

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S130314A

The Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED] (“Petitioner”). Petitioner asks whether its “Cloud Collaboration Service” (“Product”) is subject to sales tax and whether it owes any sales or use tax on its purchase of hardware and software.

We conclude that Petitioner’s service constitutes prewritten software, the sale of which is subject to New York State and local sales taxes. Petitioner’s hardware will not be subject to sales or use tax if it is not delivered or used in New York. If Petitioner purchases software in New York that is intended exclusively for resale to its customers, such purchases would be exempt from sales tax.

Facts

Petitioner sells Product, which supports by remote means a customer’s telecommunication system. The crux of Petitioner’s service is to assist the customer’s own telecommunication system in the processing and routing of communications. Specifically, Product is an alternative to the customer using its own software and related hardware to support its telecommunication system.

Petitioner owns, leases or licenses the hardware and software used to provide Product. This software is installed on Petitioner’s servers located outside New York. Petitioner’s customers do not download any software owned or licensed by Petitioner. The hardware components used to provide these services are also located outside New York. Petitioner’s customers are responsible for providing connectivity of sufficient bandwidth between the customer’s location and Petitioner’s data center, as well as connectivity to the Internet and the Public Switched Telephone Network (“PSTN”). The PSTN or other connections can reside throughout the customer locations and are terminated into Petitioner’s data center through customer-owned gateways managed by Petitioner. Customers remain the “customer of record” with third-party providers of PSTN, Internet access or other transmission services.

Petitioner’s Product does not provide the ability to transmit messages or information across any telephone, Internet or other network lines. Rather, Product enhances the functionality of the customer’s own telephone system by providing instructions to the customer’s equipment for the processing and routing of incoming and outgoing communications.

Petitioner’s Product includes the following capabilities:

1. Voice -- Petitioner's server communicates with the customer's gateway device (i.e. the customer's own switch) to provide instructions for the processing and routing of incoming and ongoing calls to or from the customer's phone extensions. No calls are routed to Petitioner's server. That is, no end-to-end communication is ever routed through Petitioner's system. For example, when a customer's telecommunication system receives an incoming telephone call, Petitioner's applications will direct the customer's telecommunication system (including the customer's switch) to route the call to the appropriate internal extension without the call ever leaving the customer's telecommunication system. This system also supports a customer's other forms of communication to IP end-points, media processing devices, VoIP gateways, mobile devices, and multiple media applications.
2. Video – This component is provided through Petitioner's servers in the same manner as, and performs functions similar to, the Voice component. This component provides instructions to the customer's own computer and telecommunication systems for capturing, recording, processing, storing, transmitting, and reconstructing a sequence of images.
3. Messaging – This component directs the customer's gateway device to send an incoming call to voice mail if a customer's phone extension does not answer. The voice messages are then stored on Petitioner's servers and are available for the user to access at his or her convenience.
4. Presence – This component provides users the ability to determine when colleagues are available to communicate. The customer's own communication equipment accesses an application on Petitioner's server to utilize the presence capabilities.
5. Audio Conferencing – This component supports the customer's own audio conferencing capabilities. It is provided in the same manner as, and performs functions similar to, the Voice component.
6. Web Conferencing – This component employs a third-party application that permits desktop sharing through a web browser with phone conferencing and video. The application resides on Petitioner's server, and provides instructions to the customer's own computer and telecommunication systems for the handling of web conferencing.
7. Mobility Services – This component supports a customer's mobile devices through a third-party application. Mobile customers utilizing this application can place and receive calls over their own business's wireless local area network and telephony infrastructure, using Petitioner's server to instruct the customer's own telecommunication system in the routing of calls. No end-to-end communications is ever routed through Petitioner's server.

Petitioner bills customers that purchase Product a startup fee that includes the cost of modifying Petitioner's software to enable it to interact with and direct the customer's

telecommunication system. Petitioner also bills a monthly user license fee for Product, which is calculated based on the number of users. The “Service Descriptions” for Product state that the monthly fee includes “virtual server instance charges, required storage charges, rack space charges, power and cooling charges as well as monitoring and management charges, most moves-adds-changes and major version upgrades.

Analysis

We conclude that Petitioner’s charges for Product constitute receipts from the sale of prewritten software. Sales tax is imposed on receipts from the sale of tangible personal property, including prewritten software, “regardless of the medium by means of which the software is conveyed to the purchaser.” Tax Law § 1101(b)(6); *see also* Tax Law § 1105(a). Prewritten computer software is any computer software that is not designed and developed by the author or other creator to the specifications of a specific purchaser. Tax Law § 1101(b)(14). Prewritten software remains prewritten software, even if modified or enhanced to the specifications of a specific purchaser, except to the extent that there is a reasonable, separately-stated charge for such modification or enhancement. *Id.*

“Sale” is defined as “[a]ny 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) or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement therefor.” Tax Law § 1105(b)(5). Sales and Use Tax Regulation 526.7 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.” Regulation 526.7(e)(4) further provides that, with respect to a “license to use, “a transfer of possession has occurred if there is 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. *See* TSB-A-08(62)S.

The essence of Petitioner’s Product is software. Petitioner’s Product facilitates the operation of a customer’s telecommunications system by allowing the customer to remotely access its software. This software then “instructs” the customer’s own equipment to perform various functions, such as instructing the customer’s switching apparatus on how to route a telephone call or to direct a call to voice mail if the user does not answer.

Petitioner’s receipts from Product constitute receipts from the sale of prewritten computer software because its customers have the right to use, control, and direct the use of, Petitioner’s software to facilitate the operation of the customers’ telecommunication systems. A customer contracts with Petitioner to modify Petitioner’s software to allow it to interact with the customer’s telecommunication system and to instruct the customer’s telecommunication equipment to perform various functions. By contracting with Petitioner to purchase a license to use Product, the customer is directing the use of Petitioner’s software to interact with its telecommunications

system. Thus, the customer obtains constructive possession of the software. *See* 20 NYCRR 526.7(e)(4).

The situs of a software license for purposes of determining the proper local tax rate and jurisdiction is the location associated with the license to use. *See* TSB-A-12(3)S; TSB-A-03(5)S. Petitioner should collect tax based on the portion of the receipts attributable to its customers' telecommunications systems located in New York. *Id.* For this purpose, Petitioner may rely on information received from its customers about the location of their telecommunication systems. *See* Tax Law §§ 1132(c)(1); 1142(4).

Petitioner's start-up charges are separate from the charges for the license to use its software. Because these charges are for modifying Petitioner's software to enable it to interact with and direct the customer's telecommunication system, they constitute receipts from custom software and are not subject to sales tax, as long as the charge for the customization is reasonable and separately stated on the invoice or billing statement provided to the customer. *See* TSB-M-93(3)S –*State and Local Sales and Compensating Use Taxes Imposed on Certain Sales of Computer Software*; TSB-A-09(44)S; TB-ST-128.

Petitioner is the retail purchaser of the hardware that it uses to provide Product. Petitioner will not owe sales or use tax on its purchases of such hardware if the hardware is not delivered to or used by Petitioner within New York State. To the extent that Petitioner purchases software in New York that is intended exclusively for resale to its customer, those purchases would be exempt from sales tax as long as the Petitioner is registered for sales tax purposes and timely furnishes the vendor with a properly completed resale certificate.

DATED: July 6, 2017

/S/

DEBORAH R. LIEBMAN
Deputy 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. The information provided in this document does not cover every situation and is not intended to replace the law or change its meaning.