

This rule was adopted on December 16, 2008 and becomes effective January 16, 2009. It may be used to determine tax liability on and after the effective date, until the codified version is available from the code reviser's office.

NEW SECTION

**WAC 458-20-15501 Computer hardware, computer software, information service, and computer services. (1) Introduction.** This section explains the business and occupation (B&O), retail sales, and use tax treatment of activities related to computer hardware, computer software, information service, and computer services. Such activities include, but are not limited to, selling, leasing, manufacturing, installing, repairing, and maintaining computer hardware and software, as well as developing, duplicating, configuring, licensing, downloading, and accessing computer software.

This section contains examples that identify a number of facts and then state a conclusion. The examples should be used only as a general guide. The tax results in all situations must be determined after a review of all facts and circumstances.

The information provided in this section is divided into five parts:

(a) Part I provides information on taxation of computer systems.

(b) Part II provides information on taxation of computer hardware.

(c) Part III provides information on taxation of computer software.

(d) Part IV provides information on taxation of information services and computer services.

(e) Part V provides reference to WAC 458-20-155 (Information and computer services) on the distinction between sales of products and sales of services.

**PART I - TAXATION OF COMPUTER SYSTEM**

**(101) Taxation of computer systems.**

(a) **What is a computer?** A "computer" is an electronic device that accepts information in digital or similar form and manipulates it for a result based on a sequence of instructions. RCW 82.04.215. Examples of a computer include, but are not limited to, mainframe computer, laptop, workstation, and desktop computer. "Computer" also includes automatic data processing equipment, which is a computer used for data processing purposes. "Computer" does not include any computer software or

peripheral devices.

(b) **Computer systems and computer networks distinguished.** A "computer system" is a functional unit, consisting of one computer and associated computer software, whereas a computer network is two or more computers and associated computer software that uses common storage. A computer system may or may not include peripheral devices.

(c) **Wholesale sale of computer systems.** Gross proceeds of sales of computer systems to persons other than consumers (e.g., sales for resale without intervening use) are subject to B&O tax under the wholesaling classification. To verify the wholesale nature of the sale, the seller should obtain a resale certificate from the buyer as provided by WAC 458-20-102 (Resale certificates).

(d) **Retail sale of computer systems.** Gross proceeds of sales of computer systems to consumers are subject to B&O tax under the retailing classification. Persons making retail sales are responsible for collecting retail sales tax at the time of sale and remitting the tax to the department, unless the sale is specifically exempt by law. If the seller is required to collect Washington sales tax (such as in the case of the seller having nexus with Washington), but does not collect Washington sales tax, the buyer is responsible for remitting retail sales tax (commonly referred to as deferred sales tax), unless the sale is specifically exempt by law. If the seller is not required to collect Washington sales tax, then the buyer is responsible for remitting use tax, unless the transaction is specifically exempt by law. Separately stated charges for custom software sold with the computer system are subject to service B&O tax. See subsection (302) of this section

(e) **Manufacturing of computer systems.** Persons manufacturing computer systems are subject to manufacturing B&O tax upon the value of the products. See WAC 458-20-112 (Value of products) and 458-20-136 (Manufacturing, processing for hire, fabricating). Manufacturers of computer systems who sell their products at retail or wholesale are also subject to either the retailing or wholesaling B&O tax, as the case may be. In such cases the manufacturer must report under both the "production" (manufacturing) and "selling" (wholesaling or retailing) B&O tax classifications and may claim a multiple activities tax credit (MATC). See WAC 458-20-19301 (Multiple activities tax credits) for detailed information about the MATC.

(i) Separately stated charges for custom programming sold with the computer system are not subject to manufacturing B&O tax, but are subject to service B&O tax. See subsection (302) of this section.

(ii) Separately stated charges for computer software sold and installed after the sale of a computer system are not subject to manufacturing B&O tax.

(iii) The combining of a computer system with certain peripheral devices is considered a packaging activity not subject to manufacturing B&O tax, when the following occurs:

(A) The peripheral devices remain in the original packaging;

(B) The person does not attach its own label to the peripheral devices;

(C) The person maintains a separate inventory of the peripheral devices for sale apart from the sale of the computer system; and

(D) The charge for the sale of peripheral devices is separately stated from the charge for the sale of computer systems.

(102) **Examples.**

(a) ABC Computers, Inc., an in-state manufacturer, manufactures and sells at retail computer systems. ABC sells a computer system to Steve for one flat charge. The computer system includes a disk drive, memory, CPU, keyboard, mouse, monitor, and bundled prewritten computer software. ABC is subject to retailing B&O tax and must collect retail sales tax on the sale to Steve. In addition, ABC is subject to manufacturing B&O tax on the value of the product sold (which is generally the sales price). ABC is entitled to claim a multiple activities tax credit.

(b) ADE Computers, Inc., manufactures and sells computer systems at retail to customers. ADE sells to Julie a computer system with certain peripheral devices at separate charges. The computer system without the peripheral devices consists of a disk drive, memory, CPU, and bundled prewritten computer software. The peripheral devices include a keyboard, mouse, and monitor. All peripheral devices remain in the original packaging of the manufacturers. ADE does not attach its own label to the peripheral devices. Finally, ADE maintains a separate inventory of the peripheral devices for sale apart from the sale of ADE's computer systems. ADE is subject to retailing B&O tax and must collect retail sales tax from Julie on the sales of the computer system including the peripheral devices. ADE is subject to manufacturing B&O tax on the value of the computer system excluding the peripheral devices. ADE is entitled to claim a multiple activities tax credit. ADE is not subject to manufacturing B&O tax on the value of the peripheral devices, because the combining of a computer system with the peripheral devices in this case constitutes packaging activities.

(c) AFG Computers, Inc., an in-state company, manufactures and sells at retail computer systems. AFG sells a computer system to Joe for a lump sum. Joe purchases from AFG, as part of the sales package, prewritten computer software developed by a third-party software developer. AFG installs the prewritten

computer software to Joe's computer. AFG is subject to retailing B&O tax and must collect retail sales tax from Joe on the sale of the computer system, including the bundled prewritten computer software. Also, AFG is subject to manufacturing B&O tax on the value of the computer system, including the value of the prewritten computer software. AFG is entitled to claim a multiple activities tax credit.

(d) Same facts as (c) of this subsection, except that AFG sells and installs the prewritten computer software after Joe purchases and takes possession of the computer system. AFG is subject to retailing B&O tax and must collect retail sales tax from Joe on the sale of the computer system and the prewritten computer software. Also, AFG is subject to manufacturing B&O tax on the value of the computer system. AFG is entitled to claim a multiple activities tax credit. AFG is not subject to manufacturing B&O tax on the value of the prewritten computer software, because the installation of the software by AFG is not a part of AFG's manufacturing activity.

## **PART II - TAXATION OF COMPUTER HARDWARE**

### **(201) Taxation of computer hardware, both internal and external peripheral devices.**

(a) **What is computer hardware?** For purposes of this section, "computer hardware" includes, but is not limited to, the mechanical, magnetic, electronic, or electrical components of a computer system such as towers, motherboards, central processing units (CPU), hard disk drives, memory, as well as internal and external peripheral devices such as compact disk read-only memory (CD-ROM) drives, compact disk rewriteable (CD-RW) drives, zip drives, internal and external modems, wireless fidelity (Wi-Fi) devices, floppy disks, compact disks (CDs), digital versatile disks (DVDs), cables, mice, keyboards, printers, monitors, scanners, web cameras, speakers, and microphones.

(b) **Wholesale sale of computer hardware.** Gross proceeds of sales of computer hardware to persons other than consumers (e.g., sales for resale without intervening use) are subject to B&O tax under the wholesaling classification. To verify the wholesale nature of the sale, the seller should obtain a resale certificate from the buyer as provided by WAC 458-20-102 (Resale certificates).

(c) **Retail sale of computer hardware.** Gross proceeds of sales of computer hardware to consumers are subject to B&O tax under the retailing classification. Persons making retail sales are responsible for collecting retail sales tax at the time of sale and remitting the tax to the department, unless the sale is specifically exempt by law.

(d) **Manufacturing of computer hardware.** Persons

manufacturing computer hardware are subject to manufacturing B&O tax upon the value of the products. See WAC 458-20-112 (Value of products) and 458-20-136 (Manufacturing, processing for hire, fabricating). Manufacturers of computer hardware who sell their products at retail or wholesale are also subject to either the retailing or wholesaling B&O tax, as the case may be. In such cases the manufacturer must report under both the "production" (manufacturing) and "selling" (wholesaling or retailing) B&O tax classifications and may claim a multiple activities tax credit (MATC). See WAC 458-20-19301 (Multiple activities tax credits) for detailed information about the MATC.

(202) **Examples.**

(a) ALM Computers, Inc., purchases used computers. ALM replaces a built-in CD-ROM drive with a CD-RW drive and adds a zip drive, additional memory, and an upgraded CPU. ALM is engaged in manufacturing activity subject to manufacturing B&O tax with respect to that computer.

(b) AJK Computers, Inc., acquires damaged computers for refurbishment and sale. AJK removes damaged hardware components and replaces them with new components without upgrading these components. Refurbishing computers in this manner is not a manufacturing activity. Retail sales of such refurbished computers are subject to retailing B&O tax and retail sales tax.

(c) APQ Computers, Inc., purchases computers for refurbishment and sale. APQ replaces the failed zip drive on one of the computers with an upgraded zip drive because the upgrade is the nearest version of the failed component that is available. The manufacturer has discontinued manufacturing the original version of the zip drive because of a flaw in the design. APQ is not engaged in manufacturing activity with respect to that computer. Retail sale of that refurbished computer is subject to retailing B&O tax and retail sales tax.

(d) ATV Computers, Inc., is hired by a call center company to repair damaged computers. ATV removes damaged hardware components and replaces them with new components without upgrading these components. Refurbishing computers in this manner is not a manufacturing activity; however, it is a retail service. Refurbishing computers in this manner is subject to retailing B&O tax and retail sales tax must be collected. See WAC 458-20-173 (services on tangible personal property) for more information on repairs and maintenance.

(203) **Taxation of other activities associated with computer hardware.**

(a) **Installing computer hardware.** Gross proceeds of sales for installing computer hardware are subject to wholesaling or retailing B&O tax, as the case may be. Installation of computer hardware for consumers is subject to retail sales tax. See WAC 458-20-145 (sourcing) for more information on sourcing retail sales of computer services. See WAC 458-20-173 (services on

tangible personal property) for more information on installations.

(b) **Repairing or maintaining computer hardware.** Gross proceeds of sales for repair or maintenance of computer hardware are subject to wholesaling or retailing B&O tax. Repair of computer hardware for consumers is subject to retail sales tax. See WAC 458-20-145 (sourcing) for more information on sourcing retail sales. See WAC 458-20-173 (services on tangible personal property) for more information on repairs and maintenance. Also, see WAC 458-20-257 (Warranties and maintenance agreements) for information about repair performed as part of a warranty or maintenance agreement.

### **PART III - TAXATION OF COMPUTER SOFTWARE**

(301) **What is computer software?** RCW 82.04.215 provides that "computer software" is a set of coded instructions designed to cause a computer or automatic data processing equipment to perform a task. All software is classified as either prewritten or custom. "Computer software" includes only those sets of coded instructions intended for use by an end user and specifically excludes retained rights in software and master copies of software. Computer software does not include data.

(a) **How is computer software delivered?** Computer software may be delivered either by intangible means such as electronically or by tangible means such as tangible storage media.

(b) **What is automatic data processing equipment?** "Automatic data processing equipment" includes computers used for data processing purposes and their peripheral equipment.

(c) **What are retained rights?** "Retained rights" means any and all rights, including intellectual property rights such as those rights arising from copyrights, patents, and trade secret laws, that are owned or are held under contract or license by a software developer, author, inventor, publisher, licensor, sublicensor, or distributor. RCW 82.04.215.

(d) **What are master copies of software?** "Master copies" of software means copies of software from which a software developer, author, inventor, publisher, licensor, sublicensor, or distributor makes copies for sale or license. RCW 82.04.215.

(i) **Development of a master copy of software.** Development of a master copy of software by a software developer, or a third party hired by the software developer, that is used to produce copies of software for sale or commercial or industrial use, is not a manufacturing activity. A third-party charge for development of a master copy of software is a charge for custom software development and is subject to service and other activities B&O tax.

(ii) **Use of prewritten computer software by software**

**developer.** The internal use of prewritten computer software by the developer of that software is not subject to use tax because the software developer is not an end user of its own internally developed software. For example, VV Software, Inc., an in-state software developer, creates accounting software generally used by small businesses. VV plans to sell its newly created software to other companies. VV also plans to make a copy of this software and use it for its accounting operation. The copy of software used by VV for its accounting operation is not subject to use tax.

(302) **What is custom software?** "Custom software" is software created for a single person. RCW 82.04.215. The use of library files in software development does not preclude such software from being characterized as custom software, as long as the software is created for a single person. The nature of custom software does not change when ownership is transferred to a person with no rights retained by the transferor.

For purposes of this section, "library files" are a collection of precompiled and frequently used routines that a software developer can use in developing the software.

(a) **Creation of custom software.** Gross income received for creating custom software is subject to service and other activities B&O tax.

(b) **Duplication of custom software.** Duplication of custom software for the same person, or by the same person for the person's own use, does not change the character of the custom software. RCW 82.04.29001. Duplication of custom software for the same person, or by the same person for its own use, is not subject to manufacturing B&O tax.

If a person duplicates custom software for sale to or use by another person other than the original purchaser, the software becomes prewritten computer software as defined in subsection (303) of this section and is subject to manufacturing B&O tax if the prewritten computer software is delivered by tangible storage media.

(c) **Sale of custom software.** If custom software is sold to another person other than the original purchaser, the software loses its character as custom software and becomes prewritten computer software as defined in subsection (303) of this section.

(d) **Use of custom software.** Use of custom software is not subject to use tax.

(e) **Example.** PFC, Inc., offers data base management software on-line to its client through remote access for a monthly fee. PFC developed its software for the specific client and stored the software on its server. PFC is not subject to manufacturing B&O tax or use tax because the data base management software is custom software. PFC's income from the sale of the custom software to the one specific client is

subject to service and other activities B&O tax. Additionally, income received for client access and use of the software is subject to service and other activities B&O tax. PFC is hosting its own software for client access and use. See subsection (401)(g) of this section for treatment of gross income received for providing remote access to software applications such as an ASP provides.

(303) **What is prewritten computer software?** RCW 82.04.215 provides that "prewritten computer software" is computer software, including prewritten upgrades, that is not designed and developed by the author or other creator to the specifications of a specific purchaser.

The combining of two or more prewritten computer software programs or prewritten portions thereof does not result in custom software. Configuration of prewritten computer software to work with other computer software does constitute customization of prewritten computer software.

Prewritten computer software includes software designed and developed by the author or other creator to the specifications of a specific purchaser when it is sold to a person other than such purchaser.

Where a person, who is not the author or creator, modifies or enhances prewritten computer software, that person is deemed to be the author or creator only of the modifications or enhancements made. Prewritten computer software, or a portion thereof, that is modified or enhanced to any degree, remains prewritten computer software, even though the modification or enhancement is designed and developed to the specifications of a specific purchaser. Where there is a reasonable, separately stated charge or an invoice or other statement of the price given to the purchaser for the modification or enhancement, the modification or enhancement will not be considered prewritten computer software.

(a) **Wholesale sales of prewritten computer software.** Gross proceeds from sales of prewritten computer software to persons other than consumers (e.g., sales for resale without intervening use) are subject to B&O tax under the wholesaling classification, whether or not ownership or title passes to the buyer, and regardless of any express or implied restrictions upon the buyer. The method of delivery of prewritten computer software does not alter the wholesale nature of the transaction, whether it is through tangible storage media or any electronic means. Delivery of software manuals and backup copies of prewritten computer software does not alter the delivery of the actual copy of prewritten computer software to be used by the buyer in determining when and where the sale takes place. To verify the wholesale nature of the sale, the seller obtains a resale certificate from the buyer as provided by WAC 458-20-102 (Resale certificates).

(i) **Distinction between wholesale sales of prewritten computer software and royalties received for the licensing of prewritten computer software.** Sales of prewritten computer software constitute wholesale sales if the reseller, who has no right to reproduce the software for further sales, sells the same software to its customers. The true object of the sale to the reseller is the sale of the software. On the other hand, income received for granting an intangible right to reproduce and distribute copies of prewritten computer software for sale constitutes royalties. The true object of the transaction that generates royalty income is the right to reproduce and relicense the software. See subsection (308) of this section for more information on royalties.

(ii) **Examples.** The examples presume sellers have nexus with Washington.

(A) UM Computers, Inc., is a software developer that develops engineering software. UM sells the prewritten computer software at wholesale to OX Computers, Inc., in shrink-wrapped packages. UM delivers the software to OX. OX then resells the software to customers in the same shrink-wrapped packages. Sales of prewritten computer software by UM are subject to wholesaling B&O tax. Sales by OX to consumers are retail sales subject to retailing B&O tax and retail sales tax.

(B) GB Computers, Inc., is a software developer that develops engineering software. GB grants SE Computers, Inc., the right to reproduce and distribute copies of the prewritten computer software for sale. GB retains all of its ownership rights to the software and delivers one copy of the software to SE to reproduce. Amounts received from GB granting the right to reproduce and distribute prewritten computer software to SE are subject to royalties B&O tax. Sales by SE to consumers are retail sales subject to retailing B&O tax and retail sales tax.

(C) DH Computers, Inc., is a software developer that develops engineering software. DH grants the right to sell its engineering prewritten computer software to WK Computers, Inc. DH delivers the software electronically to WK. WK then sells the software to its customers, who download the software from WK. Income to DH is subject to royalties B&O tax. Sales of prewritten computer software by WK to its customers are retail sales subject to retail sales tax.

(D) AJ Soft, Inc., is a software developer of architectural drafting software. AJ Soft enters into an agreement with DJ Sales, Inc., to sell AJ Soft's drafting software. DJ Sales must pay a fee for each copy DJ Sales sells through its web site. AJ Soft does not allow DJ Sales to reproduce the drafting software. Customers download the software, but are unaware the software is downloaded directly from AJ Soft. AJ Soft is making a wholesale sale of software to DJ Sales subject to wholesaling B&O tax. DJ Sales is making a retail sale to its Washington customers

subject to retail sales tax.

(b) **Retail sales of prewritten computer software.** Gross proceeds of sales of prewritten computer software to consumers are subject to B&O tax under the retailing classification, whether or not ownership or title passes to the buyer, and regardless of any express or implied restrictions upon the buyer. The method of delivery of prewritten computer software does not alter the retail nature of the transaction, whether it is through tangible storage media or any electronic means. Delivery of software manuals and backup copies of prewritten computer software does not alter the delivery of the actual copy of prewritten computer software to be used by the buyer in determining when and where the sale takes place. Persons making retail sales are responsible for collecting retail sales tax at the time of sale and remitting the tax to the department, unless the sale is specifically exempt by law.

(c) **Use of prewritten computer software.** Prewritten computer software, regardless of the method of delivery, is generally subject to use tax upon use in this state if Washington retail sales tax was not previously paid. However, use of prewritten computer software is not taxable, if it is provided free of charge, or if it is provided for temporary use in viewing information, or both. RCW 82.12.020. This exception from use tax is limited to prewritten computer software provided free of charge or for temporary use in viewing information, such as free promotional software, donated software, free download of software, and software provided in beta testing to a third party free of charge.

For purposes of this use tax exception, "beta testing" means the last stage of testing for prewritten computer software prior to its commercial release including the release to manufacturing (RTM). Beta testing may involve sending the software to a third party for the use of the third party. Beta testing is often preceded by a round of testing called alpha testing.

(i) **Example.** DS Computers, Inc., is a software developer. In order to perform beta testing of its new accounting software prior to commercial release, DS sends a copy of the software free of charge to KG Technologies, Inc. DS is not subject to use tax for the release of the beta software to KG. KG is not subject to use tax for the use of beta software free of charge.

(ii) **Example.** DH, Inc., provides free card games on-line to its customers. The customers, however, must download DH's free software in order to be able to play card games on-line at DH's web site. Wendy downloads the software free of charge. Wendy is not subject to use tax for the use of the software.

(iii) **Example.** DW, Inc., provides free software to the public for anyone to watch videos on-line. Roger downloads the software free of charge. Roger is not subject to use tax for

the use of the software.

(d) **Manufacturing of prewritten computer software.** Persons engaged in manufacturing prewritten computer software are subject to manufacturing B&O tax upon the value of the products. See WAC 458-20-112 (Value of products) and WAC 458-20-136 (Manufacturing, processing for hire, fabricating). Manufacturers of prewritten computer software who sell their products at retail or wholesale are also subject to either the retailing or wholesaling B&O tax, as the case may be. In such cases the manufacturer must report under both the "production" (manufacturing) and "selling" (wholesaling or retailing) B&O tax classifications and may claim a multiple activities tax credit (MATC). See WAC 458-20-19301 (Multiple activities tax credits) for detailed information about the MATC.

(e) **Duplication of prewritten computer software.** Duplication of prewritten computer software for sales to or use by more than one person is subject to manufacturing B&O tax upon the value of products. Duplication of prewritten computer software outside this state is not subject to manufacturing B&O tax regardless of where software development takes place.

Duplication of prewritten computer software is a manufacturing activity only if the prewritten computer software is delivered from the seller to the purchaser by means of tangible storage media which is retained by the purchaser. RCW 82.04.120.

When a software developer contracts with a third party to duplicate prewritten computer software, the parties must take into account the value of all tangible and intangible materials or ingredients, including the software code, when determining the relative value of all materials or ingredients furnished by each party. If the third party furnishes less than twenty percent of the total value of all materials or ingredients that become a part of the produced product, then the third party is presumed to be a processor for hire and the software developer is presumed to be a manufacturer. See WAC 458-20-136 (Manufacturing, processing for hire, fabricating) for more information.

(304) **Site license of prewritten computer software.** A site license provides a consumer acquiring prewritten computer software with the right to duplicate prewritten computer software for use on its own computers, based on the number of computers, the number of workers using the computers, or some other criteria. A site license agreement may cover one site or multiple sites of a purchaser.

(a) **Retail sales of a site license.** Gross proceeds of sales of a site license to a consumer are subject to B&O tax under the retailing classification, whether or not ownership or title passes to the consumer, and regardless of any express or implied restrictions upon the consumer. Delivery occurs when

and where the prewritten computer software subject to the site license is received by the consumer, whether it is through tangible storage media or any electronic means, regardless of the method of delivery. See WAC 458-20-145 (sourcing) for more information on sourcing prewritten computer software. See also WAC 458-20-197 (When tax liability arises) and WAC 458-20-199 (Accounting methods) for details regarding reporting procedures and revenue recognition of retail sales of a site license. Delivery of software manuals and backup copies of prewritten computer software does not alter the delivery of the actual copy of prewritten computer software to be used by the consumer in determining when and where the sale takes place. Persons making retail sales are responsible for collecting retail sales tax at the time of sale and remitting the tax to the department, unless the sale is specifically exempt by law.

If the prewritten software is hosted by the licensor or a third party for remote access by the licensee (e.g., an Application Service Provider (ASP)), then see subsection (401)(g) of this section.

**(b) Duplication of prewritten computer software by a person under a site license.** A seller of a site license is subject to manufacturing B&O tax for its own duplication of prewritten computer software. Duplication of prewritten computer software is subject to manufacturing B&O tax only if the prewritten computer software is delivered from the seller to the purchaser by means of tangible storage media which is retained by the purchaser. RCW 82.04.120. Purchaser of a site license is not subject to manufacturing B&O tax for the duplication of prewritten computer software for its own use, pursuant to a site license agreement with the seller.

**(c) Use of a site license partly in this state and partly outside this state.** Where the use of a site license is partly in this state and partly outside this state, the part of the site license used by the person in this state is subject to use tax, provided Washington state sales tax was not previously paid. For example, a person purchases and takes delivery of a site license in California. Pursuant to the multiple site license agreement, this person is licensed to use one thousand copies of prewritten computer software, of which four hundred copies will be used in Washington. Use tax is due on the four hundred copies of prewritten computer software used in this state. If the prewritten software purchased by the licensee is delivered in Washington, then the entire charge for the site license is subject to retail sales tax if purchased from a seller responsible for collecting Washington's sales tax.

**(d) Sales and use of additional copies of prewritten computer software under the same site license.** In some cases, the buyer of a site license may subsequently purchase additional copies of prewritten computer software under the same site

license agreement. The seller may or may not deliver any additional copy of the software to the buyer, because the original copy of the software has already been delivered.

(i) **Retail sales of additional copies of prewritten computer software under the same site license.** Retail sales of the additional copies of software occurs when and where the seller delivers any additional copy of prewritten computer software to the buyer, whether it is through tangible storage media or any electronic means, regardless of the method of delivery. See WAC 458-20-145 (sourcing) for more information on sourcing retail sales of prewritten computer software. If the seller does not deliver any additional copy of the software to the buyer, then the sales occur when the sales agreements are made to purchase the additional copies and where the original copy or copies of prewritten computer software was delivered. If the original sale of the site license was subject to manufacturing B&O tax, then the sale of additional licenses are also subject to manufacturing B&O tax.

Delivery of software manuals and backup copies of prewritten computer software does not alter the delivery of the actual copy of prewritten computer software to be used by the buyer in determining when and where the sale takes place.

(ii) **Use of additional copies of prewritten computer software under the same site license.** Where the use of the additional copies of software is partly in this state and partly outside this state and was not previously subject to Washington sales tax, the part of the additional copies of software used by the person in this state is subject to use tax.

(e) **Examples.**

(i) DEF Computers, Inc., is located in Washington and sells in this state at retail a multiple site license of its prewritten computer software to P's Design, Inc. A copy of the prewritten computer software is electronically delivered to P's Design in Washington. P's Design then electronically duplicates the software and distributes the software in Washington and several other states for its use. Neither DEF nor P's Design is subject to manufacturing B&O tax. DEF, however, is subject to retailing B&O tax, and it must collect retail sales tax from P's Design for the entire sale of the software.

(ii) Same facts as (e)(i) of this subsection, except that in addition, DEF delivers a backup copy of the software to P's Design outside Washington. The backup copy of the software is for disaster recovery purposes and is not downloaded to any of P's Design's computers for use. There is no separate charge for the delivery of the backup software. The software manuals are mailed to P's Design in Washington. DEF is still subject to retailing B&O tax, and it must collect retail sales tax from P's Design for the entire sale of the software. Delivery of the software manuals and the backup copy of the software are not

relevant in determining when and where the sale takes place. This transaction is not subject to manufacturing B&O tax.

(iii) Same facts as (e)(i) of this subsection, except that in addition, P's Design subsequently purchases 50 additional copies of the software from DEF under the same site license agreement. P's Design merges with another company, and the additional copies are needed for the use of its new employees. No additional copy of the software is delivered to P's Design in fulfilling this new agreement. Neither DEF nor P's Design is subject to manufacturing B&O tax. DEF, however, is subject to retailing B&O tax, and it must collect retail sales tax from P's Design for the subsequent sale of the 50 additional copies of software because the original copy of the software was delivered in Washington. However, if the original sale of the license had included delivery of the prewritten software by a tangible storage device (and was therefore subject to manufacturing B&O tax), then the licensor is also subject to manufacturing B&O tax based on the value of the additional licenses.

(iv) GH Computers, Inc., sells at retail a multiple site license of its prewritten computer software to Quick, Inc. GH is located outside Washington, while Quick is located in Washington and in other states and outside the U.S. The desktop software is licensed on an unlimited basis, which means that there are no restrictions of its use by Quick. The software is delivered to Quick outside Washington. Quick then electronically duplicates the software and distributes the software to all of its 500 employees, of which 100 employees are located in Washington. The software is electronically downloaded into the desktop computers of all employees and is immediately put into use. Use tax is due on the value of the 100 copies of prewritten computer software used in Washington.

(v) Same facts as (e)(iv) of this subsection, except that under the original site license agreement, Quick is entitled to reproduce, distribute, and use up to 500 copies of the desktop software. Then Quick merges with another company, and additional copies are needed for the use of its new employees. Quick, therefore, subsequently purchases 100 additional copies of the software from GH under the same site license agreement. No additional copy of the software is delivered to Quick in fulfilling this new agreement. Quick distributes the additional copies of the software to its 100 new employees, of which 50 employees are located in Washington. Use tax is due on the value of the 50 additional copies of prewritten computer software used in Washington.

(vi) JJ Computers, Inc., sells at retail a multiple site license of its prewritten computer (server) software to Rest, Inc. JJ is located outside Washington, but Rest is located in Washington and in other states. The server software is delivered to Rest outside Washington. Rest then electronically

duplicates the software and distributes the software to its three servers for immediate use. One of the servers is located in Washington, and the other two servers are located outside Washington. Use tax is due on the value of the copy of the prewritten computer (server) software on the server in Washington.

(305) **Key to activate computer software.** A key, or an enabling or activating code, may be required in some instances to activate computer software and put the software into use, and the key may be delivered to a purchaser after the software is already delivered and in possession of the same purchaser. In such instances, the entire sale of computer software occurs when both the key and the software are delivered to the purchaser. The sale takes place where the software is received by the purchaser in accordance with RCW 82.32.730. However, if the receiving location for the software is unavailable to the vendor because the software was delivered by a third party, then the sale takes place where the key is received in accordance with RCW 82.32.730. There is no separate sale of the key from the software, regardless of how such sale may be characterized by the vendor or by the purchaser.

See subsection (304) of this section for more information if a site license of prewritten computer software is involved. If the sale of the prewritten software is subject to manufacturing B&O tax, then the sale of the key required by that prewritten software is also subject to manufacturing B&O tax. The income from the sale of a key is part of a sale of prewritten computer software, whether the sales transactions are together or separate.

(a) **Example.** JKL Computers, Inc., an in-state business, sells at retail prewritten computer software to Rebecca. JKL delivers the software to Rebecca in this state. The prewritten computer software, however, cannot be activated without a key. JKL subsequently delivers the key in this state to Rebecca for a separate price. JKL is subject to retailing B&O tax, and it must collect retail sales tax from Rebecca on the entire sale of the software including the separate charge for the key. The entire sale takes place in this state (where the software is delivered) when both the software and the key are delivered to Rebecca. There is no separate sale of the key, regardless of the fact that JKL delivers the key to Rebecca for a separate charge.

(b) **Example.** Same facts as (a) of this subsection, except that JKL subsequently delivers the key outside this state to Rebecca for a separate price. JKL is subject to retailing B&O tax, and it must collect retail sales tax from Rebecca on the entire sale of the software including the separate charge for the key. The entire sale takes place in this state (where the software is delivered) when both the software and the key are

delivered to Rebecca. There is no separate sale of the key, regardless of the fact that JKL delivers the key to Rebecca for a separate charge.

(c) **Example.** MNO Computers, Inc., is an in-state software developer. TKO Computers, Inc., an out-of-state original equipment manufacturer (OEM), agrees in contract with MNO to distribute MNO's prewritten computer software. TKO delivers MNO's inoperable software to Sally as part of the sale of the computer system. Sally, however, must purchase a key directly from MNO in order to activate and use the software. MNO has no knowledge of where the software was initially delivered to Sally, but MNO knows that the key is delivered to Sally in this state. MNO is subject to retailing B&O tax, and it must collect retail sales tax from Sally on the entire sale of the key and the inoperable software. The entire sale takes place in this state because the key is delivered in this state and MNO has no knowledge of where the inoperable software was initially delivered by TKO. Assuming TKO delivers MNO's software to Sally electronically, then duplication of the key would not be subject to manufacturing B&O tax. If TKO delivers the software on tangible storage media, then the key would be subject to manufacturing B&O tax.

(306) **Client access license and server license for the server software.** A server license, paid for at the time the server software is purchased, grants the buyer the right to install the server software on the buyer's server. A client access license (CAL) grants the buyer the right to access the server software. The CAL is not computer software and is not downloaded into the buyer's computer.

Charges for server licenses and CAL are a part of the sale of the server software, even if the charges are separately stated. The sales take place where the server software is delivered to the buyer.

In cases where server software is delivered to the buyer and used in multiple locations, see subsection (304) of this section on site licenses for more information.

(a) **Example.** ZZ Computers, Inc., an in-state business, sells at retail server software to Jack. ZZ delivers the server software to Jack in Washington. ZZ also provides Jack with client access licenses allowing Jack the right to access the server software from his personal computers. The sale of server software to Jack is subject to retailing B&O tax, and ZZ must collect retail sales tax from Jack for the same sale.

(b) **Example.** Same facts as (a) of this subsection, except that ZZ makes two separate sales at retail of two types of prewritten computer software to Jack. One is server software, and the other is client software (which is different from client access licenses). ZZ delivers the server software to Jack in Washington where Jack's server is located. ZZ delivers the

client software to Jack outside Washington where all of Jack's personal computers are located. Only the sale of server software to Jack is subject to retailing B&O tax, and ZZ must collect retail sales tax from Jack for the same sale.

**(307) Other activities associated with computer software.**

**(a) Customizing prewritten computer software.** Gross income received for customizing prewritten computer software is subject to service and other activities B&O tax. RCW 82.04.29001.

**(i) What is customizing prewritten computer software?** RCW 82.04.215 provides that "customization of prewritten computer software" is any alteration, modification, or development of applications using or incorporating prewritten computer software for a specific person.

"Customization of prewritten computer software" includes individualized configuration of software to work with other software and computer hardware but does not include routine installation. Customization of prewritten computer software does not change the underlying character or taxability of the original prewritten computer software.

**(ii) Combined charge for prewritten computer software, customization, and routine installation.** If a lump-sum charge is made for a sale of prewritten computer software, customization of prewritten computer software, and routine installation, the entire charge is considered to be a sale of prewritten computer software. See (a)(iv) of this subsection for more information on routine installation.

**(iii) Separately stated charge for customization of prewritten computer software.** Where there is a reasonable separately stated charge on an invoice or other statement of the price given to the purchaser for customization of prewritten computer software (including installation that is not routine, see (a)(i) of this subsection), such customization is subject to service and other activities B&O tax. If a charge for customization of prewritten computer software is not separately stated from a sale of prewritten computer software, the entire charge is considered a sale of prewritten computer software.

**(iv) Customization of prewritten computer software versus routine installation.** Customization of prewritten computer software does not include routine installation. "Routine installation" means the process of loading program files and installation files onto a computer. Routine installation does not include installation of the customized elements of prewritten computer software.

**(v) Separately stated charge for routine installation from customization of prewritten computer software.** Where there is a separately stated charge on an invoice or other statement of the price given to the purchaser for routine installation from customization of prewritten computer software, routine installation is subject to retailing B&O tax and retail sales

tax. If a charge for routine installation is not separately stated from customization of prewritten computer software, the predominant nature of the transaction determines taxability.

(vi) **Examples.**

(A) Tee, Inc., is in need of financial modeling software that can tie into most of its existing computer systems. Because of its unique business, however, Tee needs the industry-wide computer software offered by PQR Computers, Inc., that is modified to meet the needs of Tee. Both Tee and PQR are in-state corporations, and the software is delivered in this state. PQR provides a separately stated charge to Tee for customization of prewritten computer software performed in this state that is supported by the terms of the sales agreement. PQR is subject to retailing B&O tax, and it must collect retail sales tax from Tee for the sale of prewritten computer software in Washington. PQR, in addition, is subject to service and other activities B&O tax for the customization of prewritten computer software in Washington.

(B) Same facts as (a)(vi)(A) of this subsection, except that, in addition, PQR provides a separately stated charge to Tee for routine installation of prewritten computer software in this state. This charge represents installation of only the prewritten portion of the software. In addition to the tax treatments in (a)(vi)(A) of this subsection, PQR is subject to retailing B&O tax and it must collect retail sales tax from Tee for the routine installation in Washington.

(b) **Installing or uninstalling computer software.**

(i) Gross income received from installing or uninstalling custom software is subject to service and other activities B&O tax.

(ii) Gross proceeds of sales for routine installation of prewritten computer software are subject to retailing B&O tax and retail sales tax. See (a)(iv) of this subsection for more information on routine installation. See WAC 458-20-145 (sourcing) for more information on sourcing retail sales of prewritten software and routine installation. Routine installation of prewritten computer software includes charges for labor and services in respect to the installation, such as travel costs for the routine installation of the software. As of July 1, 2008, if the routine installation occurs through remote access by someone outside the state of Washington, then the installation is sourced to where first use occurs. For example, XYZ Computers, Inc., is hired by Dan for routine installation of prewritten software onto Dan's computers. XYZ's out-of-state employee remotely accesses Dan's computers in Washington to install the prewritten software on his computers. If XYZ has nexus with Washington, then it must collect and remit the sales tax. If XYZ does not have nexus, then Dan must pay use tax.

Gross proceeds of sales of uninstalling prewritten computer software are subject to retailing B&O tax and retail sales tax.

For example, XYZ Computers, Inc., is hired by Dan to remove spy ware from his computers. Spy ware is prewritten computer software. Removal of spy ware requires uninstalling the spy ware from the computer. XYZ sends an employee to Dan's location to remove spy ware from its computers. Charges for removal of spy ware are subject to retailing B&O tax and retail sales tax.

(c) **Repairing, altering, or modifying computer software.** Repair of prewritten computer software for more than one person may be distributed as a fix or patch by tangible storage media or electronically in the nature of software upgrades and updates. The sale of prewritten computer software upgrades and updates is a sale of prewritten computer software subject to retailing B&O tax and retail sales tax. See WAC 458-20-145 (sourcing) for more information on sourcing retail sales of computer services.

Alteration or modification of prewritten computer software performed for a specific person is subject to the service and other activities B&O tax. Such alteration or modification of prewritten computer software for a specific person constitutes customization of prewritten computer software. See RCW 82.04.215.

Alteration or modification of custom software is subject to service and other activities B&O tax.

(i) **Example.** STU Computers, Inc., a Washington company, is hired by Betty to perform repairs via remote access on her prewritten computer software in Washington. STU is performing alteration or modification of prewritten computer software for a specific person and is subject to service and other activities B&O tax.

(ii) **Example.** VW Computers, Inc., an out-of-state service provider, is hired by Clyde to perform alterations or modifications via remote access on his prewritten computer software located in this state. VW's facility is located outside this state. VW may be subject to service and other activities B&O tax if it has nexus with Washington. See WAC 458-20-194 (Apportionment).

(d) **Maintaining computer software.** Computer software maintenance agreements typically include, but are not limited to, support activities such as telephone consulting, help desk services, remote diagnostic services, and software upgrades and updates.

(i) **Tax treatment of computer software maintenance agreements in general.** Sales of stand-alone computer software maintenance agreements that include telephone consulting, help desk services, remote diagnostic services, and other professional services are taxable under the service and other activities B&O tax. However, if the services are part of a sale

of an extended warranty on or after July 1, 2005, then the sale is subject to retailing B&O tax and retail sales tax. See WAC 458-20-257 (Warranties and maintenance agreements) for information about extended warranties.

Stand-alone sales of updates or upgrades to prewritten computer software are retail sales of tangible personal property subject to retailing B&O tax and retail sales tax.

(ii) **Prewritten computer software maintenance agreement with mixed elements.** The sale of a prewritten computer software maintenance agreement that includes professional service components such as telephone consulting and retail components such as upgrades and updates of prewritten computer software is a retail sale subject to retailing B&O tax and retail sales tax.

In cases where the charges for the professional service component(s) and the retail component(s) are separately stated within a prewritten computer software maintenance agreement and invoice, then each activity is taxed according to the nature of the activity.

(iii) **Duplication of prewritten computer software upgrades and updates.** Duplication of prewritten computer software upgrades and updates is subject to manufacturing B&O tax upon the value of products, if the software upgrades and updates are delivered by means of tangible storage media which is retained by the purchaser. This is the case regardless of any maintenance agreement with mixed elements involved. The measure of tax is presumed to be the contract price of the maintenance agreement, unless the person can prove otherwise. See WAC 458-20-112 (Value of products) for more information.

If the software upgrades and updates are delivered from the seller by means other than tangible storage media which is retained by the purchaser, then the software upgrades and updates are not subject to manufacturing B&O tax.

(iv) **Maintenance agreement on custom software and customized elements of prewritten computer software.** Sales of maintenance or support services relating to custom software or the customized elements of prewritten computer software are subject to the service and other activities B&O tax. Such services, including upgrades and updates, are rendered in respect to the custom or customized software and take on the underlying character and taxability of the custom or customized software.

(v) **Examples.**

(A) On December 15, 2005, CBA Computers, Inc., sells at retail a prewritten computer software maintenance agreement to Frank for his software. The software maintenance agreement includes an extended warranty for the software, software upgrades and updates, and telephone consulting services. CBA delivers the software upgrades and updates electronically, as well as provides the maintenance services to Frank at one

charge. CBA is subject to retailing B&O tax, and it must collect retail sales tax from Frank for the sale of the mixed agreement.

(B) Same facts as (d)(v)(A) of this subsection, except that CBA delivers the software upgrades and updates on compact disks. CBA is subject to retailing B&O tax, and it must collect retail sales tax from Frank for the sale of the mixed agreement. In addition, CBA is subject to manufacturing B&O tax on duplication of software upgrades and updates. The measure of tax is presumed to be the contract price of the maintenance agreement, unless CBA can prove otherwise.

(C) Same facts as (d)(v)(A) of this subsection, except that CBA provides a separately stated charge for each component of the maintenance agreement. CBA is subject to retailing B&O tax, and it must collect retail sales tax from Frank for the charges on software upgrades and updates and on the extended warranty purchased after July 1, 2005. CBA is subject to service and other activities B&O tax for the charge on telephone consulting services.

(D) FED Computers, Inc., sells at retail a computer software maintenance agreement to Greta for her software. The maintenance agreement covers only software upgrades and updates. Greta's software is prewritten computer software with customized elements. FED provides the maintenance services to Greta at one charge. FED is subject to retailing B&O tax, and it must collect retail sales tax from Greta for the sale of the entire maintenance agreement of the prewritten computer software.

(E) Same facts as (d)(v)(D) of this subsection, except that FED provides a separately stated charge for maintaining the customized elements. FED is subject to service and other activities B&O tax for the charge on maintaining the customized elements. FED is subject to retailing B&O tax, and it must collect retail sales tax from Greta for the charge on maintaining prewritten computer software.

(e) **Computer software training.** Gross income received for training on the use of custom software is subject to service and other activities B&O tax. Gross income received for training on the use of prewritten computer software is subject to service and other activities B&O tax, if the charge for such training is separately stated from the sale of prewritten computer software. If the charge for software training is not separately stated from the sale of prewritten computer software, the entire charge is considered to be a sale of prewritten computer software subject to retailing B&O tax and retail sales tax.

(308) **Licensing computer software - royalties.** Income received from charges in the nature of royalties for the licensing of computer software is taxable under the royalties B&O tax classification.

(a) **What are royalties?** RCW 82.04.2907 provides that

"royalties" is compensation for the use of intangible property, such as copyrights, patents, licenses, franchises, trademarks, trade names, and similar items. The true object of a transaction involving royalties is to grant an intangible right to reproduce and distribute copies of computer software for sale. It does not, however, include compensation for the licensing of prewritten computer software to the end user. The manner in which computer software is sold (e.g., volume of transactions, subscription license, term license, or perpetual license) or the manner in which payment amount is determined (e.g., fixed fee per copy, percentage of receipts, lump sum, etc.) does not alter the royalty nature of the transaction.

(b) **Royalties versus site license.** Regarding royalties, the true object of the transaction is to grant an intangible right to reproduce and distribute copies of computer software for sale. In contrast, the true object of a site license is the sale to an end user of prewritten computer software for use on its computers. See subsection (304) of this section for more information on site licenses.

(c) **Royalties versus wholesale sales of prewritten computer software.** See subsection (303)(a) of this section for more information.

(d) **Examples.**

(i) HG Computers, Inc., an original equipment manufacturer (OEM), acquires prewritten computer software from LL Software, Inc., under a license to reproduce and distribute the prewritten computer software as part of a bundled computer hardware and software package HG sells to end users. LL retains all of its ownership rights to the software. The gross income received by LL from granting intangible rights to reproduce and distribute prewritten computer software to HG is subject to royalties B&O tax.

(ii) Same facts as (d)(i) of this subsection, except that, in addition, HG acquires a site license from LL for the purposes of using the prewritten computer software as an end user. LL delivers the software to HG. Amounts received by LL for the sale of a site license are subject to retailing B&O tax and retail sales tax.

(309) Special use tax exemption for computer hardware and computer software donated to certain schools or colleges. Use tax does not apply to the use of computer hardware and computer software irrevocably donated to any public or private nonprofit school or college, as defined under chapter 84.36 RCW. RCW 82.12.0284.

#### **PART IV - TAXATION OF INFORMATION SERVICES AND COMPUTER SERVICES**

(401) **Activities associated with information services and computer services.** For services described below that are

subject to service and other activities B&O tax, see WAC 458-20-194 (Doing business inside and outside the state) for more information on the apportionment of service and other activities B&O tax for taxpayers who maintain places of business both within and without the state that contribute to the rendition of the services.

(a) **Sales of information services.** Gross income received for information services is subject to service and other activities B&O tax.

(i) **What are information services?** "Information services" means every business activity, process, or function by which a person transfers, transmits, or conveys data, facts, knowledge, procedures, and the like to any user of such information through any tangible or intangible medium. "Information services" does not include transfers of tangible personal property such as computer hardware or standard prewritten software programs. Neither does "information services" include telecommunication services defined under RCW 82.04.065.

Effective August 1, 2007, and in accordance with RCW 82.08.705 and 82.12.705, a sales and use tax exemption is provided for sales of electronically delivered standard financial information, if the sale is to an investment management company or a financial institution. Standard financial information is defined as "any collection of financial data or facts, not compiled for a specific consumer, including financial market data, bond ratings, credit ratings, and deposit, loan, or mortgage reports." See RCW 82.08.705.

(ii) **Examples.**

(A) XX Statistical Data, Inc., sells statistical data at the specific request of each customer. XX does not compile such statistical information to be available for all customers. Instead, each customer submits its own request of the statistical information based on its needs. XX compiles, analyzes, and summarizes the statistical information it gathers and sends the information to customers in a tangible medium. XX is subject to service and other activities B&O tax for the sales of statistical information, because XX is providing an information service at the specific request of each customer.

(B) ZZ Statistical Data, Inc., allows its customers to perform on-line research of statistical information through its data base. ZZ bills its customers a monthly fee for having on-line access to the data base for research. Its customers do not download any information onto their computers. ZZ is subject to service and other activities B&O tax for providing information services to its customers.

(C) WW Travel, Inc., bills its customers a monthly fee for having access to a travel reservation system that includes a charge for dedicated telephone lines. WW is subject to service and other activities B&O tax for providing information services,

rather than a telecommunications service. The provider of dedicated telephone lines to WW must collect retail sales tax from WW on the sale of telecommunications service. WW is the consumer of telecommunications service.

(D) VV Telephone, Inc., provides a satellite-based tracking and communications system that includes instant messaging between vehicles in transit and dispatch centers. Both the vehicles and the dispatch centers are operated by its customers, and information is both generated and received by the customers. This is not a sale of information service. The true object of the transaction is the transmission of data between the vehicles and the dispatch centers through VV's communications system. VV is providing telecommunications services subject to retailing B&O tax, and it must collect retail sales tax on the sale of telecommunications services. See RCW 82.32.520 for sourcing of telecommunications services.

(E) AA Data, Inc., provides a daily report of bond ratings for electronic download by its investment management company consumers. Each investment management company downloads the same report. As of August 1, 2007, AA provides standard financial information that falls within the exemption found in RCW 82.08.705 and 82.12.705. Therefore, AA does not collect or remit retail sales tax.

(b) **Sales of data processing services.** Gross income received for data processing services is subject to service and other activities B&O tax.

"Data processing services" includes, but is not limited to, word processing, data entry, data retrieval, data search, information compilation, payroll processing, business accounts processing, data production, and other computerized data and information storage or manipulation. "Data processing services" also includes the use of a computer or computer time for data processing whether the processing is performed by the provider of the computer or by the purchaser or other beneficiary of the service.

(i) **Example.** JK Processing, Inc., provides payroll processing services to other businesses. JK is subject to service and other activities B&O tax for providing data processing services.

(ii) **Example.** KL Processing, Inc., processes payroll data related to its employees. KL is not subject to manufacturing B&O tax or use tax for the electronic processing of its own data.

(c) **Sales of internet services.** Gross income received for internet services are subject to service and other activities B&O tax.

(i) **What is the internet?** "Internet" means the international computer network of both federal and nonfederal interoperable packet switched data networks, including the

graphical subnetwork called the world wide web. RCW 82.04.297.

(ii) **What are internet services?** "Internet service" is a service furnished by an internet service provider (ISP) that allows users access to the internet. The ISP must provide the service through use of computer processing applications that either provide the user with additional or restructured information or permit the user to interact with stored information through the internet or a proprietary subscriber network. "Internet service" includes the following services furnished by the ISP:

- Provision of internet electronic mail;
- Access to the internet for information retrieval; and
- Hosting of information for retrieval over the internet.

"Internet service" does not include telecommunications service as defined in RCW 82.04.065.

(iii) **What is a proprietary subscriber network?** "Proprietary subscriber network" means proprietarily or privately owned network in which its services are available to the public for fees. Proprietary subscriber network does not include intranets.

(iv) **Examples.**

(A) ISP, Inc., is an internet service provider that provides customers with access to the internet. ISP does not furnish any telephone lines to its customers in providing this access. ISP maintains its operation in Washington. Amelia is charged a monthly internet access fee from ISP for access to the internet in Washington. ISP is subject to service and other activities B&O tax for the monthly internet access fee charged to Amelia.

(B) Same facts as (c)(iv)(A) of this subsection, except that ISP provides customers with access to the internet along with telephone lines used to provide that access. Amelia is charged a combined monthly fee for access to the internet in Washington using the telephone lines. ISP is subject to service and other activities B&O tax for the combined fee, because the true object of the transaction is to provide access to the internet, rather than to provide telecommunications service.

(C) Telecomm Co. provides customers with telephone lines for telecommunications, including long distance service, and for access to the internet (internet services). Zoe is charged a combined monthly fee for access to the internet and for communication services in Washington using the telephone lines. Telecomm Co. is subject to retailing B&O tax for the combined fee because the primary purpose of the transaction is to provide telecommunications service, rather than to provide access to the internet. However, if Telecomm Co. separately states or can reasonably identify from its books and records the fees for telecommunications service and internet access, then Telecomm Co. will be subject to retail and service classifications

respectively.

(D) DD Computers, Inc., provides access to information through its web site for which it charges its users a fee. DD charges Stan, an out-of-state customer, a transaction fee to use DD's web site to search and retrieve real estate appraisal information. DD is not providing internet service because DD is not an ISP and does not provide customers with access to the internet. DD, however, is providing Stan access to its web site for informational search and retrieval which is subject to service and other activities B&O tax.

(d) **Sales of intranet services.** Gross proceeds of sales of intranet services are sales of telecommunications service defined under RCW 82.04.065 and are subject to retailing B&O tax and retail sales tax.

"Intranet service" means the service of providing a private or intracompany network used by a person to facilitate the sharing or accessing of internal information by the person's employees or other authorized parties.

(e) **Sales of Voice over Internet Protocol (VoIP) services.** "VoIP service" is a service that enables subscribers to use the internet as the transmission medium for telephone calls by sending voice data in packets in internet protocol. Gross proceeds of sales of VoIP services are sales of telecommunications service defined under RCW 82.04.065 subject to retailing B&O tax and retail sales tax.

(f) **Sales of network system support services.** Gross income received for network system support services is subject to service and other activities B&O tax. "Network system support" activities include analyzing and interpreting problems using diagnostic software, monitoring network to ensure network availability to users, and performing network system configurations. Network system support activities may be performed through remote telephone support or on-site consulting.

(g) **Sales of remote access to prewritten software. I.e., application service providers (ASPs) or software as a service (SAAS).** Gross income received for providing remote access to applications on the host's servers are subject to service and other activities B&O tax, when the service is performed in Washington. Sellers of remote access to applications (e.g., ASPs) may be able to apportion income if they perform activities in multiple states (i.e., servers used in multiple states to host the software). See WAC 458-20-194 (apportionment).

"ASP" means a provider that generally offers customers with electronic access to applications on the ASP's server. ASP generally does not provide computer software for customers to download. ASP, however, may provide downloadable codes in order for customers to access its applications on its server that are only incidental to the services provided to customers.

(i) **Example.** BE Software, Inc., offers a variety of prewritten software products on-line, but not for download, to its customers for a monthly subscription fee. BE Software is subject to service and other activities B&O tax for its subscription fees received.

(ii) **Example.** Same facts as (g)(i) of this subsection, except that, in addition, BE provides computer software for customers to download before the on-line software can be used. The downloaded software does not provide any function other than confirm registration and provide access codes necessary for a customer to be able to use the on-line software. The downloaded software is provided as part of the monthly subscription fee. Once the subscription ends, the access software the customers downloaded will not perform any function. BE Software is subject to service and other activities B&O tax for its subscription fees received, because the true object of the transaction is to provide on-line software to its customers.

(iii) **Example.** Same facts as (g)(i) of this subsection, except that, in addition, BE offers an option to allow its customers to download a limited number of software applications for an additional fee. Kelly purchases and downloads a number of additional prewritten software packages from BE in this state. BE is subject to retailing B&O tax, and BE must collect retail sales tax from Kelly on the additional fee for the sale of downloaded software.

(h) **Sales of web site development or hosting services.** Gross income received for web site development or hosting services are subject to service and other activities B&O tax.

"Web site development service" means the design and development of a web site provided by a web site developer to a customer. "Web site hosting service" means providing server space to host a customer's web site.

(i) **Sales of on-line advertising services.** Gross income received for on-line advertising services are subject to service and other activities B&O tax. See RCW 82.04.280 and 82.04.214 for tax treatment of the electronic form of a printed newspaper.

For example, BB.com sells souvenir items through the internet. BB.com provides on-line advertising services for third parties. Income received for on-line advertising services is subject to service and other activities B&O tax.

(j) **Sales of data warehousing services.** Gross income received for data warehousing services is subject to service and other activities B&O tax. "Data warehousing service" means the service of a provider offering server space for a customer to store its data and to access, retrieve, or use the data as needed.

(i) **Example.** HH Recovery, Inc., provides substitute computer systems so that its customers may access its computer facilities for disaster recovery purposes, if such customers

experience unplanned computer system failures. Lance pays a monthly subscription fee for this service. HH is subject to service and other activities B&O tax for the sale of data warehousing services to Lance.

(ii) **Example.** Same facts as (j)(i) of this subsection, except that, in addition, HH performs "live" data backup for disaster recovery purposes. HH purchases prewritten computer software to perform "live" backup of data. HH is subject to use tax for the use of prewritten computer software to perform "live" backup of data.

#### **PART V - DISTINCTION BETWEEN SALES AND SERVICES**

(501) **Current WAC 458-20-155 makes a distinction between sales and services.** Liability for sales or use tax depends upon whether the subject of the sale is a product or a service. Professional and personal services rendered to a client are not generally subject to retail sales or use tax. If the consumer's true object of the transaction is obtaining professional or personal services, similar to those performed by a public accountant, architect, lawyer, etc., then the retail sales or use tax is not applicable. The retail sales and use tax is not applicable because these services are performed to meet a consumer's specific needs and any property transferred in the transaction is considered the medium in or on which those services are rendered and is merely the tangible evidence of a professional service rendered.

If the true object of the transaction is a product made available to any consumer and not created to meet the particular needs of a specific consumer, regardless of the method of delivery, then the transaction is taxable under the retailing B&O tax classification and taxable as a retail sale. The term "product" includes tangible personal property, such as prewritten software. This is no different from a usual inventory of tangible personal property held for sale or lease, and the sale or lease of such products is a sale at retail subject to retail sales tax or use tax.

Please see WAC 458-20-155 for more information.