FINAL PRIVATE LETTER RULING

REQUEST LETTER

13-003

COMPANY 1
ADDRESS1

February 25, 2013

Via Federal Express

Ms. [*sic*] Dee Talbot
Utah State Tax Commission
210 North 1950 West
Salt Lake City, Utah 84134

Re: Request For Sales and Use Tax Private Letter Ruling

Dear Ms. Talbot:

The purpose of this letter ("Letter") is to request a sales and use tax ruling on behalf of COMPANY 2 ("COMPANY 2," and together with its affiliates, COMPANY 2) upon which COMPANY 2 may rely.

COMPANY 2 is a leading multi-brand technology solutions provider to business, government, education and healthcare customers in the U.S. and Canada, providing comprehensive and integrated solutions for its customers' technology needs through its extensive hardware, software and value-added service offerings. COMPANY 2 offers over 100,000 products from over 1,000 brands and a multitude of advanced technology solutions. Its offerings range from discrete hardware and software products to complex technology solutions such as virtualization, collaboration, security, mobility, data center optimization, and cloud computing.

As described in more detail below, COMPANY 2 offers a cloud-based service offering (the "Cloud Collaboration Service Offering" or the "Offering") to customers nationwide.[1] The Cloud Collaboration Service Offering will provide certain cloud-based applications and related services (the "Cloud Collaboration Services" or the "Services") that support a customer's telecommunication equipment, including its voice, video, messaging, presence, audio, web conferencing, and mobile capabilities. This Letter specifically requests a ruling concerning the applicability of sales and use taxes in your state to the Cloud Collaboration Service Offering.

[1] COMPANY 2 began marketing the Cloud Collaboration Service Offering on July 1, 2012. The Offering is still in the implementation phase and COMPANY 2 has not yet billed any customers.

BACKGROUND

Overview of the Cloud Collaboration Service Offering

Generally, a business's phone systems, computers and other telecommunications equipment utilize various software applications and hardware in order to operate and function in the manner necessary for the business's needs. For instance, although a business may have a telecommunications provider that provides it with telephone lines to make outgoing and receive incoming calls, the business will need hardware and software that internally instructs the business's telecommunications equipment as to how to process and route those calls. Historically, customers have handled these functions internally, and such functions have not been subject to sales tax. Through the Cloud Collaboration Service Offering, COMPANY 2 will simply be providing these non-taxable functions as a service to its customers from an offsite location.

Specifically, the Cloud Collaboration Service Offering replaces certain customer-owned and maintained software applications and related computer hardware that support a customer's telecommunications equipment with a COMPANY 2-hosted alternative. In this hosted alternative, COMPANY 2 owns (or is the lessee or licensee of) and maintains certain hardware and software. The benefit of the Cloud Collaboration Service Offering is that customers can utilize the hardware and software Cloud applications on an as-needed basis from COMPANY 2, thereby reducing the customer's capital investment and on-going technology support and maintenance expenditures for such systems. The customer utilizes the hosted applications by means of the customer's existing telecommunications, Internet, or network connections, for which it pays its own third party telecommunications provider. In essence, in exchange for a monthly fee, COMPANY 2 will operate back-office equipment and software applications that provide necessary or enhanced functionality for a customer's phone systems and other telecommunication equipment. The customer will provide the telecommunications equipment.

COMPANY 2 will acquire, operate and maintain all the hardware and software necessary to provide the Services and ensure optimal performance. The hardware and software required for providing the Services will be installed on servers located in CITY 1, STATE 1. COMPANY 2 employees based in CITY 1, STATE 1 will provide onsite professional services to maintain the hardware and software, and COMPANY 2 employees based in CITY 2, STATE 2 will remotely monitor performance, perform necessary adds, moves, changes, and deletions, and provide troubleshooting for issues that arise during performance.

The Manner in Which The Services Are Provided

The Services will be provided by COMPANY 2 on a remote basis through the use of COMPANY 2-owned COMPANY 3 ("COMPANY 3") clusters located at a COMPANY 2 data center. The COMPANY 3 clusters will deploy a variety of available COMPANY 2-owned, client software applications that are utilized by customer-owned phones and workstations located at customer sites. As described further below, the applications generally provide the customer's telecommunication equipment with certain necessary or enhanced functionalities.

Customers will be responsible for providing connectivity of sufficient bandwidth between the customer's location and COMPANY 2's data center. COMPANY 2 relies on the customer's QoS-enabled, voice-grade Local Area Network and Wide Area Network over which it provides the Services throughout a customer's geographic locations. Connectivity to the Public Switched Telephone Network ("PSTN") is not included in the Cloud Collaboration Service Offering. All connections between the customer and COMPANY 2's data center are through a customer's existing or newly-ordered PSTN circuits, phone lines and Internet connections. The PSTN or other connections can reside throughout the customer locations, and are terminated into the COMPANY 2 data center through customer-owned, COMPANY 2-managed gateways. Customers are always the "customer of record" for any PSTN, Internet or other service for the transportation or transmission of messages or information; the applications do not transport or transmit messages or information. All customer communications with third parties are through customer-contracted PSTN connections that are not provided by COMPANY 2. COMPANY 2's customers continue to communicate with third parties over the PSTN, and continue to pay their telecommunications provider the same charges and taxes for such capabilities, both before and after signing up for the COMPANY 2 Cloud Collaboration Service Offering. PSTN communications with third parties are never physically routed through COMPANY 2's data center equipment.

COMPANY 2 may also host and deploy certain customer-owned software applications that provide enhanced functionalities for a customer's phone systems and other telecommunication equipment. Such hosted services are available as add-on services for additional fees (as described below), and are utilized by customers in the same manner as the COMPANY 2-owned and hosted software applications.

Agreements and Monthly Charges

To purchase the Cloud Collaboration Service Offering, customers will enter into a contract with COMPANY 2 that includes a customer service order, a service description for the Offering, and a detailed pricing invoice. A representative copy of each is attached as Attachment A.

Under the contract with a customer, COMPANY 2 will charge the customer a monthly user license fee,[2] calculated based on the number of users. The monthly fee covers the charges for hardware, software, 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. To the extent the customer purchases add-on services (including the hosting of customer-owned software applications), separate fees are charged for each such service. Charges for maintenance and management of any customer-owned software applications are also separately stated on the monthly invoice.

[2] The fee is denominated as a "license" fee, but COMPANY 2 does not in fact license or lease any software or tangible personal property to the customer under the contract.

Description of the Services Provided by the Embedded Software Applications

As described above, the COMPANY 2-owned software applications available through the Offering support a customer's own voice, video, messaging, presence, audio/web conferencing, and mobile capabilities. A brief description of the supporting services provided by the various applications is set forth below:

Voice. A COMPANY 2 server, utilizing the COMPANY 3, communicates with the customer's voice gateway device (*i.e.*, the customer-owned switch) to provide instructions to the customer's voice gateway device for the processing and routing of incoming and outgoing calls among the customer's phone extensions; the call is not routed through COMPANY 2's server. No end-to-end communication is ever routed through COMPANY 2's server. This COMPANY 3 system also supports a customer's other forms of communication to its IP endpoints, media-processing devices, VoIP gateways, mobile devices, and multimedia applications, as generally described below. A diagram depicting these voice services is attached as Attachment B.

Video. Video is the technology of electronically capturing, recording, processing, storing, transmitting, and reconstructing a sequence of still images representing scenes in motion. Video utilizes components such as the COMPANY 3IP end-points, COMPANY 3SYSTEM 2 desktop clients, or purpose-built video endpoints such as the COMPANY 3 SYSTEM 1 or larger units. The video support services will be provided by COMPANY 2's server through a COMPANY 3 cluster in the same manner as outlined above with respect to a customer's voice communication capabilities.

Messaging. When a customer phone extension does not answer an incoming call, the COMPANY 2 server, utilizing the COMPANY 3, instructs the customer's voice gateway device to send the call to voicemail. The voice messages are then stored on the COMPANY 2 servers and available for the user to access and manage at his or her convenience. The voice messaging support services provided by the Cloud Collaboration Service Offering will allow users to access and manage voice messages stored on COMPANY 2-owned servers in a variety of ways, using an email inbox, web browser, COMPANY 3 Unified IP Phone, Smartphones, and COMPANY 3 SYSTEM 2, among other components.

Presence. Presence support services are provided by COMPANY 2 through a COMPANY 3 Unified Presence application that provides users the ability to determine when colleagues are available. The COMPANY 3 Unified Presence application offers the flexibility of rich, open interfaces that allow enablement of instant messaging and rich, network-based presence for a wide variety of business applications. As is the case with respect to the other services, the customer's own communications equipment accesses the Presence application hosted on COMPANY 2's servers to utilize the presence capabilities.

Audio Conferencing. With respect to a customer's audio conferencing capabilities, COMPANY 2 supports a customer-owned COMPANY 3 router and the

phone devices through its hosted COMPANY 3, in a manner similar to that which is described above with respect to the voice support services.

Web Conferencing. COMPANY 3 PRODUCT 1 application is an optional, subscription-based component of the Offering. PRODUCT 1 is a cloud-based web conferencing application that permits desktop sharing through a web browser with phone conferencing and video. PRODUCT 1 operates through a user's computer or wireless device, an audio connection (either through the computer or through a phone), and a webcam (optional).

Mobility Services. COMPANY 2 supports a customer's mobile devices through use of the COMPANY 3SYSTEM 2 application. Mobile clients utilizing COMPANY 3 SYSTEM 2 can place and receive calls over their own corporate wireless local area network and telephony infrastructure, using COMPANY 2's server to instruct the routing of calls, and essentially turns a mobile phone into another extension on the COMPANY 3. COMPANY 2's server itself does not provide the routing for the call or otherwise function as a switch. No end-to-end communication is ever routed through COMPANY 2's server.

With respect to each of the support services described above, a customer utilizes the COMPANY 2-owned and hosted software with its own equipment and through its own telecommunication, Internet or other network connection. At no time does the customer download or otherwise posses the software that is hosted by COMPANY 2. In addition, COMPANY 2 does not provide the telecommunication, Internet or network connections necessary for the customer to utilize the Services. The net result is that the customer has done nothing more than out-source certain activities previously performed in-house that were never subject to sales tax.

RULINGS REQUESTED

1. The hardware and software that COMPANY 2 purchases, leases or licenses from third parties is purchased, leased or licensed by COMPANY 2 for use or consumption and not for resale.

2. The Services provided by the Cloud Collaboration Service Offering are non-taxable services and not a lease or license of hardware or software.

3. Alternatively, if it is determined that the Cloud Collaboration Service Offering constitutes a lease, license or other transfer of software to a customer, such transfer is exempt from tax as electronically delivered software.

4. The Services provided by the Cloud Collaboration Service Offering are not taxable telecommunications services.

5. For sales and use tax purposes, the Services provided by the Cloud Collaboration Service Offering are provided in STATE 1.

ANALYSIS

The hardware and software that COMPANY 2 purchases, leases or licenses from third parties is purchased, leased or licensed by COMPANY 2 for use or consumption and not for resale.

COMPANY 2 purchases, leases or licenses the hardware and software that it uses to provide the services offered in connection with its Cloud Collaboration Service Offering from various third parties. COMPANY 2 does not resell, lease, license or otherwise transfer use or possession of such software or hardware to its customers. At all times, the software applications are hosted on COMPANY 2-owned servers located at COMPANY 2's data center in STATE 1. Therefore, the hardware and software is purchased, leased or licensed, as applicable, for use and consumption by COMPANY 2 rather than for resale to its customers.

The Services provided by the Cloud Collaboration Service Offering are non-taxable services and do not constitute a lease or license of hardware or software.

The Cloud Collaboration Service Offering constitutes the provision of non-taxable services and does not constitute the lease or license of hardware or software in connection therewith. COMPANY 2 owns all of the hardware and the licenses for all of the software necessary to provide the Services. A customer pays a monthly fee to utilize the software applications (hosted on COMPANY 2-owned equipment) through which the Services are provided; a customer does not enter into any lease or license for the software or the equipment, acquires no right to possess such software or equipment (and no right to download, duplicate or manipulate the software), and acquires no right to use such software or equipment independent of the receipt of the Services. Notably, the customer service order that a customer executes states that such agreement "is not intended to, and will not, constitute a lease of any real or personal property."

In this regard, several states have ruled that access to software solely through the Internet is not generally considered a taxable transfer of software but rather is a non-taxable service. *See, e.g.,* Kansas Opinion Letter No. O-2012-001 (concluding that a taxpayer's provision of access to and use of software and servers to customers was not a taxable sale or lease of software or hardware, but rather was a non-taxable service); Colorado Private Letter Ruling No. PLR-11-7 (December 20, 2011) (holding that a hosted software solution to transfer large data files via the Internet was a non-taxable service because the provider had physical custody over the property and staff that program and control the systems, and the user did not have significant control over the servers and software); Virginia Public Document No 12-2 (January 19, 2012) (concluding that a taxpayer's provision of an online authentication solution for customers seeking to perform secure electronic commerce and communications over the internet was a non-taxable service, even though the taxpayer electronically sent a digital certificate to the customer that the customer installed on its web server); Virginia Public Document No. 10-264 (December 15, 2010) (finding that providing access to a web-based global database to allow customers to perform searches and create reports, as well as the customer's purchase of certain workflow add-ons that provide a variety of related enhanced functionalities, was a non-taxable service because there was no transfer of tangible personal property); Kansas Private Letter Rulings No. P-2009-005 (June 26, 2009) and P-2011-010 (December 27, 2011) (holding that the monthly fee charged to customers to remotely access a pre-written computer software program located on an out-of-state server

was not subject to Kansas sales or use tax); Indiana Letter of Finding No. 04-20110291 (March 28, 2012) (holding that taxpayer's sale of web-based computer programs did not involve the right to use pre-written computer software); Iowa Policy Letter 12300002 (January 11, 2012) (finding that a taxpayer's sales of online access to certain hosted software was not considered taxable as a sale of tangible personal property because the customer does not possess the software); Nebraska Information Guide No. 6-511-2011, Sales and Use Tax Guide for Computer Software (July 27, 2011) ("[c]harges by an ASP for services that allow customers remote access to software applications via the Internet or other online connection, sometimes referred to as cloud computing, are not taxable when the ASP retains title to the software and does not grant a license with ownership rights to the customer").

As described above, COMPANY 2 does not enter into any sale, lease or license agreements with customers that sign up for the Offering. At no time is any software or application transferred to a customer, and the customer cannot access the hosted software code nor manipulate the software in any way. Rather, COMPANY 2 provides services using its own equipment and software that it licenses. The licensed software is maintained on a hosted COMPANY 2 server on COMPANY 2-owned equipment at a COMPANY 2 location, and the equipment and software is at all times maintained by, and under the control of, COMPANY 2 employees. For the same reason, the Offering does not constitute a lease of computer equipment, as no transfer of title to the computer equipment occurs, and the customer does not have any rights to possession or control of such computer equipment. Thus, the Offering constitutes the provision of non-taxable services and does not constitute a taxable lease or license of hardware or software to customers.

In addition, the Offering does not constitute a taxable information service because COMPANY 2 does not compile or manipulate data, or provide written reports of compiled or manipulated data to its customers.

The Cloud Collaboration Service Offering, if determined to be a transfer of software to customers, is exempt from tax as electronically delivered pre-written software.

Even if it is determined that the Cloud Collaboration Service Offering constitutes a lease or other transfer of software to customers, the Offering should nevertheless still be exempt from tax because any such transfer would occur through electronic means, and would therefore not be considered a taxable sale of tangible personal property. In this regard, a number of states have determined that the electronic transfer of pre-written software is exempt from tax. For instance, the Florida Department of Revenue has taken the position that the sale of pre-written software delivered electronically is exempt from tax because no transfer of tangible personal property occurs. *See* Florida Department of Revenue TAA 03A-200 (April 30, 2003) and TAA 05A-026 (June 2, 2005); *see also Florida Department of Revenue v. Quotron Systems Inc.*, 615 So. 2d 774 (Fla. Dist. Ct. App. 1993) (electronic transmission of financial information to subscriber's video display terminals was not subject to sales or use tax; transaction did not constitute sale or rental of tangible personal property). The Florida Department of Revenue has also applied the electronic delivery exception to a situation in which customers paid subscription fees for remote access to certain business and financial software applications. *See* Florida Department of Revenue TAA 10A-052 (December 3, 2010). In addition, states such as Iowa and California provide express statutory and regulatory exemptions from their sales tax for electronically

delivered pre-written software. *See, e.g.*, Cal Code Regs. tit. 18 § 1502(f)(1)(d) and Iowa Code § 423.3(67). In a recent policy ruling, the Iowa Department of Revenue concluded that a "hosted software" arrangement did not constitute a taxable sale of tangible personal property, but rather was exempt as electronically delivered software, because the software was only available for use electronically. *See* Iowa Policy Letter 12300002 (January 11, 2012). Thus, even if the Cloud Collaboration Service Offering was found to constitute a transfer of software, it should nevertheless be exempt from tax because any transfer would occur electronically.

The Services provided by the Cloud Collaboration Service Offering are not taxable telecommunications services.

Certain states impose tax on telecommunications services. Such taxes are generally imposed on the charges for the *transmission* of messages or information, rather than for the content of the message or information that is transmitted. *See generally* Walter Hellerstein, *State Taxation*, ¶ 15.10[1] (WG&L 2012). COMPANY 2 does not itself provide a customer with the ability to transmit messages or information across any telephone, Internet or other network lines, and thus, is not providing a taxable telecommunications service. Indeed, COMPANY 2's customers continue to communicate over the PSTN, and continue to pay their telecommunications provider the same charges and taxes, both before and after signing up for the COMPANY 2 Cloud Collaboration Service Offering. Rather, as described above, the Offering provides a customer with the ability to access various applications that enhance the *functionality* of a customer's own communication *equipment*.

While COMPANY 2 is providing services over a customer's phone or Internet connection, it is not COMPANY 2 that provides the ability to transmit or route information and communicate across such lines. The customer's telephone/Internet provider provides the connection line through which the customer utilizes the software applications provided by the Offering. Furthermore, because COMPANY 2 is not providing the transmission or routing of messages, data or information, there are no such charges listed on the customer's statement of work, customer service order or invoice for the Offering.

In short, through the Offering, COMPANY 2 will be providing the described functionality previously performed by the customer in-house, none of which was subject to sales tax, *and nothing more*. COMPANY 2 will not be providing the services that are provided to a customer by its third-party telecommunications carrier; rather, it will merely be hosting the hardware and software historically located at the customer site that is utilized to enhance the customer's own telecommunication capabilities. Indeed, as stated above, a customer's contract with its telecommunications carrier for telecommunications services will remain in place and unaltered both before and after the customer signs up for the Offering.

Thus, for the foregoing reasons, the Offering does not constitute a taxable telecommunications service.

The Services provided by the Cloud Collaboration Service Offering are provided in STATE 1

The software-applications licensed by COMPANY 2 that are the engine of the Cloud Collaboration Service Offering are run on COMPANY 2-owned hardware that is located in

STATE 1. COMPANY 2 personnel located in STATE 1 provide on-site professional services to maintain the hardware and the software. Even though the Services may be utilized by customers nationwide, the Cloud Collaboration Services are performed by COMPANY 2 wholly from the state of STATE 1 (although certain remote services are provided from STATE 2 , including remote monitoring and troubleshooting, necessary adds, moves, changes and deletions). Therefore, such Services should only be taxable, if at all, by STATE 1. In this regard, several states have determined that hosted software transactions should be sourced to the location of the server on which the hosted software is stored. *See, e.g.,* Tennessee Department of Revenue Letter Ruling 11-58 (October 10, 2011) (concluding that a taxpayer's remote access of software was not subject to tax by Tennessee when the software was located on a server outside of Tennessee); Utah Private Letter Rulings No. 08-012 (January 21, 2009) and No. 09-003 (April 7, 2009) (prior to amendments to Utah's sales and use tax statute, concluding that certain transactions in which Utah customers remotely accessed software were not taxable by Utah because the Company's servers on which the software was housed were not located in Utah); Kansas Private Letter Ruling No. P-2011-010 (December 27, 2011) (noting that remotely-accessed software was not subject to tax because no software was delivered to a customer in Kansas; rather, the software was stored on the service provider's servers located outside of Kansas). In this case, the hosted software is housed and operated in STATE 1 (with certain remote management and troubleshooting taking place from STATE 2). Therefore, the Services should be treated as provided in STATE 1.

* * * * *

Thank you for your consideration of this request. Please do not hesitate to contact me if you have any questions, or would like any additional information. *We respectfully request a conference in the event you tentatively conclude that an adverse ruling would be warranted*. A power of attorney authorizing the undersigned to represent COMPANY 2 in this matter is attached as Attachment C. This ruling request pertains only to periods beginning after June 30, 2012, and none of COMPANY 2 or any of its affiliates operating in your state is under audit for sales and use tax for such periods.

Very truly yours,

NAME 1

cc: NAME 2, TITLE 1, COMPANY 2
NAME 3, TITLE 2, COMPANY 2
NAME 4, COMPANY 1

RESPONSE LETTER

PRIVATE LETTER RULING 13-003

December 4, 2013

NAME 1
COMPANY 1
ADDRESS1

RE: Private Letter Ruling Request – Sales Taxability of the "Cloud Collaboration Service Offering"

Dear NAME 1:

This letter is in response to your request for information on how Utah's sales and use tax laws apply to the "Cloud Collaboration Service Offering" ("Offering") sold by COMPANY 2 ("COMPANY 2").

I. Facts

You explained the following facts. Through the Offering, COMPANY 2 provides to customers certain cloud-based applications and related services that support customers' telecommunications equipment. These applications and related services include voice, video, messaging, presence, audio, web conferencing, and mobile capabilities. Through this Offering, COMPANY 2-owned software instructs customers' telecommunications equipment on how to process and route customers' incoming and outgoing calls. By purchasing this Offering, customers avoid having to purchase and maintain the hardware and software otherwise necessary to instruct their telecommunications equipment. To receive the Offering, a customer pays COMPANY 2 a monthly fee that is based on the number of users. Customers utilize the Offering through the customers' existing telecommunications, Internet, and/or network connections, for which the customers pay their own third-party telecommunications providers; COMPANY 2 does not provide customers with these connections. To provide the Offering, COMPANY 2 owns and operates hardware and software in STATE 1, which is maintained by its employees in STATE 1 and STATE 2. The COMPANY 2-owned hardware and software includes items such as computer servers, COMPANY 3 ("COMPANY 3"), COMPANY 3 IP end-points, COMPANY 3SYSTEM 2 desktop clients, video endpoints such as COMPANY PRODUCT 2 or larger units, COMPANY 3 Unified Presence application, COMPANY 3 PRODUCT 1 application, COMPANY 3 SYSTEM 2 application, etc.

In addition to the Offering as described above, a customer may also purchase hosting and

management activities from COMPANY 2. For separately-stated monthly fees COMPANY 2 will host and manage customer-owned software at COMPANY 2's data center, which seems to be located in STATE 1. According to the attached "Service Description for COMPANY 2Cloud Collaboration," customers' software could include: COMPANY 3 Unified Contact Center Express, COMPANY 3 Emergency Responder—Enhanced 911 solution, Singlewire InformaCast emergency notification system, COMPANY 3 Unified Attendant Console, and COMPANY 3 Phone VPN functionality.

COMPANY 2's contract with its customers includes a "Customer Service Order," a "Service Description for COMPANY 2 Cloud Collaboration," and a "Customer Service Order," samples of which you provided.

II. Issues

You have asked about the Utah sales and use tax treatment of the customers' purchases of the Offering and of COMPANY 2's purchases of hardware and software used to provide the Offering. In response, the customers' purchases of the Offering are subject to Utah sales tax if the customers are located in Utah and COMPANY 2's purchases of hardware and software are not subject to Utah sales and use tax when those purchases occur outside of Utah. The analyses for these conclusions are provided below the "Applicable Law" section.

III. Applicable Law

Utah Code § 59-12-103(1) imposes Utah sales and use tax on various transactions including the following in part:

> A tax is imposed on the purchaser . . . for amounts paid or charged for the following transactions:
> (a) retail sales of tangible personal property made within the state;
> (b) amounts paid for:
> (i) telecommunications service, other than mobile telecommunications service, that originates and terminates within the boundaries of this state;
> (ii) mobile telecommunications service that originates and terminates within the boundaries of one state only to the extent permitted by the Mobile Telecommunications Sourcing Act, 4 U.S.C. Sec. 116 et seq.; or
> (iii) an ancillary service associated with a:
> (A) telecommunications service described in Subsection (1)(b)(i); or
> (B) mobile telecommunications service described in Subsection (1)(b)(ii);
> . . . .
> (g) amounts paid or charged for services for repairs or renovations of tangible personal property, unless Section 59-12-104 provides for an exemption from sales and use tax for:
> (i) the tangible personal property; and
> (ii) parts used in the repairs or renovations of the tangible personal property described in Subsection (1)(g)(i), whether or not any parts are actually

used in the repairs or renovations of that tangible personal property;

. . . .

(k) amounts paid or charged for leases or rentals of tangible personal property if within this state the tangible personal property is:
  (i) stored;
  (ii) used; or
  (iii) otherwise consumed;

(l) amounts paid or charged for tangible personal property if within this state the tangible personal property is:
  (i) stored;
  (ii) used; or
  (iii) consumed; and

(m) amounts paid or charged for a sale:
  (i) (A) of a product transferred electronically; or
    (B) of a repair or renovation of a product transferred electronically; and
  (ii) regardless of whether the sale provides:
    (A) a right of permanent use of the product; or
    (B) a right to use the product that is less than a permanent use, including a right:
      (I) for a definite or specified length of time; and
      (II) that terminates upon the occurrence of a condition.

Utah Code § 59-12-102 defines multiple terms, including the following in part:

(26) "Computer" means an electronic device that accepts information:
  (a) (i) in digital form; or
    (ii) in a form similar to digital form; and
  (b) manipulates that information for a result based on a sequence of instructions

(27) "Computer software" means a set of coded instructions designed to cause:
  (a) a computer to perform a task; or
  (b) automatic data processing equipment to perform a task.

. . . .

(92) (a) . . . . "prewritten computer software" means computer software that is not designed and developed:
    (i) by the author or other creator of the computer software; and
    (ii) to the specifications of a specific purchaser.

. . . .

(94) (a) Except as provided in Subsection (94)(b), "product transferred electronically" means a product transferred electronically that would be subject to a tax under this chapter if that product was transferred in a manner other than electronically.

(b) "Product transferred electronically" does not include:
  (i) an ancillary service;
  (ii) computer software; or
  (iii) a telecommunications service.

. . . .

(98) (a) "Purchase price" and "sales price" mean the total amount of consideration:

(i) valued in money; and

(ii) for which tangible personal property, a product transferred electronically, or services are:

(A) sold;

(B) leased; or

(C) rented.

(b) ***"Purchase price" and "sales price" include:***

(i) the seller's cost of the tangible personal property, a product transferred electronically, or services sold;

(ii) ***expenses of the seller***, including:

(A) the cost of materials used;

(B) a labor cost;

(C) a service cost;

(D) interest;

(E) a loss;

(F) the cost of transportation to the seller; or

(G) a tax imposed on the seller;

. . . .

(106) "Retail sale" or "sale at retail" means a sale, lease, or rental for a purpose other than:

(a) resale;

(b) sublease; or

(c) subrent.

. . . .

(108)(a) "Sale" means any transfer of title, exchange, or barter, conditional or otherwise, in any manner, of tangible personal property or any other taxable transaction under Subsection 59-12-103(1), for consideration.

(b) "Sale" includes:

. . . .

(v) ***any transaction under which right to*** possession, operation, ***or use*** of any article of tangible personal property is granted under a lease or contract and the transfer of possession would be taxable if an outright sale were made.

. . . .

(123) (a) Except as provided in Subsection (123)(d) . . . , "tangible personal property" means personal property that:

(i) may be:

(A) seen;

(B) weighed;

(C) measured;

(D) felt; or

(E) touched; or

(ii) is in any manner perceptible to the senses.

(b) ***"Tangible personal property" includes:***

. . . .

(v) ***prewritten computer software***, regardless of the manner in which the prewritten computer software is transferred.

. . . .

(d) "Tangible personal property" does not include a product that is transferred electronically.

. . . .

(127)(a) "Telecommunications service" means the electronic conveyance, routing, or transmission of audio, data, video, voice, or any other information or signal to a point, or among or between points.

. . . .

(c) "Telecommunications service" does not include:

. . . .

(xi) tangible personal property.

. . . .

(Emphasis added.)

Utah Code § 59-12-211(12) provides the location of certain sales of the use of computer software as follows:

(a) Notwithstanding any other provision of this section and except as provided in Subsection (12)(b), ***if a purchaser uses computer software and there is not a transfer of a copy of that software to the purchaser***, the location of the transaction is determined in accordance with Subsections (4) and (5).

(b) If a purchaser uses computer software described in Subsection (12)(a) at more than one location, the location of the transaction shall be determined in accordance with rules made by the commission in accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act.

(Emphasis added.)

When § 59-12-211(12) applies, subsections (4) and (5) of § 59-12-211 locate transactions at an address for the purchaser.[1]

Utah Code § 59-12-104 provides various exemptions from Utah sales and use tax, with subsection (25) providing a resale exemption as follows:

The following sales and uses are exempt from the taxes imposed by this chapter:

. . . .

(25) a product purchased for resale in this state, in the regular course of business, either in its original form or as an ingredient or component part of a

[1] For more direction on the application of § 59-12-211 to the COMPANY 2 situation, you may contact the Taxpayer Services Division, Technical Research Unit by phone at 801-297-7705, by email at taxmaster@utah.gov or by mail at 210 N 1950 W, Salt Lake City UT 84134.

manufactured or compounded product . . .

IV. Analysis

COMPANY 2's sales of the Offering to customers in Utah is subject to Utah sales tax under § 59-12-103(1)(a), which taxes "amounts paid or charged for . . . retail sales of tangible personal property made within the state . . ."

The sales of the Offering are retail sales. Retail sales are broadly defined in § 59-12-102(106) to include "a sale, lease, or rental for a purpose other than . . . resale . . ." Sales are likewise broadly defined in § 59-12-102(108) to include "any transaction under which right to possession, operation, or ***use*** of any article of tangible personal property is granted under a lease or contract and the transfer of possession would be taxable if an outright sale were made" (emphasis added). The sale of the Offering involves transferring ***use*** of the software owned by COMPANY 2 for a purpose other than resale; thus, the sale of the Offering is a retail sale under Utah law.

The COMPANY 2-owned software used by customers is tangible personal property. Under § 59-12-102(123)(b)(v), tangible personal property includes prewritten computer software. Under § 59-12-102(92)(a), prewritten computer software is "not . . . designed and developed . . . by the . . . creator of the computer software . . . to the specifications of a specific purchaser." With the Offering, the COMPANY 2-owned software, much of which was developed by COMPANY 3, was designed for use by a broad user base, not for use by just one customer. Thus, the COMPANY 2-owned software used by its customers is prewritten computer software and is likewise tangible personal property.

The sales of the Offering are made within Utah when the customers are located in Utah. Under §§ 59-12-211(12) and 59-12-211(4)-(5), when a purchaser uses computer software and there is not a transfer of that software to the purchaser, the transaction for the use of the software is located at an address for the purchaser. Thus, sales of the Offering to customers in Utah are located in Utah, and not all sales of the Offering are located in STATE 1, as you asserted in your letter.[2]

Although the hardware owned by COMPANY 2 and the management and maintenance services provided by its employees are necessary to provide customers with the Offering, these items are not the product(s) essentially sold to the customers purchasing the Offering. Rather, the sale of the Offering is essentially the sale of the use of prewritten computer software. The Commission has applied the Utah Supreme Court's instruction on the object or essence of a transaction theory, which includes the following:

> [T]he essence of the transaction theory focuses on the nature of what was sold and whether it primarily entails tangible personal property. . . . This theory examines the transaction as a whole to determine whether the essence of the transaction is

[2] As a side note, in your letter you concluded that the customers' previous in-house activities relating to owning, managing, and maintaining hardware and software used to instruct telecommunications equipment were never subject to Utah sales and use tax. We express no opinion.

> one for services or for tangible personal property. The analysis typically requires a determination either that the services provided are merely incidental to an essentially personal property transaction or that the property provided is merely incidental to an essentially service transaction.
>
> *B.J.-Titan Services v. State Tax Comm'n*, 842 P.2d 822, 825 (Utah 1992).

After considering the characteristics of the Offering in general, the Commission concludes that the object of the transaction for the Offering is the use of the prewritten computer software. Customers purchase the Offering to use the prewritten computer software to support their telecommunications equipment; the COMPANY 2's hardware and the technical services to manage and maintain COMPANY 2's hardware and software are incidental to the customers' use of the software. The assertion in your letter that "[t]he monthly fee covers the charges for hardware, software, 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" does not change the Commission's conclusion. Notably, under § 59-12-102(98)(b)(ii), a sales price includes amounts covering a seller's expenses for items such as materials, labor, and services.

In your letter, you asserted that if the Commission finds that sales of the Offering involve transfers of software to customers then such transfers would be exempt from tax as transfers of electronically-delivered software. This conclusion is incorrect for two reasons: First, under § 59-12-102(94)(b), a product transferred electronically cannot include computer software. Second, under § 59-12-103(1)(m), products transferred electronically ***are*** subject to Utah sales and use tax. Utah does not have an exemption for transfers of electronically-delivered software.

Additionally in your letter, you asserted that the sales of the Offering were not sales of telecommunications services. For background, under Utah law § 59-12-102(127) defines telecommunications service and § 59-12-103(1)(b) subjects sales of certain telecommunications services to Utah sales tax. You are correct that the sales of the Offering are not sales of telecommunications services and thus they are not subject to tax under § 59-12-103(1)(b). However, as explained above, the sales of the Offering are still subject to Utah sales tax under § 59-12-103(1)(a).

Also in your letter, you assert that the hardware and software COMPANY 2 purchases, leases or licenses from third parties are purchased, leased or licensed by COMPANY 2 for COMPANY 2's use or consumption and not for resale. Your conclusion is partially correct and incorrect. Based on the facts you presented, COMPANY 2's purchases, leases, and licenses of hardware and software from third parties are not subject to Utah sales or use tax because the purchases of the hardware and software occur outside the state. Thus, the activities are not transactions subject to Utah tax under § 59-12-103(1)(a), (k) or (l). Because COMPANY 2 does not have a taxable transaction when it acquires the hardware and software, the Utah resale exemption found in § 59-12-104(25) cannot be applied. On the other hand, if instead COMPANY 2 were to acquire or use hardware and software in Utah, then the Utah resale exemption could be applied to software purchased for resale, but not to the hardware. Software that is purchased by COMPANY 2 to be resold as an ingredient or component part of the

Offering would be exempt under § 59-12-104(25). However, the hardware cannot qualify for the exemption found in § 59-12-104(25) because the use of the hardware is not resold. Instead, the hardware's use is incidental to the sale of the use of the software.

In your letter you mentioned that COMPANY 2 would host customer-owned software applications and maintain and managed customer-owned software applications for separately-stated monthly fees. After reviewing the materials you attached to your letter, it is unclear whether these products are separate from or a subsection of the Offering already discussed. Regardless, these separately-stated charges are not subject to Utah sales and use tax if they are performed outside of Utah. Based on your letter and the attached items, it appears that the COMPANY 2's hosting and management activities would occur at a data center in STATE 1. Section 59-12-211(12), which locates certain transactions in Utah, does not apply to transactions involving customer-owned software; with customer-owned software there has been a transfer of the software, not just use. However, if COMPANY 2 provides *in Utah* any hosting, maintenance, or management activities then such activities could be subject to Utah sales tax under § 59-12-103(1)(g) and (k).

In summary, the sales of the Offering to customers located in Utah are taxable under § 59-12-103(1)(a) as retail sales of tangible personal property.

V. Conclusion

As explained in this letter, the sales of the Offering to customers located in Utah are taxable under § 59-12-103(1)(a). Additionally, COMPANY 2's purchases of the hardware and software necessary to provide the Offering are not subject to Utah sales and use tax because the purchases occur outside of Utah. If the purchases were to occur within Utah, then the purchases of the *software* might qualify for the Utah resale exemption found in § 59-12-104(25), but those for the *hardware* would not.

This private letter ruling is based on current law and could be changed by subsequent legislative action or judicial interpretation. Also, our conclusions are based on the facts as described. If you feel the Commission has misunderstood the facts as you have presented them, you have additional facts that may be relevant, or you have any other questions, you are welcome to contact the Commission.

For the Commission,

D'Arcy Dixon Pignanelli
Commissioner

DDP/aln
13-003