

BEFORE THE APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition For Correction of	)	<u>D E T E R M I N A T I O N</u>
Denial of Application for Credits of	)	
	)	No. 97-236
	)	
...	)	Registration No. ...
	)	
	)	

[1] RULES 136, 155, AND 240; RCW 82.62.010, RCW 82.04.110 AND -.120: B&O TAX CREDITS -- MANUFACTURING -- DISTRESSED AREAS -- INTERNET SERVICES. Merely providing Internet services, such as creating Web pages, without producing tangible personal property for sale, or for commercial or industrial use does not qualify a person for the B&O tax credits program for distressed areas.

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

NATURE OF ACTION:

A company (the taxpayer) appeals a ruling that it does not qualify for tax credits that are allowed manufacturers who create jobs in specific distressed areas in this state.<sup>1</sup>

FACTS:

De Luca, A.L.J. -- The taxpayer provides various services related to Internet access. For instance, it

1. sells Internet access to customers;
2. sells e-mail accounts (access) to customers;
3. resells private telephone line service to customers for more certain access to the Internet;
4. sells instruction manuals;

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

5. sells advertising space on the Internet, including charges for creating Web pages for customer advertising;
6. provides customers with copies of licensed software to connect to the Internet, and will load the software for the customers for a charge;
7. sells upgraded versions of software to increase customers' hours on the Internet from limited to unlimited.

The taxpayer filed an application in 1996 with the Department of Revenue (the Department) for the business and occupation (B&O) tax credits allowed manufacturers who create jobs in specific distressed areas in this state. See Chapter 82.62 RCW, infra. The Department's Special Programs Division denied the application. The taxpayer appealed the ruling to the Department's Taxpayer Information & Education Section (TI&E). TI&E also denied the application by ruling that the taxpayer did not meet the definition of "manufacturing" in RCW 82.62.010 (5) because it did not provide "computer-related services" as required by the statute.

#### ISSUE:

Does the taxpayer's Internet service activities qualify as "manufacturing" for purposes of the B&O tax credit allowed manufacturers who create jobs in specific distressed areas in this state?

#### TAXPAYER'S EXCEPTIONS:

The taxpayer contends it is entitled to the B&O tax credits because RCW 82.62.010 (5) clearly defines "manufacturing" to include computer programming and computer-related services, which are the types of activities the taxpayer claims it performs. For example, the taxpayer creates Web pages for its customers to advertise on the Internet. To create a Web page, a person needs to obtain a type of software known as a Web-authoring program. Once the Web page has been created from the software, the Internet service provider will add the Web page or files to the Web. Web pages can range from simple text to more complex items containing text, charts, graphics, etc.

#### DISCUSSION:

Chapter 82.62 RCW provides that persons engaged in manufacturing or research and development in certain areas in the state can qualify for B&O tax credits. The purpose of the law is to stimulate the economy and create employment opportunities in specific distressed areas of Washington. The distressed area program also sets forth the process to apply for the credits. To be eligible, a person must be engaged in either manufacturing or research and development. Research and development is not an issue before us. RCW 82.62.010 states that:

(5) "Manufacturing" means all activities of a commercial or industrial nature wherein labor or skill is applied, by hand or machinery, to materials so that as a result thereof a new, different, or useful substance or article of tangible personal property is produced for sale or commercial or industrial use and shall include the production or

fabrication of specially made or custom made articles. "Manufacturing" also includes computer programming, the production of computer software, and other computer-related services, and the activities performed by research and development laboratories and commercial testing laboratories.

WAC 458-20-240 (Rule 240) implements Chapter 82.62 RCW. The rule states that "manufacturing" has the meaning given in RCW 82.04.110 and WAC 458-20-136 (Rule 136). Rule 240 adds that the definition of manufacturing also includes the language in RCW 82.62.010 (5) that pertains to computer programming, the production of computer software, and other computer-related-services. See also RCW 82.04.120 which, along with Rule 136, defines "manufacturing" identically to the definition in RCW 82.62.010 (5), supra, but without its last sentence.

All of these statutes and rules define "manufacturing" to require that a substance or article of tangible personal property be produced for sale or commercial or industrial use. For purposes of the distressed area B&O tax credits program, the question is whether the taxpayer is engaged in computer programming, producing computer software, or other computer-related services in relation to "manufacturing."

WAC 458-20-155 (Rule 155) pertains to information and computer services. The rule explains the difference between sales and services by providing:

Liability for sales tax or use tax depends upon whether the subject of the sale is a product or a service. If information services, computer services or data processing services are performed, such that the only tangible personal property in the transaction is the paper or medium on which the information is printed or carried, the activity constitutes the rendering of professional services, similar to those rendered by a public accountant, architect, lawyer, etc., and the retail sales tax or use tax is not applicable to such charges. This includes the sales of software in connection with custom programs written to meet a particular customer's specific needs. The programs are considered to be the tangible evidence of a professional service rendered to a client and not subject to retail sales tax or use tax.

If, on the other hand, the sale, lease, or licensing of the computer program is a sale or lease of a product, even though produced through a computer system or process, it is taxable as a retail sale. Standard, prewritten software programs do not constitute professional services rendered to meet the particular needs of specific customers, but rather, are essentially sales of articles of tangible personal property. Articles of this type are no different from a usual inventory of tangible personal property held for sale or lease and, irrespective of any incidental modifications to the program medium or its environment (e.g., adaptation to computer room configuration) to meet a particular customer's needs, the sale or lease of such standard software is a sale at retail subject to retail sales tax or use tax.

The taxpayer's activities, including preparing custom Web pages, do not result in the production of tangible personal property, which is a necessary element for an activity to be considered

manufacturing. RCW 82.04.120 and Rule 136, supra. The taxpayer's activities also do not result in the sale of tangible personal property for Rule 155 purposes, supra. In other words, the computer programming, the production of computer software, and computer-related services described in Chapter 82.62 RCW must be done in relation to the activity of manufacturing as defined in RCW 82.04.110 and -.120, (i.e., producing tangible personal property). In giving effect to the legislature's intent in enacting a statute, the statute as a whole must be considered and harmonized with related statutes. Stewart Carpet Serv., Inc. v. Contractors Bonding & Ins. Co., 105 Wn.2d 353, 715 P.2d 115 (1986); State v. Bernhard, 108 Wn.2d 527, 741 P.2d 1 (1987). Consequently, the taxpayer is not a manufacturer for purposes of the distressed area B&O tax credits program.

#### DECISION AND DISPOSITION:

The taxpayer's petition is denied.

Dated this 24th day of November, 1997.