

Memorandum of Decision: 04-20210119
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 Company's transactions with various software vendors. Company was entitled to a refund of tax on transactions under which Company obtained software services, occurring prior to July 1, 2018, where Company did not acquire a possessory interest in the vendors' 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 for the acquisition or use of prewritten computer software.

STATEMENT OF FACTS

Taxpayer is an Indiana-based company which submitted a claim for refund for approximately \$138,000 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," 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.

A 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 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. 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)(l). 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 statute and 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) *and 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 refund denials concerning the following vendors and provided documentation to support its argument. In certain instances, Taxpayer provided copies of the underlying contract, written agreement, invoices, or terms of use.

Avalara

Taxpayer purchased tax automation software from Avalara. Along with publicly available information, Taxpayer provided invoices and terms and conditions between itself and Avalara.

According to its agreements with Avalara, Taxpayer has a temporary, non-exclusive, and non-transferrable right to access the software for a designated amount of time. The software cannot be reproduced, modified, sold, destroyed, or leased to others by Taxpayer. Any modifications Taxpayer would like to see in the software may be requested of Avalara, who may make those changes while keeping ownership of all related intellectual property rights. Upon termination of the agreement, Taxpayer will lose access to the software and Avalara with either return or delete Taxpayer's data.

Ceridian

Taxpayer purchased human capital management software from Ceridian. Along with publicly available information, Taxpayer provided invoices and its agreement for products and services with Ceridian.

According to the agreements with Ceridian, Taxpayer has a non-exclusive, non-transferrable right to access the software for a designated number of Taxpayer's employees over a designated period of time. Changing the number of employees with access will change the amount Ceridian charges for the software. Taxpayer cannot distribute the software or make it available for others to use. Copying, altering, reproducing, or failing to return materials to Ceridian is prohibited. Taxpayer also does not have the right to download the software onto their own servers; it must instead use the software through an internet browser. Ceridian maintains the physical facilities

and equipment to make the software available. If Taxpayer does not use Ceridian's software in 6 months, Ceridian has the right to terminate the agreement.

Microsoft

Taxpayer purchased data analysis, web application management, customer relationship management, and business productivity software from Microsoft. Along with publicly available information, Taxpayer provided invoices and agreements between itself and Microsoft.

According to the agreement with Microsoft, Taxpayer purchased a fixed-term license for access to the Microsoft software. Taxpayer may download, install, and use certain products on its own computers, but others must be used only through online access to Microsoft's servers. Taxpayer cannot lease, transfer, reverse engineer, or host for third parties any software or portion of the software. The term of this agreement, and Taxpayer's ability to renew the agreement, are specifically stated. If the agreement is terminated, Taxpayer must destroy the software and discontinue use.

Oracle

Taxpayer purchased wireless remote access services for the Oracle enterprise platform including resource planning, collaboration, data manipulation and analysis, and document management. Along with publicly available information, Taxpayer provided invoices and a related agreement between itself and Oracle.

Taxpayer pays for access to software stored on data center space owned or leased by Oracle. Taxpayer cannot modify, reverse engineer, reproduce, or download the software onto their own computer systems. Taxpayer only retains the right to access this software until the agreement expires. At that point, Oracle will delete or render inaccessible its production environments and delete Taxpayer's data. Taxpayer can only export its transactional data and attachments it uploaded to the Oracle server.

Qualys

From Qualys, Taxpayer purchased vulnerability management software. Taxpayer provided an invoice for this purchase, as well as terms of use.

Taxpayer must access the Qualys software through a web browser and cannot download the software onto its computers. Taxpayer cannot modify or alter the software and does not possess title or any rights in the software. The software must be uninstalled within 30 days of the contract termination.

Sales Tax Information Bulletin 8 (July 1, 2018), 20180725 Ind. Reg. 045180312NRA, explains how to analyze software transactions which occurred prior to July 1, 2018:

[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 purchases taxable, pre-written software from those in which the customer is paying for access to and use of software that 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.

Based on the documentation provided, the Department agrees that these transactions 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.

Taxpayer has also claimed that several of its invoices with Ceridian are only for services that are not taxable in Indiana. Ceridian's contract with Taxpayer contemplates additional expenses for professional services to modify data presentation by Ceridian's software. These additional invoices identify modifications to the data presentation and are therefore expenses for Ceridian to modify its own software to improve its usability for the taxpayer. These services are exempt from tax as no tangible personal property or possessory interest in software changed hands.

FINDING

Taxpayer's protest is sustained.

June 6, 2022

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