

**Memorandum of Decision: 04-20211036
Gross Retail and Use Tax
For The Years 2017 and 2018**

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

The Department agreed that Company was entitled to a refund of Indiana sales tax paid on transactions with software vendors that occurred prior to July 1, 2018, for which Company did not acquire a possessory interest in the software.

ISSUE

I. Gross Retail and Use Tax - Prewritten Computer Software and Software as an Exempt Service.

Authority: IC § 6-2.5-1-27; IC § 6-2.5-2-1; IC § 6-2.5-3-1; IC § 6-2.5-3-2; IC § 6-2.5-4-17; IC §§ 6-2.5-5 et seq.; IC § 6-2.5-13-1; *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480 (Ind. Tax Ct. 2011); *Indiana Dep't of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Mynsberge v. Department of State Revenue*, 716 N.E.2d 629 (Ind. Tax Ct. 1999); *State Bd. of Tax Comm'rs v. Jewell Grain Co.*, 556 N.E.2d 920 (Ind. 1990); *Tri-States Double Cola Bottling Co. v. Department of State Revenue*, 706 N.E.2d 282 (Ind. Tax Ct. 1999); [45 IAC 2.2-3-14](#); [45 IAC 2.2-5-3](#); [45 IAC 2.2-5-6](#); [45 IAC 2.2-5-8](#); [45 IAC 2.2-5-9](#); [45 IAC 2.2-5-10](#); Sales Tax Information Bulletin 8 (December 2016); Sales Tax Information Bulletin 8 (July 1, 2018).

Taxpayer argues that it is entitled to a refund of Indiana sales tax paid on transactions of the acquisition or use of prewritten computer software.

STATEMENT OF FACTS

Taxpayer is an Indiana based company. Taxpayer submitted a claim for refund for approximately \$189,000 paid as sales tax on transactions involving pre-written computer software.

The Indiana Department of Revenue ("Department") denied the refund stating that "SaaS [Software as a Service] are considered taxable." The Department referred Taxpayer to Information Bulletin 8 for further details. Taxpayer disagreed with the denial and submitted a protest to that effect. An administrative hearing was held during which Taxpayer's representative explained the basis for the protest. This Memorandum of Decision results. Additional facts will be provided as necessary.

I. Gross Retail and Use Tax - Prewritten Computer Software and Software as an Exempt Service.

DISCUSSION

Taxpayer filed a claim for refund of sales and/or use tax paid in 2017 and 2018 on transactions involving software. The Department denied the claim, and Taxpayer filed a protest of that denial. The issue is whether Taxpayer is entitled to a refund of sales tax paid on software purchases executed prior to July 1, 2018.

The taxpayer is required to provide documentation explaining and supporting its challenge that the Department's position is wrong; poorly developed and non-cogent arguments are subject to wavier. *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. 2011). 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).

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 a 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).

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).

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). As to any of Taxpayer's vendor agreements to supply software maintenance or software updates, IC § 6-2.5-4-17 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.

As a general rule, all purchases of tangible personal property - including pre-written 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 are also applicable to use tax. [45 IAC 2.2-3-14\(2\)](#).

In considering Taxpayer's argument that the purchase of software services is not subject to sales tax, the Department bears in mind that IC § 6-2.5-2-1 is a tax imposition statutory provision and therefore, is strictly construed against the imposition of tax. *Mynsberge v. Department of State Revenue*, 716 N.E.2d 629, 633 (Ind. Tax Ct. 1999). See also *State Bd. of Tax Comm'rs v. Jewell Grain Co.*, 556 N.E.2d 920, 921 (Ind.1990); *Tri-States Double Cola Bottling Co. v. Department of State Revenue*, 706 N.E.2d 282, 285 n. 9 (Ind. Tax Ct. 1999).

Taxpayer protested the results of the refund investigation concerning programs sold by Workday, Inc. and Microsoft and provided documentation in the form of contracts, written agreements, and invoices to support its argument.

Under the Master Subscription Agreement with Workday, Inc., Taxpayer purchased a subscription for certain programs from Workday, Inc. Taxpayer was granted a license to the programs that was non-exclusive and non-transferable and to be used for the internal business purposes of Customer and Affiliates. Workday, Inc. maintained ownership of its intellectual property, while Taxpayer continuously owned its customer data. Taxpayer was not allowed to modify, copy, license, sublicense, sell resell, rent, lease transfer, assign, distribute, time share, offer in a service bureau or otherwise make the service available to a third party.

Either Taxpayer or Workday, Inc. may terminate the agreement with 30 days written notice. Upon termination, Workday, Inc. agrees to make Taxpayer's data available for retrieval for 90 days. After that time, Taxpayer's information will be deleted or destroyed in the Workday, Inc. system. As previously mentioned, because the agreement with Workday, Inc. provides a subscription to Taxpayer, there is no software to return or destroy.

Under the Microsoft Services Agreement, Microsoft provides a license to Taxpayer and reserves all rights to the software. The license prevented Taxpayer from changing anything with the software program. Taxpayer also could not share the services unless authorized by Microsoft. Under the related "Microsoft Server and Cloud Enrollment (Direct)" contract, it is specified that upon expiration or termination of the agreement for "Online Services" (i.e. cloud based programs), Microsoft will keep the customer data for 90 days so the customer can remove the data. After that time, Microsoft will delete the customer data. Again, because Microsoft provides a subscription to Taxpayer for certain cloud based programs, there is no software to return or destroy.

Software transactions which occurred prior to July 1, 2018, are governed by the Department's information bulletins which represent the Department's review and analysis at the time of the transaction.

Sales Tax Information Bulletin 8 (July 1, 2018), 20180725 Ind. Reg. 045180312NRA, is clear on the relevance and application of the 2011 and 2016 Bulletins:

[T]ransactions involving remotely accessed software occurring prior to July 1, 2018, will need to be analyzed using guidance published in the prior version of this bulletin.

As such, the vendor transactions which occurred during and after December 2016 are governed by Sales Tax Information Bulletin 8 (December 2016), 20170125 Ind. Reg. 045170026NRA. Information Bulletin 8 provides guidelines for distinguishing transactions in which a customer is purchasing taxable, pre-written software or the customer is paying for access to and use of software the customer does not own. As explained in Sales Tax Information Bulletin 8 (December 2016):

Charges for accessing prewritten software maintained on [a] vendor or third party's computer servers are not subject to tax when accessed electronically via the Internet if the customer is not transferred the software, does not have an ownership interest in the software, and does not control or possess the software on the server.

In deciding whether the buyer has acquired "an ownership interest" in the software, the 2016 Bulletin further provides:

In order to determine whether a purchaser obtains a possessory or ownership interest in pre-written software, the following factors that indicate a possessory or ownership interest should be considered:

- Whether the Indiana customer obtains or is granted the right to access or download copies of the software to the customer's own computers, servers, or network;
- Whether the Indiana customer gains or is granted the right to modify or customize the pre-written software;
- Whether the Indiana customer gains or is granted the right to make copies of the pre-written software for the customer's own use;
- Whether the Indiana customer is required to pay additional amounts for enhancements, modifications, or updates to the software;
- Whether the provider has a policy of providing a duplicate copy of the software at minimal or no charge if the customer loses or damages the software;
- Whether the Indiana customer gains or obtains the right to use, deploy, or access the software for an unlimited or indeterminate period of time;
- Whether the software must be returned or destroyed at the end of a specifically limited license period;
- The relative price paid for accessing or using the software compared to the price charged for obtaining a possessory or ownership interest in that same, similar, or comparable software.

Considering the documentation provided, the Department agrees that transactions with Workday, Inc. and Microsoft were not subject to Indiana's sales tax because the transactions called for the provision of software services and granted Taxpayer no possessory interest in the underlying pre-written software during or after the subscription term.

FINDING

Taxpayer's protest is sustained.

June 6, 2022

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