

## Draft Regulation—Prewritten Software Accessed Remotely

The Vermont Department of Taxes is soliciting comments on **draft** regulatory language related to the collection of sales tax on prewritten software accessed remotely. In order to provide more clarity, the Department will publish regulations to provide further guidance in the application of the tax. Upon completion of this informal comment period, the Department intends to initiate the formal rulemaking process during which further comments can be submitted.

Please note that the fact sheet (Pub. FS-1001) expired on 6/30/2014 and is no longer in effect. This should not be relied on for guidance.

### Background

The legislative moratorium on collection of sales tax on prewritten software accessed remotely expired on June 30, 2013. Purchases before July 1, 2013, are not taxable, but purchases since then are taxable.

#### *Prewritten Software:*

Vermont has defined tangible personal property to include “prewritten software.” It is taxable whether it is bought or leased for the customer’s use on a disk, as a download, or accessed on a remote server. A transaction that solely involves custom software, a personal service, or professional service is not taxable.

#### *Vermont Transaction?*

Just as with other purchases that are subject to the sales tax, purchases of prewritten software accessed remotely must be Vermont transactions in order for the sales or use tax to be due. Vermont sales tax is destination based, meaning that the Vermont sales tax is due when a taxable product is sold to a customer in Vermont. For **Vermont vendors**, that means that they must collect the Vermont sales tax when selling products to customers in Vermont, but not in other states. For **Vermont customers**, that means that they must remit the Vermont use tax for a product they will use in Vermont that was not taxed at point of sale.

Please direct comments regarding the current draft of the regulation by October 1, 2014, to the Commissioner’s Office at [tax.commissioner@state.vt.us](mailto:tax.commissioner@state.vt.us) or 802-828-3763.

# Draft Regulation

## —Prewritten Software Accessed Remotely— For Public Comment as of 7/10/14

### Reg. §1.9701(5)-1 Retail sale

The term “retail sale” means a sale for any purpose other than for resale, sublease, or subrent. The term “sale” includes any transfer of title or possession or both, exchange or barter, rental lease or license to use or consume, conditional or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement therefore.

Sales to contractors, subcontractors or repair persons of materials or supplies for use by them in erecting structures or otherwise improving, altering or repairing real property are retail sales. Once tangible personal property is incorporated into the real property, the sale of the real property is not subject to sales and use tax, regardless of whether the incorporated tangible personal property is itemized by the seller.

A transfer of prewritten computer software by a sale, license, subscription, lease or other means for consideration is a retail sale notwithstanding that the software is accessed remotely by the purchaser. The determination of whether there is a retail sale of the software is based on whether the use or control given the purchaser with respect to the software allows the purchaser merely the means to access the seller’s or third party’s services and/or data or whether the purchaser is able to use the software to independently perform tasks.

A. The following transactions are not taxable:

1. The sale of specified digital products as defined in 32 V.S.A. Section 9701(46). Specified digital products are not prewritten software;
2. A transaction is not taxable where the focus of the transaction is the provision of services or the transfer of intangible property rights and not the transfer of prewritten software; no separate charge is made for the transfer of prewritten software; and the value of the prewritten software transferred, including the value of services added to the prewritten software transferred, is less than 10 percent of the total charge for the transaction. See 32 V.S.A. Section 9741(35);
3. A transaction that bundles the retail sale of prewritten software and a service is not taxable where the prewritten software is essential to the use of the service, and is provided exclusively in connection with the service, and the true object of the transaction is the service. See Regulation 1.9701(4)-3(C)(1);
4. The sale of data processing and information services that allow data to be generated, acquired, stored, processed, or retrieved and delivered by an electronic transmission to

a purchaser where such purchaser's primary purpose for the underlying transaction is the processed data or information;

5. The sale of data storage, management, and recovery services;
  6. The sale of website design and website hosting services. Such services, when performed by the seller rather than the customer, are not considered the sale of prewritten software;
  7. Transactions where the seller creates and runs reports on its software which are provided to the purchaser in any form;
  8. Transactions where the seller accepts data from the purchaser and processes it on its own software;
  9. Transactions where the seller provides maintenance of its software and the maintenance is sold to the purchaser separately from any software, software updates or software upgrades;
  10. Transactions where the seller is providing additional, different or restructured information to the customer (e.g., credit card or check verification services, ATM terminal driving services);
  11. Transactions where the seller provides personal or professional services (e.g. custom software, legal, accounting);
  12. Transactions where the customer is running its own software, which was not obtained from the seller, on seller's hardware in a "cloud computing" environment. This may be described as providing Infrastructure as a Service (IaaS). The IaaS business model provides the consumer with processing, storage, network capabilities, and other fundamental computing resources where the consumer is able to deploy and run software. This transaction will not be considered taxable merely because the seller of such computing resources provides access to operating system software as an incident to such services, in order to enable the customer to run its own application software.
- B. Subject to A above, these factors indicate that there is a taxable transfer of prewritten computer software:
1. The contract or agreement indicates that a license, lease or other contractual right to use prewritten computer software is being transferred for consideration;
  2. The purchaser can access a seller's prewritten software on the purchaser's own server or the server of the seller or a third party to enter its own information and manipulate that information; however, the entry of search queries by the purchaser in the seller's database is not considered to be manipulation of the purchaser's information;

3. The purchaser can use the prewritten software with little or no intervention by the seller other than “help desk” assistance;
4. The purchaser can use an organizational tool or function that is a function of seller’s software;
5. The purchaser may download the seller’s prewritten software, or a portion of it, to any device.

This is not intended to be an exclusive list.

C. Examples:

1. Purchaser subscribes to online content by registering at Seller’s website. That is not a retail sale of software;
2. Seller conveys to purchaser a license to electronically search Seller’s or a third party’s database of legal sources and view and download items in the database or lists of items in the database. Purchaser can use the software to enter queries and customize the search by date, subject, jurisdiction and similar limiting factors. This *not* is a retail sale of prewritten computer software;
3. Purchaser electronically transmits payroll information to Seller every two weeks via Seller’s website. Seller stores the information, calculates withholding for applicable taxes, creates and remits checks to employees and taxing jurisdictions and transmits a record of these activities to purchaser. This is not a retail sale of prewritten computer software;
4. Purchaser enters the hours worked by its employees weekly onto software licensed from Seller and instructs the software to calculate withholding, create and print checks, and store the employee information. Purchaser does this without assistance from Seller, except for occasional trouble-shooting and upgrades to the software. This is a retail sale of prewritten computer software;
5. Seller offers online conferencing software to Purchasers who are able to navigate, choose, and use tools, such as power point, spreadsheets and tables made available through Seller’s software to set up on-line meetings and conferences. The sale of the on-line conferencing product is a retail sale of prewritten computer software;
6. Seller offers a customizable website that allows Purchaser to create its own on-line events using text, video, audio and voice technologies to interact among multiple venues. Purchaser uploads data onto the internet which is stored on Seller’s server and receive a license to use the software used to create its event. Purchaser cannot control Seller’s operating systems, hardware or network infrastructure while producing the

event, but uses the software design tools to create and brand its event. Sometimes a Purchaser also purchases event project management services. The sale of subscriptions to Seller’s website is a retail sale subject to tax. The project management services may be personal or professional services that would not be subject to tax if sold separately but are taxable as part of a bundled transaction because the object of the sale is use of the software.

The General Sourcing rules as set out in §1.9701(8)-3 of this regulation apply to retail sales of computer software.

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Reg. §1. 9701(7) Tangible Personal Property

“Tangible personal property” means personal property which may be seen, weighed, measured, felt, touched or in any other manner perceived by the senses. The statutory definition specifically includes electricity, water, gas, steam, and prewritten computer software, even if the software is delivered electronically.

“Delivered electronically” means delivered by the purchaser by means other than tangible storage media.

“Prewritten computer software” means computer software, including prewritten upgrades, which is not designed and developed by the author or other creator to the specifications of a specific purchaser. The combining of two or more prewritten computer software programs or prewritten portions thereof does not cause the combination to be other than prewritten computer software. Prewritten computer software includes software designed and developed by the author or other creator to the specifications of a specific purchaser when it is sold to a person other than the specific purchaser. Where a person modifies or enhances computer software of which the person is not the author or creator, the person shall be deemed to be the author or creator only of such person’s modifications or enhancements. Prewritten computer software or a prewritten portion thereof that is modified or enhanced to any degree, where such modification or enhancement is designed and developed to the specifications of a specific purchaser, remains prewritten computer software; provided, however, that where there is a reasonable, separately stated charge or an invoice or other statement of the price given to the purchaser for such modification or enhancement, such modification or enhancement shall not constitute prewritten computer software.

- A. Tangible personal property includes, but is not limited to:
  - 1. raw materials, such as wood, metal, rubber and minerals;

2. manufactured items such as jewelry, furniture, machinery, clothing, lighting fixtures, appliances and building materials;
  3. artistic items such as sketches, paintings, photographs, moving picture films, tapes and dvds, and recording when on a tangible medium;
  4. stamps and other philatelic items when purchased other than for use as postage; coins and other numismatic items when purchased other than for use as a medium of exchange;
  5. precious metals such as bullion, ingots, and wafers;
  6. prewritten computer software.
- B. Tangible personal property does not include:
1. Real property;
  2. Items such as books, movies, or music delivered electronically (excepting prewritten software as provided by statute);
  3. Stamps when purchased for use as postage; coins and other numismatic items when purchased as a medium of exchange;
  4. Intangible personal property such as rights and credits, insurance policies, bills of exchange, stocks and bonds and similar evidences of indebtedness or ownership, unless they are sold for historical display or collection purposes.
- C. Prewritten computer software means computer software, including prewritten upgrades, which is not designed and developed by the author or other creator to the specifications of a specific purchaser. The combining of two or more prewritten computer software programs or prewritten portions thereof does not cause the combination to be other than prewritten computer software. Prewritten computer software includes software designed and developed by the author or other creator to the specifications of a specific purchaser when it is sold to a person other than the specific purchaser. Where a person modifies or enhances computer software of which the person is not the author or creator, the person shall be deemed to be the author or creator only of such person's modifications or enhancements. Prewritten computer software or a prewritten portion thereof that is modified or enhanced to any degree, where such modification or enhancement is designed and developed to the specifications of a specific purchaser, remains prewritten computer software; provided, however, that where there is a reasonable, separately stated charge or an invoice or other statement of the price given to the purchaser for such modification or enhancement, such modification or enhancement shall not constitute prewritten computer software.