

Computer Software Survey Detail Responses

March 24, 2005

States responding: Alabama, Arizona, Arkansas, District of Columbia, Georgia, Indiana, Iowa, Kansas, Kentucky, Massachusetts, Michigan, Minnesota, New Jersey, New York, North Carolina, North Dakota, Ohio, Pennsylvania, Rhode Island, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, Wisconsin, Wyoming

Q - Are you in favor of amending the rules to allow use of the MPU for all computer software regardless of the form in which the software is delivered?

Yes – (16) AL, AZ, DC, GA, IN, IA, KS, MA, MN, NJ, RI, UT, VT, WA, WI, WY

Comments:

Kansas – Sales and use tax laws historically have tried to source the taxation of goods to the State where the goods are used. This proposal is consistent with that approach.

Massachusetts – Would provide for uniform treatment of a product regardless of the method of delivery.

Minnesota – Another option would be to disallow the use of the MPU for all prewritten computer software since it is defined as tangible personal property whether delivered electronically or in tangible form.

Washington - As explained in the draft issue paper, this makes sense. However, this might be setting a precedent beyond software transactions. The same justification for using an MPU for software delivered in a tangible format could be used for the purchase of any tangible personal property delivered to a central location and then distributed by the buyer for use in several jurisdictions.

Wisconsin - Since we have already allowed such treatment for software delivered electronically, which is tangible personal property, I think it only fair that it be applied to the non-electronic version as well when there is concurrent use.

No – (12) AR, KY, MI, NY, NC, ND, OH, PA, SD, TN, TX, VA

Comments:

Arkansas - only taxes software sold in tangible form. Ark code presumes property delivered within the state is delivered for storage or consumption. Delivery location is easy to audit to determine the correct sourcing location.

Kentucky - Software delivered in tangible form should be sourced like other TPP (it is not concurrently available for use in more than one jurisdiction). If the software is delivered into a state that has no sales tax and subsequently is transferred to a state or states with sales tax, then the purchaser should be liable for use tax on the purchase price of the software in the states of usage.

Michigan - Software delivered in tangible form is no different than any other item of tangible personal property (the seller knows the location of the delivery), unlike

electronically delivered software (where the seller does not know the location of the delivery).

New York - New York's sales tax is a "transactions tax" with the liability for the tax occurring at the time of the transaction. Generally, a taxed transaction is an act resulting in the receipt of consideration for the transfer of title to or possession of (or both) tangible personal property. Tax becomes due at the time of transfer of title to or possession of (or both) the property. As a "destination tax," the point of delivery or point at which possession is transferred by the vendor to the purchaser, or the purchaser's designee, controls both the tax incidence and the tax rate. In the situation described in the issue paper, a transaction has occurred where tangible personal property is sold with a known point of delivery. As alluded to in the Issue Paper subsequent uses of the tangible personal property in jurisdictions outside the jurisdiction where delivery occurred (including uses in other local jurisdictions) would be subject to the compensating use tax.

North Carolina - Sales tax is a transaction tax, the actions that a purchaser takes with the delivered property following the completion of a sale should not affect the taxation. The MPU is designed to address the unusual situation where concurrent use of a product occurs because an item is not delivered in tangible form. Computer software delivered on a storage medium is delivered in a tangible form and should be treated like other tangible personal property.

Ohio - Needs further explanation and study.

Pennsylvania – It is unenforceable and will be a substantial revenue loss in PA.

Tennessee - believes allowing the use of an MPU for all computer software regardless of form in which the software is delivered conflicts with the intent of the sourcing rules by going to sourcing that is ultimate consumption for something that is clearly tangible personal property. In fact, sourcing rules do not affect whether the purchaser owes use tax in the jurisdiction of consumption. Sourcing rules are based on point of possession not ultimate consumption. However, Tennessee would support the creation of a form that is a seller's MPU jointly completed by both the seller and purchaser that would source and apportion the tax in the same manner as if the purchaser had claimed an MPU and reported the tax. Tennessee does not support seller's having an option to not collect tax at all. Tax in Tennessee is imposed on the vendor.

Texas - Texas currently only allows a claim of multistate benefit (i.e., MPU) for most taxable services (other than those like telecommunications services or repairs to tangible personal property that were imposed prior to September 1, 1987) and for certain types of direct mail printers. Texas taxes software as tangible personal property and if the software is shipped or delivered by the seller to a Texas location, Texas taxes the total charges even if some of the software is later moved and is used by the purchaser outside of Texas.

Virginia - All sales of tangible personal property should be sourced using the 310 sourcing rules.

1. How do you interpret the current rules in Section 312, when the seller is aware that a service or software will be concurrently available for use in more than one jurisdiction, but the purchaser does not provide an MPU?

All states responding indicated that the seller must source the sale according to the rules in 310(A), thus sourcing the sale to a single location.

2. Are you in favor of modifying Section 312 to allow sellers the option to collect sales tax based on information provided by the purchaser when the purchaser does not provide an MPU?

Yes – (6) AZ, GA, IN, KY, MA, TN

No – (22) AL, AR, DC, KS, IA, MI, NJ, NC, ND, NY, OH, RI, SD, TX, UT, VT, VA, WA, WI

Comments:

New York – Don't understand the question. Section 310 already requires sellers to collect tax based on information provided by the purchaser. Section 312 is only relevant for situations where an MPU is provided.

3. If you answered yes to #2 above, and the seller chooses not to collect sales tax based on the information provided by the purchaser, do you think that the seller is obligated to source under Section 310(A)?

Yes – (6) AZ, GA, IN, KY, MA, TN

Comments:

Tennessee - Seller should be required to collect based on MPU if purchaser provides information for Seller's MPU. If purchaser does not provide MPU or information for seller's MPU, seller is still obligated to collect tax based on 310A. Agreement should include provision like in direct mail that purchaser is not relieved of any liability in jurisdictions if the software is concurrently available.

No – Michigan - If the seller has sufficient information to permit allocation, then the purchaser should allocate.

4. Are you in favor of modifying Section 312 to require sellers to collect sales tax based on information provided by the purchaser? (This would be consistent with the rules for Direct Mail Sourcing in Section 313.)

Yes – (15) AL, AZ, DC, GA, IN, IA, KY, MN, NJ, NC, OH, RI, TN, VT, WI

No – (13) AR, KS, MA, MI, ND, PA, SD, VA, TX, UT, VA, WA, WY

Comments:

Kansas - For direct mailings, the person doing the mailing knows where the items will be delivered. This is a common business practice for the direct mailing industry. For other businesses, it appears that seller's knowledge of the delivery addresses could be sporadic at best. Therefore, this could become a little known rule that is only raised during audits to penalize the seller for non-collection. If this approach is to be taken, it should identify

what business sectors or business practices would require a seller to source its sales for the buyer based on MPU.

Massachusetts - Seems potentially burdensome for sellers if they don't want to do it and thus contrary to general objectives of SSTP.

Texas - We believe sellers are required to collect sales tax from the purchaser under Section 310(A). We believe the ultimate default sourcing rule in Section 310(A)(5) to source based on the seller's place of business from which the goods or services are delivered (origin basis) is a fair presumption if the purchaser refuses to give an MPU or to provide the seller information to source based on Section 310(A)(1)-(4). Currently, most states where the seller is located are likely to presume the sale of taxable items is subject to sales tax in that state unless the seller has actual records showing that the items were in fact shipped or delivered to another state. If an audit of a purchaser reveals the use of taxable items in a state, that destination state is free to set up that tax in an audit. The purchaser will then have an incentive to go back to the original seller to request a refund by providing sufficient information to show that the sale was exempt as an interstate shipment in the origin state. This is the current system of tax administration that makes it in both the seller's and purchaser's interest to voluntarily comply with the law and keep accurate records.

Washington - The information provided by purchasers of direct mail is address-specific. The seller of direct mail is actually sending the mail to various jurisdictions. The seller of software is not in the same position as the seller of direct mail in knowing where the items are delivered/will be concurrently used.)

Software Maintenance Contracts

Note: The chart and all comments concerning application of software to custom and prewritten software and computer maintenance contracts are included in the document titled: Summary of Responses to the Computer Software and Related Services Survey.

1. Does your state use an apportionment factor to impose tax on software maintenance contracts (such as MN's 80/20 rule described in the SOFTEC paper)?

Yes – (4)

- Iowa - uses a 50/50 rule
- Minnesota uses 80/20 rule described in paper
- Virginia - Generally, Virginia law imposes the sales tax on 50% of the value of a maintenance contract when the contract requires the provision of both parts and labor. If the maintenance contract is for labor (services) only, no tax would apply. This same rule would apply to computer maintenance contracts.
- Wisconsin – would allow whatever reasonable percentage the seller provides.

Comments:

Georgia - The Department is looking at the taxation of software maintenance agreements with a possibility of changing tax policy of non-taxation to imposing tax on a 50/50 rule.

Tennessee - Question: Is this 80/20 a cap or threshold which is not allowed by the agreement? To impose tax on a percentage of the sales price is not allowed. Tennessee had a similar situation in which 15% of a combined charge for bathing and grooming of animals was exempt. This was considered a violation of the caps and threshold provisions. Tennessee believes this is a bundled transaction in states where they tax only TPP and not services and the sale of the maintenance contract was optional and not mandatory. If mandatory, Tennessee believes the definition of sales price takes care of this and there should not be a definition for mandatory maintenance contracts that could be used to undermine the uniform administration of the definition of sales price. This is an attempt by the industry to get a uniform unbundling rule for maintenance contracts without calling it an unbundling rule. Tennessee believes if the states want to do this we will have to do it in the bundling rules.

2. If your state taxes “mandatory computer maintenance contracts,” is that because your state considers the cost of the contract to be part of the sales price of taxable goods.

Yes – (21) AL, AZ, AR, IA, IN, KY, MA, MI, MN, NJ, NC, ND, OH, RI, SD, TN, UT, VT, WA, WI, WY

Other:

Arkansas - Tax if upgrades are in tangible form

Georgia - doesn't impose tax on mandatory computer contracts, but considering a 50/50 rule

Kansas - The Kansas statute that taxes software specifically taxes software maintenance services. K.S.A. 79-3602(s) taxes:

the gross receipts received from the sale of computer software, the sale of the service of providing computer software other than ~~prewritten~~ *custom* computer software and the sale of the services of modifying, altering, updating or maintaining computer software, whether the computer software is installed or delivered electronically by tangible storage media physically transferred to the purchaser or by load and leave;

The department has construed this provision as taxing software updates and modification, but not telephone support lines, training seminars, etc. However, telephone support lines, training seminars, etc. are taxed unless they are separately stated.

Texas - Texas taxes the maintenance as a taxable service. Tax Code Section 151.0101(a)(5) taxes repair, remodeling, maintenance, and restoration of software unless the service provider did not sell or license the software to the customer.

New York - Generally, upgrades are software and are taxed accordingly when a separately stated charge is made.

Virginia – Virginia does not distinguish between “mandatory” and “optional” maintenance contracts. If the charge for the maintenance contract is bundled with the sale of taxable computer software and is not separately invoiced, the charge for the maintenance contract is considered part of the sales price and is subject to tax. If the

charge for the maintenance contract is not bundled and is separately stated on the invoice, the charge would be subject to the tax treatment generally applied to other maintenance contracts.

3. Is the sale of a software maintenance contract that provides both upgrades and help and training services for a single price a bundled transaction?

Yes – (20) DC, IN, IA, KS, KY, MA, MN, NJ, ND, OH, RI, SD, VA, TN, TX, VT, VA, WA, WI, WY

Comments:

Kansas – This is a bundled transaction. A proposed regulation that is currently in the process of review and approval states that if telephone support and training services aren't separately stated charges, the entire transaction is taxable.

Iowa – would treat as two separate products

Ohio - It is unclear how the two concepts (bundled transaction versus “single product with multiple components”) yield a different result. Currently, we would tax the transaction because it contains consequential tpp (the upgrades) that is not separately stated.

Texas - Texas does not tax a separately stated charge for software training. See Rule 3.308(b)(3) concerning charges for software training.

Wisconsin - the industry recognizes these products as distinct and identifiable by the fact that they want them to be taxed differently and give them separate names, etc.

No – (7) AL, AZ, AR, GA, MI, NC, UT

Comments:

Arkansas - Looks like this may fall within Bundled transaction Paper (C) (3) (a) of 11/17/04 paper drafted 11/8/04.

Georgia - The Department is looking at the taxation of software maintenance agreements with a possibility of changing tax policy of non-taxation to imposing tax on a 50/50 rule.

Michigan - There is no adopted definition of “bundled transaction”. Michigan considers a software maintenance contract that provides both upgrades and help/training services to be a single transaction with distinct components.

New York – No response – This would seem to depend on individual facts and circumstances surrounding the transaction. NY has issued Advisory Opinions where the facts indicate that support services were separately sold. (See for example TSB-A-98(59)S: “Petitioner makes available basic support services which are free of charge during the warranty period (the "Support Services"). These services include a telephone hotline service that allows the licensee to report problems with the functionality and productive use of the Program. These services also include making the Updates available. Additional Support Services, including on-site support and project management support, are available for a fee.”)