

Memorandum of Decision: 04-20211002
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 in part that Retailer was entitled to a refund of Indiana sales tax paid on Retailer's transactions with various software vendors. Retailer was entitled to a refund of tax on transactions under which Retailer obtained software services, occurring prior to July 1, 2018, where Retailer 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 of 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 \$259,000 paid as sales tax on transactions involving prewritten 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-I(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-I(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-I(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 prewritten 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.

Concur

Taxpayer purchased expense management software from Concur. Along with publicly available information, Taxpayer provided invoices, a sales order form, and a user agreement to demonstrate the details of the transactions in question.

According to the user agreement, Taxpayer is only allowed to access the expense management data through Concur's software and cannot download this data onto its own computers. Taxpayer is prohibited from modifying, customizing, or copying the software. The agreement also states that all rights and ownership of the software, the website, and the related information remain with Concur. Upon termination of the agreement, Taxpayer immediately loses access to the software and the related data.

Duo

Taxpayer purchased multi-factor authentication software from Duo. Along with publicly available information, Taxpayer provided an invoice and a related agreement between itself and Duo.

According to the agreement with Duo, Taxpayer is only granted a "non-exclusive, non- sublicensable, non-transferrable license to access and use" the software provided by Duo.

Taxpayer is not permitted to modify, share, copy or distribute the software. Duo can modify or update the software at its discretion. Although the agreement will automatically renew, providing 45 day written notice will end the agreement. Upon termination, Taxpayer would lose access to the software.

Microsoft

Taxpayer provided invoices and service agreements related to Microsoft purchases. None of the invoices provided show sales tax collected by Microsoft. No evidence was submitted showing that Taxpayer paid use tax on those transactions.

Oracle

Taxpayer purchased cloud-based software from Oracle for a variety of uses including human resources, resource planning, data manipulation, document management, performance management, supply chain management, financial analysis, and security. Along with publicly available information, Taxpayer provided invoices and a related agreement between itself and Oracle.

Schedule C of Taxpayer's agreement with Oracle for providing "Cloud Services" does not allow Taxpayer to modify, reverse engineer, reproduce, or download the software onto their own computer systems. Taxpayer may only use this software in the cloud which Oracle controls. Taxpayer is also prohibited from hiring a third-party to service the software - only Oracle may provide support for these programs. Oracle is permitted to modify the software infrastructure and security, as well as add or remove access to third-party content. Taxpayer agrees to purchase additional access if they exceed the users or storage allowed by their initial purchase. Immediately upon termination of the agreement, Taxpayer no longer has access to Oracle's software. If requested, Oracle will give the Taxpayer 60 days to retrieve their data from the cloud before Oracle terminates any saved data.

Schedule H of Taxpayer's agreement with Oracle explains the terms of the contract regarding hardware. Taxpayer does not elaborate on why this Schedule is included in its contract. While most of the invoices show Taxpayer remitting sales tax to Oracle, some show that no tax was collected. No evidence was submitted showing use tax paid on those transactions.

Paragon

Taxpayer purchased the following software from Paragon: an IBM management suite, a virtual execution environment for use with IBM, and a security software. Taxpayer provided invoices for these purchases as well as terms of use from IBM.

Taxpayer is charged a fee by IBM based on the number of users who have access to its software. Access to the software is based on a defined term in the agreement and will terminate or be renewed at the end of that term. When the agreement is terminated, Taxpayer will no longer have access to the software. The software includes updates and a set amount of maintenance. More maintenance and access to enhanced services can be purchased through a separate contract. IBM prohibits Taxpayer from selling access to its software or reverse engineering any portion of the software. No contracts or explanation are provided regarding Taxpayer's purchase of the security software.

Salesforce

Taxpayer purchased software from Salesforce for customer service, customer data sharing, application development, and analytics. Along with publicly available information, Taxpayer provided invoices and a subscription agreement.

Taxpayer's agreement with Salesforce states that the software purchases are subscriptions. New subscriptions may be added and removed at the same price and under the same contract on a pro-rated basis. Taxpayer is not allowed to sell, license, lease, or distribute the content purchased under the agreement. Taxpayer also is prevented from downloading, copying, or reverse engineering any part of the software. Any modifications Taxpayer would like to see in the software may be requested of Salesforce, who may make the changes while keeping ownership of all related intellectual property rights. Once the agreement expires or is terminated, Taxpayer no longer has access to the software.

Toshiba

Taxpayer purchased a document management software from Toshiba. No contract or analysis of who retains ownership interest in this software was provided.

Vertex

Taxpayer purchased on-demand tax software from Vertex. Along with publicly available information, Taxpayer provided an invoice and a copy of its agreement with Vertex.

Taxpayer's contract with Vertex gives Taxpayer the ability to use the software and to allow its affiliates to use the software, but these uses are explicitly limited to those which the contract enumerates. Vertex retains ownership and intellectual property rights to the software and any information developed or delivered to Taxpayer through the course of its agreement with Vertex. Taxpayer is prohibited from selling, transferring, distributing, or licensing the software to a third party. Taxpayer cannot copy, modify, or create derivative products from the software. Taxpayer can request the addition of new services or software access during the agreement, which will be provided at an additional fee, but these will come with a separate agreement. Vertex reserves the right to modify its software and will inform the Taxpayer in writing when it does so. Taxpayer does not have access to the software after the termination of the agreement.

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, prewritten 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 prewritten 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 transactions with Concur, Duo, Salesforce, and Vertex 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 prewritten software during or after the subscription term. Transactions with Paragon for IBM software were not subject to Indiana sales tax for the same reason. The Department also agrees that transactions with Oracle were not subject to Indiana's sales tax, to the extent that these transactions did not include the purchase of any hardware.

The Department finds that Taxpayer is not entitled to a refund of taxes paid on transactions with Toshiba, Microsoft, or Paragon not involving IBM, because the information provided about these transactions is ambiguous

and/or the nature of the transactions (what Taxpayer is buying and what the vendor is selling) is unclear. The Department will not issue refunds for transactions involving Oracle, Microsoft, or any other vendor where invoices and other documentation cannot show that sales tax or use tax has been paid. On all other points of Taxpayer's refund claim. The protest is sustained.

FINDING

Taxpayer's protest is sustained to the extent explained above.

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