Sales tax on prewritten software

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Current Vermont Law

Vermont sales tax applies to the retail sale of tangible personal property, unless an exemption applies. 32 V.S.A. § 9771(1).

- Tangible personal property includes prewritten software:
  - "Tangible personal property" means personal property which may be seen, weighed, measured, felt, touched, or in any other manner perceived by the senses. "Tangible personal property" includes electricity, water, gas, steam, and prewritten computer software. 32 V.S.A. § 9701(7).

- Unlike tangible personal property, charges for a service are generally not taxable, unless specifically enumerated. 32 V.S.A. § 9771.

What are we talking about

Prewritten computer software

Purchased on storage media in Vermont = taxable

Downloaded to a computer in Vermont = taxable

Accessed remotely via the internet = <u>not</u> taxable

How did Vermont get here?

Streamlined Sales and Use Tax Agreement (SSUTA)

- The SSUTA has definitions for "tangible personal property," "prewritten software," "delivered electronically," and "load and leave."

- The SSUTA allows states to exempt prewritten software "delivered electronically" or by "load and leave."

- Vermont regulations currently include these SSUTA definitions and a number of other related definitions.

Vermont Sales Tax Regulations

"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. Vt. Reg. § 1.9701(7)-2.

Legislative context

- 2010: Dept. of Taxes issued a technical bulletin interpreting the law as imposing sales tax on prewritten software regardless of how accessed.

- 2012, Act 143, Sec. 52
  - Imposed moratorium on sales tax on prewritten software accessed remotely until July 1, 2013, and
  - allowed refunds of tax paid from Jan. 1, 2007-July 1, 2013.

- 2013-2014: Dept. issued guidance outlining taxation/exemption of remotely accessed prewritten software, then circulated draft regulations for comment.

- 2015: Act 51 created a session law exemption for prewritten computer software accessed remotely.

- 2019: Act 71 required Dept. to do outreach and education for tech sector on industry responsibilities under current law and under a possible repeal of the exemption.

Other states

	17 States + D.C. Tax	28 States Exempt	5 States ≠ Sales Tax
1	Arizona	Alabama	Alaska
2	Connecticut	Arkansas	Delaware
3	Hawaii	California	Montana
4	Iowa	Colorado	New Hampshire
5	Louisiana	Florida	Oregon
6	Mississippi	Georgia	
7	New Mexico	Idaho	
8	Ohio	Illinois	
9	Pennsylvania	Indiana	
10	Rhode Island	Kansas	
11	South Carolina	Kentucky	
12	South Dakota	Louisiana	
13	Tennesee	Maine	
14	Texas	Maryland	
15	Utah	Michigan	
16	Washington	Mississippi	
17	Washington DC	Missouri	
18	West Virginia	Nebraska	
19		Nevada	
20		New Jersey	
21		North Carolina	
22		North Dakota	
23		Oklahoma	
24		Rhode Island	
25		Vermont	
26		Virginia	
27		Wisconsin	
28		Wyoming	

Other terms

"Software as a Service" ("SaaS"), "Infrastructure as a Service"("IaaS"), and "Platform as a Service"("PaaS")

- These terms are not uniformly defined in law (or in the computing industry):
  - ◦ SaaS is a service provider hosting software applications over the internet for a customer.
  - ◦ IaaS is a service provider owning, maintaining, operating, and housing equipment (such as hardware, servers, network components, etc.) used to support a customer's operations, which the customer accesses via the internet in order to use the equipment.
  - ◦ PaaS is a service containing elements of both IaaS and SaaS.

- All are currently treated as tax exempt in Vermont.

What happens if exemption is repealed?

What is Taxable and Nontaxable?

Product	Taxable	Nontaxable
Custom software written exclusively for the customer's business		✓
Prewritten software on tangible storage media	✓	
Prewritten software downloaded from the internet	✓	
Prewritten software accessed remotely on the internet or SaaS	✓ ←	✓
Infrastructure as a Service (IaaS)		✓
Platform as a Service (PaaS)		✓
Development and technical support services		✓
Digital photographs		✓
Digital audio-visual works	✓	
Digital audio works	✓	
Digital books	✓	
Ringtones	✓	

What happens if exemption is repealed?

Software as a Service becomes taxable and subject to the 6% sales tax
- ◦ Example: TurboTax over the internet
  - ◦ Generally, any "canned" software that can be accessed over the cloud becomes taxable

What stays non-taxable?
- ◦ **Infrastructure as a Service:** access to computer infrastructure where the customer does not own the infrastructure, or pays an IT contractor to operate it
  - ◦ Example: Amazon Cloud Services
- ◦ **Platform as a Service:** service that gives consumer hardware or software tools that consumers can use to develop, run, or manage own software.
  - ◦ Example: Squarespace website design

How much money will this raise?

$6-7 million in FY21
- Estimate from May 2019 was $5-6 million
- Based upon national data on software sales to consumers and businesses from the Bureau of Economic Analysis
  - Estimated total sales of U.S. prepackaged software: $266 billion
    - Up from $235 billion in 2017
- Assumes that 30% of all software purchased by businesses and consumers is accessed remotely
  - US cloud service revenue: at least $50 billion and growing fast (Gartner Consulting)

Assumes a modest downward adjustment for compliance ramp up in first year.