

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

TSB-A-10(59)S
Sales Tax
November 23, 2010

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S100922C

On September 22, 2010, the Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED]. Petitioner asks whether its electronic discovery litigation support services are subject to New York State and local sales or use taxes.

We conclude that Petitioner's litigation support services are not subject to sales or use taxes, regardless of the media on which the reports are delivered.

Facts

Petitioner provides collections and forensics, processing, search and review, and document review services to companies and the litigation departments of law firms. Petitioner performs its operations from its offices in New York State. Petitioner's clients are typically large corporations that use Petitioner's services cooperatively with their legal counsel to manage the electronic discovery process for litigation and regulatory matters.

Petitioner describes its electronic discovery litigation services as follows: A client or law firm provides Petitioner with data to process and search on various media (e.g., e-mail, server, hard drive, CD Rom). This information is usually gathered in order to respond to a subpoena, a discovery-related request for information or in connection with a formal complaint in litigation. The data are maintained on the original medium and returned to the client after installation on Petitioner's servers. A client may request that documents identified during the search phase be presented in a basic format (e.g., a TIFF image) or in its native format.

Petitioner's proprietary software processes the client's data and then normalizes documents into a similar format. This software has the ability to process hundreds of different file types, and puts the documents into a format for review. Petitioner's proprietary software also performs a number of activities and functions, which allow a client to more efficiently perform review functions on documents loaded onto Petitioner's servers. These functions include:

- Foldering/document categorization by topic, including dynamic foldering (organizing documents by custodian or e-mail thread, as specified by the client).
- Search features.
- Marking and redacting, including annotation, highlighting and redaction tools.
- Trending analysis – this feature tracks the review process by the number of documents reviewed by a particular reviewer and the time it takes to complete the review, and creates reports to analyze the reviewer's productivity.
- E-mail threading – recreates e-mail correspondence in a thread showing the various responses in sequence.
- Near duplicate analysis – flags potential duplicate documents for review.
- De-duplications – eliminates duplicate documents (e.g., same e-mail in more than one person's e-mail file).

- Automated workflow, so clients can plan and direct the flow of documents and ensure that the right data are getting to the reviewers on schedule
- Foreign language support.
- Ability to add/modify fields in real time.
- Automated topic clustering.

Petitioner charges clients a processing fee based on the amount of data processed and a hosting fee based on the amount of data that are stored. Data are stored until a case closes, at which time the data are archived, returned to the client, or destroyed. Clients then have the ability to access the processed data to sort, organize, add notes, edit, etc., through a license granted to clients that allows clients to access to the processed data. Clients do not have the ability to access or manipulate Petitioner's proprietary software.

While the data are stored, clients can request that files be created in a TIFF format to assist in the document review process. Once relevant data (e.g., data responsive to a discovery demand) have been identified by the client, Petitioner sorts and organizes the data. Petitioner writes the data to a universally accessible version, which is transferred back to the client. The form of output is a TIFF file or native format. Petitioner also charges fees based on the number of pages delivered and the delivered medium. The charge for the delivered medium varies by the type of medium (e.g., \$10-20 per CD, \$35-20 per DVD, \$200-300 per hard drive). Petitioner indicates that the charge for the delivered medium is nominal in relation to the overall charge for the service. In some cases, the medium of delivery is electronic transfer, for which there is no charge.

Upon completion of the engagement, the processed data are either archived for a storage fee, returned to the client, or destroyed. The client's data are not provided to any other person or used by Petitioner for any other use. Petitioner does not take title to the client's data.

Petitioner also assists its clients with certain consulting and other services, all of which are related to the client's data, including targeted searches of data, sorting and organizing documents, and user training, among other things. These services are separately available and the charges for these services are separately stated at a set hourly rate.

Analysis

We conclude that Petitioner's litigation support services are information services, but they are personal and individual in nature, and therefore not subject to New York State and local sales taxes.

As relevant here, Tax Law section 1105(c)(1) imposes tax on the receipts from the sale, except for resale of the service of:

[F]urnishing information by printed, mimeographed or multigraphed matter, or by duplicating written or printed matter in any other manner, including the services of collecting, compiling or analyzing information of any kind or nature and furnishing reports thereof to other persons, but excluding the furnishing of information which is personal or individual in nature and which is or may not be substantially incorporated into reports furnished to other persons, and excluding the services of . . . persons acting in a representative capacity

Petitioner's litigation support services are information services because they include analyzing, compiling, and organizing a client's information. Petitioner's services do more than merely recast or reformat the client's information. For example, Petitioner adds to the information by categorizing like documents, identifying potential duplicates and eliminating duplicates, organizing e-mails into sequential threads, and

enabling documents to be searched by type, custodian, etc. This analysis adds to “intelligence” contained in the original documents, and therefore constitutes an information service. *See ADP Automotive Claims Services, Inc. v. Tax Appeals Tribunal*, 188 AD2d 245 (3d Dep’t 1993). The ability for a client to mark and redact documents has some attributes of the use of software. However, because this is a single aspect of a more comprehensive service, and this aspect is integrally related to the overall service provided by Petitioner, we conclude that the primary function of Petitioner’s service is the provision of an information service, and not the sale of prewritten computer software.

However, we further conclude that Petitioner’s services are excluded from the tax on information services because they are personal and individual in nature. Petitioner organizes and analyzes the client’s own documents and does not provide the original documents, or the analysis, compilation, or organization, to any party other than the client. The fact that the client, in the context of a litigation discovery process, may subsequently provide the original documents to a third party does not change this result.

Petitioner’s optional services of targeted data searches, sorting and organizing documents may constitute information services to the extent that they add to the intelligence contained in a client’s original documents. However, because these services, like the litigation support services discussed above, are performed on the client’s own documents, and no information or analysis, compilation, or organization is provided to third parties, these services are excluded from tax as personal and individual in nature. Petitioner’s optional consulting and training services are not services that are subject to sales tax. *See* TSB-A-09(46)S; TSB-A-09(33)S; *KPMG, LLP*, TSB-A-00(7)S. Petitioner’s charges for archiving data in electronic form are not subject to tax. *See Connected Corp.*, TSB-A-05(40)S; *Immediate Medical Records, Inc.*, TSB-A-92(7)S.

Petitioner also asks whether the delivered media (i.e., DVDs, CDs, hard drives, electronic transfer) are subject to sales tax. Tax Law section 1105(a) imposes sales tax on “the receipts from every retail sale of tangible personal property.” Tangible personal property includes “[c]orporeal personal property of any nature.” Tax Law §1101(b)(6). Some of the delivered media Petitioner describes (e.g., DVDs, CDs and hard drives) are tangible personal property. Nevertheless, because personal or individual information services are not subject to tax regardless of the form in which the information is provided to clients, tangible personal property that is an integral part of the provision of these services is not separately taxable. Accordingly, because Petitioner’s delivered media are an integral part of the provision of its nontaxable information services, we conclude that the charge for the delivered media is not a receipt for tangible personal property. However, Petitioner’s purchases of tangible media that it uses to deliver its services to its clients are subject to State and local sales and use tax. *See* TSB-A-10(20)S.

DATED: November 23, 2010

/S/

DANIEL SMIRLOCK
Deputy Commissioner and Counsel

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.