

No. 83673-6

FAIRHURST, J. (dissenting) — While I agree with the majority that the primary purpose test should determine the OmniTRACS service's tax classification, I disagree with how the majority applies the test in this case. The primary purpose test should consider why Qualcomm's customers purchase the OmniTRACS service alone, not why they buy the entire OmniTRACS system. Because the customer buys the OmniTRACS service primarily to overcome the classic communications dilemma of transmitting information over vast physical distances, I conclude it was properly taxed as a “[n]etwork telephone service” as defined in former RCW 82.04.065(2) (1997).

- I. The primary purpose test should apply to only the OmniTRACS service, not the entire OmniTRACS system

The Washington Department of Revenue (DOR) has long used the primary purpose test to determine whether a product should be taxed as a retail sale or a service when the product has elements of both. *See, e.g.*, DOR, Determination No. 89-009A, 12 Wash. Tax Dec. 1, 5 (1993), available at <http://taxpedia.dor.wa.gov/zipfiles.htm>. Often, price determines the unit to which the primary purpose test

applies; that is, a separately priced item is assigned a single tax category based on the customer's primary purpose in purchasing that item.¹ But if one sale or service is merely incidental to another sale or service, the primary purpose test may require a single tax category for the related items even though they are priced separately.

For example, in one DOR decision, the taxpayer charged its customers separately for use of its data processing service and for dedicated telephone lines to access that service. DOR, Determination No. 90-128, 9 Wash. Tax Dec. 280-1, 2 (1990), *available at* <http://taxpedia.dor.wa.gov/zipfiles.htm>. The taxpayer's form contract devoted several pages to describing the data processing service, while the only mention of telephone access was a single phrase noting the customer's obligation to pay for "on-line availability." *Id.* at 5. The taxpayer did not dispute that its data processing service was classifiable as "information services,"² but it argued that the telephone line charges should be separately taxable as a "network telephone service."³ *Id.* at 3-4. DOR disagreed, concluding the telephone line

¹The idea that pricing often determines what comprises a single taxable unit flows from the language of the statute itself. Sales tax is imposed on "each" retail sale. RCW 82.08.020. A "sale" is "any transfer of the ownership of, title to, or possession of property for a valuable consideration." RCW 82.04.040(1). Consistent with this language, DOR explains that its long standing position has been that "separate and distinct products or services sold together will be taxed individually if there is a reasonable basis to determine the price of the individual products or services." Resp't's Suppl. Br. at 10.

²"[I]nformation 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." WAC 458-20-155.

charges must be taxed as “information services” because “the furnishing of the telephone lines is not the object of the transaction, but merely incidental to the personal services being rendered.” *Id.* at 4.

DOR again applied the primary purpose test to determine whether a transaction was “information services” or a “network telephone service” in DOR, Determination No. 98-202, 19 Wash. Tax Dec. 771, 774-76 (2000), *available at* <http://taxpedia.dor.wa.gov/zipfiles.htm>. There, the taxpayer travel agency paid a monthly fee to use a reservation system that allowed it to compare prices and book flights, hotels, and rental cars. *Id.* at 775. Part of the monthly fee went to providing telephone lines that allowed the taxpayer to be continuously online and connected to the reservation system. *Id.* DOR concluded that the entire monthly fee should be taxed as “information services” rather than “network telephone services” because the telephone line costs were merely incidental to the travel agency’s true purpose of being able to access information and book reservations. *Id.* at 776.

Here, unlike in the data processing service or reservation system in the

³“Network telephone service” means the providing by any person of access to a local telephone network, local telephone network switching service, toll service, or coin telephone services, or *the providing of* telephonic, video, *data*, or similar communication or *transmission for hire, via* a local telephone network, toll line or channel, cable, *microwave*, or similar *communication* or transmission system. Former RCW 82.04.065(2) (emphasis added).

foregoing DOR decisions, the OmniTRACS system contains no “information services” to which the OmniTRACS service could be incidental except functions provided by the OmniTRACS service itself. “[I]nformation services” is defined as “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.” WAC 458-20-155 (emphasis added). The term does not encompass the sale of prewritten software, which is instead tangible personal property subject to retail sales tax. *Id.*⁴

⁴WAC 458-20-155 explains:

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.

Qualcomm concedes its hardware and software are subject to retail sales tax.⁵ The logical corollary is that the functions performed by the hardware and software in the OmniTRACS system are not “information services.” In fact, the data processing functions that the majority concludes make the OmniTRACS system “information services,” such as generating information about a truck’s performance and compiling it into maps or reports, are actually nothing more than the product of tangible personal property owned by or licensed to Qualcomm’s customers. To conclude that the OmniTRACS service is “information services” on the basis of hardware and software that are admittedly not “information services” is a serious logical problem.

Furthermore, the majority’s assertion that the OmniTRACS service is merely incidental to the overall OmniTRACS system defies the nature of the product. Transmission of data is the foundation upon which the OmniTRACS system is built. The communications feature of the system is repeatedly emphasized in Qualcomm’s marketing materials. It is labeled the “OmniTRACS *Mobile Communications*

⁵See Clerk’s Papers at 117, DOR Determination No. 05-0377, at 2 n.4 (unpublished) (the published, redacted version is available at DOR Determination No. 05-0377, 27 Wash. Tax Dec. 51, 52 n.2) (“The taxpayer also sold hardware and software relating to these services. To the extent these sales were subject to Washington taxation, the taxpayer does not dispute that these sales were properly classified under the retailing classification.”), *available at* <http://taxpedia.dor.wa.gov/zipfiles.htm>.

System” and described as offering “streamlined messaging” and “custom messaging packages.” Clerk’s Papers (CP) at 67-69 (emphasis added). Qualcomm’s six-page form contract contains an entire page explaining pricing for the monthly OmniTRACS service, as well as several paragraphs dedicated to the OmniTRACS service’s use and function. CP 184-90. This stands in sharp contrast to the data processing company’s form contract that contained a single reference to “on-line availability.” 9 Wash. Tax Dec. 280-1, 2. Overall, Qualcomm’s materials emphasize that moving information between a dispatch center and the trucks’ distant locations is a vital part of the benefit that Qualcomm’s customers receive. Unlike the telephone connection to a data processing service or travel reservation service, the OmniTRACS service’s transmission of information is an end in itself.

The fact that the OmniTRACS service is not useful without the hardware and software does not mean that the primary purpose test should apply to the entire OmniTRACS system. Plenty of items are classified separately for tax purposes but have no practical value standing alone. Traditional phone service provides an excellent example. Like the hardware and software in Qualcomm’s system, a phone is an item of tangible personal property subject to retail sales tax. The customer often simultaneously buys a phone and signs up for a monthly plan allowing access

to a telephone network. Without the monthly network service, the phone itself would be useless, and the monthly service would likewise be worthless without the phone. But the purchaser understands that the phone and the service are two separate and equally valuable components of an integrated system, and accordingly, the two are taxed separately. In fact, the majority says that taxing telephone service separately from telephone equipment was the legislature's goal when it originally created the tax category of "network telephone service." Majority at 11.

II. The primary purpose of the OmniTRACS service is transmission of data

Once it has been established that the primary purpose test should apply to the OmniTRACS service alone, the question is what primarily motivates Qualcomm's customers to purchase the OmniTRACS service. The service does perform limited processing functions, such as triangulation to determine the trucks' locations, date- and time-stamping of the incoming messages, and storage of messages until customers choose to retrieve them. But when one considers the primary obstacle a trucking company wants to surmount--the miles of physical distance between its dispatch center and its fleet of trucks--transmission of information emerges as the dominant purpose. Just like a traditional telephone, the OmniTRACS service allows nearly instant communication between parties scattered across the country. The

information processing that occurs, while useful, could not take place if the information was not first transmitted.

The fact that the service “does not serve as a replacement for a driver’s cell phone” is a red herring. *See* majority at 21 (quoting Br. of Amici Curiae Washington Trucking Associations and American Trucking Associations, Inc.). In *W. Telepage, Inc. v. City of Tacoma Department of Financing*, 140 Wn.2d 599, 998 P.2d 884 (2000), we established that a “network telephone service” under former RCW 82.04.065(2) need not provide two-way, free flowing communication by holding that a one-way paging service was a “network telephone service.” Just as an on-call physician might have a cell phone for personal use and a pager for emergency patient calls, a truck driver might have a cell phone for personal use and the OmniTRACS service for routine, work-related messages. The fact that each service has different practical advantages and uses does not undermine the conclusion that the core purpose of both is to transmit information from one point to another.

III. Conclusion

The primary purpose test should be applied by evaluating the customer’s purpose in purchasing only the OmniTRACS service, not the entire OmniTRACS

system. Looking at just the OmniTRACS service shows that transmission of information is the customer's main objective, while information processing is an important but secondary goal. Because the primary purpose of the OmniTRACS service is to transmit data for hire, it is taxable as a "network telephone service" under former RCW 82.04.065(2). I would affirm the Court of Appeals.

AUTHOR:

Justice Mary E. Fairhurst

WE CONCUR:

Chief Justice Barbara A. Madsen

Justice Debra L. Stephens
