National Cable & Telecommunications Association
25 Massachusetts Avenue, NW
Suite 100
Washington, DC 20001-1431
(202) 222-2300

James Assey
Executive Vice President
(202) 222-2519
(202) 222-2515 Fax
jassey@ncta.com

December 2, 2014

Mr. Jonathan Sallet
General Counsel
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: Open Internet, GN Dockets 14-28 and 10-127

Dear Mr. Sallet:

Following up on our meeting on October 29, 2014, I wanted to provide you with information regarding the potential state tax implications of a decision by the Commission to classify broadband service as a telecommunications carrier service subject to Title II of the Communications Act. As explained below, in addition to the significant federal implications – including the potential assessment of USF contributions and FCC regulatory fees – reclassification could subject cable operators and consumers (as well as other broadband service providers) to new and increased state and local taxes and fees. These tax and fee increases could increase the cost of providing broadband service and increase the prices that consumers pay for broadband, both of which run counter to the statutory objective of universal access to broadband for all Americans.

Overview

Many state and local governments impose higher or additional taxes on regulated industries like telecommunications or other utilities than on general businesses.[1] Historically, these industries were regulated monopolies and passed additional taxes on to consumers because they were not subject to much, if any, competition. While the competitive landscape has shifted and telecommunications companies now compete broadly with one another, state tax structures have lagged behind. Many states and local governments continue to impose - and many, in fact, have increased - taxes and fees on regulated utilities like telecommunications service providers.

[1.] *See, e.g.*, David Tuerck, Paul Bachman, Steven Titch, and John Rutledge, *Taxes and Fees on Communications Services*, Heartland Institute (2007); *2004 State Study and Report on Telecommunications Taxation*, Telecommunications Task Force of the Council On State Taxation (COST) (CCH 2004).

In contrast, most states currently tax broadband service providers in the same or similar manner as other general businesses. Reclassifying broadband service as a regulated telecommunications service may subject cable operators that provide broadband and their customers to materially higher taxes and fees, either because a statute specifically references the federal definitions or because a state tax authority interprets state law in a manner that follows the federal definitions. Moreover, reclassification may encourage other states to change their respective tax laws to achieve the same effect. As described below, cable operators and their customers could face increases with respect to three types of taxes and fees: property taxes; transaction-based taxes and fees; and income, franchise, and gross receipts taxes. The examples identified below are intended to be illustrative, not exhaustive.

Property Taxes

Several states "centrally assess" the property of telecommunications companies, utilities, and common carriers.[2] In contrast, local tax assessors typically assess broadband providers' property.[3] Centrally assessed taxpayers often pay tax on the value of their intangible property and often at a higher rate than locally assessed property.[4] Consequently, in almost all cases, central assessment leads to a significantly higher tax when compared to local assessment.

Reclassification may subject cable operators that provide broadband to onerous central assessment regimes in certain states. In Utah, for example, all property of public utilities, including those of telephone and telegraph corporations, must be assessed annually by the State Tax Commission.[5] In Louisiana, property used in the operation of telegraph and telephone companies is valued by the Louisiana Tax Commission, as opposed to general businesses that are subject to local valuation.[6]

Transaction-Based Taxes and Fees

Most states impose taxes and fees on the sale of telecommunications services that do not apply to the sale of broadband (Internet access) services.[7] Examples of these telecommunications taxes and fees include universal service fund fees – up to 8.5% on intrastate services – telecommunications service relay fees, emergency communications fees, public utility

---

2. *See, e.g.*, Me. Rev. Stat. Ann. tit. 36, §§ 457, 458.

3. *See, e.g.*, Me. Rev. Stat. Ann. tit. 36, §§ 502, 505, 457(1)(A).

4. *See Cable One, Inc. v. Arizona Dept. of Rev*, 304 P.3d 1098 (Ariz. Ct. App. 2013).

5. Utah Code Ann. § 59-2-201.

6. La. Rev. Stat. Ann. §§ 47:1851(M), 1854.

7. *E.g.*, Fla. Stat. Ann. § 202.12(1)(a), 203.01(1)(b), 202.19(2) (imposing the communications services tax at a combined rate up to 14.63%); Fla. Stat. Ann. § 212.05, 212.055 (imposing the general sales tax at a combined rate of 7.5%). Note, the distinction between telecommunications taxes and fees is not always readily apparent and has been the source of litigation. *See, e.g., Fulton County, Georgia v. T-Mobile, South, LLC d/b/a T-Mobile USA*, 699 SE2d 802 (Ga. App. 2010).

commission fees, and other fees unique to each state.[8] If the Commission were to regulate broadband service under Title II of the Communications Act, many of these state and local taxes and fees could apply to broadband services providers and consumers unless otherwise preempted by federal law.

Notwithstanding the Internet Tax Freedom Act's moratorium against most state taxes on Internet access service, states and localities, including several communities in Oregon and Colorado, have argued that the fees they apply were imposed for a "specific privilege, service or benefit conferred" and therefore do not fall within the definition of "tax" under the moratorium. Similarly, the California End-User Fee is imposed on all regulated telecommunications service providers based on their end-user intrastate service revenue.

Net Income, Franchise, and Gross Receipts Taxes

Classifying broadband service as a regulated telecommunications service may change the types of taxes paid by broadband providers as well as how taxes are "apportioned" (calculated and then divided among the states).[9] In New York, for example, a regulated utility, including a telecommunications company, is subject to tax under one set of rules if its predominant activity is a utility type service (Article 9 - gross receipts taxes) and another if it is not (Article 9-A - income/capital based tax).[10] A change to Title II regulation for broadband providers could result in the imposition of a vast array of new Article 9 taxes based on a broadband provider's capital stock, gross receipts, and franchise value. While broadband providers might obtain some relief from current Article 9-A taxes, the change could increase the total amount of taxes paid by broadband providers and broadband consumers in New York State.

Similarly, in the District of Columbia, regulated public utilities, including telephone companies, are subject to the District's gross receipts tax and a franchise (income) tax imposed on general businesses.[11] Telephone companies are taxed at the rate of 11% on gross receipts from

---

[8.] S.C. Code Ann. § 58-9-2530 (South Carolina relay service fee); Tex. Health & Safety Code Ann. § 771.071 (Texas wireline E-911 fee imposed on each local exchange access line or equivalent); Tex. Util. Code Ann. § 56.021 (Texas universal service fund surcharge imposed on receipts from intrastate telecommunications service); Fla. Stat. Ann. § 337.401(3)(c) (right-of-way fees for charter counties or municipalities in Florida).

[9.] *See, e.g.*, R.I. Gen. Laws § 44-13-2.2(a); *see also* Mo. Rev. Stat. § 143.451(6) (in Missouri, companies operating interstate telephone lines may elect to apportion income using a special single factor apportionment method. Upon election, the apportionment factor to be used is the ratio of the amount the company has invested on December 31st of each year in telephonic facilities, real estate, and real estate improvements divided by the amount of the company's total investment on December 31st of each year in telephonic facilities, real estate, and real estate improvements); Colo. Rev. Stat. § 39-22-303.5(2); Colo. Code Regs. § 1 CCR 201-3, Sp. Reg. 8A (in Colorado, the standard single sales factor apportionment applies, but there are special rules for how telecommunications providers are required to calculate their sales factor based upon the Multistate Tax Commission's special rules for telecommunications providers) and Utah Admin. R. § R865-6F-33(similar to Colorado, Utah has adopted the Multistate Tax Commission's special telecommunications apportionment rules).

[10.] Compare N.Y. Tax Law §§ 186-e, 186-a, 184, 183 (Article 9 taxes imposed on telecommunications providers) and N.Y. Tax Law §§ 208, 208-A, 208-B (Article 9-A taxes imposed on general business corporations).

[11.] D.C. Code § 47-2501(c).

sales included in nonresidential customer bills, and at the rate of 10% on gross receipts from sales included in residential customer bills.[12] Broadband providers currently do not pay this tax.

In South Carolina, public utilities (including regulated telephone companies) pay a separate license tax based on the value of the company's property, and its gross receipts.[13] This levy on public utilities, particularly the gross receipts component of the tax, typically results in a higher tax burden than the general business corporation license fee. Finally, a number of states, such as Indiana and Tennessee, require telecommunications companies to pay an annual public utility commission fee based on an assessment of gross revenues.[14]

* * *

As NCTA consistently has stated throughout this proceeding, cable operators are committed to maintaining an open Internet and the Commission has ample authority under section 706 to adopt rules to ensure such the Internet remains open. Title II is unnecessary to achieve the Commission's goals in this proceeding and, as described above, reclassification of broadband services and providers will directly undermine the Commission's goal of universal access to broadband for all Americans.

Respectfully submitted,

James Assey

Cc: Phil Verveer
GN Docket Nos. 14-28 and 10-127

12. D.C. Code §§ 47-2501(a)

13. S.C. Code Ann. § 12-20-50.

14. Ind. Code § 8-1-6-1(a); Tenn. Code Ann. § 65-4-301(a)(1).