Cite as 6 WTD 247 (1988)

BEFORE THE INTERPRETATION AND APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Ruling of Tax Liability of)	D E T E R M I N A T I O N
)	No. 88-296
. . .)	Registration No. . . .

[1] **RULE 19301:** B&O TAX - CREDIT - MULTIPLE ACTIVITIES (MATC) - CANADIAN TAX - "SALES" - DETERMINATION. The Department will look to the substance of the foreign activity involved which is subjected to a foreign tax - and not merely the name given it by that jurisdiction's taxing authority - to determine whether the activity taxed was a "sale" under Washington law. If the activity giving rise to the foreign tax is a "sale" as defined by the Washington Revenue Act, the foreign tax paid by the taxpayer will be considered to be one on "sales" albeit that its name may differ under another taxing jurisdiction.

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

TAXPAYER REPRESENTED BY: . . .
. . .

DATE OF HEARING: March 15, 1988

NATURE OF ACTION

Request for ruling of eligibility of Canadian tax for basis of Multiple Activities Tax Credit (MATC).

FACTS:

Burroughs, A.L.J. -- The taxpayer is a Washington State corporation that designs and manufactures computer software in the state of Washington. The taxpayer, in its petition, claims that a portion

of the software packages which it manufactures is sold to Canadian customers. The taxpayer reports all such resulting income for Washington state tax purposes under the manufacturing classification, which classification the taxpayer claims has been reviewed and approved by the Department. The Canadian government classifies the income as "royalties," and withholds (per its treaty with the United States) 10% of the gross amount charged. The taxpayer records sales at 100% and records a foreign tax expense of 10% in its books and ledgers. The taxpayer claims that, irrespective of the fact that Canada taxes under the "royalties" classification, the transactions are in reality sales.

Article XII of the treaty under which the taxpayer is taxed defines "royalty" as follows:

> The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work . . . , any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, tangible personal property . . .

ISSUE:

Whether the Canadian tax is a "gross receipts tax . . . paid to another state with respect to the sales of the products . . . manufactured in this state" for the purposes of the multiple activities tax exemption (MATC).

DISCUSSION:

RCW 82.04.440, as amended by Chap. 3, Washington Laws, 1987 2nd Ex. Sess., provides for the multiple activities exemption. It reads, in pertinent part, as follows:

> (4) Persons taxable under . . . RCW 82.04.240 . . . with respect to . . . manufacturing products in this state shall be allowed a credit against those taxes for any (i) gross receipts taxes paid to another state with respect to the sales of the products so extracted or manufactured in this state, ... The amount of the credit shall not exceed the tax liability arising under this chapter with respect to the extraction or manufacturing of those products.
>
> (5) For the purpose of this section:
>
> (a) "Gross receipts tax" means a tax:
>
> (i) Which is imposed on or measured by the gross volume of business, in terms of gross receipts or in other

> terms, and in the determination of which the deductions allowed would not constitute the tax an income tax or value added tax; and
>
> (ii) Which is also not, pursuant to law or custom, separately stated from the sales price. (Emphasis added.)

Under the terms of this provision, then it must first be determined whether the "taxes paid to another state" were for "sales of the products . . . so manufactured in this state," and, secondly, whether the foreign tax involved was a "gross receipts" tax.

In determining whether the Canadian tax at issue is one on "sales," it must first be recognized that various taxing jurisdictions may define "sale" differently than does the state of Washington. Thus, transactions considered "sales" in this state might be taxed under another term in another jurisdiction, or transactions not considered "sales" in this state might actually be taxed as "sales" elsewhere.

An established principle of statutory construction is that

> Legislative definitions generally control in construing the statutes in which they appear. . .
>
> Childers v. Childers, 89 W.2d 592, 598 (1978)

[1] For purposes of determining the availability of the MATC, then, the Department will look to the substance of the foreign activity involved which is subjected to the foreign tax - and not merely the name given it by that jurisdiction's taxing authority - to determine whether the activity taxed was a "sale" under Washington law. If the activity giving rise to the foreign tax is a "sale" as defined by the Washington Revenue Act, the foreign tax will be considered to be one on "sales" albeit that the taxable activity might be described differently in a foreign jurisdiction.

RCW 82.04.040 defines "sale" as

> any transfer of the ownership of, title to, or possession of property for a valuable consideration and includes any activity classified as a "sale at retail" or "retail sale" under RCW 82.04.050. It includes renting or leasing, conditional sale contracts, leases with option to purchase, and any contract under which possession of the property is given to the purchaser but title is retained by the vendor as security for the payment of the purchase price . . . .

WAC 458-20-155 (Rule 155), which concerns computer services, further provides as follows:

> If . . . the sale, lease, or licensing of the computer program is a sale or lease of a product . . . 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. . . . [T]he sale or lease of such standard software is a sale at retail subject to retail sales tax or use tax.

and

> The terms "sale" (RCW 82.04.040) and "retail sale" (RCW 82.04.050) include any transfer of possession of tangible personal property for a consideration. This includes transfers of computer hardware and standard, prewritten software for a charge, regardless that outright ownership or title may not pass to the user, and regardless of any express or implied restrictions upon the user. (Emphasis added.)

At our request the taxpayer provided for our review representative agreements with several of its clients. In those agreements, the taxpayer was identified as "Licensor," and the provisions therein clearly provided for clients' use of certain prewritten computer software programs. The Department's prior determination that the taxpayer is taxable as a manufacturer of these programs (as opposed to writing programs to meet particular customers' needs, taxable under the service classification) is further indication that the programs at issue are "standard, prewritten software," whose transfer of possession should be properly considered a "sale."

Because the granting of a license for the use of standard, prewritten software for a charge is a "sale" under the Washington Revenue Act, this activity performed in a foreign jurisdiction will also be considered a "sale" for purposes of applying the MATC, regardless of the fact that in this case it is defined and taxed by the United States/Canadian treaty as a "royalty."

Because the tax is a full 10% of the gross amount of the "royalties" charged and is not separately stated, we likewise consider the tax to be a "gross receipts" tax.

Accordingly, the taxpayer is advised that the MATC will apply.

RULING:

The taxpayer is entitled to take a MATC credit against its Washington manufacturing business and occupation tax for taxes paid to the Canadian Department of Revenue on its income from its

license agreements with Canadian customers for the right to use its prewritten computer software.

This legal opinion may be relied upon for reporting purposes and as support of the reporting method in the event of an audit. This ruling is issued pursuant to WAC 458-20-100(18) and is based upon only the facts that were disclosed by the taxpayer. In this regard, the department has no obligation to ascertain whether the taxpayer has revealed all of the relevant facts or whether the facts disclosed are actually true. This legal opinion shall bind this taxpayer and the department upon these facts. However, it shall not be binding if there are relevant facts which are in existence but have not been disclosed at the time this opinion was issued; if, subsequently, the disclosed facts are ultimately determined to be false; or if the facts as disclosed subsequently changes and no new opinion has been issued which takes into consideration those changes. This opinion may be rescinded or revoked in the future; however, any such rescission or revocation shall not affect prior liability and shall have a prospective application only.

DATED this 28th day of July 1988.