

Memorandum of Decision: 04-20170601R
Gross Retail and Use Tax
For the Year 2013

NOTICE: IC § 4-22-7-7 permits the publication of this document in the Indiana Register. The publication of this document provides the general public with information about the Indiana Department of Revenue's official position concerning a specific set of facts and issues. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Memorandum of Decision.

HOLDING

Insurance Company was not entitled to a refund of sales tax paid on the purchase of prewritten computer software purchased from various vendors and delivered to Indiana; Indiana law provided a "temporary storage" exemption for use tax but not sales tax. Insurance Company was not entitled to an apportioned refund of sales tax paid on the purchase of software maintenance agreements based on the ratio of its in-state and out-of-state employees when the software was purchased by and/or delivered to its Indiana location.

ISSUES

I. Gross Retail and Use Tax - Computer Software.

Authority: IC § 6-2.5-1-27; IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-3-1(a); IC § 6-2.5-3-2(a); IC § 6-2.5-3-2(e); IC §§ 6-2.5-5 et seq.; IC § 6-2.5-13-1(d)(1); IC § 6-2.5-13-1(d)(2); *Indiana Dep't of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480 (Ind. Tax Ct. 2012); *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Rhode v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044 (Ind. Tax Ct. 2002); *Indiana Dep't of State Revenue v. Kimball Int'l Inc.*, 520 N.E.2d 454 (Ind. Ct. App. 1988); *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96 (Ind. Ct. App. 1974); [45 IAC 2.2-3-14\(2\)](#); [45 IAC 2.2-3-16](#) (repealed); [45 IAC 2.2-5-3\(b\)](#); [45 IAC 2.2-5-6\(a\)](#); [45 IAC 2.2-5-8\(a\)](#); [45 IAC 2.2-5-9\(a\)](#); [45 IAC 2.2-5-10\(a\)](#); Sales Tax Information Bulletin 8 (December 2016); Sales Tax Information Bulletin 8 (November 2011).

Taxpayer argues that the Department erred in denying it a refund of tax on the purchase of computer software and software maintenance agreements claiming that the software was accessed and used by many of its employees located outside Indiana and - in some instances - housed on computer servers located outside the state.

II. Gross Retail and Use Tax - Software Maintenance Agreements.

Authority: IC § 6-2.5-1-14.5; IC § 6-2.5-4-17; *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96 (Ind. Ct. App. 1974); Sales Tax Information Bulletin 8 (November 2011).

Taxpayer maintains that it is entitled to a refund of sales/use tax paid on the purchase of software maintenance agreements on the ground that the software is utilized both within and without Indiana or that the maintenance provider did not supply computer updates, fixes, or any other tangible personal property during the term of the agreement.

III. Gross Retail and Use Tax - Exempt Service Transactions.

Authority: [45 IAC 2.2-4-2](#); [45 IAC 2.2-4-2\(a\)](#).

Taxpayer states it is entitled to a refund of sales tax paid on exempt, service-only transactions.

STATEMENT OF FACTS

Taxpayer is an out-of-state company which provides various insurance services including individual policies, retirement plans, and group insurance policies. Taxpayer submitted a refund request seeking the return of approximately \$420,000 of sales and use tax paid on the purchase of prewritten computer software, maintenance agreements, and what it categorized as "professional services."

The Indiana Department of Revenue ("Department") reviewed Taxpayer's claim and, in a letter dated March 2017, denied the refund in full.

Taxpayer disagreed with the Department's decision denying the refund and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representatives explained the basis for the protest. This Memorandum of Decision results.

I. Gross Retail and Use Tax - Computer Software.

DISCUSSION

The issue is whether Taxpayer has established that it was entitled to a refund of sales tax paid on the purchase of prewritten computer software on the ground that the software was hosted by vendors on computer servers that were located outside Indiana.

A. Taxpayer's Burden in Claiming a Refund

When a taxpayer challenges taxability in a specific instance, the taxpayer is required to provide documentation explaining and supporting its challenge. Poorly developed and non-cogent arguments are subject to waiver. *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138, 1145 (Ind. Tax Ct. 2010); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480, 486 n.9 (Ind. Tax Ct. 2012). When an agency is charged with enforcing a statute, the jurisprudence defers to the agency's reasonable interpretation of that statute "over an equally reasonable interpretation by another party." *Indiana Dep't of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014).

B. Indiana's Gross Retail Tax.

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). "When the product is received by the purchaser at a business location of the seller, the sale is sourced to that business location." IC § 6-2.5-13-1(d)(1). "When the product is not received by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser . . . occurs" IC § 6-2.5-13-1(d)(2).

C. Indiana's Complementary Use Tax.

Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). "'Use' means the exercise of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a).

In effect and practice, the use tax is generally functionally equivalent to the sales tax. See *Rhoades v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002). However, Indiana's use tax - not sales tax - allows an exception for the "temporary storage" of tangible personal property delivered into Indiana but destined for use outside the state. IC § 6-2.5-3-2(e).

D. Computer Software and Indiana's Sales/Use Tax.

IC § 6-2.5-1-27 incorporates "prewritten computer software" in the definition of tangible personal property subject to sales/use tax:

"Tangible personal property" means personal property that:

- (1) can be seen, weighed, measured, felt, or touched; or
- (2) is in any other manner perceptible to the senses.

The term includes electricity, water, gas, steam, and prewritten computer software.

A person who acquires property in a retail transaction (a "retail purchaser") is liable for the tax on the transaction. IC § 6-2.5-2-1(b).

E. Sales and Use Tax Exemptions.

As a general rule, all purchases of tangible personal property - including computer software - are subject to sales

or use tax unless specifically exempted by statutes or regulations. [45 IAC 2.2-5-3\(b\)](#); [45 IAC 2.2-5-6\(a\)](#); [45 IAC 2.2-5-8\(a\)](#); [45 IAC 2.2-5-9\(a\)](#); [45 IAC 2.2-5-10\(a\)](#). Various sales tax exemptions are outlined in IC §§ 6-2.5-5 et seq. which generally are applicable to use tax. [45 IAC 2.2-3-14\(2\)](#).

A statute which provides any tax exemption, however, is strictly construed against the taxpayer. *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." *Id.* at 101 (internal citations omitted). In applying any tax exemption, the general rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." *Indiana Dep't of State Revenue v. Kimball Int'l Inc.*, 520 N.E.2d 454, 456 (Ind. Ct. App. 1988).

F. Taxpayer's Software Purchases.

Taxpayer purchased prewritten computer software from various vendors such as Ariba, Inc., Avaya, Inc., and IBM. According to the Department's March 2017 decision initially denying the refund, "The majority of the software invoices showed tangible personal property [software] was shipped to Indiana. The remaining invoices did not have a ship to address, but the "bill to" address was in Indiana." (*Emphasis added*). The Department's decision also noted that Taxpayer's assistant vice president provided a statement indicating a "percentage of [the] software was used outside Indiana."

Taxpayer maintains that "prewritten computer software maintained on computer servers outside of Indiana is subject to tax when accessed electronically via the Internet." As authority for its position, Taxpayer cites to the Department's Sales Tax Information Bulletin 8 (December 2016), 20170125 Ind. Reg. 045170026NRA. According to Taxpayer, this Bulletin supports its position that "[p]rewritten software maintained on computers outside of Indiana that are not accessed electronically in Indiana . . . are not subject to Indiana tax." In this case, regardless of ownership interest, sourcing rules, or delivery location the Department's guidance on this issue is found at Sales Tax Information Bulletin 8 (November 2011), 20111228 Ind. Reg. 045110765NRA, (*superseded by Sales Tax Information Bulletin 8 (December 2016)*), which was in effect at the time of the transactions and is dispositive of the software issues raised here by Taxpayer.

Prewritten computer software maintained on computer servers outside of Indiana also is subject to tax when accessed electronically via the Internet (i.e., "cloud computing"). The accessing of prewritten computer software by Indiana residents constitutes a transfer of the software because the customers gain constructive possession and the right to use, control, or direct the use of the software. Sales Tax Information Bulletin 8 (November 2011).

Taxpayer cannot rely on [45 IAC 2.2-5-54\(b\)](#) because the software was delivered or shipped to Indiana, it cannot rely on Indiana's former "Multiple Point of Use" (MPU) statute, IC § 6-2.5-13-2, because that statute was repealed in 2009, and it cannot rely on the IC § 6-2.5-3-2(e) "temporary storage exemption" because that exception only applies to "use tax" and Taxpayer is here asking for a refund of "sales tax."

In addition, the Department questions whether the taxable value of the software can be "sliced and diced" based on the geographically proportionate location of the ultimate users of that software when Taxpayer typically paid a unitary price for each software package. Because the software is ultimately accessed by users in multiple locations, the Department finds no support for the proposition that Taxpayer can now partially reallocate the unitary sales tax charge for software based on the ultimate number of software users located within and outside Indiana.

In this case, the Bulletin is clear; remotely accessed prewritten computer software is "tangible personal property" and subject to Indiana's sales/use tax. Equally clear is IC § 6-2.5-13-1(d)(1) which provides that "[w]hen the product is received by the purchaser at a business location of the seller, the sale is sourced to that business location." IC § 6-2.5-13-1(d)(1). In this case, the Department does not agree that payments to the software vendors are exempt from Indiana's sales tax.

FINDING

Taxpayer's protest is respectfully denied.

II. Gross Retail and Use Tax - Software Maintenance Agreements.

DISCUSSION

Taxpayer argues that it is entitled to refund of sales/use tax paid on the cost of software maintenance agreements because "no property was transferred during the period covered by the agreements."

IC § 6-2.5-1-14.5 defines "Computer software maintenance contract" as "a contract that obligates a person to provide a customer with future updates or upgrades of computer software."

Indiana law, IC § 6-2.5-4-17, further provides:

A person is a retail merchant making a retail transaction when the person enters into a computer software maintenance contract to provide future updates or upgrades to computer software. (*Effective July 1, 2010*).

In addition, Sales Tax Information Bulletin 8 (November 2011), 20111228 Ind. Reg. 045110765NRA, provides that a taxable maintenance agreement is necessarily coupled with the transfer of "tangible personal property."

The term "computer software maintenance contract" means a contract that obligates a person to provide a customer with future patches, updates, upgrades, or repairs of computer software.

In support of its argument here, Taxpayer provided correspondence from one of its employees assuring the Department that the maintenance agreement did not provide for software updates, patches, or "fixes."

Taxpayer also concludes that it is entitled to an apportioned amount of sales tax paid on maintenance agreements when the agreement calls for the support of software utilized by both in-state and out-of-state employees. For example, Taxpayer seeks a refund of 89 percent of the sales tax paid on an IBM maintenance agreement presumably on the ground that the maintenance agreement supports software utilized primarily (89 percent) by out-of-state employees.

In this case, Taxpayer is purchasing software maintenance agreements in order to maintain and update software used by Taxpayer's in-state and out-of-state employees. Taxpayer essentially argues that it is entitled to rely on what is in effect a "multiple point of use" standard to apportion the sales tax between its in-state employees and out-of-state employees because the underlying software is used by both sets of employees. However, in the case of these taxable unitary transactions, there is simply no avenue by which the tax liability is apportionable based on the relative number of in-state and out-of-state employees who access the software.

As to the remaining agreements, Taxpayer has not provided information necessary to determine that - during the term of the subject maintenance agreement - the vendor provided no software updates, patches, or "fixes." For example, Taxpayer has not provided copies of the written agreements between itself and the subject agreement vendors. Instead, Taxpayer relies on its executive's "say so" that the price paid to the vendors is exempt from sales tax. The Department assumes no bad faith on its employee's statement. However, the Department is mindful of the rule that "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96, 101 (Ind. Ct. App. 1974). The Department is unable to agree that a taxpayer's bare assertion as to the taxability of its maintenance agreements when there is no documentation to buttress that assertion.

FINDING

Taxpayer's protest is respectfully denied.

III. Gross Retail and Use Tax - Exempt Service Transactions.

DISCUSSION

Taxpayer states that it purchased "various professional services from vendors that erroneously collected sales and use tax" and that it is now entitled to a refund of those taxes.

In its initial decision denying that portion of the refund, the Department responded in its March 2017 explanation. "[B]ased off the invoices provided by the [T]axpayer, it could not be determined that the items were professional services. Instead, these items appear to be tangible personal property sold at retail . . . [and] the [T]axpayer did not provide any additional information showing that these items were services."

Taxpayer relies on [45 IAC 2.2-4-2](#) as authority for its position that these purchases are exempt from sales/use tax.

[45 IAC 2.2-4-2](#) provides as follows:

- (a) Professional services, personal services, and services in respect to property not owned by the person rendering such services are not "transactions of a retail merchant constituting selling at retail", and are not subject to gross retail tax. Where, in conjunction with rendering professional services, personal services, or other services, the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail unless:
- (1) The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property;
 - (2) The tangible personal property purchased is used or consumed as a necessary incident to the service;
 - (3) The price charged for tangible personal property is inconsequential (not to exceed 10[percent]) compared with the service charge; and
 - (4) The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.
- (b) Services performed or work done in respect to property and performed prior to delivery to be sold by a retail merchant must however, be included in taxable gross receipts of the retail merchant.
- (c) Persons engaging in repair services are servicemen with respect to the services which they render and retail merchants at retail with respect to repair or replacement parts sold.
- (d) A serviceman occupationally engaged in rendering professional, personal or other services will be presumed to be a retail merchant selling at retail with respect to any tangible personal property sold by him, whether or not the tangible personal property is sold in the course of rendering such services. If, however, the transaction satisfies the four (4) requirements set forth in 6-2.5-4-1(c)(010), paragraph (1) [subsection (a) of this section], the gross retail tax shall not apply to such transaction.

The regulation on which Taxpayer depends, [45 IAC 2.2-4-2](#), contains a provision exempting the purchase of services from sales tax. [45 IAC 2.2-4-2\(a\)](#) states that, "Professional services, personal services, and services in respect to property not owned by the person rendering such services are not transactions of a retail merchant constituting selling at retail, and are not subject to gross retail tax." However, "Where, in conjunction with rendering professional services . . . the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail . . ." *Id.*

As to the following payments, Taxpayer has provided documentation which is sufficient to meet its burden of establishing that the transactions were one for which Taxpayer was purchasing and paying for exempt labor services.

- DST Technologies, Invoice 001-25719, December 24, 2013;
- Ebix, Inc., Invoice 0322206-IN, July 31, 2013;
- Ebix, Inc., Invoice 0358323-IN, December 31, 2013;
- Ebix, Inc., Invoice 0312469-IN, June 30, 2013;
- Ebix, Inc., Invoice 0329686-IN, August 31, 2013;
- Ebix, Inc., Invoice 0336560-IN, September 30, 2013;
- Ebix, Inc., Invoice 0343049-IN, December 31, 2013;
- Ebix, Inc., Invoice 0312469-IN, October 31, 2013;
- Ebix, Inc., Invoice 0352171-IN, November 30, 2013.

Taxpayer has met its burden of establishing that it is now entitled to a refund of tax paid on the nine transactions listed in Part III.

FINDING

Taxpayer's protest is sustained in part.

SUMMARY

For the reasons discussed above, Taxpayer's protest is sustained, in part, and denied, in part. Taxpayer's protest

of the nine (9) transactions under Issue III is sustained. However, the remainder of Taxpayer's protest is denied.

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