers.

they sell “Internet services” to subscribers, and found that petitioners’ Internet subscription fees are subject to the *service* B&O tax, not the retail B&O tax.<sup>12</sup> Although the ETA opined that some telecommunications services amount to “the provision of transmission to and from the site of an internet provider” and may be taxed at the retail B&O rate, when the Department *actually* examined the *petitioners’* Internet services, it determined that their revenues should be taxed at the *service* B&O rate. The Court of Appeals misinterpreted the ETA; Comcast’s Internet revenues should not be taxed at telephone service rates.

By misapplying the definition of “network telephone service,” the Court of Appeals would approve the City’s practice of taxing Comcast at the telephone tax rate of 6% while the City taxes “mere Internet service providers, such as Speakeasy” at the 0.415% B&O service tax rate. 136 Wn. App. at 187 ¶ 36. The Court of Appeals’ interpretation of the 1997 State act results in “mere” dial-up ISPs being taxed at a lower rate than emerging cable technology, in direct contradiction of the purposes stated in section 1 of that act. The Court should reverse the Court of Appeals’ decision so that the act will serve the Legislature’s intent.

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<sup>12</sup> Comcast’s has filed a concurrent motion asking that the Court supplement the record and take judicial notice of the Department of Revenue’s audit reports. See pp. 1-2 of the Community Telecable audit report; pp. 1, 3 of the Comcast of Washington I report; and pp. 1, 3 of the Comcast of Washington IV report.

**D. The Court of Appeals Erred by Holding that the City May Tax Interstate Services.**

In 2002, the FCC held that cable modem Internet service is an “*interstate* information service.” 17 FCC Rcd. at 4802 ¶ 7, 4848 ¶ 96 (emphasis added).<sup>13</sup> Comcast argued below that RCW 35.21.714 prohibits the City from imposing its telephone utility tax on Comcast’s Internet services revenue because that statute prohibits cities from imposing such taxes on interstate service. The court below disagreed, “holding that the statute merely ‘requires cities to give a deduction for the portion of network telephone service that represents a *charge to another telecommunications company* for interstate services.’” *Qwest*, 161 Wn.2d at 364-65 ¶ 23 (quoting *Community Telecable*, 136 Wn. App. at 182) (italics in original). After reviewing the statute’s legislative history,<sup>14</sup> this Court disapproved of the Court of Appeals’ interpretation of the statute, holding that it “precludes city taxation of charges for interstate service *regardless* of whether those charges are to another telecommunications company.” 161 Wn.2d at 368 ¶ 30 (italics in original).

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<sup>13</sup> The FCC asserted jurisdiction under 47 U.S.C. § 152(a) based on the interstate and foreign character of the communications involved in Internet service. *See also Brand X*, 545 U.S. at 976, 1002 (acknowledging FCC jurisdiction). The FCC’s holding is consistent with the factual record here. Undisputed facts show that Comcast’s email servers, domain name servers, and provisioning servers have always been located outside the State of Washington. CP 35-36, ¶¶ 5, 7; CP 31-33, ¶¶ 3, 5, 8; CP 913, ¶ 22.

<sup>14</sup> This Court noted in *Qwest* that the only difference between RCW 35.21.714(1) and RCW 35A.82.060, the statute at issue in the *Qwest*, was that the former applies to noncode cities whereas the latter applies to code cities. *Qwest*, 161 Wn.2d at 363 n.12. “[T]he statutes share identical legislative history.” *Id.*

For the same reasons that this Court in *Qwest* disapproved of the Court of Appeals' holding in *Community Telecable*, the Court should now reverse that holding and the Court of Appeals' decision. The FCC's holding that cable Internet service is an interstate service leads directly to the conclusion that Seattle may not tax Comcast's Internet service. *Qwest*, 161 Wn.2d at 369 ¶ 33 ("whether a charge is for interstate or intrastate service is a matter of law"). Given that RCW 35.21.714(1), properly interpreted, prohibits city telephone taxation of interstate services, the Court of Appeals' decision should be reversed.<sup>15</sup>

#### V. Conclusion

Comcast asks the Court to reverse the Court of Appeals' decision and to reinstate the order granting summary judgment to Comcast.

Respectfully submitted,

Davis Wright Tremaine LLP  
Attorneys for Comcast

Dated: November 30, 2007

By



Randy Gainer, WSBA No. 11823  
Dirk Giseburt, WSBA No. 13949

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<sup>15</sup> The City has wrongly contended that this Court should not reach this issue because Comcast allegedly did not raise it below or support it with citation to authority. Answer, 19. Comcast raised the issue in its summary judgment motion, CP 139 n.6, in its brief to the Court of Appeals, 15 n.2, and in its petition to this Court, each time citing RCW 35.21.714. Citation to statutory authority is obviously citation to authority. Further, this Court may affirm the trial court's entry of summary judgment on any appropriate basis. *See, e.g., Seattle v. McCready*, 123 Wn.2d 260, 269, 868 P.2d 134, 138 (1994); *Nast v. Michels*, 107 Wn.2d 300, 308, 730 P.2d 54, 59 (1986).

**Certificate of Service**

I hereby certify that on this 30<sup>th</sup> day of November, 2007, I caused to be served by first class mail, postage prepaid, a true and correct copy of the Petitioners' Supplemental Brief filed in connection with the above-referenced matter upon the following counsel of record at the following addresses:

Kent C. Meyer  
600 Fourth Avenue, Fourth Floor  
P.O. Box 94769  
Seattle, WA 98124-4769

Robert L. Mahon  
Perkins Coie LLP  
1201 Third Avenue, Suite #4800  
Seattle, WA 98101-3099

Jon Brian Davis  
Sutherland, Asbill & Brennan, LLP  
1275 Pennsylvania Avenue, NW  
Washington, D.C. 20004-2415

A copy of the above-referenced document was also sent by first-class mail, postage prepaid to the following:

The Honorable Rob McKenna  
Attorney General of the State of Washington  
1125 Washington Street S.E.  
P. O. Box 40100  
Olympia, WA 98504-0100

Dated this 30<sup>th</sup> day of November, 2007.

  
Deborah Linkowski

## APPENDIX A

## APPENDIX A

**Selected Sections of Internet Tax Freedom Act**  
**(Pub. L. 105-277, Div. C, Title XI,**  
**§§ 1100-1104, 112 Stat. 2681-719 (1998)),**  
**As amended by Pub. L. 107-75, § 2, 115 Stat. 708 (2001),**  
**Codified at 47 U.S.C. § 151 note (2003)**

### **Section 1101. Moratorium.**

**(a) Moratorium.** — No State or political subdivision thereof may impose any of the following taxes during the period beginning October 1, 1998, and ending November 1, 2003 —

- (1) taxes on Internet access, unless such tax was generally imposed and actually enforced prior to October 1, 1998; and
- (2) multiple or discriminatory taxes on electronic commerce.

....

**(d) Definition of generally imposed and actually enforced.** — For purposes of this section, a tax has been generally imposed and actually enforced prior to October 1, 1998, if, before that date, the tax was authorized by statute and either—

- (1) a provider of Internet access services had a reasonable opportunity to know by virtue of a rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that such agency has interpreted and applied such tax to Internet access services; or
- (2) a State or political subdivision thereof generally collected such tax on charges for Internet access.

### **Section 1104. Definitions.**

For the purposes of this title:

....

**(2) Discriminatory tax.** — The term 'discriminatory tax' means —

- (A) any tax imposed by a State or political subdivision thereof on electronic commerce that —
  - (i) is not generally imposed and legally collectible by such State or such political subdivision on transactions involving similar

property, goods, services, or information accomplished through other means;

(ii) is not generally imposed and legally collectible at the same rate by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means, unless the rate is lower as part of a phase-out of the tax over not more than a 5-year period;

(iii) imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or information accomplished through other means;

(iv) establishes a classification of Internet access service providers or online service providers for purposes of establishing a higher tax rate to be imposed on such providers than the tax rate generally applied to providers of similar information services delivered through other means; or

(B) any tax imposed by a State or political subdivision thereof, if —

(i) except with respect to a tax (on Internet access) that was generally imposed and actually enforced prior to October 1, 1998, the sole ability to access a site on a remote seller's out-of-State computer server is considered a factor in determining a remote seller's tax collection obligation; or

(ii) a provider of Internet access service or online services is deemed to be the agent of a remote seller for determining tax collection obligations solely as a result of —

(I) the display of a remote seller's information or content on the out-of-State computer server of a provider of Internet access service or online services; or

(II) the processing of orders through the out-of-State computer server of a provider of Internet access service or online services.

**(3) Electronic commerce.** — The term 'electronic commerce' means any transaction conducted over the Internet or through Internet access, comprising the sale, lease, license, offer, or delivery of property, goods, services, or information, whether or not for consideration, and includes the provision of Internet access.

**(4) Internet.** — The term 'Internet' means collectively the myriad of computer and telecommunications facilities, including equipment and

operating software, which comprise the interconnected world-wide network of networks that employ the Transmission Control Protocol/Internet Protocol, or any predecessor or successor protocols to such protocol, to communicate information of all kinds by wire or radio.

**(5) Internet access.** — 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 telecommunications services.

....

**(9) Telecommunications service.** — The term 'telecommunications service' has the meaning given such term in section 3(46) of the Communications Act of 1934 (47 U.S.C. 153(46)) and includes communications services (as defined in section 4251 of the Internal Revenue Code of 1986).

## APPENDIX B

## APPENDIX B

### Selected Sections of Internet Tax Freedom Act (Pub. L. 105-277, Div. C, Title XI, §§ 1100-1104, 112 Stat. 2681-719 (1998))

### As amended by Internet Tax Nondiscrimination Act (Pub. L. 108-435, 118 Stat. 2615 (2004)) Codified at 47 U.S.C. § 151 note (2005)

#### **Section 1101. Moratorium.**

**(a) Moratorium.** — No State or political subdivision thereof may impose any of the following taxes during the period beginning November 1, 2003, and ending November 1, 2007:

- (1) Taxes on Internet access.
- (2) Multiple or discriminatory taxes on electronic commerce.

#### **Section 1104. Grandfathering of States that Tax Internet Access.**

**(a) Pre-October 1998 Taxes.** —

(1) In general. — Section 1101(a) does not apply to a tax on Internet access that was generally imposed and actually enforced prior to October 1, 1998, if, before that date —

- (A) the tax was authorized by statute; and
- (B) either —

(i) a provider of Internet access services had a reasonable opportunity to know, by virtue of a rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that such agency has interpreted and applied such tax to Internet access services; or

(ii) a State or political subdivision thereof generally collected such tax on charges for Internet access.

(2) Termination. —

(A) In general. — Except as provided in subparagraph (B), this subsection shall not apply after November 1, 2007.

(B) State telecommunications service tax. —

(i) Date for termination. — This subsection shall not apply after November 1, 2006, with respect to a State telecommunications service tax described in clause (ii).

(ii) Description of tax. — A State telecommunications service tax referred to in subclause (i) is a State tax —

(I) enacted by State law on or after October 1, 1991, and imposing a tax on telecommunications service; and

(II) applied to Internet access through administrative code or regulation issued on or after December 1, 2002.

**(b) Pre-November 2003 Taxes. —**

(1) In general. — Section 1101(a) does not apply to a tax on Internet access that was generally imposed and actually enforced as of November 1, 2003, if, as of that date, the tax was authorized by statute and —

(A) a provider of Internet access services had a reasonable opportunity to know by virtue of a public rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that such agency has interpreted and applied such tax to Internet access services; and

(B) a State or political subdivision thereof generally collected such tax on charges for Internet access.

(2) Termination. — This subsection shall not apply after November 1, 2005.

**Section 1105. Definitions.**

For the purposes of this title:

....

**(2) Discriminatory tax. —** The term 'discriminatory tax' means —

(A) any tax imposed by a State or political subdivision thereof on electronic commerce that —

(i) is not generally imposed and legally collectible by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means;

(ii) is not generally imposed and legally collectible at the same rate by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means, unless the rate is lower as part of a phase-out of the tax over not more than a 5-year period;

(iii) imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or information accomplished through other means;

(iv) establishes a classification of Internet access service providers or online service providers for purposes of establishing a higher tax rate to be imposed on such providers than the tax rate generally applied to providers of similar information services delivered through other means; or

(B) any tax imposed by a State or political subdivision thereof, if —

(i) the sole ability to access a site on a remote seller's out-of-State computer server is considered a factor in determining a remote seller's tax collection obligation; or

(ii) a provider of Internet access service or online services is deemed to be the agent of a remote seller for determining tax collection obligations solely as a result of —

(I) the display of a remote seller's information or content on the out-of-State computer server of a provider of Internet access service or online services; or

(II) the processing of orders through the out-of-State computer server of a provider of Internet access service or online services.

**(3) Electronic commerce.** — The term 'electronic commerce' means any transaction conducted over the Internet or through Internet access, comprising the sale, lease, license, offer, or delivery of property, goods, services, or information, whether or not for consideration, and includes the provision of Internet access.

**(4) Internet.** — The term 'Internet' means collectively the myriad of computer and telecommunications facilities, including equipment and operating software, which comprise the interconnected world-wide

network of networks that employ the Transmission Control Protocol/Internet Protocol, or any predecessor or successor protocols to such protocol, to communicate information of all kinds by wire or radio.

**(5) Internet access.** — 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. The term 'Internet access' does not include telecommunications services, except to the extent such services are purchased, used, or sold by a provider of Internet access to provide Internet access.

....

**(9) Telecommunications service.** — The term 'telecommunications service' has the meaning given such term in section 3(46) of the Communications Act of 1934 (47 U.S.C. 153(46)) and includes communications services (as defined in section 4251 of the Internal Revenue Code of 1986).

## APPENDIX C

## APPENDIX C

**Selected Sections of Internet Tax Freedom Act  
(Pub. L. 105-277, Div. C, Title XI,  
§§ 1100-1104, 112 Stat. 2681-719 (1998))**

**As amended by Internet Tax Nondiscrimination Act  
(Pub. L. 108-435, 118 Stat. 2615 (2004))**

**and by Internet Tax Freedom Act Amendments Act of 2007  
(Pub. L. 110-108, 121 Stat. 1024 (2007))  
Codified at 47 U.S.C.A. § 151 note (2007)**

### **Section 1101. Moratorium.**

**(a) Moratorium.** — No State or political subdivision thereof shall impose any of the following taxes during the period beginning November 1, 2003, and ending November 1, 2014:

- (1) Taxes on Internet access.
- (2) Multiple or discriminatory taxes on electronic commerce.

**(b) Preservation of state and local taxing authority.** — Except as provided in this section, nothing in this title [this note] shall be construed to modify, impair, or supersede, or authorize the modification, impairment, or superseding of, any State or local law pertaining to taxation that is otherwise permissible by or under the Constitution of the United States or other Federal law and in effect on the date of enactment of this Act [Oct. 21, 1998].

**(c) Liabilities and pending cases.** — Nothing in this title [this note] affects liability for taxes accrued and enforced before the date of enactment of this Act [Oct. 21, 1998], nor does this title [this note] affect ongoing litigation relating to such taxes.

.....

### **Section 1104. Grandfathering of states that tax Internet access**

**(a) Pre-October 1998 taxes.** —

- (1) In general. — Section 1101(a) [of this note] does not apply to a tax on Internet access that was generally imposed and actually enforced prior to October 1, 1998, if, before that date —

(A) the tax was authorized by statute; and

(B) Either —

(i) a provider of Internet access services had a reasonable opportunity to know, by virtue of a rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that such agency has interpreted and applied such tax to Internet access services; or

(ii) a State or political subdivision thereof generally collected such tax on charges for Internet access.

**(2) Termination. —**

(A) In general. — Except as provided in subparagraph (B), this subsection shall not apply after November 1, 2014.

(B) State telecommunications service tax. —

(i) Date for termination. — This subsection shall not apply after November 1, 2006, with respect to a State telecommunications service tax described in clause (ii).

(ii) Description of tax. — A State telecommunications service tax referred to in subclause (i) is a State tax —

(I) enacted by State law on or after October 1, 1991, and imposing a tax on telecommunications service; and

(II) applied to Internet access through administrative code or regulation issued on or after December 1, 2002.

**(3) Exception. —** Paragraphs (1) and (2) shall not apply to any State that has, more than 24 months prior to the date of enactment of this paragraph [Oct. 31, 2007], enacted legislation to repeal the State's taxes on Internet access or issued a rule or other proclamation made by the appropriate agency of the State that such State agency has decided to no longer apply such tax to Internet access.

**(b) Pre-November 2003 taxes. —**

**(1) In general. —** Section 1101(a) [of this note] does not apply to a tax on Internet access that was generally imposed and actually enforced as of November 1, 2003, if, as of that date, the tax was authorized by statute and —

(A) a provider of Internet access services had a reasonable opportunity to know by virtue of a public rule or other public proclamation made by the appropriate administrative agency of the State or political subdivision thereof, that such agency has interpreted and applied such tax to Internet access services; and

(B) a State or political subdivision thereof generally collected such tax on charges for Internet access.

(2) Termination. — This subsection shall not apply after November 1, 2005.

**(c) Application of definition. —**

(1) In general. — Effective as of November 1, 2003 —

(A) for purposes of subsection (a), the term ‘Internet access’ shall have the meaning given such term by section 1104(5) of this Act [of this note], as enacted on October 21, 1998; and

(B) for purposes of subsection (b), the term ‘Internet access’ shall have the meaning given such term by section 1104(5) of this Act [of this note] as enacted on October 21, 1998, and amended by section 2(c) of the Internet Tax Nondiscrimination Act (Public Law 108-435).

(2) Exceptions. — Paragraph (1) shall not apply until June 30, 2008, to a tax on Internet access that is —

(A) generally imposed and actually enforced on telecommunications service purchased, used, or sold by a provider of Internet access, but only if the appropriate administrative agency of a State or political subdivision thereof issued a public ruling prior to July 1, 2007, that applied such tax to such service in a manner that is inconsistent with paragraph (1); or

(B) the subject of litigation instituted in a judicial court of competent jurisdiction prior to July 1, 2007, in which a State or political subdivision is seeking to enforce, in a manner that is inconsistent with paragraph (1), such tax on telecommunications service purchased, used, or sold by a provider of Internet access.

(3) No inference. — No inference of legislative construction shall be drawn from this subsection or the amendments to section 1105(5) [of this note] made by the Internet Tax Freedom Act Amendments Act of 2007 [Pub.L. 110-108, Oct. 31, 2007, 121 Stat. 1024] for any period

prior to June 30, 2008, with respect to any tax subject to the exceptions described in subparagraphs (A) and (B) of paragraph (2).

### Section 1105. Definitions

For the purposes of this title [this note]:

**(1) Bit tax.** — The term ‘bit tax’ means any tax on electronic commerce expressly imposed on or measured by the volume of digital information transmitted electronically, or the volume of digital information per unit of time transmitted electronically, but does not include taxes imposed on the provision of telecommunications.

**(2) Discriminatory tax.** — The term ‘discriminatory tax’ means —

(A) any tax imposed by a State or political subdivision thereof on electronic commerce that —

(i) is not generally imposed and legally collectible by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means;

(ii) is not generally imposed and legally collectible at the same rate by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means, unless the rate is lower as part of a phase-out of the tax over not more than a 5-year period;

(iii) imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or information accomplished through other means;

(iv) establishes a classification of Internet access service providers or online service providers for purposes of establishing a higher tax rate to be imposed on such providers than the tax rate generally applied to providers of similar information services delivered through other means;  
or

(B) any tax imposed by a State or political subdivision thereof, if —

(i) the sole ability to access a site on a remote seller’s out-of-State computer server is considered a factor in determining a remote seller’s tax collection obligation; or

(ii) a provider of Internet access service or online services is deemed to be the agent of a remote seller for determining tax collection obligations solely as a result of —

(I) the display of a remote seller's information or content on the out-of-State computer server of a provider of Internet access service or online services; or

(II) the processing of orders through the out-of-State computer server of a provider of Internet access service or online services.

**(3) Electronic commerce.** — The term 'electronic commerce' means any transaction conducted over the Internet or through Internet access, comprising the sale, lease, license, offer, or delivery of property, goods, services, or information, whether or not for consideration, and includes the provision of Internet access.

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

**(5) Internet access.** — The term 'Internet access' —

(A) means a service that enables users to connect to the Internet to access content, information, or other services offered over the Internet;

(B) includes the purchase, use or sale of telecommunications by a provider of a service described in subparagraph (A) to the extent such telecommunications are purchased, used or sold —

(i) to provide such service; or

(ii) to otherwise enable users to access content, information or other services offered over the Internet;

(C) includes services that are incidental to the provision of the service described in subparagraph (A) when furnished to users as part of such service, such as a home page, electronic mail and instant messaging (including voice- and video-capable electronic

mail and instant messaging), video clips, and personal electronic storage capacity;

(D) does not include voice, audio or video programming, or other products and services (except services described in subparagraph (A), (B), (C), or (E)) that utilize Internet protocol or any successor protocol and for which there is a charge, regardless of whether such charge is separately stated or aggregated with the charge for services described in subparagraph (A), (B), (C), or (E); and

(E) includes a homepage, electronic mail and instant messaging (including voice- and video-capable electronic mail and instant messaging), video clips, and personal electronic storage capacity, that are provided independently or not packaged with Internet access.

**(6) Multiple tax. —**

(A) In general. — The term ‘multiple tax’ means any tax that is imposed by one State or political subdivision thereof on the same or essentially the same electronic commerce that is also subject to another tax imposed by another State or political subdivision thereof (whether or not at the same rate or on the same basis), without a credit (for example, a resale exemption certificate) for taxes paid in other jurisdictions.

(B) Exception. — Such term shall not include a sales or use tax imposed by a State and 1 or more political subdivisions thereof on the same electronic commerce or a tax on persons engaged in electronic commerce which also may have been subject to a sales or use tax thereon.

(C) Sales or use tax. — For purposes of subparagraph (B), the term ‘sales or use tax’ means a tax that is imposed on or incident to the sale, purchase, storage, consumption, distribution, or other use of tangible personal property or services as may be defined by laws imposing such tax and which is measured by the amount of the sales price or other charge for such property or service.

**(7) State. —** The term ‘State’ means any of the several States, the District of Columbia, or any commonwealth, territory, or possession of the United States.

**(8) Tax. —**

(A) In general. — The term ‘tax’ means —

(i) any charge imposed by any governmental entity for the purpose of generating revenues for governmental purposes, and is not a fee imposed for a specific privilege, service, or benefit conferred; or

(ii) the imposition on a seller of an obligation to collect and to remit to a governmental entity any sales or use tax imposed on a buyer by a governmental entity.

(B) Exception. — Such term does not include any franchise fee or similar fee imposed by a State or local franchising authority, pursuant to section 622 or 653 of the Communications Act of 1934 (47 U.S.C. 542, 573), or any other fee related to obligations or telecommunications carriers under the Communications Act of 1934 (47 U.S.C. 151 et seq.).

**(9) Telecommunications. —** The term ‘telecommunications’ means ‘telecommunications’ as such term is defined in section 3(43) of the Communications Act of 1934 (47 U.S.C. 153(43)) and ‘telecommunications service’ as such term is defined in section 3(46) of such Act (47 U.S.C. 153(46)), and includes communications services (as defined in section 4251 of the Internal Revenue Code of 1986 (26 U.S.C. 4251)).

**(10) Tax on Internet access. —**

(A) In general. — The term ‘tax on Internet access’ means a tax on Internet access, regardless of whether such tax is imposed on a provider of Internet access or a buyer of Internet access and regardless of the terminology used to describe the tax.

(B) General exception. — The term ‘tax on Internet access’ does not include a tax levied upon or measured by net income, capital stock, net worth, or property value.

(C) Specific exception. —

(i) Specified taxes. — Effective November 1, 2007, the term ‘tax on Internet access’ also does not include a State tax expressly levied on commercial activity, modified gross receipts, taxable margin, or gross income of the business, by a State law specifically using one of the foregoing terms, that —

(I) was enacted after June 20, 2005, and before November 1, 2007 (or, in the case of a State business and occupation tax, was enacted after January 1, 1932, and before January 1, 1936);

(II) replaced, in whole or in part, a modified value-added tax or a tax levied upon or measured by net income, capital stock, or net worth (or, is a State business and occupation tax that was enacted after January 1, 1932 and before January 1, 1936);

(III) is imposed on a broad range of business activity; and

(IV) is not discriminatory in its application to providers of communication services, Internet access, or telecommunications.

(ii) Modifications. — Nothing in this subparagraph shall be construed as a limitation on a State's ability to make modifications to a tax covered by clause (i) of this subparagraph after November 1, 2007, as long as the modifications do not substantially narrow the range of business activities on which the tax is imposed or otherwise disqualify the tax under clause (i).

(iii) No inference. — No inference of legislative construction shall be drawn from this subparagraph regarding the application of subparagraph (A) or (B) to any tax described in clause (i) for periods prior to November 1, 2007.

#### **Sec. 1106. Accounting rule**

**(a) In general.** — If charges for Internet access are aggregated with and not separately stated from charges for telecommunications or other charges that are subject to taxation, then the charges for Internet access may be subject to taxation unless the Internet access provider can reasonably identify the charges for Internet access from its books and records kept in the regular course of business.

**(b) Definitions.** — In this section:

(1) Charges for internet access. — The term 'charges for Internet access' means all charges for Internet access as defined in section 1105(5) [of this note].

(2) Charges for telecommunications. — The term ‘charges for telecommunications’ means all charges for telecommunications, except to the extent such telecommunications are purchased, used, or sold by a provider of Internet access to provide Internet access or to otherwise enable users to access content, information or other services offered over the Internet.

## APPENDIX D

## APPENDIX D

### WASHINGTON LAWS, 1997

#### CHAPTER 304

[Substitute Senate Bill 5763]

#### PROHIBITING TAXATION OF INTERNET SERVICE PROVIDERS AS TELEPHONE SERVICES PROVIDERS

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

Be it enacted by the Legislature of the State of Washington:

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

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

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

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

(1) "Selected business services" means:

(a) Stenographic, secretarial, and clerical services.

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

(c) Data processing services, including but not limited to word processing, data entry, data retrieval, data search, information compilation, payroll processing, business accounts processing, data production, and other computerized data and information storage or manipulation. Data processing services also includes the use of a computer or computer time for data processing whether the processing is

performed by the provider of the computer or by the purchaser or other beneficiary of the service.

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

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

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

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

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

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

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

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

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

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

(l) Aerial and land surveying, geological consulting, and real estate appraising.

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

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

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

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

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

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

(f) Financial services provided by a financial institution. The term "financial institution" means a corporation, partnership, or other business organization chartered under Title 30, 31, 32, or 33 RCW, or under the National Bank Act, as amended, the Homeowners Loan Act, as amended, or the Federal Credit Union Act, as amended, or a holding company of any such business organization that is subject to the Bank Holding Company Act, as amended, or the Homeowners Loan Act, as amended, or a subsidiary or affiliate wholly owned or controlled by one or more financial institutions, as well as a lender approved by the United States secretary of housing and urban development for participation in any mortgage insurance program under the National Housing Act, as amended. The term

"financial services" means those activities authorized by the laws cited in this subsection (2)(f) and includes services such as mortgage servicing, contract collection servicing, finance leasing, and services provided in a fiduciary capacity to a trust or estate.

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

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

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

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

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

(1) "Competitive telephone service" means the providing by any person of telecommunications equipment or apparatus, or service related to that equipment or apparatus such as repair or maintenance service, if the equipment or apparatus is of a type which can be provided by persons that are not subject to regulation as telephone companies under Title 80 RCW and for which a separate charge is made.

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

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

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

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

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

Passed the Senate April 19, 1997.

Passed the House April 10, 1997.

Approved by the Governor May 9, 1997.

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