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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> |
| Assessment of                                   | ) |                                  |
|                                                 | ) | No. 14-0243                      |
|                                                 | ) |                                  |
| ...                                             | ) | Registration No. ...             |
|                                                 | ) |                                  |

[1] RULE 15503; RULE 224; RCW 82.08.190; RCW 82.08.195: B&O TAX – DIGITAL AUTOMATED SERVICE – ONLINE SEARCHABLE DATABASE – BUNDLED TRANSACTIONS. A taxpayer that provides retail-taxable online searchable database services, which are digital automated services, as well as service-taxable information technology consulting services, webcasts, and educational seminars, and charges one non-itemized fee for these combined services, is offering a bundled transaction. Because one of the component products, the online searchable database, is subject to the retail sales tax, the entire bundled transaction is subject to the retail sales tax.

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.

Sohng, A.L.J. – Information technology firm protests retail sales tax imposed on subscription-based access to its proprietary research library and other related services on the grounds that access to the proprietary research library is not a digital automated service because it primarily involves the application of human effort. The petition is denied in part and remanded in part.<sup>1</sup>

### ISSUES

Is a service package under which an information technology firm grants customers the right to access its proprietary research library, the right to receive personal consulting from professional analysts, and the right to attend technology conferences and seminars a “bundled transaction” that is subject to retail sales tax under RCW 82.08.195?

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### FINDINGS OF FACT

[Taxpayer] is an [out-of-state] corporation headquartered [outside Washington]. Taxpayer is a global information technology (“IT”) research and advisory firm that provides proprietary

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

technology-related information and services to high-tech and telecommunications companies, professional services firms, and government agencies. Taxpayer's information and services aid its customers in making IT decisions. Taxpayer offers its services primarily through three separate operating segments: (1) Consulting,<sup>2</sup> (2) Events,<sup>3</sup> and (3) Research.<sup>4</sup>

Within the Research segment, Taxpayer enters into Service Agreements under which Taxpayer grants its clients (the "Clients") a license to use its services. The Service Agreements provide the number and identity of the licensed users within the Clients' organization who may access Taxpayer's services. The Service Agreements set forth the level and type of services that Taxpayer will provide, as well as the amount of the lump-sum fees that Client must pay for such services (the "Research Fees"). Clients are not obligated to make any additional payments other than the Research Fees. Each Client is assigned a dedicated service delivery team, which typically consists of one manager-level employee and one partner-level employee. The service delivery team is generally responsible for servicing the Client's needs and facilitating the Client's utilization of Taxpayer's services under the Service Agreement.

Taxpayer offers dozens of different service packages, depending on the needs of the Client or the seniority level of the licensed users who will have access to the services. The service packages are specifically tailored for different job titles within the Client's organization, from Chief Information Officers to junior IT professionals.<sup>5</sup> Each service package typically includes a combination of the following: (i) online access to proprietary documents in its research library (the "Research Library"); (ii) analyst inquiries; (iii) analyst consulting; (iv) briefings; (v) webcasts; and (vi) summit or symposia tickets,<sup>6</sup> described in further detail below (collectively, the "Research Services").

(i) *Research Library*

Taxpayer creates all of the substantive content contained the Research Library, the operation of which requires one or more software programs.<sup>7</sup> The provision of access to the Research Library comprises the majority of the Research Services Taxpayer provides its Clients. The documents in the Research Library cover specific IT topics and consist of published reports, briefings, updates, alerts, newsletters, and other related tools.<sup>8</sup> Clients log in to the Research Library through the

<sup>2</sup> . . . Consulting provides fact-specific consulting services to help clients use and manage their IT to enhance business performance. Taxpayer's Supplemental Appeal Petition, at 3 (Mar. 27, 2014).

<sup>3</sup> . . . Events organizes symposia, summits, and seminars for senior level IT and business strategists. These events feature informational and education sessions led by analysts and include cutting-edge technology showcases, peer exchange workshops, one-on-one meetings with analysts, consulting diagnostic workshops, and keynote addresses by leaders in the technology field. *Id.*

<sup>4</sup> . . . Research provides objective insight on critical and timely IT initiatives for Chief Information Officers and other IT professionals through research notes, meetings, phone conferences, briefings, proprietary tools, peer networking services, and executive and membership programs. *Id.*

<sup>5</sup> For instance, Taxpayer offers service packages entitled "...," "...," "...," "...," "...," and "...."

<sup>6</sup> Taxpayer provided the following statistics regarding Clients' use of its research services in 2011: . . . views of documents in the Research Library; . . . analyst inquiries; . . . days of analyst consulting; . . . briefings, . . . reprints and webcasts, and . . . tickets to summits or symposia.

<sup>7</sup> See Taxpayer's Supplemental Appeal Petition, at 5 (Mar. 27, 2014).

<sup>8</sup> Taxpayer's 2010 Annual Report states:

. . .

internet and can search it by topic, date, or author to access relevant material. Taxpayer retains ownership rights over all content in the Research Library at all times. Taxpayer continually updates and provides new content for the Research Library to ensure that Clients receive the most current information. However, Taxpayer does not perform such updates at the request of any particular Client. Taxpayer restricts the frequency and manner in which a licensed user within the Client organization may forward research content internally. Generally, Clients may download and print content from the Research Library only once and must pay an extra fee to reprint or re-download content.

(ii) *Analyst Inquiries*

Analyst inquiries are one-on-one telephone conferences between Taxpayer's research analysts and the Client. Research analysts are subject matter experts in one or more specialized fields (e.g., IT security, cloud computing, crowd-sourcing, etc.) who provide professional advice to the Client. The length of the analyst inquiry may be limited to 30 or 60 minutes, depending on the particular service package the Client has purchased.

(iii) *Analyst Consulting*

Analyst consulting is similar to analyst inquiries, above, but the analyst travels to be on-site at the Client's business location and provides advice in-person, rather than over the telephone. On some occasions, the analyst provides advice via video-conference. Analyst consulting may include contract review.

(iv) *Briefings*

Briefings are workshop-like meetings conducted in-person with the analyst and the Client, usually at the Client's location. Briefings focus on specific subject matters, such as a particular product or industry trend.

(v) *Webcasts*

Webcasts are online seminars delivered by analysts to multiple Clients simultaneously over the internet. Webcasts focus on a specific subject matter and are not specific to any particular Client.

(vi) *Symposia*

Symposia are live conferences and conventions with attendees from the IT industry. Chief Information Officers and other senior-level technology officers from across the United States attend and make presentations at these events.

Most Clients purchase service packages that include access to the Research Library, plus one or more of the latter five services enumerated above. However, Taxpayer does offer access to the Research Library alone, without any other services. Taxpayer states that only a small minority of Clients purchase access to only the Research Library.

During the appeals process, Taxpayer provided several sample sales invoices, which show that Clients pay single, lump-sum Research Fees for their particular service package. The amount of the Research Fee varies, depending on the term of the license, the number of licensed users

within the Client organization, the frequency of analyst inquiries/consulting/briefing, and the nature and frequency of the other services provided under the Service Agreement. A typical invoice reads, in pertinent part, as follows:

| Description      | Amount  |
|------------------|---------|
| ...              |         |
| Subtotal         | \$ ...  |
| Total Amount Due | USD ... |

Taxpayer also provided several sample Service Agreements, which show that Clients pay single, lump-sum Research Fees. The corresponding Service Agreement to the invoice above reads, in pertinent part, as follows:

| Service Name | Level of Access | Number of Users | Contract Term Start Date | Contract Term End Date           | Annual Fee | Total Fee |
|--------------|-----------------|-----------------|--------------------------|----------------------------------|------------|-----------|
| ...          | ...             | 1               | 7/1/2010                 | 6/30/2011                        | \$ ...     | \$ ...    |
|              |                 |                 |                          |                                  |            |           |
|              |                 |                 |                          |                                  |            |           |
|              |                 |                 | Total Services:          | (Excluding applicable sales tax) | \$ ...     | \$ ...    |

Each Service Agreement references an attached “Service Description,” which provides a detailed description of the Research Services that Taxpayer must deliver. Neither the invoices, the Service Agreements, nor the Service Descriptions separately itemize the prices of the component Research Services provided within each package, such as analyst inquiry, analyst consulting, briefings, access to Research Library, etc. Rather, the invoices and underlying contracts identify the service package, describe the services in detail, and list the total amount of the Research Fee.

The Audit Division examined Taxpayer’s books and records for the period January 1, 2007 through December 31, 2011 (the “Audit Period”). Taxpayer did not report any of its Washington revenue earned by the Research segment during the Audit Period. For the period January 1, 2007 through July 25, 2009, the Audit Division asserted service and other activities business and occupation (“B&O”) tax on the Research Fees, which Taxpayer does not contest. From July 26, 2009 through December 31, 2010, the Audit Division asserted retailing B&O tax on the Research Fees on the grounds that providing access to the Research Library was a digital automated service.<sup>9</sup> From January 1 through December 31, 2011, the Audit Division asserted retailing B&O tax and retail sales tax on the Research Fees, also on the grounds that providing access to the Research Library was a digital automated service. Taxpayer appeals the Audit Division’s conclusion that the Research Fees are retail sales beginning July 26, 2009.

<sup>9</sup> Pursuant to a Special Notice on Online Searchable Databases that the Department issued on November 2, 2010, the Audit Division accepted Taxpayer’s reporting of revenue from the Consulting and Events segments and declined to assert retail sales tax on the Research Fees from July 26, 2009 through December 31, 2010.

. . . On May 20, 2013, the Audit Division issued Assessment No. . . . , in the amount of \$ . . . , including \$ . . . in taxes,<sup>10</sup> \$ . . . in penalties, and \$ . . . in interest.

## ANALYSIS

At issue here is whether the Research Fees that Taxpayer earns under the Service Agreements are subject to retail sales tax under the bundled transaction laws as digital automated services. Effective July 1, 2008, the Washington Legislature enacted the bundled transaction provisions (codified RCW 82.08.190, .195, and RW 82.12.195) to comply with the Streamlined Sales and Use Tax Agreement (or “SSUTA”).<sup>11</sup> Laws of 2007, ch. 6, § 501. The bundled transaction statutes explain how to tax transactions that involve both retail and non-retail sales. In order to determine whether the transactions under the Service Agreement involve both retail and non-retail sales, we must examine whether each component service is retail or non-retail.

### 1. Research Library

We will first address whether providing access to the Research Library is a “digital automated service” subject to retail sales tax. Washington imposes retail sales tax on each retail sale in this state. RCW 82.08.020. In 2010, the Washington Legislature enacted . . . comprehensive legislation, retroactive to July 26, 2009, governing the excise taxation of digital products. 2010 Wash. Laws ch. 111. The term “retail sale” includes sales to consumers of digital automated services . . . RCW 82.04.050(8)(a). “Digital automated service” is defined as “any service transferred electronically that uses one or more software applications.” RCW 82.04.192(3)(a). “Transferred electronically” means “obtained by the purchaser by means other than tangible storage media. It is not necessary that a copy of the product be physically transferred to the purchaser. So long as the purchaser may access the product, it will be considered to have been electronically transferred to the purchaser.” RCW 82.04.192(8).

WAC 458-20-15503 (“Rule 15503”) is the Department’s administrative rule that explains the taxation of digital products. Rule 15503(102) provides additional guidance regarding the meaning of “transferred electronically”:

[T]he purchaser obtains the product by means other than tangible storage media. Generally, this means the product is transferred using the public internet, a private network, or some combination. However, it is not necessary that the product be delivered to the purchaser. As long as the purchaser may access the product, it will be considered to have been electronically transferred to the purchaser. For example, whether a digital

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<sup>10</sup> The taxes consisted of \$ . . . in retail sales tax, \$ . . . in retailing business and occupation (“B&O”) tax, \$ . . . in service and other activities B&O tax, and \$ . . . in use tax.

<sup>11</sup> SSUTA is the “result of the cooperative effort of 44 states, the District of Columbia, local governments and the business community to simplify sales and use tax collection and administration by retailers and states. The Agreement minimizes costs and administrative burdens on retailers that collect sales tax, particularly retailers operating in multiple states.” *Frequently Asked Questions*, Streamlined Sales Tax Governing Board, Inc., [http://www.streamlinedsalestax.org/index.php?page=gen\\_1](http://www.streamlinedsalestax.org/index.php?page=gen_1) (last visited July 29, 2014); see also *Qualcomm, Inc. v. Dep’t of Revenue*, 171 Wn.2d 125, n.8, 249 P.3d 167 (2011); *Indiana Dep’t of Revenue v. Kitchin Hospitality, LLC*, 907 N.E.2d 997, 1000, n.2 (Ind. 2009). States that wish to participate must enact laws, rules, and regulations that conform to SSUTA’s provisions.

movie is downloaded by the user or streamed by the user, it is considered to be "transferred electronically." Alternatively, the same movie purchased on tangible media (e.g., DVD, etc.) is the purchase of tangible personal property and is not considered to be either the sale of a digital product or transferred electronically.

(Emphasis added.) Clients gain access to the Research Library by logging in via the internet. In short, content from the Research Library is transferred using the internet. Thus, the product is "transferred electronically" under Rule 15503 and RCW 82.04.192(8). And because operating and providing access to the Research Library use one or more computer software applications, they are digital automated services as defined by RCW 82.04.192(3)(a).

To be considered a retail sale, however, the sale of a digital automated service must be to a *consumer* . . . . RCW 82.04.050(8)(a). RCW 82.04.190(11)(a) defines "consumer" as "[a]ny end user of a digital product or digital code." "Digital product" means digital goods and digital automated services. RCW 82.04.192(7). "End user" does not include a "taxpayer who receives by contract a digital product for further commercial . . . distribution . . . of the product, in whole or in part, to others." RCW 82.04.190(11)(b)(i). Clients are "consumers" under RCW 82.04.190(11)(a) because they are the end-users of the Research Library and cannot further distribute the product commercially. [Therefore,] providing access to the Research Library (a digital automated service) [by Taxpayer to its clients] is a retail sale under RCW 82.04.050(8)(a)(iii). Taxpayer's petition is denied as to this issue.

Taxpayer argues that providing access to the Research Library falls under the exception to the definition of digital automated service contained in RCW 82.04.192(3)(b) for "any service that primarily involves the application of human effort by the seller, and the human effort originated after the customer requested the service." Rule 15503(302)(d) provides additional guidance:

**Professional or personal services** represented in electronic form are not a digital good. This exclusion applies where the service primarily involves the application of human effort by the service provider, and the human effort originated after the customer requested the service. For example, an electronic engineering report created at the customer's request that reflects an engineer's professional analysis, calculations, and judgment, which is sent to the customer electronically, is considered evidence of a professional service and not a digital good.

Taxpayer asserts that the human effort exception applies because it must continually update, maintain, and create content in the Research Library to provide the most useful and relevant information for Clients. While we acknowledge that the creation of content in the Research Library requires significant human effort, we disagree that the exception applies here. To qualify for the exception, the application of human effort . . . must occur *after* the Client enters into the Service Agreement and at the Client's request. When the Client enters into the Service Agreement, the proprietary content and information already exist and the Client has immediate access to such information in the Research Library. The Client does not . . . specifically request that Taxpayer continually update the content in the Research Library after the Service Agreement has been entered into. While Taxpayer may continually research and update the existing information after a Client has subscribed, this activity is not performed at the specific

request of any particular Client after that Client has signed the Service Agreement, as required by RCW 82.04.192(3)(b) and Rule 15503(302)(d). Taxpayer's provision of digital automated service does not involve the application of human effort after the Client requested the service and the exception under RCW 82.04.192(3)(b) does not apply. Taxpayer's petition is denied as to this issue.

Next, Taxpayer argues that because the Research Library is not an online searchable database (an "OSD"), it is not a digital automated service. Even if we concede that the Research Library is not an OSD, that does not preclude it from being a digital automated service. Being classified as an OSD is not a requirement for being a digital automated service under RCW 82.04.192. However, in this case, the Research Library does qualify as an OSD.

With respect to OSDs, the Department issued a Special Notice on November 2, 2010, which provides, in part:

The Department has determined that online searchable databases (OSD) are digital automated services (DAS). As such, they do not qualify for the exemption provided for digital goods used solely for a business purpose.

OSDs are subject to retail sales or use tax unless some other exemption applies.

The Special Notice does not define the term online searchable database, but provides the following description:

OSDs, such as online legal research services, are DAS because they are transferred electronically and use one or more software applications. While these services provide "data, facts, or information" similar to a [digital good], they also provide additional functions, such as search, retrieve, and storage capabilities (software applications).

Taxpayer argues that the Research Library is not an OSD because all of the content therein is proprietary, unlike what it contends is the case for Lexis-Nexis or Westlaw. However, the Special Notice contains no requirement that data in an OSD be non-proprietary; therefore, we do not find this fact to be relevant. We conclude that the Research Library is a digital automated service and also an OSD. In addition to providing data and facts (namely, content in the Research Library), it also provides additional functions, such as searching and retrieving, as described in the Special Notice. Taxpayer's petition is denied as to this issue.

## 2. Analyst Inquiries, Analyst Consulting, Briefings, Webcasts, & Symposia

Next, we must determine whether the other services Taxpayer provides (analyst inquiries, analyst consulting, briefings, webcasts, and symposia) are retail or non-retail services. Analyst inquiries, analyst consulting, and briefings are all services in which analysts provide professional IT advice to Clients through different delivery mechanisms. These services are essentially IT consulting services delivered in-person (analyst consulting, briefings) or over the telephone or videoconference (analyst inquiry). Webcasts and symposia are educational seminars delivered to

multiple Clients simultaneously via the internet (webcasts) or in-person at large conferences and conventions (symposia).

RCW 82.04.290(2) provides a “catch-all” tax classification for taxpayers engaged in business activities not explicitly taxed under another section of RCW 82.04. RCW 82.04.290(2). The statute provides:

Upon every person engaging within this state in any business activity other than or in addition to an activity taxed explicitly under another section in this chapter or subsection (1) or (3) of this section; as to such persons the amount of tax on account of such activities shall be equal to the gross income of the business multiplied by the rate of 1.5 percent.

WAC 458-20-224(2)(“Rule 224”) provides that taxpayers providing personal or professional services, such as accountants, architects, attorneys, physicians, engineers, and teachers are subject to tax under the service and other activity classification of the B&O tax. Rule 224(2) states:

Persons engaged in any business activity, other than or in addition to those for which a specific rate is provided in the statute, are taxable under a classification known as service and other business activities, and so designated upon return forms. In general, it includes persons rendering professional or personal services to persons (as distinguished from services rendered to personal property of persons) such as accountants, aerial surveyors and map makers, agents, ambulances, appraisers, architects, assayers, attorneys, automobile brokers, barbers, baseball clubs, beauty shop owners, brokers, chemists, chiropractors, collection agents, community television antenna owners, court reporters, dentists, detectives, employment agents, engineers, financiers, funeral directors, refuse collectors, hospital owners, janitors, kennel operators, laboratory operators, landscape architects, lawyers, loan agents, music teachers, oculists, orchestra or band leaders contracting to provide musical services, osteopathic physicians, physicians, real estate agents, school bus operators, school operators, sewer services other than collection, stenographers, warehouse operators who are not subject to other specific statutory tax classifications, teachers, theater operators, undertakers, veterinarians, and numerous other persons.

The IT consulting services, webcasts, and educational seminars provided by expert analysts are equivalent or analogous to the professional services enumerated in Rule 224(2), above. Such professional services are generally not considered retail sales. *See* 82.04.050; Rule 224. Specifically, the IT consulting services and the right to attend symposia fall under the service and other activities classification of the B&O tax, and are not retail sales. RCW 82.04.290(2); Rule 224.

### 3. Bundled Transaction Analysis

Because Taxpayer provides both retail services (access to the Research Library) and non-retail services (IT consulting, seminars) in a single transaction for a single fee, it may be a bundled



transaction. *See* RCW 82.08.190. Generally, a bundled transaction is subject to retail sales tax if the sale of any of its component products is individually subject to retail sales tax. RCW 82.08.195(1). We must determine whether the Research Services sold under the Service Agreement meet the definition of a “bundled transaction.” RCW 82.08.190(1)(a) defines a bundled transaction as “the retail sale of two or more products. . . where: (i) The products are otherwise distinct and identifiable; and (ii) The products are sold for one nonitemized price.” Thus, the elements of a bundled transaction are:

1. The retail sale of two or more products;
2. That are distinct and identifiable; and
3. Sold for one nonitemized price.

The term “product” is defined as “tangible personal property, digital goods, digital codes, digital automated services, other services, extended warranties, and anything else that can be sold or used.” RCW 82.32.023 (emphasis added). Each component of Research Service is a “product” because it can (and is) used. As we have already concluded, providing access to the Research Library is a retail sale (as a digital automated service), and the IT consulting services, webcasts, and educational seminars are non-retail sales. The sale of all of these products under the Service Agreement constitutes the “retail sale of two or more products” under RCW 82.08.190(1)(a).

We next examine whether the Research Services meet the second element of a “bundled transaction.” RCW 82.08.190 does not define what constitutes “distinct and identifiable products,” but it does indicate what that term excludes. RCW 82.08.190(2) explains that “distinct and identifiable products” excludes:

- (a) Packaging such as containers, boxes, sacks, bags, and bottles, or other materials such as wrapping, labels, tags, and instruction guides, that accompany the retail sale of the products and are incidental or immaterial to the retail sale thereof. Examples of packaging that are incidental or immaterial include grocery sacks, shoeboxes, dry cleaning garment bags, and express delivery envelopes and boxes;
- (b) A product provided free of charge with the required purchase of another product. A product is provided free of charge if the sales price of the product purchased does not vary depending on the inclusion of the product provided free of charge; or
- (c) Items included in the definition of sales price in RCW 82.08.010.

(Emphasis added.) RCW 82.08.010(1)(a) provides:

"Sales price" means the total amount of consideration . . . including cash, credit, property, and services, for which tangible personal property, extended warranties, digital goods, digital codes, digital automated services, or other services or anything else defined as a "retail sale" under RCW 82.04.050 are sold, leased, or rented, valued in money, whether received in money or otherwise. No deduction from the total amount of consideration is allowed for the following: (i) The seller's cost of the property sold; (ii) the cost of materials used, labor or service cost, interest, losses, all costs of transportation to the

seller, all taxes imposed on the seller, and any other expense of the seller; (iii) charges by the seller for any services necessary to complete the sale, other than delivery and installation charges; (iv) delivery charges; and (v) installation charges.

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(Emphasis added). In other words, the term “sales price” includes the five items that are nondeductible under RCW 82.08.010(1)(a), including “any services necessary to complete the sale.” Here, the right to receive IT consulting and to attend webcasts and symposia are not “necessary to complete the sale” of the right to access the Research Library. Indeed, Taxpayer’s own business practice demonstrates this. Taxpayer does, on occasion, allow Clients to purchase access to the Research Library only, without any of the other services. Thus, we conclude that neither the IT consulting services nor right to attend webcasts and symposia are necessary to complete the sale of access to the Research Library. Because they are not included in the definition of “sales price,” the products under the Service Agreement are “distinct and identifiable”

Finally, we look to the last element: whether the services were sold for “one nonitemized price.” The invoices and Service Agreements clearly show that there was no separate itemization for the various services Taxpayer offered. Rather, the invoices and Service Agreements showed only single fees. Therefore, we conclude that the third element has been satisfied and the Research Services are a bundled transaction under RCW 82.08.190. And because one of the component products (the Research Library) of the bundled transaction is subject to retail sales tax, the full nonitemized Research Fees are likewise subject to retail sales tax under RCW 82.08.195. Taxpayer’s petition is denied as to this issue.<sup>12</sup>

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#### DECISION AND DISPOSITION

Taxpayer’s petition is denied in part and remanded in part.

Dated this 29th day of July, 2014.

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<sup>12</sup> RCW 82.04.190(4) provides very limited exceptions to the general bundled transaction rules. Taxpayer does not argue that any of these exceptions applies here, so we decline to address them.