

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

August Term, 2012

(Argued: January 11, 2013)

Decided: July 22, 2013)

Docket No. 12-803

IN RE: WORLDCOM, INC.,

Debtor.

INTERNAL REVENUE SERVICE,

Appellant,

—v.—

WORLDCOM, INC.,

Debtor-Appellee.

Before:

KEARSE, KATZMANN, *Circuit Judges*, and RAKOFF, *District Judge*.*

Appeal from a judgment of the United States District Court for the Southern District of

* The Honorable Jed S. Rakoff, of the United States District Court for the Southern District of New York, sitting by designation.

1 New York (Forrest, *J.*), affirming the decision of the bankruptcy court (Gonzalez, *C.J.*), which
2 granted the WorldCom Debtors’ objection to the IRS’s proof of claim and the Debtors’ motion
3 for a refund of federal communication excise taxes previously paid by WorldCom. We hold that
4 the dial-up Internet service purchased by WorldCom from local telephone companies, known as
5 COBRA, was a “local telephone service” that provided “access to a local telephone system, and
6 the privilege of telephonic quality communication with substantially all persons . . . constituting a
7 part of such local telephone system.” 26 U.S.C. § 4252(a). WorldCom must therefore pay the
8 three-percent excise tax federal law imposes on the purchase of any local telephone service, *id.*
9 § 4251, and the Debtors are not entitled to a refund from the IRS. For the reasons stated below,
10 the judgment of the district court is **REVERSED**, and the case is **REMANDED** for further
11 proceedings consistent with this Opinion.

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19

20 KATZMANN, *Circuit Judge*:

21 This case calls on us to decide if the bankrupt telecommunications company WorldCom
22 must pay federal excise taxes on the purchase of a telecommunications service that connected
23 people using dial-up modems to the Internet. Appellant, the Internal Revenue Service (“IRS”),
24 appeals from a judgment of the United States District Court for the Southern District of New
25 York (Forrest, *J.*), which upheld the decision of the Bankruptcy Court (Gonzalez, *C.J.*) to grant

1 the objection of the reorganized debtors (“Debtors”)¹ to the IRS’s proof of claim for taxes owed
2 and the Debtors’ refund motion for the taxes WorldCom had already paid.

3 In the late 1990s, WorldCom purchased a service from local telephone companies called
4 “central-office-based remote access,” or “COBRA,” that gave people the ability to use their
5 modems to connect to WorldCom’s network (and the Internet) over their regular telephone line.
6 The tax code adds a three-percent excise tax to the purchase of a “local telephone service.” 26
7 U.S.C. § 4251. A “local telephone service” is any service that provides “access to a local
8 telephone system, and the privilege of telephonic quality communication with substantially all
9 persons having telephone or radio telephone stations constituting a part of such local telephone
10 system.” *Id.* § 4252(a). On appeal, the IRS contends that the district and bankruptcy courts erred
11 in concluding that COBRA was not taxable as a local telephone service.

12 For the reasons set forth below, we hold that WorldCom purchased a “local telephone
13 service” when it paid for COBRA services, and that WorldCom must therefore pay federal
14 communication excise taxes on those transactions. Accordingly, we reverse the judgment of the
15 district court and remand the case for further proceedings consistent with this Opinion.

16 BACKGROUND

17 I. *Factual Background*

18 The following background is drawn from the bankruptcy court’s factual findings, adopted

¹ Although the caption names WorldCom, Inc. as the formal debtor-appellee, this adversary proceeding involves several of the debtors in the jointly administered bankruptcy. The principal debtor changed its name from WorldCom, Inc. to MCI Inc. and is currently operating as Verizon Business Global LLC. The subsidiary debtors are principally UUNet Technologies, Inc. and MCI WorldCom Network Services Inc. For convenience, we refer to the relevant debtors as the “Debtors,” following the convention of the parties and the district court. For readability, we refer to the transactions at issue as purchased by “WorldCom.”

1 by the district court and unchallenged by either party on appeal:²

2 In the late 1990s, WorldCom, originally a long-distance telephone service provider, began
3 building a massive Internet network to provide data services. As part of building that network,
4 WorldCom purchased a now-obsolete telecommunications service known as
5 “central-office-based remote access,” or “COBRA” from local telephone companies. COBRA
6 allowed local telephone subscribers to connect to the Internet using a dial-up modem.³

7 In order to connect to the Internet through COBRA, a subscriber’s modem would call the
8 COBRA access number over the subscriber’s normal telephone line (the public switched
9 telephone network or “PSTN” line). After dialing the COBRA number, the modem signal
10 traveled over the PSTN, the same network on which traditional telephone calls travel. The signal
11 then passed through a switch at the local telephone company’s central office that routed the
12 signal over the telephone company’s COBRA-specific high-capacity telephone lines, known as
13 “primary rate interface” or “PRI” lines. The PRI lines carried the signal to a network access
14 server, which converted the phone signal to an Internet-appropriate format (TCP/IP) using digital
15 signal process (“DSP”) cards. The network access server sent this TCP/IP data signal to a router
16 through another PRI line contained within the network access server, and the router then
17 transmitted the signal, along with other aggregated dial-up data signals, to WorldCom’s network
18 on a high-speed data line through the egress of the network access server. The system also

² The parties accuse each other of waiving various arguments by not challenging the bankruptcy court’s factual findings. But neither party actually challenges the facts as found by the bankruptcy court, only the legal import of those factual findings on taxability.

³ We provide here only the factual background that is necessary to resolving the issues present in this appeal. For further background on WorldCom and COBRA, see *In re WorldCom, Inc. (WorldCom I)*, 371 B.R. 19, 23–24 (Bankr. S.D.N.Y. 2007).

1 worked in reverse and could convert a data signal from the Internet to a phone signal that could
2 be carried through the local telephone lines back to the user's modem. COBRA provided local
3 telephone customers with a two-way connection to the Internet.⁴

4 WorldCom plugged the output Internet data stream from the local telephone company's
5 network access server into its own network, and sold access to the stream to Internet Service
6 Providers ("ISPs"), like AOL, which in turn sold access to the Internet to people with dial-up
7 modems. The PRI lines and all aspects of the network access server up through the egress port
8 where WorldCom plugged in its network were considered COBRA equipment and were used by
9 the local telephone companies as part of providing COBRA service to WorldCom. WorldCom
10 paid the local telephone companies a monthly fee for access to COBRA.

11 The parties agree that the COBRA system was theoretically capable of transmitting an
12 ordinary telephone call. The PRI lines that carried a modem signal to the network access server
13 could also carry a regular voice communication signal. Instead of connecting to the network
14 access server, those PRI lines could have plugged into a "PBX," which is a switch that allows for
15 voice communication over PRI lines. The COBRA-specific PRI lines, however, did not include
16 a PBX switch. As purchased by WorldCom, COBRA was not set up for voice communication.

17 WorldCom also could not reconfigure the PRI lines, which, along with the other COBRA
18 equipment, were controlled by the local telephone companies. It could access COBRA only
19 remotely to disable a modem if it was malfunctioning or make limited software changes.
20 Accordingly, within the system provided by the COBRA service, once the network access server
21 converted a telephone signal from a modem into Internet-friendly TCP/IP packets (the

⁴ For diagrams depicting COBRA and its related processes, see J. App'x 536 & 538.

high-speed data stream), it was no longer possible to transmit a traditional voice communication. A WorldCom employee's husband could not use COBRA to call his wife's office and ask her whether she wanted to get lunch.⁵

II. Procedural History

WorldCom filed its Chapter 11 bankruptcy petition on July 21, 2002, and the bankruptcy court confirmed the reorganization plan on October 31, 2003. *In re WorldCom, Inc. (WorldCom I)*, 371 B.R. 19, 24–25 (Bankr. S.D.N.Y. 2007). After the court confirmed the plan, the IRS filed a proof of claim requesting that the Debtors pay \$16,276,440.81 in excise taxes on WorldCom's purchase of COBRA services. *WorldCom I*, 371 B.R. at 25. The Debtors objected to the IRS's claim and additionally moved for a refund of the \$38,297,513 in excise taxes WorldCom had already paid on COBRA.

The bankruptcy court (Gonzalez, *J.*) held an evidentiary hearing on February 1, 2006. By opinion dated June 1, 2007, the bankruptcy court ruled in favor of the Debtors, granting both the refund motion and their objection to the IRS's proof of claim. *WorldCom I*, 371 B.R. at 32. The IRS appealed *WorldCom I* to the district court. On August 7, 2009, the district court (Jones, *J.*) concluded that the bankruptcy court erred in ruling that section 4252(a) required WorldCom to have the privilege to both initiate and receive telephonic quality communication. *In re*

⁵ Before the bankruptcy court, the IRS argued that COBRA could transmit "voice over Internet protocol," or "VoIP." The bankruptcy court, however, concluded that the COBRA contract did not permit VoIP that would require the telephone company to convert the telephone signal into an Internet signal, that the COBRA service as configured could not carry VoIP signals, and that, with respect to computer-to-computer VoIP (*e.g.*, Skype), the technology then in use was too slow to transmit VoIP. Accordingly, the bankruptcy court concluded that COBRA could not transmit telephonic quality communication through VoIP. The IRS does not challenge this factual finding on appeal.

1 *WorldCom, Inc. (WorldCom II)*, No. 07 Civ. 7417, 2009 WL 2432370, at *3–4 (S.D.N.Y. Aug.
2 7, 2009) (holding that as long as two-way communication occurred, it was irrelevant which party
3 initiated the call) (citing *USA Choice Internet Servs., LLC v. United States (USA Choice II)*, 522
4 F.3d 1332, 1338–39 (Fed. Cir. 2008)). Accordingly, the district court reversed and remanded to
5 the bankruptcy court for further factual findings on whether COBRA was a “local telephone
6 service.”

7 On remand, the parties submitted additional proposed findings of fact and conclusions of
8 law, and on June 15, 2011, the bankruptcy court again ruled in favor of the Debtors. *In re*
9 *WorldCom, Inc. (WorldCom III)*, 449 B.R. 655 (Bankr. S.D.N.Y. 2011). The bankruptcy court
10 concluded that the only service WorldCom had purchased was the ability to plug into the
11 high-speed Internet data stream provided by the local telephone companies, *i.e.*, the egress from
12 the network access server. Because that data stream could not support “telephonic quality
13 communication,” which, in the bankruptcy court’s interpretation, meant regular phone calls, and
14 because WorldCom could not reconfigure COBRA to provide it with telephonic quality
15 communication, the bankruptcy court concluded that WorldCom had not purchased a “local
16 telephone service” as defined by the statute. The court distinguished WorldCom’s purchase of
17 COBRA services from other cases finding that similar Internet services were taxable. *See USA*
18 *Choice II*, 522 F.3d at 1341; *Comcation, Inc. v. United States*, 78 Fed. Cl. 61, 65 (2007). In
19 those cases, the taxpayer purchased a service that provided it with the raw telephone signals,
20 which the company itself converted to an Internet signal. According to the bankruptcy court,
21 because the companies in those cases had access to the telephone lines, they were provided with
22 signals capable of “telephonic quality communication.”

1 The IRS again appealed to the district court. On December 22, 2011, the district court
2 (Forrest, *J.*) affirmed the judgment of the bankruptcy court. *In re WorldCom, Inc. (WorldCom*
3 *IV)*, No. 11 Civ. 5463, 2011 WL 6434007 (S.D.N.Y. Dec. 22, 2011). The district court
4 emphasized that WorldCom itself did not connect dial-up users to the Internet and characterized
5 COBRA as simply an “intermediate” step in the Internet-connection process. *Id.* at *5–7.
6 According to the court, this was another reason to distinguish COBRA from the services at issue
7 in *Comcation* and *USA Choice II*, where the ISP plaintiffs connected subscribers to the Internet
8 directly. The district court then evaluated whether this “intermediate” step “c[ould] constitute a
9 stand alone ‘local telephone service’” for purposes of section 4252(a). *Id.* at *5. After retracing
10 the process of how the COBRA service operated in practice, the district court concluded that the
11 “nanosecond” of time that the modem signal spent traversing the PRI lines before being
12 converted into an Internet data stream by the network access server was “[s]urely not” “what
13 Congress meant to tax as a ‘local telephone service.’” *Id.* at *7.

14 The district court further concluded that COBRA did not provide the ability to
15 communicate with “substantially all persons” who are part of “such [asserted] telephone system”
16 as required by statute. *Id.* at *7 (brackets in original). The court determined that COBRA was
17 distinct from the local telephone system, and because it “[wa]s a self-contained service” within
18 the telephone company’s facility, there was no way for any “person” to access the telephonic
19 quality communication that the COBRA PRI lines could theoretically support. *Id.* Even though
20 COBRA interfaced with the normal local telephone network—which the court delineated as a
21 separate “service”—people who used their modems to connect to the Internet through COBRA
22 could not communicate with the COBRA system, nor could WorldCom communicate with them.

1 The court entered judgment in favor of the Debtors on December 28, 2011. This appeal
2 followed.

3 DISCUSSION

4 Because neither party disputes the bankruptcy court's factual findings or the district
5 court's adoption of those findings, we address only the legal conclusions of the district court.
6 Our review of those conclusions is *de novo*. *In re CBI Holding Co.*, 529 F.3d 432, 449 (2d Cir.
7 2008). Federal tax assessments are presumed to be correct and constitute prima facie evidence of
8 liability. *See Welch v. Helvering*, 290 U.S. 111, 115 (1933); *United States v. McCombs*, 30 F.3d
9 310, 318 (2d Cir. 1994). The taxpayer bears the burden to prove that the assessment was
10 incorrect. *McCombs*, 30 F.3d at 318. This burden applies within bankruptcy proceedings.
11 *Raleigh v. Ill. Dep't of Revenue*, 530 U.S. 15, 26 (2000).

12 I. Local Telephone Service

13 Federal law imposes a three-percent excise tax on amounts paid for three kinds of
14 "communications services": "local telephone service"; "toll telephone service"; and
15 "teletypewriter exchange service." 26 U.S.C. § 4251. The IRS contends that COBRA is a local
16 telephone service, which the statute defines as:

17 (1) the access to a local telephone system, and the privilege of telephonic quality
18 communication with substantially all persons having telephone or radio telephone stations
19 constituting a part of such local telephone system, and

20 (2) any facility or service provided in connection with a service described in paragraph (1).

21 *Id.* § 4252(a).

22 Whether COBRA constitutes a "local telephone service" is a question of statutory
23 interpretation. In interpreting any statute, we start with its text, *Auburn Hous. Auth. v. Martinez*,

1 277 F.3d 138, 143 (2d Cir. 2002), giving the language its ordinary meaning, *Taniguchi v. Kan*
2 *Pac. Saipan, Ltd.*, 132 S. Ct. 1997, 2002 (2012). Section 4252(a)(1) sets forth two requirements
3 for a local telephone service, both of which must be satisfied: (a) “access to a local telephone
4 system”; and (b) “the privilege of telephonic quality communication” with “substantially all” of
5 the people who are part of that system. We address each element in turn.

6 A. Access to a local telephone system

7 We begin with the element of “access to a local telephone system.” Although we have
8 not previously addressed the proper interpretation of section 4252(a), the Federal Circuit has
9 confronted its scope. After reviewing ordinary definitions of “access,” the Federal Circuit found
10 that “general dictionary definitions of ‘access’ provide little insight” into what is covered by the
11 tax. *USA Choice II*, 522 F.3d at 1337. But the court noted it had previously interpreted “access”
12 in the context of access to a teletypewriter exchange system under section 4252(c) of the statute,
13 where it held that “the ‘technological meaning of the word access . . . in the communications
14 field in general . . . mean[s] the interface or connection between . . . the central exchange and the
15 [customer terminal].’” *Id.* (quoting *Trans-Lux Corp. v. United States*, 696 F.2d 963, 965 (Fed
16 Cir. 1982)) (alterations and brackets in *Trans-Lux*). Based on this interpretation of the closely
17 related teletypewriter exchange service definition, the Federal Circuit concluded that “‘access’
18 simply means connectivity.” *Id.*

19 The Federal Circuit’s definition of access was adopted by the district court in this case,
20 *see WorldCom II*, 2009 WL 2432370, at *3, and is undisputed by the parties. We agree. “Access
21 to a local telephone system” simply means a service that provides a connection to a local
22 telephone system.

1 We must still determine, however, what level of connectivity is sufficient to provide
2 “access.” Several of our sister circuits have noted that because section 4252(a) speaks of “access
3 to a local telephone system,” Congress intended that the service provide a direct connection to a
4 specific local system. *See, e.g., OfficeMax, Inc. v. United States*, 428 F.3d 583, 599–600 (6th
5 Cir. 2005). We agree that “access” in the context of the purchase of a local telephone service is
6 limited to direct connectivity to a specific local telephone system. Interpreting “access” to cover
7 indirect connections would mean, for example, that a toll or long-distance telephone service,
8 which provides indirect access to every local telephone system, would also be considered a local
9 telephone service. This would collapse the separate definitions of “local telephone service” and
10 “toll telephone service” under the statute. *See id.* (noting that contrary interpretation would
11 “blur[] the line between” sections 4252(a) and 4252(b)); *accord Reese Bros., Inc. v. United*
12 *States*, 447 F.3d 229, 240–41 (3d Cir. 2006); *Am. Bankers Ins. Grp. v. United States*, 408 F.3d
13 1328, 1338 (11th Cir. 2005) (noting that a contrary interpretation would make “the entire United
14 States . . . part of one ‘local telephone system’” (other internal quotation marks omitted)); *Am.*
15 *Online, Inc. v. United States*, 64 Fed. Cl. 571, 582 (2005). Similarly, the *USA Choice II* court
16 suggested that a service like Vonage, whose Voice over Internet Protocol (“VoIP”) technology
17 “uses the internet to transmit telephone signals, rather than using the traditional public switched
18 telephone network,” does not provide direct “access” to a local telephone system. *USA Choice*
19 *II*, 522 F.3d at 1343 (citing *Verizon Servs. Corp. v. Vonage Holdings Corp.*, 503 F.3d 1295, 1298
20 (Fed Cir. 2007)).

21 With this understanding of “access” in mind, we conclude that COBRA provided
22 WorldCom with access to a local telephone system. The connection between a dial-up user and

WorldCom through COBRA began with a local telephone customer's ordinary PSTN line. When the subscriber dialed the COBRA number, the telephone company routed the signal from the subscriber's modem and PSTN line to COBRA's PRI lines, which connected to WorldCom's network through the telephone company's network access server. Thus, COBRA provided direct "connectivity" to a local telephone system. Moreover, the record demonstrates that COBRA was a service provided by *individual* local telephone companies. WorldCom contracted separately with each local telephone company, like BellSouth, to gain access to that company's local telephone system. COBRA did not transform the "entire United States [into] . . . one 'local telephone system.'" *Am. Bankers Ins. Grp.*, 408 F.3d at 1338. The access element is satisfied.

B. The privilege of telephonic quality communication

With access defined, we turn to the second—and more hotly contested—element of local telephone service: whether COBRA provided WorldCom with "the privilege of telephonic quality communication with substantially all persons having telephone or radio telephone stations constituting a part of such local telephone system." 26 U.S.C. § 4252(a)(1). The IRS contends that COBRA did so by connecting dial-up users to WorldCom's network through modems and telephonic PRI lines, just like the similar dial-up Internet services that were found taxable by the Federal Circuit in *USA Choice II* and the Court of Federal Claims in *Comcation*. The Debtors respond that, unlike the services at issue in *USA Choice II* and *Comcation*, WorldCom had access only to the Internet data stream from the telephone company's network access server. Without the ability to use or reconfigure COBRA to talk to the dial-up users on the phone, they argue, COBRA did not provide "the privilege of telephonic quality communication."

We must therefore define "telephonic quality communication." Starting with

1 “telephonic,” dictionaries contemporaneous to the enactment of the last substantive revision to
2 the relevant statutory provision define “telephonic” as “[o]f, pertaining to, of the nature of, or
3 conveyed by a telephone.” 2 The Compact Edition of the Oxford English Dictionary 3252
4 (1971); *accord* Webster’s New Collegiate Dictionary 873 (1961) (adjective form of “telephone,”
5 defined as, *inter alia*, “[t]o send or communicate by telephone”); *see also* *Taniguchi*, 132 S. Ct.
6 at 2002–03 & n.2 (interpreting “ordinary meaning” of statutory term with reference to
7 contemporaneous dictionaries).

8 Next, because section 4252 uses the term “telephonic *quality* communication,” 26 U.S.C.
9 § 4252(a)(1) (emphasis added), we must determine how “quality” modifies “telephonic.” Like
10 the statute’s use of the word “access,” general dictionary definitions of “quality” shed little light
11 on Congress’s intent. *See USA Choice II*, 522 F.3d at 1337. Quality can mean: an attribute,
12 property, special feature, or characteristic; nature, kind, or character; the degree or grade of
13 excellence; or a particular class, kind, or grade of anything, as determined by its quality. 2 The
14 Compact Edition of the Oxford English Dictionary 2383; Webster’s New Collegiate Dictionary
15 691. The meaning of the word depends on context and connotation.

16 However, “[a] provision that may seem ambiguous in isolation is often clarified by the
17 remainder of the statutory scheme—because the same terminology is used elsewhere in a context
18 that makes its meaning clear.” *United Sav. Ass’n of Tex. v. Timbers of Inwood Forest Assocs.,*
19 *Ltd.*, 484 U.S. 365, 371 (1988). Here, comparing the definition of “local telephone service” to
20 the related provision of section 4252 defining “toll [long-distance] telephone service” shows that
21 we must give meaning to the word “quality” independent of “telephonic.” Section 4252(b) sets
22 forth two alternative definitions of toll telephone service, one that uses the term “telephonic

1 quality communication,” and another that refers to a service that provides the customer with the
2 “privilege of an unlimited number of telephonic communications,” unmodified by the word
3 quality. Compare 26 U.S.C. § 4252(b)(1) (defining toll telephone service as, in relevant part, “a
4 telephonic *quality* communication” (emphasis added)), with *id.* § 4252(b)(2) (alternatively
5 defining toll telephone service as “service which entitles the subscriber . . . to the privilege of an
6 unlimited number of *telephonic communications*” (emphasis added)).⁶ Because Congress has
7 distinguished between a service that provides the privilege of “telephonic communications” and
8 “telephonic quality communication,” we cannot treat “telephonic quality” as equivalent to
9 “telephonic.” See *Duncan v. Walker*, 533 U.S. 167, 174 (2001) (“We are . . . reluctant to treat
10 statutory terms as surplusage in any setting.” (internal quotation marks and brackets omitted)).

11 If we define “quality” in the context of “telephonic quality communication” as meaning
12 an “attribute, property, or characteristic,” we would make “quality” redundant with “telephonic.”
13 Saying that a communication that has the “property” or “characteristic” of being telephonic is no
14 different from simply calling a communication telephonic. See also 2 The Compact Edition of
15 the Oxford English Dictionary 3252 (defining “telephonic” in part with “of the nature of”). On
16 the other hand, applying the alternate dictionary definitions of “quality” as meaning “the degree
17 or grade of excellence” or “a particular class, kind or grade of anything, as determined by its
18 quality,” gives meaning to “quality” by broadening the scope of telephonic communications to
19 those communications in the same “class, kind or grade” as a communication by telephone.

⁶ Congress enacted these two definitions of toll telephone service in 1965 to reflect the two ways that AT&T—the country’s only long-distance telephone provider at the time—billed customers for long distance service. *OfficeMax*, 428 F.3d at 590; see also H.R. Rep. No. 89-433, at 30 (1965); S. Rep. No. 89-324, at 35 (1965).

1 We therefore conclude that quality, as used in this statute, refers to the technological
2 capacity of the channel to transmit voice signals, regardless of whether or not the channel is used
3 for voice communication. If the “grade” of the communication is one that is of the same level as
4 a telephonic communication, then the communication is telephonic quality. In other words, a
5 telephonic quality communication is a communication that is carried over a communication
6 channel that could also carry an ordinary telephone call.⁷

7 Our interpretation not only gives substance to the word “quality,” but is also supported by
8 another provision of section 4252. “The meaning of a particular section in a statute can be
9 understood in context with and by reference to the whole statutory scheme, by appreciating how
10 sections relate to one another. In other words, the preferred meaning of a statutory provision is
11 one that is consonant with the rest of the statute.” *Auburn*, 277 F.3d at 144 (citing *Robinson v.*
12 *Shell Oil Co.*, 519 U.S. 337, 341 (1997)). In addition to taxing local and toll telephone services,
13 the tax code also imposes the communications excise tax on “teletypewriter exchange service.”
14 26 U.S.C. § 4251. Teletypewriter exchange services—now, like COBRA, obsolete—did not
15 provide voice communication; they were an early form of data exchange that connected printers
16 to a network for the purpose of sending *text*-based messages. *See* 28 The New Encyclopædia
17 Britannica 475 (15th ed. 2002); *see also* 26 U.S.C. § 4252(c) (defining as “access from a

⁷ This definition also appears to be in accord with industry usage of the term “telephonic quality.” *See Taniguchi*, 132 S. Ct. at 2005 (relying on “technical” definition as supporting “ordinary” statutory interpretation). In *USA Choice I*, the Court of Federal Claims noted that “[w]hen using the term ‘telephonic quality,’ the government’s expert used ‘what [he] believe[d] would be the industry understood definition[, that is] a communication channel over which it [i]s possible to have a two-way conversation with the use of telephones.’” *USA Choice Internet Servs., LLC v. United States (USA Choice I)*, 73 Fed. Cl. 780, 783 n.7 (2006) (all but first brackets in original), *aff’d*, 522 F.3d at 1341 n.2; *accord WorldCom III*, 449 B.R. at 661 & n.9.

1 teletypewriter or other data station”).

2 After defining what a “teletypewriter exchange service” is, section 4252(c) notes that
3 “[t]he term ‘teletypewriter exchange service’ does not include any service which is ‘local
4 telephone service’ as defined in subsection (a).” 26 U.S.C. § 4252(c). By adding this provision
5 to the definition of teletypewriter exchange service, it is clear that Congress envisioned the
6 possibility that a text-based teletypewriter service could also qualify as a local telephone service,
7 even absent the provision of any voice communication. Otherwise, there would be no need to
8 clarify that a service cannot be treated as both a “teletypewriter exchange service” and “local
9 telephone service.” To hold that “telephonic quality communication” means only voice
10 communication would render this provision surplusage.

11 From this, we conclude that a data communication transmitted by a modem is a
12 telephonic quality communication. In this case, both the government’s witness and the Debtors’
13 witness agreed that modems transmit data from a computer over telephone lines using the “the
14 same exact [frequency] range” as the human voice, J. App’x 493; *accord id.* at 506. The
15 Debtors’ expert also agreed that a modem connection “requires a telephonic quality grade
16 telephone line.” *Id.* at 496. Indeed, both the district court and bankruptcy court found that the
17 parties agreed that up until the modem signal reached the network access server there existed
18 “telephonic quality communication.” *WorldCom IV*, 2011 WL 6434007, at *6; *WorldCom III*,
19 449 B.R. at 658. Similarly, the Federal Circuit in *USA Choice II* noted that “a successful
20 connection between one of USA Choice’s server modems and another subscriber’s modem
21 required telephonic quality.” *USA Choice II*, 522 F.3d at 1341. And in *Comcation*, the Court of
22 Federal Claims explained that, “once a call was established [to Comcation’s network] on the PRI

1 lines, two-way, telephonic-quality communication occurred,” because information from the
2 subscriber and the Internet “flowed back and forth over these [PRI] lines.” *Comcation*, 78 Fed.
3 Cl. at 66 (rejecting argument that ISP did not have “privilege” to “communicate with” local
4 telephone customers because ISP could not initiate calls).

5 We recognize, however, that there is one authority that may be contrary to our
6 interpretation. In a revenue ruling from 1979, the IRS was asked to evaluate whether a data
7 processing and transmission service that used modems and local telephone lines was taxable, and
8 whether the equipment provided to the business in connection with that service was likewise
9 taxable. *See* Rev. Rul. 79-245, 1979-2 C.B. 380. Although the IRS found that the service could
10 be taxed as a “local telephone service” under section 4252(a)(1), it determined that the modems
11 and computer equipment provided to the business were not taxable as facilities provided in
12 connection with that service under section 4252(a)(2). *Id.* The IRS concluded that because “the
13 type of telephone signal produced by . . . modems is usable only for nonvoice data transmission
14 to other computer station,” and because “only a relatively few stations in [the local] telephone
15 system are used in this computer service,” “a modem is not a facility provided in connection with
16 the privilege of telephonic quality communication with substantially all persons having stations
17 in the local system.” *Id.*⁸

⁸ Although we acknowledge this potential conflict, the IRS cites Revenue Ruling 79-245 in this case only to point out that the communications service there was deemed taxable. *See* Appellant’s Reply Br. 15. It does not at all discuss the portion of the revenue ruling that undercuts the position it takes here. The IRS simply assumes the definition given to telephonic quality by the Federal Circuit in *USA Choice II* is correct and urges us to adopt it. *See* Appellant’s Br. 29–30. For their part, the Debtors never discuss Revenue Ruling 79-245. Nevertheless, because statutory interpretation is a “holistic endeavor,” we address the potentially contrary authority here. *See United Sav. Ass’n of Tex.*, 484 U.S. at 371.

1 It is not clear whether the IRS reached this conclusion primarily because the service
2 provided access to only a limited number of stations, or because “nonvoice data transmission”
3 was not of telephonic quality. In the end, the IRS found the service taxable because the business
4 could choose to plug a regular telephone instead of a modem into the port for the service, thereby
5 affording it the privilege of telephonic quality communication, “even though [it] may not be
6 exercised.” *Id.*; *accord USA Choice II*, 522 F.3d at 1341–42. Although not altogether certain,
7 the strong implication of the IRS’s reasoning, however, is that computer-to-computer
8 communications over telephone wires are not “telephonic quality communication.” *See*
9 *WorldCom III*, 449 B.R. at 661 (interpreting Revenue Ruling 79-245 as “equating telephonic
10 quality communication with voice communication” (emphasis omitted)).

11 We do not think this revenue ruling overcomes the text of the statute. The deference
12 owed to IRS revenue rulings is presently an unsettled area of law. *See United States v. Cleveland*
13 *Indians Baseball Co.*, 532 U.S. 200, 220 (2001) (declining to decide whether revenue rulings are
14 entitled to *Chevron* deference). Prior to the Supreme Court’s opinion in *United States v. Mead*
15 *Corp.*, 533 U.S. 218 (2001), we afforded “great deference” to IRS revenue rulings, and explained
16 that they are “presumed to have the force of legal precedent unless unreasonable or inconsistent
17 with the provisions of the Internal Revenue Code.” *Weisbart v. U.S. Dep’t of Treasury*, 222 F.3d
18 93, 98 (2d Cir. 2000) (internal quotation marks omitted). We have recognized, however, that this
19 standard was potentially undermined by the Supreme Court’s holding in *Mead* that
20 administrative rulings are not entitled to deference unless they carry the “force of law.” *See*
21 *Reimels v. Comm’r*, 436 F.3d 344, 347 n.2 (2d Cir. 2006); *see also Fortis, Inc. v. United States*,
22 420 F. Supp. 2d 166, 178–79 (S.D.N.Y. 2004). We now hold, consistent with every other circuit

1 to have addressed the issue since *Mead*, that revenue rulings are not entitled to *Chevron*
2 deference. See, e.g., *Kornman & Assocs., Inc. v. United States*, 527 F.3d 443, 454 & n.9 (5th Cir.
3 2008); *Aeroquip-Vickers, Inc. v. Comm’r*, 347 F.3d 173, 181 (6th Cir. 2003); *Omohundro v.*
4 *United States*, 300 F.3d 1065, 1067–68 (9th Cir. 2002); *Del Commercial Props., Inc. v. Comm’r*,
5 251 F.3d 210, 214 (D.C. Cir. 2001).

6 “[A]dministrative implementation of a particular statutory provision qualifies for
7 *Chevron* deference when it appears that Congress delegated authority to the agency generally to
8 make rules carrying the force of law, and that the agency interpretation claiming deference was
9 promulgated in the exercise of that authority.” *Mead*, 533 U.S. at 226–27. But, “[u]nlike
10 treasury regulations, the IRS does not invoke its authority to make rules with the force of law
11 when promulgating revenue rulings.” *Kornman*, 527 F.3d at 454 (citing 26 C.F.R.
12 § 601.601(d)(2)(v)(d)). Even though a revenue ruling is the “official IRS position on application
13 of tax law to specific facts,” *Weisbart*, 222 F.3d at 98 (internal quotation marks omitted), the
14 Supreme Court has made clear that official agency interpretations lacking the force of law are not
15 entitled to *Chevron* deference. See *Mead*, 533 U.S. at 233–34 (holding tariff rulings are not
16 entitled to *Chevron* deference); *Christensen v. Harris Cnty.*, 529 U.S. 576, 587 (2000) (holding
17 agency opinion letters are not entitled to *Chevron* deference). As we previously implied in
18 *Reimels*, *Weisbart* has been abrogated by *Mead*.

19 Although not entitled to *Chevron* deference, particular revenue rulings may be given
20 deference to the extent that they are persuasive—in other words, we will afford them *Skidmore*
21 deference. See *Mead*, 533 U.S. at 234–35 (citing *Skidmore v. Swift & Co.*, 323 U.S. 134, 139–40
22 (1944)); accord *WorldCom I*, 371 B.R. at 30–32 (rejecting *Chevron* deference and evaluating

1 whether revenue rulings are entitled to deference under *Skidmore*). “The weight [accorded to an
2 administrative] judgment in a particular case will depend upon the thoroughness evident in its
3 consideration, the validity of its reasoning, its consistency with earlier and later pronouncements,
4 and all those factors which give it power to persuade, if lacking power to control.” *Mead*, 533
5 U.S. at 228 (quoting *Skidmore*, 323 U.S. at 140). As relevant here, we do not defer to Revenue
6 Ruling 79-245 under *Skidmore* because we do not find it persuasive.

7 The IRS’s one-page legal analysis makes no effort to interpret the word “quality.” Nor
8 does it attempt to square “telephonic quality communication” in the local telephone service
9 definition with either “telephonic communications” in the toll telephone service definition or the
10 teletypewriter definition’s exclusivity rule. The ruling “contains no analysis of text or legislative
11 history or any other relevant interpretive guidance.” *Fed. Nat’l Mortg. Ass’n v. United States*,
12 379 F.3d 1303, 1308 (Fed. Cir. 2004). Similarly, the ruling “neither elucidates nor invokes
13 support for its conclusion” that modems do not qualify as conveying telephonic quality
14 communication. *Id.* By contrast, other courts that have squarely addressed the issue of whether
15 dial-up Internet services similar to COBRA are taxable have concluded that modems *do* engage
16 in telephonic quality communication by communicating over telephone lines. *See USA Choice*
17 *II*, 522 F.3d at 1334, 1341; *Comcation*, 78 Fed. Cl. at 64. We therefore give Revenue Ruling
18 79-245 no weight, in accord with our sister circuits that have declined to defer to similarly
19 cursory revenue rulings. *See Fed. Nat’l Mortg. Ass’n*, 379 F.3d at 1308–09; *O’Shaughnessy v.*
20 *Comm’r*, 332 F.3d 1125, 1130–31 (8th Cir. 2003).⁹

⁹ We likewise reject any potential argument that we should defer to Revenue Ruling 79-245 pursuant to the “legislative re-enactment doctrine,” which presumes that Congress is “aware of an administrative or judicial interpretation of a statute and . . . adopt[s] that

1 To be of telephonic quality a communication must use “a communication channel over
2 which it is possible to have a two-way conversation with the use of telephones,” *USA Choice II*,
3 522 F.3d at 1341 n.2 (alteration omitted). The local telephone and PRI lines used by modems are
4 such a channel. Therefore, data communication through a modem over telephone lines is
5 “telephonic quality communication.”

6 Now that we have defined the “privilege of telephonic quality communication,” we must
7 decide if COBRA provides it. The IRS argues that by routing a dial-up user’s modem signal over
8 PRI lines that were capable of carrying a phone call, COBRA provided WorldCom with the
9 privilege of telephonic quality communication. But the Debtors claim that because COBRA
10 transformed that modem signal into an Internet-compatible, non-voice quality TCP/IP data
11 stream within the network access server, and because WorldCom had access to only the data
12 stream, COBRA did not provide the privilege of telephonic quality communication. The Debtors
13 contend that “all [the] requirements [of section 4252(a)] . . . must extend through the *entirety* of
14 the connection. It is not sufficient that a portion of the path contains one of these elements.”
15 Appellee’s Br. 24 (emphasis added).

16 Despite the certainty of the Debtors’ assertion, they cite no portion of the statute, nor any
17 relevant case law, that supports such an interpretation. The plain language of section 4252(a)’s
18 phrase “the privilege of telephonic quality communication” does not answer whether the service
19 purchased has to provide the privilege of telephonic quality communication throughout the

interpretation when it re-enacts a statute without change.” *Lorillard v. Pons*, 434 U.S. 575, 580
(1978) (citations omitted). There is no evidence that this particular revenue ruling has been
“fully brought to the attention of the public and the Congress,” in a way that justifies invoking
the doctrine. *Am. Bankers Ins. Grp.*, 408 F.3d at 1335–36 (holding doctrine not applicable to
revenue ruling on long-distance phone calls in interpreting communications excise tax).

1 entirety of the service’s system, or if it is sufficient if only a *portion* of the system provides that
2 privilege. We have fallen into a statutory crevice. To fill it, we look beyond the plain text of the
3 statute. *In re Boodrow*, 126 F.3d 43, 49 (2d Cir. 1997) (“[T]he text is only the starting point,’
4 especially when the language is ambiguous.” (quoting *Kelly v. Robinson*, 479 U.S. 36, 43
5 (1986))).

6 But before we do so, we address the government’s contention that we do not need to look
7 beyond the plain text because COBRA is clearly taxable when section 4252(a) is read in
8 conjunction with another provision of the communications excise tax statute, section 4254(a).
9 Section 4254(a) sets out the general rule for calculating the excise tax, which is that “[i]f a bill is
10 rendered the taxpayer for local telephone service or toll telephone service[,] . . . the amount on
11 which the tax with respect to such services shall be based shall be the sum of all charges for such
12 services included in the bill.” 26 U.S.C. § 4254(a). Because the modem connection between the
13 dial-up users and the network access server is of “telephonic quality” and has been previously
14 held to be taxable by *USA Choice II* and *Comcation*, the IRS argues that COBRA simply
15 provides the same “service” plus a network access server, and that the whole charge is therefore
16 taxable.

17 We disagree for several reasons. First, we think the IRS misreads the applicability of
18 *USA Choice II* and *Comcation*. The IRS contends that because those courts found similar
19 services taxable, we can shoehorn COBRA into that finding as providing a little “more.” But this
20 mistakes the holdings of *USA Choice II* and *Comcation* for agreement with the IRS’s reasoning.
21 Those courts did not address the issue of whether the “service” changes when the customer does
22 not have access to the PRI lines. *See USA Choice II*, 522 F.3d at 1341 (“USA Choice’s decision

1 to connect these lines to modems in its network servers rather than to telephones through
2 equipment such as a multiplexor or PBX[—]though perfectly understandable for a commercial
3 ISP—resulted in self-imposed limits that did not fundamentally alter the nature of the services
4 that USA Choice had the privilege to use.” (internal quotation marks, citation, and brackets
5 omitted)). Looking, as we must, at the text, it would be entirely circular to use section 4254(a)’s
6 explanation of how to calculate the tax assessed on a local telephone service to define what a
7 local telephone service is. The IRS’s argument works only if we already assume that the section
8 of COBRA that uses PRI lines is a taxable “local telephone service,” and therefore fails.

9 Although the plain text of the statute does not answer whether a service must provide
10 “telephonic quality communication” throughout the entirety of the system in order to be taxable,
11 “Congress passes legislation with specific purposes in mind. When the ordinary tools of
12 statutory construction permit us to do so, we must attempt to discover those purposes”
13 *N.Y.C. Health & Hosps. Corp. v. Perales*, 954 F.2d 854, 862 (2d Cir. 1992). Keeping in mind
14 that “[s]tatutory construction . . . is a holistic endeavor,” *United Sav. Ass’n of Tex.*, 484 U.S. at
15 371, we may “look at legislative history to determine the intent of Congress,” *Auburn*, 277 F.3d
16 at 143–44.

17 The history of the communications excise tax is long and turbulent. Congress first
18 imposed a tax on the purchase of communications services shortly after the Spanish-American
19 War, twenty years after the invention of the telephone. *See OfficeMax*, 428 F.3d at 585–86
20 (tracing legislative iterations of the tax). Although initially designed as a temporary tax passed to
21 finance the deficit caused by the War, Congress repeatedly reenacted and extended the tax,
22 adjusting the scope of its coverage and changing the rates applicable to various services, before

1 making the tax permanent at its current rate of three percent in 1990 for all services covered. *Id.*
2 (noting that attempt to repeal the tax in 2000 was vetoed by President Clinton).

3 The most recent substantive change to the definitions of taxable services occurred in
4 1965, when Congress enacted the Excise Tax Reduction Act of 1965, Pub. L. No. 89-44 § 302,
5 79 Stat. 136, 145. *See Am. Online*, 64 Fed. Cl. at 578. As is most relevant here, the 1965 Act
6 enacted the current definitions of local telephone service, toll telephone service, and
7 teletypewriter exchange service. *See Trans-Lux Corp.*, 696 F.2d at 967. The definitions were
8 “likely . . . updated and modified in order to reflect and to meet the changing technology and
9 market conditions of the industry . . . [,] in order ‘to make it clear that it is the service as such
10 which is being taxed and not merely the equipment being supplied.’” *Id.* (quoting H.R. Rep. No.
11 89-433, at 30 (1965); S. Rep. No. 89-324, at 35 (1965)).¹⁰ This history suggests that Congress
12 intended to tax any communication service as a “local telephone service” so long as it connected
13 a customer to a local telephone system and allowed that customer to use the telephone lines to
14 communicate with the subscribers to that system, regardless of whether the service also used
15 non-telephonic equipment to accomplish that communication.

16 Although the bankruptcy and district courts acknowledged this congressional purpose,
17 they misapplied it when evaluating the service that COBRA provided. By focusing solely on the
18 part of the COBRA system that WorldCom connected to and had control over—the data stream

¹⁰ The prior version of the statute, enacted in 1958, defined “general telephone service” as “any telephone or radio telephone service furnished in connection with any fixed or mobile telephone or radio telephone station which may be connected (directly or indirectly) to an exchange operated by a person engaged in the business of furnishing communication service.” Excise Tax Technical Changes Act of 1958, Pub. L. No. 85-859 § 133, 72 Stat. 1275, 1290. The 1965 amendments broadened this definition to “telephonic quality communication,” unmooring the statute from any particular equipment configuration.

1 that came out of the egress to the network access server—the bankruptcy and district courts did
2 not apprehend the scope of the service the local telephone companies sold to WorldCom. The
3 COBRA service was not just a “data stream,” sitting on a shelf to be picked up by any telecom
4 shopper looking for Internet access. Such a conclusion gives too much emphasis to the
5 equipment used by the local telephone companies—the network access server—and ignores the
6 system as a whole.

7 What COBRA provided, as made clear by the bankruptcy court’s factual findings, was a
8 communication *pathway* between local telephone customers and WorldCom’s network. COBRA
9 allowed WorldCom to connect dial-up modem users to the Internet through those users’ regular
10 telephone lines. And in order to connect them to the Internet, the part of that pathway that used
11 modems required telephonic quality communication.

12 That WorldCom connected its equipment to the COBRA system only after the local
13 telephone company converted the modem signals to a high-speed data stream does not change the
14 fact that the service relied on modem signals being carried over PRI lines that afforded
15 telephonic quality communication. Without PRI lines there would be no COBRA service and
16 nothing for WorldCom to resell to the ISPs. As other courts have noted, the statutory definition
17 of local telephone service shows that Congress intended to tax those users who rely on the
18 traditional telephone system for whatever reason. *See USA Choice II*, 522 F.3d at 1341 (noting
19 the tax applies to customers who use their phone lines, regardless of whether to make phone calls
20 or to plug in a fax machine). Accordingly, because COBRA relied on telephonic quality PRI
21 lines to allow WorldCom’s network to communicate with dial-up subscribers, COBRA provided
22 WorldCom with the “privilege of telephonic quality communication.”

1 The Debtors, relying on the same legislative history from 1965 that emphasizes the “shift
2 [of] the focus of the tax to the services rather than the equipment being provided.” *USA Choice*
3 *II*, 522 F.3d at 1339; *see* H.R. Rep. No. 89-433, at 30, argue that the PRI lines were merely part
4 of the local telephone company’s COBRA equipment and not part of the actual service provided
5 to WorldCom. We disagree. First, the bankruptcy court found that one of the “COBRA
6 system[’s]. . . three basic components” was routing “dial-up connections . . . from [the telephone
7 company’s central office] switches to the COBRA system through ingress Primary Rate Interface
8 (‘PRI’) lines.” *WorldCom I*, 371 B.R. at 24. Indeed, on remand from the district court, the
9 Debtors’ proposed findings of fact stated that the PRI lines were “used by the [telephone
10 companies] as part of their provision of COBRA service.” J. App’x 1391–92; *see also*
11 *WorldCom III*, 449 B.R. at 662 (referring to PRI lines as “part of the COBRA service”). Second,
12 the Debtors’ expert witness and employee, John Anderson, testified that the PRI lines were a
13 component of the COBRA service purchased by WorldCom. Third, WorldCom’s contracts with
14 local telephone companies listed the PRI lines as part of the COBRA service.

15 To give a more intuitive example (though perhaps dated for some), consider a fax
16 machine. Fax machines transmit data signals over ordinary telephone lines. When a person
17 pushes “start” on a fax machine, the machine scans the piece of paper, converts the image into a
18 signal, and transmits it over a telephone line to the number dialed. The fax machine on the other
19 end of the call receives the signal, converts the signal back into the image originally scanned, and
20 prints a copy. Given that we have defined “telephonic quality” as meaning any communication
21 that relies on a telephonic-grade connection, a fax connection is of telephonic quality. But the
22 connection over the telephone lines is not the only thing the fax machine relies on to

1 communicate. To finish the communication, the fax machine converts the signal into a printed
2 image. The piece of paper printed is certainly not of “telephonic quality.”

3 Accepting the Debtors’ argument that the connection must remain of telephonic quality
4 through the entirety of the connection, a service that connects fax machines over the local
5 telephone system would not be taxable. We would have to conclude that only the printer/scanner
6 part of the fax machine that the customer uses is the “service,” and that the telephone lines used
7 by the machines are merely “equipment.” But if that is the case, what, other than an ordinary
8 telephone call, could be taxable as a telephonic quality communication? Such an interpretation
9 would bring us back to treating “telephonic quality communication” in sections 4252(a)(1) and
10 (b)(1) as equivalent to “telephonic communications” in subsection (b)(2). We do not think that
11 Congress intended the taxability of a “local telephone service” to turn on whether a service that
12 allows a customer to communicate using a telephonic quality connection adds additional services
13 or equipment beyond that connection.

14 Moreover, to hold that COBRA did not provide the privilege of telephonic quality
15 communication would create a strange result where telecommunication companies that used their
16 own network access servers to convert a phone signal to a data stream, like USA Choice and
17 Comcation, would have to pay the tax, but companies that relied on the local telephone company
18 to convert the signals for them, like WorldCom, would not. This appears at odds with the
19 statute’s intent for two reasons. First, whether a service is taxable would hinge on what
20 equipment the local telephone company provided, not the nature of the service. *See* S. Rep. No.
21 89-324, at 35; H.R. Rep. No. 89-433, at 30.

22 Second, when Congress enacted the 1965 Act it added the “private communications

1 service” exemption to the tax to avoid such a discrepancy in another context. *See* 26 U.S.C.

2 § 4252(d). As the Federal Circuit explained:

3 Congress enacted the private communication services exemption in order to correct the
4 competitive imbalance that had developed between telephone company-furnished services
5 and subscriber-owned equipment. Under the 1958 Excise Tax Technical Changes Act, a
6 subscriber to the telephone company’s Centrex or PBX systems (communication systems that
7 allowed both intrapremise and interpremise communication) was subjected to the federal
8 excise tax on his entire payment to the telephone company for service and equipment. But if
9 the subscriber purchased its intercom equipment outright from a communications equipment
10 manufacturer, the equipment was free of the federal excise tax. Because the telephone
11 companies were losing business to companies that provided telephone and microwave
12 equipment that could be purchased and operated by the users themselves, Congress created an
13 exemption to the excise tax on local telephone service.

14 *Trans-Lux Corp.*, 696 F.2d at 967 (citations omitted); *accord W. Elec. Co. v. United States*, 564
15 F.2d 53, 57 (Ct. Cl. 1977) (en banc); H.R. Rep. No. 89-433, at 30–31 (noting inequity of taxing
16 intercom services where telephone company owned equipment but not taxing substantially
17 identical service where subscriber owned equipment). The Debtors’ argument would create a
18 similar inequity here, despite the identical purpose and function of the systems, regardless of
19 ownership.

20 The Debtors also urge us to rely on the canon of statutory interpretation that any doubt as
21 to taxability should be resolved in favor of the taxpayer. That canon’s validity has been called
22 into question by both the Supreme Court and this Court. *White v. United States*, 305 U.S. 281,
23 292 (1938) (“We are not impressed by the argument that, as the question here decided is
24 doubtful, all doubts should be resolved in favor of the taxpayer.”); *Wolder v. Comm’r*, 493 F.2d
25 608, 611 n.4 (2d Cir. 1974). Because the other traditional tools of statutory interpretation lead us
26 to conclude that COBRA is taxable, we decline to rely on the canon here. *See Chickasaw Nation*
27 *v. United States*, 534 U.S. 84, 94 (2001) (“[C]anons are not mandatory rules. They are guides

1 that need not be conclusive.” (internal quotation marks omitted)).

2 It is somewhat odd to fit Internet technology into a statutory definition that has not been
3 updated since the Mad Men era. Although Congress frequently revised the communications
4 excise tax in the first half of the twentieth century to account for changing technology, the 1965
5 Act was intended to be the last iteration of the tax before it was phased out entirely by 1969. *See*
6 *Am. Bankers Ins. Grp.*, 408 F.3d at 1333. In light of this history, courts have refused to rewrite
7 the definition of “toll telephone service” to account for changes in how telephone companies
8 charge for long distance service. *See, e.g., id.* (“[I]f the statutory language no longer fits the
9 infrastructure of the industry, the IRS needs to ask for congressional action to bring the statute in
10 line with today’s reality. It cannot create an ambiguity that does not exist or misinterpret the
11 plain meaning of statutory language to bend an old law toward a new direction.” (quoting *Am.*
12 *Online*, 64 Fed. Cl. at 578)).

13 But although congressional clarity would make our inquiry easier, we cannot simply say
14 the statute is “too old” and decline to apply it to this newer technology. The reasoning in
15 *American Bankers* does not foreclose us from using the purpose of the statute to resolve an
16 ambiguity; it simply cautions us not create one where the language is clear. Unlike the toll
17 telephone service cases, there is an ambiguity in the definition of “local telephone service” that
18 we must address. And in interpreting Congress’s purpose at the time the statute was passed, we
19 find that the “privilege of telephonic quality communication” element of local telephone service
20 covers any service that makes use of the traditional telephone network for communication,
21 regardless of the form of the communication or whether the service also uses non-telephonic
22 technology to accomplish that communication. COBRA provided this privilege.

1 C. Communication with substantially all persons constituting a part of such local
2 telephone system

3 The district court also found in the alternative that because COBRA was merely an
4 “intermediate” step in connecting to the Internet, WorldCom could not use COBRA to
5 communicate with “substantially all persons” in the local telephone system. *See* 26 U.S.C.
6 § 4252(a)(1) (requiring “the privilege of telephonic quality communication with substantially all
7 persons having telephone or radio telephone stations constituting a part of such local telephone
8 system”). The COBRA system, in the district court’s view, was its own cocooned network, set
9 off from the local telephone system that the dial-up subscribers used. *See WorldCom IV*, 2011
10 WL 6434007, at *7 (holding the only communication within COBRA was “with and between the
11 equipment within the [telephone company’s] switch and [the network access server]”). We
12 disagree with the district court’s interpretation of this element of section 4252(a) and its
13 application to COBRA.

14 The portion of the statute that requires communication with “substantially all persons” in
15 a local telephone system is part of the “privilege” element of the definition—meaning that it
16 focuses on the capacity of the purchaser to communicate with “substantially all persons,” not
17 whether the purchaser actually does so. *See USA Choice II*, 522 F.3d at 1341–42 (holding ISP’s
18 decision to impose a password requirement for connecting to its servers did not deprive it of the
19 privilege to communicate with “substantially all persons” in the local telephone system). The
20 district court reasoned that because WorldCom’s network was only an intermediate step to the
21 Internet that connected dial-up users to ISPs, WorldCom could not “communicate” with the
22 dial-up users “as an intermediary sitting between any relationship of the end users and the [local
23 telephone companies] and ISPs.” *WorldCom IV*, 2011 WL 6434007, at *7. The district court

1 relied on the fact that in *USA Choice II*, “the suit was between the ISP and the I.R.S. The ISP
2 was not playing simply an intermediary role as the Debtors are here.” *Id.* at *5 n.3. According to
3 the district court, WorldCom’s intermediary role is “a critical distinguishing factor between the
4 COBRA service and the services at issue in [*USA Choice II* and *Comcation*].” *Id.* at *5.

5 But this ignores that WorldCom *chose* to resell the COBRA data stream to the ISPs. *See*
6 *WorldCom I*, 371 B.R. at 23–24 & n.1 (describing various WorldCom Internet networks, and
7 explaining that WorldCom used COBRA to resell access to smaller regional ISPs). The Debtors
8 cite nothing that prevented WorldCom from acting as an ISP. The district court’s reasoning falls
9 apart for substantially the same reasons as did the arguments in *USA Choice II* and *Comcation*: it
10 “ignore[s] evidence that these . . . restrictions relate solely to . . . self-imposed limitations.” *USA*
11 *Choice II*, 522 F.3d at 1341; *accord Comcation*, 78 Fed. Cl. at 65.

12 The district court also characterized COBRA as a self-contained service, and concluded
13 that “[t]here is no way for ‘substantially all persons’ within this service to access whatever
14 telephonic quality communication the [COBRA] PRI lines support.” *WorldCom IV*, 2011 WL
15 6434007, at *7. But this reasoning conflates the term “local telephone *service*” under section
16 4252(a) with the elements of section 4252(a), specifically “access” to a “local telephone *system*”
17 and communication with “substantially all persons” in that “local telephone *system*.” COBRA
18 provided “the privilege of telephonic quality communication with substantially all persons” in
19 the local telephone system because all of the local telephone company’s customers could call the
20 COBRA number and could communicate with WorldCom’s network through the use of a
21 modem. Because COBRA connected WorldCom to the local telephone system, it provided
22 WorldCom with “access” to that system. And because it allowed any dial-up user within that

1 system to call the COBRA number and communicate with WorldCom’s network, it also provided
2 the privilege of telephonic quality communication with “substantially all persons” within that
3 local telephone system. This is all the statute requires; the “local telephone service” and the
4 “local telephone system” do not have to be one and the same.

5 *II. Private Communications Service*

6 Finally, although not addressed by either the bankruptcy or district courts, the Debtors
7 argue that we can affirm the judgment on the alternative ground that COBRA was exempt from
8 taxation as a “private communication service” pursuant to 26 U.S.C. § 4252(d)(1). *See ACEquip*
9 *Ltd. v. Am. Eng’g Corp.*, 315 F.3d 151, 155 (2d Cir. 2003) (noting that we may affirm on any
10 ground appearing in the record). A private communication service is defined in relevant part as:

11 (1) the communication service furnished to a subscriber which entitles the subscriber—

12 (A) to exclusive or priority use of any communication channel or groups of channels, . . .
13 regardless of whether such channel, groups of channels, or intercommunication system
14 may be connected through switching with a [local telephone service],

15 . . . except that such term does not include any communication service unless a separate
16 charge is made for such service.

17 26 U.S.C. § 4252(d). The Debtors contend that WorldCom had exclusive use of the data stream
18 leading from the network access server to WorldCom’s network. WorldCom paid separately for
19 COBRA service; this payment was not comingled with any other service. Therefore, according
20 to the Debtors, WorldCom purchased a private communication service akin to an exclusive
21 intercom system, which the Court of Claims has held to be non-taxable. *See W. Elec. Co.*, 564
22 F.2d at 66.

23 This argument is meritless. First, we do not think that COBRA constitutes a distinct
24 “communications service” that is separate from the local telephone system. *See USA Choice II*,

1 522 F.3d at 1344 (holding exception “requires that the system at issue provide a ‘communication
2 service’ beyond that of mere local telephone service, not just connectivity to the local telephone
3 system *itself*,” and finding that PRI lines are not a service separate from the local telephone
4 system); *accord Comcaton*, 78 Fed. Cl. at 73–75; *see also* H.R. Rep. No. 89-433, at 31
5 (“Centrex systems—where the switching equipment is generally on the premises of the local
6 exchange rather than on that of the subscriber—generally do not . . . provide for a charge which
7 is separate and distinct from that for the local telephone service.”); *accord* S. Rep. No. 89-324, at
8 35. Second, even assuming COBRA were a separate communications service, the Debtors
9 cannot show that WorldCom was entitled to “exclusive or priority” use of the channel. Anyone
10 connected to the public telephone network could dial in to utilize COBRA’s dedicated PRI lines
11 (and connect to the Internet). *See USA Choice II*, 522 F.3d at 1346. *But see id.* at 1347–48 (Dyk,
12 *J.*, concurring in part and dissenting in part) (arguing that USA Choice did have exclusive or
13 priority use, but agreeing that service was not a distinct “communication service”). The
14 exception does not apply.

15 CONCLUSION

16 Accordingly, the judgment of the district court is **REVERSED**, and the case is
17 **REMANDED** for further proceedings consistent with this Opinion.