

Cite as Det. No. 01-036, 21 WTD 13 (2002)

BEFORE THE APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition For Correction of	)	<u>D E T E R M I N A T I O N</u>
Assessment and Refund of	)	
	)	No. 01-036
...	)	
	)	Registration No. . . .
	)	FY . . . /Audit No. . . .
	)	Docket No. . . .

- [1] RCW 82.04.280: RADIO AND TELEVISION BROADCASTING -- INTERNET. Providing access to pre-recorded programs over the Internet does not constitute radio or television broadcasting because the signal is not delivered over the airwaves.
- [2] RCW 82.04.297: CLARIFYING ACT – DEFINITION OF INTERNET SERVICES. When the legislature adopts a clarifying act, the act will apply retroactively. RCW 82.04.297 is a clarifying act, therefore the definition of Internet Services contained therein, applies retroactively.
- [3] RCW 82.04.297: AMBIGUOUS STATUTE –LEGISLATIVE INTENT. RCW 82.04.297’s definition of Internet Services is ambiguous in that it can be read to have two conflicting meanings. The legislative history shows that the legislature intended one specific meaning. Specifically, Internet Services as defined in RCW 82.04.297 include only those persons who provide access to the Internet, not those who maintain sites on the Internet.
- [4] Wa. Const., art. 2 § 19, RCW 82.04.297: SUBJECT OF BILL. The subject of a bill may not be broader than its title. The title of SB5763, which was codified as RCW 82.04.297, prohibited treating internet service providers as network telephone service providers. Because persons who maintain homepages but do not provide access to the Internet could not have been construed to have provided network telephone services, they cannot be construed to provide Internet Services.
- [5] RCW 82.04.297: DEFINITION OF INTERNET SERVICES – CONTEMPORANEOUS CONSTRUCTION. The purpose of RCW 82.04.297

was to ratify the department's treatment of Internet Services. The Department's public statement that RCW 82.04.297 applied to Internet Services Providers is entitled to significant weight.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

#### NATURE OF ACTION:

An advertising agency places clients' audio programs with radio stations. Additionally, the advertising agency maintains a Homepage accessible through the Internet where it makes some of the same audio programs available to the public. The advertising agency protests the business and occupation tax assessed under the classifications of "selected business services" (before July 1, 1998) and "services and other activities" (after June 30, 1998) on receipts from customers for placing their audio programs on the Taxpayer's Homepage.<sup>1</sup>

#### FACTS:

Coffman, A.L.J. -- The Taxpayer is an advertising agency. It works primarily for non-profit organizations. It provides traditional solicitation services to the non-profit organizations such as developing mailers, which are sent to previous contributors. In addition, many of the Taxpayer's clients have audio programs (usually 30 minutes in duration) that the Taxpayer places with radio stations to broadcast. The Taxpayer retains 15% of the fee paid by the client and remits the balance (85%) to the radio station as compensation for broadcasting the audio program. There is no dispute that this income was subject to the selected business services ("SBS")<sup>2</sup> or service and other activities ("service") business and occupation (B&O) tax classifications

In 1996, the Taxpayer developed its Internet Homepage<sup>3</sup>. Although the Homepage is available through the Internet, the taxpayer does not provide customers with direct access to the Internet. Any person, once connected to the Internet, can go to the taxpayer's Homepage and gain free access to some of the same radio programs that the taxpayer places with radio stations for broadcast. The Taxpayer charges its clients a fixed fee per month for placing the client's audio programs on its Homepage.

The Audit Division of the Department of Revenue (Department) reviewed the Taxpayer's books and records for the period January 1, 1997 through June 30, 1999 (the audit period). As a result of this review, the Audit Division reclassified the Taxpayer's receipts from placing audio programs on the Homepage. The Taxpayer had reported these receipts under the "radio and television broadcasting" B&O tax classification. However, the Audit Division, believing these

<sup>1</sup> Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

<sup>2</sup> "SBS" included several types of services that were formerly taxable under the "service" classification. The "SBS" classification was repealed effective July 1, 1998. From July 1, 1998 to the present, services that were taxable under the "SBS" classification are taxable under the "services" classification.

<sup>3</sup> The Taxpayer refers to the Homepage as the . . . .

receipts were for advertising services, assessed tax under the “SBS” and “service” B&O tax classifications and gave the Taxpayer a credit for the tax paid under “radio and television broadcasting.” The Taxpayer appealed.

The Audit Division’s response to the Taxpayer’s petition appealing the tax assessment states:

After reviewing the appeal letter filed by [the Taxpayer’s representative], the auditor’s original understanding of the [Homepage] revenues did not agree with the facts stated in the appeal letter. I telephoned [the Taxpayer’s representative] for clarification. Although I still agree with the reclassification of income as contained in the audit, my explanation for the reclassification of income has changed.

Letter from Audit Supervisor dated October 3, 2000.

Thus, the Audit Division originally treated the Homepage income as advertising income. After receiving the clarification from the Taxpayer’s representative, the Audit Division states the income is from providing Internet Services.

#### ISSUE:

Whether providing a Homepage, accessible through the Internet, where anyone can listen to audio programs is taxable under the “radio and television broadcasting” or SBS and service B&O tax classification when those same audio programs are broadcast by radio stations.

#### DISCUSSION:

##### 1. **Radio and Television Broadcasting.**

The Taxpayer claims it:

was operating an “on-line radio station” and generated revenues that were of the same type and nature of revenues generated by conventional radio stations for the same purpose -- selling commercial (or infomercial) time and that such revenue should therefore be reported consistent with that of a conventional radio station.

Letter dated February 2, 2001, page 2.

The Taxpayer’s argument is similar to the argument made by the taxpayer in Det. No. 92-363, 12 WTD 519 (1992). In Det. No 92-363, the taxpayer provided audio broadcasts to its customers either through satellite transmissions or “over side carrier authority (SCA), which is a sideband of an FM broadcast.” In either event, only customers of the Taxpayer were able to receive the signal. The Taxpayer in Det. No. 92-363 appears to have performed a service that was closer to traditional radio and television broadcasting than in this appeal. We found the service in Det. No 92-363 was not radio and television broadcasting stating:

Although the taxpayer contends that it should be taxed in the same manner as commercial ... broadcasting stations on the grounds that it is performing the same business activity, we disagree. The taxpayer's activity is clearly distinguishable from that of commercial ... broadcasting stations. Commercial stations broadcast their signals over the public airwaves of a specified region and are intended for reception by an unrestricted number of receivers. In this regard, they perform a public service by disseminating ... programming to all available [receivers] without charges or fees. Virtually all revenue is derived from the sale of advertising which is included in the freely disseminated programming. In addition, the FCC requires each commercial station to perform certain public service functions such as providing airtime for public service announcements, equal time for opposing political views, and several other requirements and restrictions. The taxpayer has no such restrictions or requirements. ... We believe that the manner by which the signal is delivered to the clients, (i.e. via FM airwaves) to be only one of many factors to be considered when determining if a taxpayer is engaged in ... broadcasting. It is certainly not the controlling factor.

(Emphasis added.)

[1] The Taxpayer's Homepage is not subject to any FCC requirements. Further, the Taxpayer's gross receipts from its Homepage are not advertising revenues, but rather the gross receipts are for providing access to clients' audio programs. Finally, we note that under Det. No. 92-363, supra, the manner of delivery of the signal over the airwaves is a factor in determining whether a person is engaged in radio broadcasting. The Taxpayer does not broadcast the audio programs in the proper manner to be classified as radio and television broadcasting.

## 2. Internet Services.

[2] As it existed during the audit period, RCW 82.04.297(3)<sup>4</sup> defines Internet Services as:

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 was added to the law by chapter 304 Laws of 1997 (SB 5763). Section 1 of SB 5763 states: "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." [Emphasis added.] We find that SB 5763 was a clarifying act and applies retroactively. See Det. No. 98-193, 18 WTD 338 (1999).

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<sup>4</sup> RCW 82.04.297 was amended effective June 8, 2000 to delete reference to SBS.

[3] We must determine whether, under RCW 82.04.297, maintaining a homepage is an Internet service. We find that it is not for the following reasons.

First, we find that the language used in RCW 82.04.297 is ambiguous. The use of the disjunctive “or” in the first sentence can be read to mean if a person provides a service through the Internet and that service:

- (1) includes computer processing applications, or
- (2) provides the user with additional or restructured information, or
- (3) permits the user to interact with stored information,

then that person has provided an Internet service. However, the sentence could also be read to mean if a person provides a service that includes computer processing applications through the Internet and that service:

- (1) provides the user with additional or restructured information, or
- (2) permits the user to interact with stored information,

then that person has provided an Internet service. The latter interpretation is consistent with the legislative intent when it enacted RCW 82.04.297.

We note the 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. Thus, the City of Tacoma was attempting to collect taxes on fees paid to those businesses that provide access to the Internet through telephone lines at a rate significantly higher (6%) than charged for other services (0.2%). See House Bill Report on SSB 5763, as reported by House Committees on Energy and Utilities and Finance (House Report), page 5.

Both the House and Final Bill Reports state the bill was designed to address the activities of those companies that provide access to the Internet.<sup>5</sup> There is no discussion in the committee

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<sup>5</sup> Specifically, the House Report states:

Access to the Internet and Proprietary Networks. Some companies are in the business of providing access to the Internet via computers that are directly linked to the Internet by telecommunications facilities. Using a computer, modem, and software that allows access to the Internet, a customer dials a local or 800 telephone number to reach the access provider’s computer, which then connects the user’s computer to the Internet.

Other companies, often referred to as “on-line service providers,” provide access to a proprietary subscriber network, and may also provide access to the Internet.

Internet access and on-line service providers (collectively referred to as “access providers”) generally charge their customers subscription or usage fees.

reports of the bill's intent to reach anyone other than Internet (and on-line service) access providers. It was not intended to reach those who maintain homepages on the Internet.

[4] Second, under Washington law, the subject of a bill can not be broader than its title. Wa. Const., art. 2, § 19.

A title may be general or restrictive, that is, it may be either broad and comprehensive and cover all legislation germane to the general subject stated, or it may be one in which a particular part or branch of the subject is carved out and selected as the subject of the legislation. A restrictive title is not regarded as liberally as is a general one, and provisions of the bill which it does not fairly embrace cannot be given force.

Rourke v. Department of Labor and Ind., 41 Wn.2d 310, 312, 249 P.2d 236 (1952). (Internal citations omitted.)

In this case the title to SB 5763 was "AN ACT Relating to prohibiting the taxation of internet service providers as network telephone service providers." We find that legislative intent of the SB 5763 was to prohibit taxing businesses that provide access to the Internet as retailers or utilities. Thus, the title of SB 5763 is restrictive. Any interpretation of RCW 82.04.297 to include persons who maintain homepages, but do not provide access to the Internet through telephone services, would be beyond the scope of the title of SB 5763 and therefore unconstitutional as applied. Because the taxpayer does not provide access to the Internet to its customers, the taxpayer does not provide Internet Services as defined in RCW 82.04.297.

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Taxation. Since Internet access requires the use of telecommunication facilities, largely the telephone network, the issue has been raised of whether Internet access should be taxed as "network telephone services" or as a "business service."

...

Although telecommunications-like services may be a small component of Internet and on-line services, Internet and on-line services are not themselves telecommunications services.

Likewise, the Final Bill Report (Synopsis as Enacted) states that under SSB 5763:

Until July 1, 1999, cities and towns may not impose any new taxes or fees specific to Internet service providers, but may tax Internet service providers under generally applicable business taxes at a rate not to exceed the rate applied to a general service classification.

The provision of Internet services is classified as selected business service activity for the purposes of applying the business and occupation tax. . . .

Existing statutes are clarified to indicate that the provision of Internet services does not constitute network telephone service.

[5] Third, the Department stated in Tax Facts,<sup>6</sup> June 1997, immediately following the passage of SB 5763:

Taxation of Internet Service Providers — Substitute Senate Bill (SSB) 5763 (Chapter 304, Laws of 1997) provides that Internet service providers be taxed under the selected business services classification of the B&O tax until the services classification expires on July 1, 1998. Internet service providers will be taxed under the service and other activities classification of the B&O tax after July 1, 1998. Cities and towns are prohibited from imposing new taxes or fees specific to Internet service providers until July 1, 1999. This legislation confirms the way Internet service providers have been taxed in the past.

Generally, the contemporaneous construction of a statute by the administrative agency charged with enforcing it is given considerable weight. State v. Schoettler, 45 Wn.2d 367, 274 P.2d 852 (1954). As noted above, RCW 82.04.297 was intended to adopt the Department's previous practice concerning Internet service providers. Therefore, in this specific case, the Department's statement is entitled to significant weight.

### 3. Service and Other Activities Classification.

Because the taxpayer provides a service that is not specifically classified for B&O tax purposes, it is subject to the B&O under the Service classification. RCW 82.04.290(2). The Audit Division classified the taxpayer's business activity under the SBS classification for a portion of the audit period. Therefore we are remanding the file to the Audit Division for the purpose of issuing a post assessment adjustment reclassifying the taxpayer's revenue from making audio programs available through its Homepage to the service B&O tax classification.

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<sup>6</sup> Tax Facts is the Department's quarterly non-technical publication. It is intended to provide general information to taxpayers. Unless specifically noted, Tax Facts does not to address specific applications of the law. Taxpayers are encouraged to contact the Department, if they have specific questions.

**DECISION AND DISPOSITION:**

The Taxpayer's petition is granted, in part, and denied, in part. The file is remanded to the Audit Division for the purpose of issuing a post assessment adjustment consistent with this determination.

Dated this 3<sup>rd</sup> day of May, 2001.