New York State Department of Taxation and Finance — Office of Counsel

Advisory Opinion: TSB-A-24(43)S

The Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED]. Petitioner asks whether three of its investment management products are subject to sales tax.

We conclude that sales of Petitioner's products constitute the sale of pre-written software, and that the annual fees that Petitioner charges for them are taxable as such.

Facts

Petitioner is a financial services firm that provides investment and risk management systems to clients, which are generally "buy side" institutions (i.e., investment managers, mutual funds, pension funds, hedge funds, insurance companies, etc.) and "sell side" institutions (i.e., broker-dealers). Among Petitioner's offerings are three products ("Products") that are made available only to clients who subscribe to Petitioner's professional service Product[1]. These Products, which are distinct and billed separately from Petitioner's professional service product , provide clients with fully integrated enterprise portfolio management support, and are: (1) Trade Order Management Solutions (Product 1), (2) Sell-side Execution and Order Management Solutions (Product 2), and (3) Asset and Investment Manager (Product 3).

The functionality of Petitioner's Products is essentially the same; the primary difference between them is who the Product is designed for. Product 1 is designed for sell-side fixed income institutions (e.g., broker-dealers that are market-makers), while Product 2 is designed for sell-side equity institutions (e.g., a broker-dealer that makes a market in stocks). By contrast, Product 3 is designed for certain types of buy-side institutions (e.g., asset managers, pension funds, etc.). Each Product provides customers with investment analysis and reporting, data control and operations, compliance evaluation and reporting, trade management workflow, daily support and ongoing service enhancements, and ancillary services. Each Product is accessed via the Internet through a software interface that is hosted on Petitioner's servers, and generally is made available to clients 24 hours a day, seven days a week.

A. Implementation & Platform

Petitioner's Products, by their nature, provide the client with access to software and allow for a large amount of information to be transferred daily between Petitioner and the client, as well as to other parties involved in a client's investment and related management activities. To do this, Petitioner provides a platform for each client. Petitioner purchases, builds, and configures the technological infrastructure, including the telecommunications, software, and databases that are necessary to support the client platform. In addition, Petitioner provides a team of implementation and account managers, including product specialists and technical employees, to implement these platforms and help clients use each Product. The implementation of Petitioner's Products is configured based on the

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[1] Petitioner states that it allots sales tax on charges for its professional service product.

needs of each client and can take upwards of a year to complete. There are generally no additional charges for this implementation. However, if integration with third-party systems is necessary, additional fees may be charged and determined on a client-by-client basis.

B. Product Components

Every platform developed by Petitioner uses databases and runs on servers that are maintained and owned by Petitioner. Once logged-in, clients generally have access to all of a Product's components. While the components are not separately available, they can be used in different proportions by different clients. These components include the following:

1. Risk Analysis

Using Petitioner's products, clients have the ability, using software on the customer's platform, to perform basic risk analysis of securities that the client owns or otherwise has risk exposure to. This includes adjusting bond maturity dates and their duration (based on the sensitivity of bond prices to interest rate fluctuations), recalculating risk and benchmarking exposure equivalents (e.g., fluctuation in foreign exchange rates), and conducting "what-if" scenario analyses. For an additional fee, clients also can receive a premium risk service that provides additional software tools to perform more sophisticated analysis and can use the results of the analyses to populate and distribute reports outside of the software. This additional software, in other words, enhances the standard risk analysis that is provided as part of Petitioner's Products[2].

2. Data Control and Operations

Petitioner provides a dedicated database for maintaining each client's trade order information, including security positions, transactions, prices, security data, and analytics. This approach is designed to enhance client data integrity and significantly reduce operational risk. This approach also maintains integrity and privacy by segregating clients' respective data.

Petitioner provides data management support for external data sources that are used by its clients with Petitioner's Products, including security pricing services, index providers (i.e., sources that benchmark the performance of securities of a market sector or industry, e.g., energy or healthcare), rating agencies, and other client-specific data sources. Some of these data are publicly available, while the rest must be purchased by the client.[3] As part of the daily support services, Petitioner's employees maintain relationships and interface with external data providers if there are any problems with the stream of data.

Petitioner's Products also maintain each client's trade order-related data, including each client's unique profit and loss and security positions, which only the client can access. In this regard, the Products, by providing access to software, maintain trade settlement, broker-dealer, and custodian data management necessary to facilitate a client's investment management process from trade execution through post-trade functions. This includes trade confirmation processing, trade compliance, and corporate action processing. At the client's direction, Petitioner also facilitates communication by transmitting data to third parties related to trade activity, including counterparties, brokers, electronic trading venues, and custodial banks. The trade execution and post-trade operational services are

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[2] Petitioner did not request an opinion specifically on the taxability of this additional software. Thus, for purposes of this Advisory Opinion, we will presume that the taxability is linked to the taxability of the products at issue on this opinion.
[3] While Petitioner does sell access to certain data, such sales are not made as part of the Products at issue. Moreover, clients need not buy any data from Petitioner to subscribe to the Products. The taxability of the sale of these data, therefore, is not addressed herein.

supported by real-time reporting on transaction status. Petitioner's Products also facilitate reconciliations of a client's positions and cash activity to other third party sources, such as a client's custodial bank.

3. Trade Management Workflow

When a client's employee enters a trade order on a Product's platform, software on the platforms sends the trade order to the desired destination for execution and generates trade status reports for the client's systems. Through the platform, the client can automate the creation of reports about the status of client investments, including the status of trades routed to or from third party electronic trade execution services (e.g., Tradeweb, iCap), and perform other activities necessary to trade management, including asset allocation to multiple accounts. These services can be integrated with external industry tools that clients use in connection with their orders and trades. This allows clients to manage their investments in one place. Petitioner provides interface support and maintenance services with third parties, such as data providers, to facilitate access to pricing and trade data. These support and maintenance services include configuring the Products to the platforms of such service providers.

4. Compliance Evaluation and Reporting

The Products allow clients to perform and comply with their various regulatory and compliance obligations. The Products include pre- and post-trade software to manage compliance by providing a real-time interface that allows clients to perform intraday compliance checks during normal business hours, and that allows global compliance officers to research and approve/reject violations. The software is "administrative-based," meaning that the user can make system-wide administrative changes in real time, including the ability to specify who has access to the system and what information can be accessed. Petitioner's Products also allow clients to create a comprehensive audit capture of all their trade activities through an audit trail tool. To ensure compliance with each portfolio's trading strategy and related requirements, clients can implement investment restrictions and compliance parameters directly into the platform themselves. Alternatively, clients can communicate their desired parameters to Petitioner's employees who can enter the parameters into the platform. The platform then takes those parameters and creates the restrictions and alerts.

The compliance component of Petitioner's Products is generally highly personalized; Petitioner's Products validate each potential trade against a client's predetermined compliance rules. If there is a violation, the Products provide an alert, by such means as a notification "window" that pops up on a client's compliance officer's screen. Petitioner's compliance evaluation service requires designated client personnel to authorize transactions relative to certain compliance levels and exceptions. Once alerted, compliance officers use a specific function within the platform to review the details of violations and to approve or reject the proposed transactions.[4]

5. Daily Support and Service Enhancements

Petitioner provides support personnel who are generally available 24 hours a day seven days a week, and are responsible for any issues relating to daily service requests, administrative tasks, and reporting issues. Petitioner's representatives regularly apply their knowledge and judgment to perform services related to each client's unique organizational process requirement. For example, because the implementation of the products is configured based on a client's needs, a representative must have a

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[4] For an additional fee, clients can receive a premium compliance product that provides professional expertise on rule construction and violations management and that also includes expanded online audit storage, support during regulatory inquiries, and other professional support and services. Petitioner is not inquiring about the taxability of this additional fee.

deep understanding of how the platform's software interacts with other software and systems. Thus, if a report indicates a problem with a security price, the representative needs to understand the client's platform, as well as consider the source of the pricing information to resolve the problem. Petitioner uses a range of skilled professionals to perform product support that includes product specialists, relationship and account managers, technology and implementation specialists (including computer programmers), and product developers.

Petitioner provides daily support to clients through real-time access to customer service, including relationship and account managers, help desk and technical support. Relationship and account managers are responsible for managing the overall relationship with a client, as well as understanding a client's operations. Trade desk support personnel are available to clients on demand and are responsible for answering client questions, such as an inquiry by a client about how to grant permission to a user to access profit and loss information for a given firm. Technical support personnel assist on highly technical and complex escalated client issues, such as resolution of a bug in the platform's software code. Petitioner's customer service provides daily support and training covering administrative requests and business process support. These teams support numerous daily requests unique to each client, which may range from interface setup and compliance coding to real-time trading issues.

As a client's needs evolve, Petitioner enhances its services and administrative support to accommodate those needs. These ongoing service enhancements and improvements are included in Petitioner's fees.

C. Fees

Petitioner charges an annual fee for each of its Products, which generally is based on the extent of a client's overall use of the Product and its complexity. Other than those mentioned above, there are no separately-charged fees for these Products. However, in some cases, the terms of the agreement between Petitioner and a client set a predefined limit on the volume of certain trading transactions that the client can process. If the client exceeds that predefined limit for a certain period, the client may owe additional charges on a per-transaction basis.

Analysis

New York imposes sales and use tax on, among other things, retail sales of tangible personal property and on certain enumerated services. See Tax Law § 1105(a)-(c). The definition of tangible personal property includes prewritten software. See Tax Law § 1101(b)(6). Prewritten computer software is defined in part as "[c]omputer software (including pre-written upgrades thereof) which is not software designed and developed by the author or other creator to the specifications of a specific purchaser." Among the services subject to sales tax are information services, excluding "the furnishing of information which is personal or individual in nature and which is not or may not be substantially incorporated in reports furnished to other persons." See Tax Law § 1101(c)(1), (9).

Because the components of Petitioner's Products (such as their trading platform and various functionalities) are not separately available for sale, each of Petitioner's Products should be taxed as a single unit. In our view, the principal aspect of each Product is that it gives the client access to the investment management platforms - which consist of software - to analyze information and make business decisions, such as buying a stock, or implementing a risk management trading rule. While the platforms use the individualized data of the clients, the software is not designed to the specifications of those clients. The activities of Petitioner's employees appear to be focused primarily on ensuring that the platform functions as intended, and helping Petitioner's clients use the platform, rather than

providing additional services unrelated to the platform. Petitioner's receipts from its Products (i.e., its annual fees), therefore, constitute receipts from the sale of software because Petitioner's customers have the right to use, control, or direct the use of the software that underlies Petitioner's Products. See 20 NYCRR 526.7(e)(4). To the extent that additional charges are made for access to additional software, which appears to be the case for access to a premium risk service that is offered, these charges also would constitute receipts from the sale of software. The location of the code embodying any of the software at issue is irrelevant, because the software can be used just as effectively by a client even if such client never receives the code on a tangible medium or by download.

Moreover, while the platforms use the individualized data of Petitioner's clients, this customization of information that is input into the software that runs on Petitioner's platforms does not equate to the design or development of the software to the specifications of a specific customer. All this software, therefore, is properly considered pre-written computer software, the sale of which is subject to sales tax. See Tax Law §§ 1105(a); 1101(b)(6) (pre-written computer software included within the definition of "tangible personal property"); 1101(b)(14) (defining "pre-written computer software"). See also, TSB-A-17(9)S; TSB-A-17(4)S.

Petitioner, however, suggests that its Products are similar to the products addressed in TSB-A-13(12)S and found to be nontaxable. Like Petitioner's Products, the product in TSB-A-13(12)S, referred to as Product A, also provided customers with a platform in which to conduct an investment management business. However, unlike Petitioner's Products, Product A, which was only made available to clients during business hours Monday through Friday, offered several significant employee-driven service deliverables that Petitioner's Products do not. For example, Product A offered a daily risk analysis service that involved employee review of performance attribution reports before their release to clients. In addition, Product A also offered an "ad hoc risk analysis component" that required the service provider, after conferring with the client about the issue, to use its own analysts to choose an existing test or to develop a new one to determine the risks associated with the issue. Standing alone, such a service is a nontaxable information service. See TSB-A-92(5)S (an investment evaluation reports found to qualify for the "personal or individual" exclusion from the tax on information services in Tax Law § 1105[c][1] because the reports were based on the particular holdings in the client's account). Further, Product A included a customized compliance evaluation and reporting service, under which the service provider itself would design trading rules to meet the compliance parameters of the client and code those trading rules into the client's trading platform. This aspect of Product A also is a nontaxable service offering. See TSB-M-93(3)S. We, therefore, find that Petitioner's Products are materially different from Product A.

Finally, the situs of the sale for purposes of determining the proper local tax rate and jurisdiction is the location associated with the right to use Petitioner's software, i.e., the location of the client or its employees (if applicable). See, e.g., TSB-A-13(22)S; TSB-A-09(15)S. If a client has employees located both in and out of New York State who use Petitioner's software, Petitioner should collect tax based on the portion of the receipts attributable to the customer's users located in New York State. See TSB-A-17(4)S.

DATED: October 8, 2024

/s/

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