

**New York State Department of Taxation and Finance**  
**Office of Counsel**  
**Advisory Opinion Unit**

TSB-A-09(41)S  
Sales Tax  
September 22, 2009

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S081202A

Petitioner [REDACTED] asks whether the receipts from its licenses for the use of its software are subject to New York State sales and use taxes.

We conclude that Petitioner's receipts from the licenses for its software are receipts from the sale of prewritten software, which are subject to sales tax to the extent that the software is accessed by the customer's employees in New York.

**Facts**

Petitioner is an international software company with an office located in New York. Petitioner has customers and employees in several states including New York. Petitioner licenses a basic software package that is usually further customized to the customer's needs. Petitioner makes separate charges to the customer for the cost of modifying the software to meet the customer's needs. Customization charges typically involve linking the base software to a customer's specific accounting system, including unique ledger account codes, file layouts, etc. In addition, the customers may require unique reports that are customized to meet the customer's requirements. Separately stated charges for customization are billed the customer as performed and are not spread out over the licensing period.

Petitioner's customers (e.g., insurance companies) use the software to provide rate quotes, insurance contracts, and other insurance documents to insureds and prospective insureds of the customer. Petitioner provided the following illustration as a typical use of its software: A vehicle owner contacts Petitioner's customer and indicates that it is interested in purchasing an automobile insurance policy. The customer logs into Petitioner's software residing on a third party's server in Virginia using a URL address provided to the customer by Petitioner. The customer enters the vehicle owner's pertinent information (name, age, sex, location, etc.) into the software via the Internet connection. Petitioner's software processes the information entered in the system and produces a quote for the insurance policy. If the vehicle owner indicates that it wants to purchase the policy, the customer can immediately print an insurance ID card on the customer's printer and the insurance policy will be processed and issued overnight. The policy documents can be printed and mailed to the vehicle owner by the customer or the documents can be e-mailed to the vehicle owner by the customer.

The software (including the custom modifications) may be installed and stored on the customer's server(s) and is accessed from one or more of the customer's locations. The customer's employees may access the software from the location where the software is stored or from other locations both inside and outside the state where the software is stored.

The software may also be installed on servers located within and without New York owned by Petitioner or its agents and accessed by the customer's employees from within and without New York.

For customers who purchase the software for use on the customer's servers, Petitioner bills a flat fee for the license to use the base software package.

When the software is stored on servers owned by Petitioner or its agents, Petitioner is responsible for the maintenance of the hardware and the software. In this case, Petitioner charges the customer an additional separately stated "hosting fee."

The customers are billed monthly. However, where applicable, customers are separately billed for customization charges at the time that the customization services are performed. As part of the monthly fees, customers receive software support (software defect fixes and updates, training and helpdesk support), database administrative services (database monitoring, tablespace management, performance tuning), and production support (batch monitoring, output print monitoring, interface monitoring, and other activities required to maintain production day to day).

### **Analysis**

Tax Law section 1105(a) imposes sales tax on the sale of tangible personal property. Prewritten computer software is included within the definition of tangible personal property, "regardless of the medium by means of which such software is conveyed to the purchaser." Section 1101(b)(6) of the Tax Law. Thus, the sale of prewritten computer software is subject to tax as the sale of tangible personal property. See sections 1101(b)(6) and 1105(a) of the Tax Law.

*Sale* is defined as "Any transfer of title or possession or both, exchange or barter, rental, lease or license to use or consume (including, with respect to computer software, merely the right to reproduce), conditional or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement therefor." Section 1101(b)(5) of the Tax Law. Section 526.7(e) of the Sales and Use Tax Regulations provides generally that "a sale is taxable at the place where the tangible personal property or service is delivered, or the point at which possession is transferred by the vendor to the purchaser or his designee." Section 526.7(e)(4) further provides that, with respect to a "license to use," a transfer of possession has occurred if there is a transfer of actual or constructive possession, or if there has been a transfer of "the right to use, or control or direct the use of, tangible personal property." The location of the code embodying the software is irrelevant, because the software can be used just as effectively by the customer, even though the customer never receives the code on a tangible medium or by download.

The accessing of Petitioner's software by Petitioner's customers constitutes a transfer of possession of the software, because the customer gains constructive possession of the software, and gains the "right to use, or control or direct the use of," the software. See *Adobe Systems, Inc Adv Op Comm T & F*, November 24, 2008, TSB-A-08(62)S.

The location of the code embodying the software is irrelevant. The software is used just as effectively by the customer whether it is stored on the customer's servers for access by the customer's employees or is stored on servers owned by Petitioner (or Petitioner's agents) from which the customer's employees access the software. Whether the software is installed on the customer's server

or is stored on Petitioner's servers, the access and use of the software by the customer's employees is effectuated. Accordingly, Petitioner's sale of the license to use its basic software package is subject to sales tax under Tax Law §1105(a) regardless of where the software is stored. *See Jeffrey J. Coren CPA*, TSB-A-09(19)S, May 21, 2009.

The situs of the sale for sales tax purposes is the location associated with the license to use (i.e., the location of the customer's employees that use the software). *See Adobe Systems, Inc. supra*. In the present case, if the locations where the customer's employees will use the software are both in and out of New York State, Petitioner is only required to collect tax based on the portion of the taxable receipts attributable to the employees' use of the software at locations in New York. (*See KPMG LLP*, Adv Op Comm T & F, January 31, 2003, TSB-A-03(5)S.) The determination of the proper local tax rate and jurisdiction is also based on the locations associated with the licensees' use.

Petitioner modifies and customizes its basic program depending upon the customer's specific needs. The combining of two or more prewritten software programs or prewritten portions of such programs does not cause the combination to be other than prewritten software. *See* section 1101(b)(14) of the Tax Law. Therefore, petitioner's receipts for the basic program remain subject to sales tax. Petitioner's charges to customers for providing modifications or customization to the basic program presumably reflect Petitioner's cost to modify the prewritten software. When there is a reasonable, separately-stated charge for customization of the basic program, the charge for the modification will not constitute a receipt from the sale of prewritten software and will not be subject to tax when performed for and sold to the customer who initially requested the custom modification. *See* section 1101(b)(14) of the Tax Law and TSB-M-93(3)S, *State and Local Sales and Compensating Use Taxes Imposed on Certain Sales of Computer Software*, March 1, 1993. It should be noted that subsequent sales of the basic program incorporating such modifications into programs provided to other purchasers would be subject to tax as the sale of prewritten software.

Petitioner's fees for software support encompass defect fixes and software updates and training and helpdesk support. Fees for software updates and patches to fix defects are subject to sales tax as the sale of prewritten software. Separately stated and reasonable fees for training and support may be excluded from the receipt subject to tax. (*See* TSB-M-93(3)S, *supra*.) However, if a lump sum charge is made to a customer that includes training and support, or if the separate charge for training and support does not reasonably reflect the value of these items, then the entire charge will be taxable.

Other portions of Petitioner's monthly fees (inclusive of the charges for hosting the software, database administration, and production support whether or not separately stated) encompass activities related to Petitioner's overhead costs in ensuring that its software performs for customers as guaranteed rather than activities separately purchased by users. Though the hosting and other services by themselves may not be included among the enumerated services that are subject to tax ( *See Alan J. Goldstein/The Computer Studio*, Adv Op Comm T&F, December 29, 1997, TSB-A-01(21)S; *CAV CORP d/b/a Stone Soup Multimedia*, Adv Op Comm T&F, December 29, 1997, TSB-A-97(87)S), when these services are sold in conjunction with prewritten computer software and it is not shown that both these services and the software are each individually offered for sale and sold other than in combination, the combination of items will be considered as one, and thus subject to tax as a single purchase. This will be true even though the charges for the services and software are separately stated. *See Penfold v State Tax Commission*, 114 AD 2d 696 [1985]. Thus, the fees Petitioner's customers

pay for hosting and those other activities (database administration, etc.) are for integral components of their licenses to use the software and are subject to tax. *See Jeffrey J. Coren CPA, supra.*

DATED: September 22, 2009

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/S  
Jonathan Pessen  
Director of Advisory Opinions  
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NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.