

**FINAL PRIVATE LETTER RULING**

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**REQUEST LETTER**

16-004

August 22, 2016

NAME-1  
Utah State Tax Commission  
210 North 1950 West  
Salt Lake City, UT 84134

**Re: Private Letter Ruling (“Ruling”) Request**

Dear NAME-1:

COMPANY (“COMPANY”) EIN #####, an affiliate of PARENT COMPANY (“Parent”), pursuant to Utah Code Ann. § 59-1-210 and Utah Admin. Code r. 861-1A-34, respectfully submits this Private Letter Ruling (“PLR”) request regarding the applicability of the Utah Sales and Use Tax to certain of COMPANY’s service offerings. The issues and transactions described herein are not currently under audit by a representative of the Utah State Tax Commission (“Commission”).

If at all possible, we respectfully request that the Commission expedite the PLR process so that COMPANY can accurately apply Utah’s sales tax on Utah customers’ purchases of COMPUTING ITEM, STORAGE ITEM, and attendant TRANSFER FEES (as further described below).

**I. Background**

**A. COMPANY Web Services**

COMPANY offers information technology infrastructure services to customers in the form of web services.<sup>1</sup> The services allow customers to access computing power and storage capacity without significant information technology capital investment. Specifically, companies may access server bandwidth and storage capacity through the internet without having to spend capital on servers, information technology support staff, or real estate to house the servers.<sup>2</sup>

COMPANY is headquartered in STATE-1. While COMPANY does not own any data centers, it does utilize large data centers located in several locations within the United States – none of which are in Utah – and several countries outside of the United States to provide its services (the “COMPANY network”). In addition to use of large data centers, COMPANY also utilizes very small clusters of servers (“Point of Presence” locations or “PoP sites”) located in many states – again, none of which are in Utah – and locations around the world in order to

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<sup>1</sup> The COMPANY Customer Agreement is found at [WEB ADDRESS -1](#) and has been reproduced in Exhibit A (attached).

<sup>2</sup> More business description found at [WEB ADDRESS -2/](#).

provision a small subset of its services. The data centers and PoP sites are owned and operated by entities affiliated with COMPANY.

#### **i. CLOUD STORAGE ITEM (STORAGE ITEM)**

COMPANY's remote storage service, called CLOUD STORAGE ITEM ("STORAGE ITEM"),<sup>3</sup> allows customers to store and retrieve content, data, applications, and software on equipment within the COMPANY network. COMPANY essentially provides customers with remote access to computer equipment so that they can store and retrieve large amounts of data at any time and from any location via the internet. Customers set up an account with COMPANY via the internet, enabling them to upload and download their content to equipment within the COMPANY network.

STORAGE ITEM is typically used by companies and individual developers. Companies may use it to backup data or store large amounts of data for which they do not have the on-premises memory capacity, or to store temporary data used in activities such as setting up a website. Individual developers generally utilize the remote storage services to backup and store data in lieu of setting up their own on-premises electronic storage infrastructure.

Customers who utilize STORAGE ITEM retain ownership of the content uploaded to the COMPANY network. COMPANY does not have the authority to use, sell, or license customer content stored within STORAGE ITEM. COMPANY merely provides access to the infrastructure necessary for customers to store their own digital content; customers do not receive access to, or possession of, tangible personal property including software in connection with the STORAGE ITEM offering. The remote storage services are also scalable – customers can increase storage space, speed, throughput, and robustness to adapt the service to their evolving storage needs. Customers must select a specific data center to provide the STORAGE ITEM services. However, the customer does not have physical access to or knowledge of the exact location of the server equipment hosting their data and COMPANY may move the customer's data from one server to another without notice.

To make it easy for customers to upload and manage stored data, COMPANY makes available, free of charge, certain software development kits ("SDK")<sup>4</sup> and a management console. The management console is a simple and intuitive web interface that allows users to create STORAGE ITEM storage "buckets"<sup>5</sup> and then upload or delete objects contained in those buckets. Essentially, these free tools allow customers to manage and make efficient use of the storage service. The free tools are optional; customers may choose to make use of the STORAGE ITEM service without utilizing these free tools.

Customers are charged both a base fee, determined by the amount of gigabytes used in a given month, as well as an incidental usage fee based on their activity while using the service. The

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<sup>3</sup> Full description found at [WEB ADDRESS -3](#)

<sup>4</sup> A software development kit ("SDK") provides a set of tools, specific language bindings, and sample or additional code to help users write code, which is a basic building block of "software". To be clear, an SDK is not equivalent to prewritten or customized software; an SDK may help a developer create a software program or application, but it does not, by itself, perform any functions, activities or tasks that are the hallmark of software.

<sup>5</sup> Essentially a file folder. More information found at [WEB ADDRESS -3](#)

base fee prices vary, decreasing, per gigabyte, as customers utilize more storage space.<sup>6</sup> The usage fee is called a “TRANSFER” fee and is described more fully below. Customers are not charged by COMPANY for internet access required to upload/store items in a bucket or retrieve information through STORAGE ITEM; customers are independently responsible for provisioning their own internet connections and telecommunications services.

## **ii. VIRTUAL COMPUTING ENVIRONMENT ITEM (COMPUTING ITEM)**

COMPANY provides a scalable, virtual computing environment with its VIRTUAL COMPUTING ENVIRONMENT ITEM (“COMPUTING ITEM”) service.<sup>7</sup> Through COMPUTING ITEM, customers can procure computing resources to perform a variety of activities, including, but not limited to, running applications, monitoring computers and computer usage, and hosting web domains – essentially anything computer equipment, especially a computer server, can do. The service’s core benefit is that it allows customers to obtain remote access to computing capacity and control of their computing resources without significant information technology investment (e.g., customers no longer have to buy their own servers or set up their own on-premises data centers). In the technology industry, the COMPUTING ITEM service is commonly referred to as Infrastructure as a Service (“IaaS”).

To use COMPUTING ITEM, customers request a configuration of memory, CPU, storage, and operating system. This configuration is called an “Instance” and is the basis for the fee the customer is charged for COMPUTING ITEM usage.

Customers are not required to use specific software to use the service and do not download any software as part of an Instance, but some basic operating system is required to direct the computing power; therefore, use of an operating system is provided with each Instance. Customers are also provided free help in the form of application programming interfaces and SDKs that allow them to more easily utilize the computing power.<sup>8</sup> These free tools are optional and are simply posted on web pages; customers may choose to make use of COMPUTING ITEM without utilizing these free tools. Customers can use the operating system to upload the applications they wish to run using COMPANY’s computing power and can use application programming interfaces to allow their existing systems to communicate to the COMPUTING ITEM service. Specifically, COMPANY makes either open source or third party operating system software available with each Instance so customers can make use of the virtual servers. The open source operating system software used in an “Open Source Instance” is freely accessible by anyone over the internet. Customers may also opt to use a third party operating system in a “Third Party Instance.”

Whether a customer selects the Open Source or Third Party Instance option, the operating system software runs on servers within the COMPANY network to provide the COMPUTING ITEM service. Customers can neither download the operating system software for their own use nor access the physical location where the servers hosting the software are located. A customer’s

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<sup>6</sup> STORAGE ITEM pricing details found at WEB ADDRESS -4.

<sup>7</sup> Full description found at WEB ADDRESS-5

<sup>8</sup> See footnote 4.

use of this operating system software is only in conjunction with the use of the COMPUTING ITEM service. No operating system software license is sold or otherwise transferred from COMPANY to customers. To be clear, COMPANY does not separately license, sell or transfer any software with its COMPUTING ITEM services. As such, COMPANY's COMPUTING ITEM service is *not* classified as a Software as a Service ("SaaS") offering by the technology industry. In fact, COMPANY's software licensing agreements with third party software vendors do not allow COMPANY to permit COMPANY's customers to download, electronically or otherwise, the operating system software and COMPANY may not in any way transfer the software to its customers.

Customers retain all intellectual property rights to all of their data and content sent to the COMPANY network. Customers must represent that they own or license the intellectual property and software that they upload to the COMPANY network. Similar to STORAGE ITEM, customers must select a specific data center to provide their computing services. Customers do not have physical access to or knowledge of the exact location of the server equipment hosting their data and COMPANY may move the customer's data from one server to another without notice.

COMPUTING ITEM service charges are based on the computing resources that the customer consumes. Customers are charged both a base fee, determined by the amount of computing power used in a given month, as well as an incidental usage fee based on their activity while using the service. The incidental usage fee is called a "TRANSFER" FEE and is described more fully below. Although the Third Party Instances cost customers more than Open Source Instances, the extra cost is not in proportion to, and has no direct correlation to, the expense COMPANY incurs in licensing the underlying operating system from a third party vendor. The increased price reflects all of the costs and fees associated with providing the particular Instance requested by the customer as well as the demand for that kind of Instance.

### **iii. TRANSFER FEES**

Customers' usage of services like STORAGE ITEM and COMPUTING ITEM are subject to a base price measured by gigabytes or computing power, respectively, and may also generate incidental usage charges called "TRANSFER" FEES that are separately stated on their monthly bills. These usage fees are based upon a customer's activity on the COMPANY network, such as when a customer wishes to process data in multiple Regions, requests access to resources (i.e., computer equipment) in a new data center, or requests that data be copied or moved within the COMPANY network.

Within the COMPANY network there are clusters of data centers in a similar geographic area that are collectively described as a "Region." For example, the data centers that COMPANY uses in STATE-1 are described collectively as the "(STATE-1)" Region. Similarly, COMPANY data centers used in STATE-2 are collectively known as the "(STATE-2)" Region. Within a Region there are "ZONES WITHIN A REGION" which refer to the different data centers that collectively make up the Region. There are multiple ZONES WITHIN A REGION within any given Region.

Requests by customers to copy data from one Region or ZONE WITHIN A REGION to another may trigger a usage fee. For example, a customer running their website using the COMPUTING ITEM service may wish to run their website applications using Open Source or Third Party Instances in two separate Regions simultaneously, requiring that servers in those two Regions work in concert with each other. This causes the customer to incur a separately stated usage fee (“TRANSFER”) attendant to their COMPUTING ITEM charge. Similarly, a customer may ask that their data be processed using instances on servers located in different ZONES WITHIN A REGION and such a request would require data to be copied to a new ZONE WITHIN A REGION triggering another usage fee.

These fees act as a metering mechanism that tracks a customer’s usage of the COMPANY services and network and are not fees for underlying telecommunications infrastructure. On the contrary, both COMPANY and its customers must obtain, and pay for, their own telecommunication access and usage fees to their respective telecommunications providers outside of, and independent from, the COMPANY service transaction. COMPANY’s imposition of “TRANSFER” FEES is consistent with COMPANY’s pay-as-you-go pricing philosophy that charges users more as they use more resources.

Finally, it is important to note that a customer can never simply purchase “TRANSFER” in isolation. The incidental usage fee is always a consequence of a customer’s active use of a different and primary service such as the COMPUTING ITEM service. The following are examples of specific situations where the customer may incur a TRANSFER FEE:

- Adding files – Currently, there is no fee to add files to the COMPANY network.
- Moving files within Regions – Fees may be charged when a customer requests coordination of processes running in different Regions. For example, if a customer asks that data stored in one Region be used in an COMPUTING ITEM compute process in another Region a fee may apply. Similarly, fees may be charged when a customer requests their data be copied to STORAGE ITEM storage (or “backed up”) in a different Region.
- Moving files within a ZONE WITHIN A REGION – If a customer requests that data be moved from a one data center to another data center in the same Region (i.e. WORDS REMOVED) then a fee may apply.
- Retrieving data – When a customer requests that their data be copied or transferred from A COMPANY service back to their own origin servers a fee will apply.

### **III. Issues**

1. Based upon the description above, is COMPANY’s STORAGE ITEM service subject to Utah Sales and Use Tax?
2. Based upon the description above, is COMPANY’s COMPUTING ITEM service with an Open Source Instance subject to Utah Sales and Use Tax?
3. Based upon the description above, is COMPANY’s COMPUTING ITEM service with a Third Party Instance subject to Utah Sales and Use Tax?

4. Based upon the description above, is the TRANSFER fee charged in conjunction with the purchase of COMPUTING ITEM or STORAGE ITEM subject to Utah Sales and Use Tax?

#### IV. Law

##### A. Sales and Use Tax

Utah imposes its sales and use tax on retail sales of tangible personal property and certain services.<sup>9</sup> Taxable sales are subject to a state-level 4.7% rate.<sup>10</sup> The state defines “*retail sale*” as a sale, lease, or rental.<sup>11</sup> The state defines “*sale*” as the transfer of title, exchange, or barter of tangible personal property or any other taxable transaction defined by Utah Code Ann. § 59-12-103(1).<sup>12</sup> A “*sale*” includes “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.”<sup>13</sup> “*Lease*” or “*rental*” means a transfer of possession or control over tangible personal property.<sup>14</sup>

##### 1. Tangible Personal Property

Utah defines the phrase “*tangible personal property*” as personal property that can be seen, weighed, measured, felt, or touched, or that is in any other manner perceptible to the senses.<sup>15</sup> The state specifically includes prewritten computer software, regardless of the method used to deliver the software, among the items that comprise tangible personal property.<sup>16</sup> According to the Commission, “[l]icense fees for remotely accessed prewritten computer software are taxable if the purchased software is used in Utah.”<sup>17</sup>

The Commission has provided guidance on the taxability of transactions that involve remotely hosted software, which are commonly referred to as “SaaS” transactions in the industry.<sup>18</sup> For example, in *PLR 10-011*, the Commission concluded that a right to use remotely hosted prewritten computer software is a taxable retail sale of tangible personal property.<sup>19</sup> The taxpayer in that ruling sold a proprietary software system, which it termed “Web Services,” that allowed its customers to remotely access the customer’s own or a third party’s computers, attend and participate in meetings online, attend online webinars, and provide attended or unattended technical support.<sup>20</sup> Based on the Commission’s analysis, when the taxpayer sold its Web Services, it essentially gave its customers the right to use the remotely hosted software, similar to

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<sup>9</sup> Utah Code Ann. § 59-12-103.

<sup>10</sup> *Id.* at (2)(a)(i)(A).

<sup>11</sup> Utah Code Ann. § 59-12-102(107).

<sup>12</sup> Utah Code Ann. § 59-12-102(109).

<sup>13</sup> *Id.* at (b)(v).

<sup>14</sup> Utah Code Ann. § 59-12-102(59).

<sup>15</sup> Utah Code Ann. § 59-12-102(124).

<sup>16</sup> *Id.* at (b)(v).

<sup>17</sup> Utah State Tax Commission Publication 64 (Revised May 2012).

<sup>18</sup> *See, e.g., id.* Utah State Tax Commission Private Letter Ruling 10-011 (Feb. 24, 2012).

<sup>19</sup> Utah State Tax Commission Private Letter Ruling 10-011 (Feb. 24, 2012).

<sup>20</sup> *Id.*

a lease (or license) or contract to use the software.<sup>21</sup> Accordingly, the taxpayer “is still selling the use of the proprietary software even though it is not transferring that software to” its customers.<sup>22</sup>

In *PLR 13-003*, the Commission concluded that taxpayer's sales of cloud-based applications and related services to Utah customers were subject to the state's sales tax.<sup>23</sup> The taxpayer provided end customers with cloud-based software applications and related services intended to replace certain customer-owned and maintained software applications and related hardware; the taxpayer's cloud-based software applications were used by customers to enhance the functionality of the customer's on-site telecommunications equipment.<sup>24</sup> The taxpayer's customers were able to provision the hardware and cloud-based software applications on an “as-needed” basis from the taxpayer.<sup>25</sup> The Commission determined, under these facts, the taxpayer was selling software for a purpose other than resale.<sup>26</sup> Although the taxpayer argued that sales of the services would have been exempt from tax as a transfer of electronically delivered software, the Commission observed that products transferred electronically are subject to sales and use tax since Utah does not specifically exempt transfers of electronically delivered software from tax.<sup>27</sup> Finally, while hosting customer-owned software applications and maintaining them for a separately-stated fee would not be an activity subject to tax if it was performed out-of-state, any hosting, maintenance, or management activities occurring in state could be subject to Utah sales tax under Utah Code Ann. § 59-12-103 and Utah Code Ann. § 59-12-103.<sup>28</sup>

In *PLR 15-005*, the Commission indicated that a taxpayer's provision of online banking, bill payment, mobile banking, and a finance and budget tool was the sale of taxable tangible personal property.<sup>29</sup> The taxpayer was an out-of-state corporation that sold a suite of banking solutions to financial institutions, including banks and credit unions, some of which were located in Utah.<sup>30</sup> The institutions purchased one or more of the software offerings from the taxpayer and were billed accordingly.<sup>31</sup> The taxpayer used its proprietary platform to provide the services and limited the institutions' ability to modify or control the platform.<sup>32</sup> The institutions were not charged for use of the platform, and, other than the downloadable mobile banking application, the taxpayer's sale of services did not include the sale, license, or transfer of software to the financial institution or its account holders.<sup>33</sup> The agreements governing the relationship between the taxpayer and the financial institution stipulated that the institutions were not granted a license to software but were merely receiving services from the taxpayer.<sup>34</sup> The taxpayer's personnel instructed the institutions on the technological requirements needed to implement the taxpayer's services.<sup>35</sup> On the basis of these facts, the Commission concluded that taxpayer's sales to financial

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<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

<sup>23</sup> Utah State Tax Commission Private Letter Ruling 13-003 (Dec. 04, 2013).

<sup>24</sup> *Id.*

<sup>25</sup> *Id.*

<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> Utah State Tax Commission Private Letter Ruling 15-005 (Apr. 15, 2015).

<sup>30</sup> *Id.*

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*

<sup>35</sup> *Id.*

institutions in Utah were subject to sales and use tax under Utah Code Ann. § 59-12-103 as “amounts paid or charged for...retail sales of tangible personal property made within the state...” since the essence of the transaction between the taxpayer and the institution was the sale of the taxpayer’s prewritten computer software.<sup>36</sup> In reaching this conclusion, the Commission noted that under the broad definition of sale, sales of the taxpayer’s services were, essentially, sales of the right to use the software applications on the taxpayer’s platform.<sup>37</sup> Such transactions were subject to sales tax if the sales were made within the state.<sup>38</sup> The Commission distinguished the sale of the taxpayer’s services from sales of non-taxable data processing by noting the primary object of the taxpayer’s transactions with financial institutions was the use of the taxpayer’s application software, not the use of an informational database.<sup>39</sup>

## 2. Services

Utah only taxes those services enumerated by Utah Code Ann. § 59-12-103.<sup>40</sup> For purposes of this request, the only relevant taxable services include telecommunications services.<sup>41</sup>

### i. Telecommunications Service

The state defines “*telecommunications services*” as “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.”<sup>42</sup> Taxable telecommunications service includes the transmission, conveyance, or routing of voice, data, audio, video, or other information or signals using computer processing applications that act on content’s form, code, or protocol for transmission, conveyance, or routing purposes.<sup>43</sup> Conversely, “*telecommunications service*” does not include data processing and information services that allow data to be generated, acquired, stored, processed, or retrieved and delivered to a purchaser by an electronic transmission if the purchaser’s primary purpose for the underlying transaction is the processed data or information.<sup>44</sup>

### ii. Data Processing Services

Utah does not impose its sales and use tax on the of data processing services.<sup>45</sup> According to the Commission, “[a]lthough the definition of a data processing and information service is not separately listed but is instead provided within the definition of ‘*telecommunications service*,’ the Utah Code still recognizes that a data processing and information service exists. Furthermore, the Utah Code does not later specifically list [data processing] as taxable in § 59-12-103.”<sup>46</sup> Based on this approach, the Commission has concluded that providing access to an online, internet-based news website with a database of archived information and content qualifies as a non-taxable data

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<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*

<sup>40</sup> Utah State Tax Commission Private Letter Ruling 10-012 (Dec. 7, 2012).

<sup>41</sup> Utah Code Ann. § 59-12-103.(1)(b)(i).

<sup>42</sup> Utah Code Ann. § 59-12-102(128)(a).

<sup>43</sup> *Id.* at (b)(i).

<sup>44</sup> *Id.* at (c)(iv).

<sup>45</sup> *See, e.g.*, Utah State Tax Commission Private Letter Ruling 10-012 (citing Utah Code. Ann. § 59-12-102(122)(c)(iv)).

<sup>46</sup> Utah State Tax Commission Private Letter Ruling 12-002 (Dec. 7, 2012).

processing and information service.<sup>47</sup> Similarly, the Commission has stated that the use of a database (which was inseparably combined with web-based application software) is not taxable because it is a data processing and information service.<sup>48</sup> The taxpayer's service in *PLR 10-012* provided customers with electronically transmitted processed data retrieved from the database; the information housed in the database was supplied by the taxpayer.<sup>49</sup>

## **B. Bundled Transactions and the Essence of the Transaction Theory**

The state defines a “*bundled transaction*” as a sale of two or more distinct and identifiable products (i.e. tangible personal property or services), at least one of which is taxable and one of which is exempt, sold for one nonitemized price.<sup>50</sup> A bundled transaction does not include, among other exceptions, a retail sale of tangible personal property and a service where the tangible personal property 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.<sup>51</sup>

Utah courts have endorsed usage of the “essence of the transaction” theory to determine whether the essence of a transaction is one for services or tangible personal property.<sup>52</sup> According to the Utah Supreme Court, the true object test 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.”<sup>53</sup> In *B.J.-Titan*, the Utah Supreme Court outlined several factors that assist in analyzing whether a transaction essentially a transfer of tangible personal property, including: (1) the value of the property to the customer in relation to the value of the services; (2) the cost of the property to the seller; (3) the customer's right to ownership or possession of the property; (4) the ability to separately itemize charges for the property and the services; (5) the extent to which the services increase the value of the property or to which the property increases the value of the services; and (6) the extent that such services are rendered in similar transactions.<sup>54</sup>

## **V. Analysis**

### **A. The STORAGE ITEM service is not subject to Utah Sales and Use Tax.**

Utah imposes its sales and use tax on the sale of tangible personal property, including prewritten computer software delivered electronically, and certain enumerated services.<sup>55</sup> As indicated in the description of the service above, users of the STORAGE ITEM service are primarily paying to have their data stored securely in a remote location accessible via the internet. STORAGE ITEM users do not receive any software—or any other item of tangible personal property—as a result of using this service; thus, the service does not qualify as a sale of tangible personal property. Furthermore, the STORAGE ITEM service does not fall within the purview of

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<sup>47</sup> *Id.*

<sup>48</sup> Utah State Tax Commission Private Letter Ruling 10-012.

<sup>49</sup> *Id.*

<sup>50</sup> Utah Code Ann. § 59-12-102(18)(a).

<sup>51</sup> *Id.* at (b)(iv).

<sup>52</sup> *B.J.-Titan Services v. State Tax Comm'n*, 842 P.2d 822, 825 (Utah 1992).

<sup>53</sup> *Id.*

<sup>54</sup> *Id.* at 826.

<sup>55</sup> Utah Code Ann. § 59-12-103(1).

any of the services enumerated as taxable by Utah Code Ann. § 59-12-103. The holdings in *PLR 10-012* and *12-002* are instructive when analyzing the STORAGE ITEM service. In both rulings, the Commission concluded that access to a *pre*-populated database represented a nontaxable data processing and information service.<sup>56</sup> In *PLR 15-005*, the Commission indicated that neither data processing services nor access to an informational database service are subject to Utah sales and use tax.<sup>57</sup> As an IaaS offering, the STORAGE ITEM service provides the storage functionality that individuals and companies would utilize in creating such databases. As such, the STORAGE ITEM service falls within the definition of a data processing and information service.<sup>58</sup> Therefore, because there is no sale of tangible personal property and the essence of the transaction is the storage and retrieval of data, the STORAGE ITEM service is a data processing and information service that is not subject to Utah sales and use tax.

**B. The COMPUTING ITEM service with an Open Source Instance is not subject to Utah Sales and Use Tax.**

As noted above, Utah imposes its sales and use tax on the sale of tangible personal property — including license fees for remotely accessed prewritten computer software<sup>59</sup> — and certain enumerated services.<sup>60</sup> The COMPUTING ITEM service with an Open Source Instance is not subject to Utah sales and use tax because the COMPUTING ITEM service does not involve a sale of computer software or a service Utah has enumerated as taxable.

First, when customers purchase the COMPUTING ITEM service, they are not purchasing prewritten computer software. As noted above, COMPANY does not separately sell or transfer any software with its COMPUTING ITEM service. The fact that COMPUTING ITEM is a computer-related service means that software is involved in the provision of the service; computer hardware will not work without operating system software. However, customers do not purchase a software license from COMPANY nor does COMPANY describe itself as a seller or licensor of software. That is consistent with the customer’s understanding of the transaction, as COMPANY is known as an IaaS provider in the industry rather than as a seller of software. Customers would not purchase the COMPUTING ITEM service simply to procure operating system software. Rather, customers seek out COMPANY’s COMPUTING ITEM service so that they can remotely access infrastructure (i.e., computing power) to run the software that they have separately created or separately purchased from an independent software vendor. As an incidental component of the COMPUTING ITEM service, a customer merely accesses operating system software remotely to make use of the purchased computing power. To be clear, the COMPUTING ITEM service does not provide customers with a physical or electronic copy of operating system software. *Rather, COMPANY procures and then internally uses the operating system software itself as part of COMPANY’s provision of the COMPUTING ITEM service.* The provision of a computing service that allows customers some remote access to operating system software to enable their use of that

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<sup>56</sup> Utah State Tax Commission Private Letter Ruling 10-012; Utah State Tax Commission Private Letter Ruling 12-002.

<sup>57</sup> Utah State Tax Commission Private Letter Ruling 15-005 (Apr. 15, 2015).

<sup>58</sup> Utah Code Ann. § 59-12-102(122)(c)(iv)(A).

<sup>59</sup> Utah State Tax Commission Publication 64 (Revised May 2012).

<sup>60</sup> Utah Code Ann. § 59-12-103(1).

computing power does not make the service taxable as the sale of a license to use prewritten computer software.<sup>61</sup>

Moreover, the COMPUTING ITEM service is unlike the Web Services analyzed in PLR 10-011. As the Commission noted, the Web Services in PLR 10-011 represented a retail sale of tangible personal property because, in providing the Web Services, the taxpayer in substance granted its customers the right to use proprietary software under a lease or contract.<sup>62</sup> In fact, as the Commission noted, the taxpayer did not use software to sell the services; instead, the software and its capabilities was the contracted-for services.<sup>63</sup> In other words, the taxpayer's customers paid "for the use of the proprietary software not for services provided by the" taxpayer.<sup>64</sup> In the case of the COMPUTING ITEM service, COMPANY's customers are paying for computing power and not software. In fact, customers run their separately purchased or created software using the computing power they purchase from COMPANY. As noted above, COMPANY uses the operating system software itself as part of the COMPUTING ITEM service. Thus, the operating system software that COMPANY uses to provide its customers the COMPUTING ITEM service is not what the customer pays for, thereby making the determination in PLR 10-011 incongruent with the COMPUTING ITEM service.

Similarly, COMPANY's service offerings are distinct from the services provided by the taxpayers in PLRs 13-003 and 15-005. In both PLRs, the taxpayers provided end customers with access to remote software applications and related services intended to replace software applications that the taxpayers' customers maintained on-premise.<sup>65</sup> The Commission concluded that the taxpayers in both PLR 13-003 and PLR 15-005 were selling software because, as the Commission observed in PLR 15-005, the primary object of the taxpayers' transactions was the use of the taxpayers' application software, not the use of an informational database or some other non-taxable data processing service.<sup>66</sup> Relying on the broad definition of retail sale, in PLR 13-003 the Commission concluded the taxpayer's services involved transferring use of the taxpayer's software to the customer.<sup>67</sup> In PLR 15-005, the Commission again relied on the broad definition of retail sale, noting the essence of the transaction between the taxpayer and the financial institutions was the sale of the right to use the software applications on the taxpayer's platform.<sup>68</sup>

COMPANY's facts are distinct. COMPANY services are not intended to replace the customer's software applications. Rather, as described above, customers purchase COMPUTING ITEM so they can access the underlying infrastructure or computing power necessary to, among other activities, run software programs – whether developed internally or purchased from independent software companies – on remote computing equipment maintained in the COMPANY data center network. Unlike the taxpayers' customers in PLR 13-003 and PLR 15-005, COMPANY's customers do not purchase COMPUTING ITEM to receive the output of pre-programmed software applications. Instead, COMPANY's customers purchase COMPUTING ITEM to, for example, remotely host software applications like the telecommunications enhancing

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<sup>61</sup> See Utah State Tax Commission Publication 64 (Revised May 2012).

<sup>62</sup> Utah State Tax Commission Private Letter Ruling 10-011.

<sup>63</sup> *Id.*

<sup>64</sup> *Id.*

<sup>65</sup> *Id.*

<sup>66</sup> See Utah State Tax Commission Private Letter Ruling 15-005.

<sup>67</sup> Utah State Tax Commission Private Letter Ruling 13-003 (Dec. 04, 2013).

<sup>68</sup> Utah State Tax Commission Private Letter Ruling 15-005.

or banking software applications that the taxpayers' customers in PLRs 13-003 and 15-005, respectively, accessed through the "cloud." While COMPUTING ITEM customers do have remote access to some operating system software, the software element is not, like the Commission conversely noted in PLR 15-005, the primary object of an COMPUTING ITEM customer's reason for procuring the COMPUTING ITEM service.

The COMPUTING ITEM service also does not qualify as a service that the state has determined is subject to tax under Utah Code Ann. § 59-12-103. Instead, the COMPUTING ITEM service is more appropriately classified as a nontaxable data processing service because the computing power provided by the COMPUTING ITEM service allows customers to perform unlimited computing activities, including processing and generating data.<sup>69</sup> As the Commission has noted, services that allow data to be processed, generated, retrieved, or stored and delivered by electronic transmission qualify as nontaxable data processing and information services.<sup>70</sup> Similarly, the Commission recently reconfirmed that information and data processing services, as services that "allow[] data to be acquired, generated, processed, retrieved, or stored, and delivered by an electronic transmission to a purchaser," are exempt under Utah Code Ann. 59-12-103.<sup>71</sup> As noted above, the COMPUTING ITEM service provides customers with remote computing resources. Specifically, the COMPUTING ITEM service, through the use of remote computing resources, allows customers to compute data; enter, maintain, and retrieve information; and store and manipulate computerized data and other information—all of which are activities that qualify as non-taxable data processing or information services.

Moreover, the sale of the COMPUTING ITEM service does not qualify as a "*bundled transaction*," which the state defines as the sale of two or more distinct and identifiable products, at least one of which is taxable, sold for one nonitemized price.<sup>72</sup> The COMPUTING ITEM service provides computing power only. Some access to an operating system is provided as part of that service, but that access is not a distinct product which COMPANY is selling. Rather, the access is merely a necessary component of the service and does not represent a separate benefit that is "bundled" with computing power. Because COMPANY is not authorized to "sell" the operating system software component of the COMPUTING ITEM service, the COMPUTING ITEM service does not meet the statutory requirement of a bundled transaction.

Assuming, *arguendo*, that the Commission believes the COMPUTING ITEM service involves taxable access to software, according to the essence of the transaction test approved by the Utah Supreme Court,<sup>73</sup> the remote computing power, and not the purchase of operating system software, is what is truly sold in an COMPUTING ITEM service transaction. The Utah Supreme Court has articulated several factors to determine the essence of a transaction, including: (1) the value of the property to the customer in relation to the value of the services; (2) the cost of the property to the seller; (3) the customer's right to ownership or possession of the property; (4) the ability to separately itemize charges for the property and the services; (5) the extent to which the services increase the value of the property or to which the property increases the value of the

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<sup>69</sup> Utah Code Ann. § 59-12-102(122)(c)(iv)(A)(I).

<sup>70</sup> Utah State Tax Commission Private Letter Ruling 10-011 (quoting Utah Code Ann. § 59-12-102(122)(c)(iv)).

<sup>71</sup> Utah Private Letter Rulings, No. 15-004, 09/28/2015. *Internal Citation Omitted*.

<sup>72</sup> Utah Code Ann. § 59-12-102(18)(a).

<sup>73</sup> See, e.g., *B.J.-Titan Services v. State Tax Comm'm*, 842 P.2d 822.

services; and (6) the extent that such services are rendered in similar transactions.<sup>74</sup> An analysis of these factors, as applied to the Open Source Instance of the COMPUTING ITEM service, are set forth below:

- With respect to factor #1, the operating system software affords very little value to a customer when compared to the remote computing power provided by the service. In fact, without the computing power, the operating system software is worthless. As a data center alternative, COMPUTING ITEM customers are not contracting with COMPANY for access to operating system software but, instead, for a cost efficient means of acquiring the computing power that would otherwise be provided by an on-premises data center.
- With respect to factor #2, with an Open Source Instance, the operating system software is freely available to anyone who has access to the internet; COMPANY simply uses the operating system to provide the computing power.
- With respect to factor #3, as noted above, customers do not receive any right to ownership or possession of the operating system software.
- With respect to factor #4, COMPANY does not have a way to charge a customer a separate price for the computing power component and the operating system component. As noted above, COMPANY's contract with the customer does not provide for the sale of, or a license to, software. In fact, COMPANY is prohibited from selling or sublicensing the operating system software to its customers; therefore, a separate charge would be wholly inappropriate and not reflective of the substance of the transaction. Furthermore, the COMPUTING ITEM service is an IaaS offering, meaning the operating software component of the service is inextricably intertwined with the computing power, thereby making separation of any perceived value derived by that limited operating system access difficult to determine.
- With respect to factor #5, the analysis is difficult because, as stated above, there is no separate and distinguishable "property" sale along with the sale of the underlying "service." To provide the service, COMPANY has to grant the user some access to an operating system. When considering the relative value of the operating system compared to that of the computing power, the operating system merely facilitates the provision of the service. However, with regard to the COMPUTING ITEM service, the computing power enhances the value of the "property," in that limited access to the operating system is worthless if it is not used to direct the computing power that a customer pays for.
- With respect to factor #6, it is unclear how this factor would apply to the COMPUTING ITEM service. As such, its relevance—if any—is outweighed by the other factors' overwhelming support of the COMPUTING ITEM service being classified as a nontaxable data processing and information service.

The totality of the factors supports the conclusion that the COMPUTING ITEM service is a nontaxable service as opposed to the retail sale of prewritten computer software such as that found in a hosted software or SaaS offering where the essence of the transaction is use of a particular software product. More specifically, the essence of an COMPUTING ITEM service

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<sup>74</sup> *Id.* at 826.

transaction is the purchase of a nontaxable data processing and information service that gives customers the power to do anything a server can do, including the electronic acquisition, generation, and processing of data.

Finally, the COMPUTING ITEM service with an Open Source Instance does not qualify as a taxable telecommunications service. While taxable telecommunications services include the transmission, conveyance, or routing of data or other information using computer processing applications that act on the data or information's form, code, or protocol for *transmission, conveyance, or routing purposes*,<sup>75</sup> data processing and information services that allow data to be *generated*, acquired, stored, *processed*, or retrieved and delivered to a purchaser by electronic transmission, if the purchaser's primary purpose for the underlying transaction is the processed data, do not qualify as taxable telecommunications services.<sup>76</sup> A customer using the COMPUTING ITEM service contracts with COMPANY for the provision of remote computing power; a customer does not contract with COMPANY for the "transmission, conveyance, or routing" of data or information among or between points.<sup>77</sup> Furthermore the COMPUTING ITEM service provides customers with remote computing power, which customers can use to generate, process, and deliver data and other information through electronic transmissions. Therefore, the COMPUTING ITEM service qualifies as the type of data processing and information services specifically excluded from the realm of taxable telecommunications services.

### **C. The COMPUTING ITEM service with a Third Party Instance is not subject to Utah Sales and Use Tax.**

For the reasons cited above, similar to the COMPUTING ITEM service with an Open Source Instance, the COMPUTING ITEM service with a Third Party Instance is also not subject to the Utah sales and use tax.

As noted above, the state's sales tax applies to transactions involving the sale of prewritten computer software and other forms of tangible personal property, and certain enumerated taxable services.<sup>78</sup> To reiterate, COMPANY does not separately sell or transfer possession of any software with its COMPUTING ITEM service; instead, the company utilizes operating system software to provide the remote computing power offered by the COMPUTING ITEM service. A customer's remote access of an operating system to make use of the purchased computing power does not make the service taxable as the sale of software. This is true regardless of whether the operating system software is freely available on the internet, as is the case with Open Source Instances discussed above, or Third Party Instances that utilize operating system software that COMPANY has procured from a third party for use by COMPANY.

In either case, the COMPUTING ITEM service does not meet the definition of a "*bundled transaction*" because the service does not involve the sale of two or more distinct and identifiable products.<sup>79</sup> COMPANY procures the third party operating system software for its own use in provisioning the COMPUTING ITEM service to customers, and, does not sell third party operating

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<sup>75</sup> Utah Code Ann. § 59-12-102(122)(b)(i).

<sup>76</sup> *Id.* at (c)(iv).

<sup>77</sup> Utah Code Ann. § 59-12-102(122)(b)(i).

<sup>78</sup> Utah Code Ann. § 59-12-103(1).

<sup>79</sup> Utah Code Ann. § 59-12-102(18)(a).

system software to customers. There is no “property provided,” thus precluding an analysis using the *B.J.-Titan* factors; however, assuming, *arguendo*, that the COMPUTING ITEM service with a Third Party Instance did qualify as a bundled transaction, the factors outlined by the *B.J.-Titan* court would still weigh in favor of the COMPUTING ITEM transaction being a service.<sup>80</sup> In fact, the only factor analysis that would change from that of an Open Source Instance (above) would be factor #2; with a Third Party Instance, COMPANY has incurred some cost to acquire the right to use a third party’s operating system software as a component of the COMPUTING ITEM service. To assess COMPANY’s COMPUTING ITEM service costs we would be required to evaluate the costs associated with COMPANY’s procurement of operating system software and other, extremely substantial, capital intensive expenses associated with the provision and maintenance of the COMPANY network (e.g., servers located in data centers around the world).

Moreover, even with a Third Party Instance, the computing power clearly outweighs the value of the incidental operating system software (i.e., factor #1). The customer has no right to possess or own the operating system software – in fact, COMPANY’s software licensing agreements with third party software vendors expressly forbid COMPANY from transferring or transmitting the operating system software to customers (i.e., factor #3). COMPANY also does not have the ability to, nor would it be appropriate to, separately itemize the computing power and operating system costs (i.e. factor #4). Finally, the operating system software is valueless without the computing power, in that its sole purpose here is to provide customers access to the computing power (i.e., factor #5). Thus, the essence of the COMPUTING ITEM transaction involving a Third Party Instance is to purchase a service and not tangible personal property, including taxable pre-written computer software. For the reasons cited above, the COMPUTING ITEM service with a Third Party Instance is not a taxable “telecommunications services” and is more appropriately described as a data processing and information service specifically exempted from the taxable telecommunication service definition.

#### **D. TRANSFER FEES are not subject to Utah Sales and Use Tax.**

For the various reasons discussed below, TRANSFER FEES are not subject to Utah sales and use tax.

First, “TRANSFER” is not a separate and unique COMPANY service. As noted above, TRANSFER FEES act as a metering mechanism that track a customer’s usage of COMPANY’s services, including COMPUTING ITEM and STORAGE ITEM. TRANSFER FEES, while separately stated on a customer’s bill, are not fees for services separate and distinct from the STORAGE ITEM and COMPUTING ITEM services. To the contrary, *these fees are always attendant to a customer’s active usage of the STORAGE ITEM and COMPUTING ITEM services.* The facts above indicate the types of situations where these fees are charged and include the coordination of COMPUTING ITEM computing power between data centers and the access of data stored on computer equipment using the STORAGE ITEM service. As such, the taxability of the fees should follow that of the services from which the fees arise – COMPUTING ITEM and STORAGE ITEM. To be clear, a customer cannot purchase “TRANSFER” by itself and attempt to transfer data from their own origin server to a third party server or location. Instead,

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<sup>80</sup> *B.J.-Titan Services v. State Tax Comm’n*, 842 P.2d 822, 825 (Utah 1992).

TRANSFER FEES will only be incurred in connection with, and incident to, a customer's active usage of COMPANY's COMPUTING ITEM or STORAGE ITEM services.

Because the TRANSFER FEES represent a customer's usage of COMPANY's COMPUTING ITEM and STORAGE ITEM services, the fees are not subject to Utah sales and use tax for the same reasons outlined above. Specifically, there is no sale or delivery of tangible personal property, including prewritten computer software.<sup>81</sup> The services that generate the fees qualify as data processing services that the Commission has already concluded are not subject to the state's sales and use tax.<sup>82</sup> With COMPUTING ITEM, TRANSFER FEES are charged when customers request access to computer equipment (i.e., access to computing power) in different data centers. With STORAGE ITEM, TRANSFER FEES are charged when customers request access to computer equipment (i.e., access to computer storage) to store data and when users later access or retrieve that stored data.

Moreover, TRANSFER FEES do not qualify as "*telecommunications services*." Although the state defines taxable "*telecommunications services*" to include the electronic transmission, conveyance, or routing of voice, data, or other information or signals to a point or between or among points, whether or not computer processing applications are used to act on the voice/data/information's form, code, or protocol for transmission, conveyance, or routing purposes,<sup>83</sup> TRANSFER FEES do not fall under the purview of "*telecommunications services*" because the TRANSFER FEES are an inseparable part of COMPANY's data processing services – COMPUTING ITEM and STORAGE ITEM.<sup>84</sup> As noted above, the TRANSFER FEES generated by the use of STORAGE ITEM and COMPUTING ITEM are triggered when customers request access to computer equipment (i.e., access to computing power or computer storage). Thus, "TRANSFER" FEES are not a communication service that allows a customer to electronically transmit, convey, or route data or other information among points.<sup>85</sup>

Finally, to be clear, the parties to the COMPANY services transaction (COMPANY and the customer) each pay their own telecommunication access and usage fees to their respective telecommunication service provider; COMPANY neither has privity to the contract between the customer and the telecommunication service provider nor is telecommunication services part of the COMPANY services transaction. Furthermore, although the title ("TRANSFER") appears to convey a telecommunications service, the title was chosen, as is often the case, for marketing and product placement purposes; the title should not be the basis for determining its taxability. As mentioned above, the fee itself is meant to simply charge customers based on their usage of COMPANY services and does not mean that COMPANY indeed provides telecommunications services. Thus, TRANSFER FEES are generated from transactions involving the type of data processing activities outlined above. These TRANSFER FEES, therefore, are expressly exempt from the definition of "*telecommunications services*."

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<sup>81</sup> Utah Code Ann. § 59-12-102(118)(b)(v).

<sup>82</sup> See, e.g., Utah State Tax Commission Private Letter Ruling 10-012 (citing Utah Code Ann. § 59-12-102(122)(c)(iv)).

<sup>83</sup> Utah Code Ann. § 59-12-102(122)(b)(i).

<sup>84</sup> *Id.* at (c)(iv).

<sup>85</sup> Utah Code Ann. § 59-12-102(122)(b)(i).

**VI. Conclusions**

For the foregoing reasons, COMPANY respectfully seeks confirmation from the Commission regarding the following conclusions, which were derived from application of Utah’s statutory, departmental, and legal guidance to the relevant facts:

1. CLOUD STORAGE ITEM (STORAGE ITEM) is not subject to Utah Sales and Use Tax.
2. VIRTUAL COMPUTING ENVIRONMENT ITEM (COMPUTING ITEM) service with an Open Source Instance is not subject to Utah Sales and Use Tax.
3. VIRTUAL COMPUTING ENVIRONMENT ITEM (COMPUTING ITEM) service with a Third Party Instance is not subject to Utah Sales and Use Tax.
4. TRANSFER FEES charged by COMPANY in conjunction with the purchase of STORAGE ITEM or COMPUTING ITEM are not subject to Utah Sales and Use Tax since the taxability of these fees follows that of the underlying service.

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Prior to the issuance of a Ruling, COMPANY respectfully requests that the Commission contact us to discuss any facts or questions that may potentially result in an adverse Ruling. With the understanding that the issues and services discussed in this Ruling Request are complex and technical, we would be amenable to, and appreciative of, the opportunity to visit your office and demonstrate the services discussed in this Ruling Request. Should any of the facts or analysis noted in this Ruling Request require clarification, or if you would like to set up a time for us to visit your offices, please do not hesitate to contact me at ###-###-####.

Under penalties of perjury, I declare that I have examined this Ruling Request, including accompanying documents, and to the best of my knowledge and belief, the facts presented in support of the requested Ruling are true, correct, and complete.

Very truly yours,

NAME-2  
Tax Senior Manager

**RESPONSE LETTER**  
**PRIVATE LETTER RULING 16-004**

March 31, 2017

NAME-2  
Tax Senior Manager  
WEB ADDRESS  
COMPANY.  
ADDRESS  
CITY-1, STATE-1 ZIP CODE

Dear NAME-2:

This letter is in response to your request for a private letter ruling for COMPANY. (“Company”), which sells in part the following items: CLOUD STORAGE ITEM (“Storage Item”) and VIRTUAL COMPUTING ENVIRONMENT ITEM (“Computing Item”). Although the Company describes itself as providing services to its customers, the issue of whether the Company is providing nontaxable services depends on the facts surrounding the transactions you have presented. The Company provides through the internet the Storage Item and the Computing Item to its customers. You have asked about the Utah sales and use tax treatment of the sales of these two items. Through your request letter, you provided us with the following facts.

I. Facts

You explained the following facts about the Company. The Company is headquartered outside of Utah. The Company provides the Storage Item and the Computing Item to its customers by using large data centers and small clusters of servers, all of which are located outside of Utah.

You explained, in part, the following about the **Storage Item**:

[The Company’s] remote storage service . . . allows customers to store and retrieve content, data, applications, and software on equipment within the [Company’s] network. [The Company] essentially provides customers with remote access to computer equipment so that they can store and retrieve large amounts of data at any time and from any location via the internet. Customers set up an account with [the Company] via the internet, enabling them to upload and download their content to equipment within the [Company’s] network.

[The Storage Item] is typically used by companies and individual developers. Companies may use it to backup data or store large amounts of data

for which they do not have the on-premises memory capacity, or to store temporary data used in activities such as setting up a website. Individual developers generally utilize the remote storage services to backup and store data in lieu of setting up their own on-premises electronic storage infrastructure.

Customers who utilize [the Storage Item] retain ownership of the content uploaded to the [Company's] network. [The Company] does not have the authority to use, sell, or license customer content stored within [the Storage Item]. [The Company] merely provides access to the infrastructure necessary for customers to store their own digital content; customers do not receive access to, or possession of, tangible personal property including software in connection with the [the Storage Item] offering. The remote storage services are also scalable – customers can increase storage space, speed, throughput, and robustness to adapt the service to their evolving storage needs. Customers must select a specific data center to provide the [Storage Item]. However, the customer does not have physical access to or knowledge of the exact location of the server equipment hosting their data and [the Company] may move the customer's data from one server to another without notice.

To make it easy for customers to upload and manage stored data, [the Company] makes available, free of charge, certain software development kits (“SDK”) and a management console. The management console is a simple and intuitive web interface that allows users to create [Storage Item] “buckets” and then upload or delete objects contained in those buckets. Essentially, these free tools allow customers to manage and make efficient use of the storage service. The free tools are optional; customers may choose to make use of the [Storage Item] without utilizing these free tools.

Customers are charged both a base fee, determined by the amount of gigabytes used in a given month, as well as an incidental usage fee based on their activity while using the service. The base fee prices vary, decreasing, per gigabyte, as customers utilize more storage space. The usage fee . . . is described more fully below. Customers are not charged by [the Company] for internet access required to upload/store items in a bucket or retrieve information through [Storage Item]; customers are independently responsible for provisioning their own internet connections and telecommunications services.

(Footnotes removed.)

In the above quotation from your request letter, you mentioned “certain software development kits.” During a meeting with the Tax Commission, you explained that software development kits (“SDK”) are samples of computer code available free of charge to any user of the web. You explained the samples are text files.

You explained, in part, the following about the **Computing Item**:

[The Company] provides a scalable, virtual computing environment with its [Computing Item]. Through [the Computing Item], customers can procure computing resources to perform a variety of activities, including, but not limited to, running applications, monitoring computers and computer usage, and hosting web domains – essentially anything computer equipment, especially a computer server, can do. The service’s core benefit is that it allows customers to obtain remote access to computing capacity and control of their computing resources without significant information technology investment (e.g., customers no longer have to buy their own servers or set up their own on-premises data centers). In the technology industry, the [Computing Item] is commonly referred to as Infrastructure as a Service (“IaaS”).

To use [the Computing Item], customers request a configuration of memory, CPU, storage, and operating system. This configuration is called an “Instance” and is the basis for the fee the customer is charged for [the Computing Item’s] usage.

Customers are not required to use specific software to use the service and do not download any software as part of an Instance, but some basic operating system is required to direct the computing power; therefore, use of an operating system is provided with each Instance. Customers are also provided free help in the form of application programming interfaces and SDKs that allow them to more easily utilize the computing power. These free tools are optional and are simply posted on web pages; customers may choose to make use of [the Computing Item] without utilizing these free tools. Customers can use the operating system to upload the applications they wish to run using [the Company’s] computing power and can use application programming interfaces to allow their existing systems to communicate to the [Computing Item]. Specifically, [the Company] makes either open source or third party operating system software available with each Instance so customers can make use of the virtual servers. The open source operating system software used in an “Open Source Instance” is freely accessible by anyone over the internet. Customers may also opt to use a third party operating system in a “Third Party Instance.”

Whether a customer selects the Open Source or Third Party Instance option, the operating system software runs on servers within the [Company’s] network to provide the [Computing Item]. Customers can neither download the operating system software for their own use nor access the physical location where the servers hosting the software are located. A customer’s use of this operating system software is only in conjunction with the use of the [Computing Item]. No operating system software license is sold or otherwise transferred from [the Company] to customers. To be clear, [the Company] does not separately license, sell or transfer any software with its [Computing Item]. As such, [the Company’s Computing Item] is *not* classified as a Software as a Service (“SaaS”) offering by the technology industry. In fact, [the Company’s] software licensing agreements with third party software vendors do not allow [the Company] to permit [the Company’s]

customers to download, electronically or otherwise, the operating system software and [the Company] may not in any way transfer the software to its customers.

Customers retain all intellectual property rights to all of their data and content sent to the [Company's] network. Customers must represent that they own or license the intellectual property and software that they upload to the [Company's] network. Similar to [the Storage Item], customers must select a specific data center to provide their computing services. Customers do not have physical access to or knowledge of the exact location of the server equipment hosting their data and [the Company] may move the customer's data from one server to another without notice.

[The Computing Item's] charges are based on the computing resources that the customer consumes. Customers are charged both a base fee, determined by the amount of computing power used in a given month, as well as an incidental usage fee based on their activity while using the service. The incidental usage fee . . . is described more fully below. Although the Third Party Instances cost customers more than Open Source Instances, the extra cost is not in proportion to, and has no direct correlation to, the expense [the Company] incurs in licensing the underlying operating system from a third party vendor. The increased price reflects all of the costs and fees associated with providing the particular Instance requested by the customer as well as the demand for that kind of Instance.

(Footnotes removed.)

In the above quotation from your request letter, you mentioned “an incidental usage fee.” During a meeting with the Tax Commission, you explained the **usage fee** is separately stated on the customers' monthly bills. You also explained the usage fee is never incurred on its own; it can only accompany a primary item such as the Storage Item or the Computing Item. For the usage fee, you stated the following, in part:

The following are examples of specific situations where the customer may incur a [usage fee]:

- Adding files – Currently, there is no fee to add files to the [Company's] network.
- Moving files within Regions – Fees may be charged when a customer requests coordination of processes running in different Regions. For example, if a customer asks that data stored in one Region be used in [a Computing Item] compute process in another Region a fee may apply. Similarly, fees may be charged when a customer requests their data be copied to [the Storage Item's] storage (or “backed up”) in a different Region.
- Moving files within A ZONE WITHIN A REGION – If a customer requests that data be moved from a one data center to another data center in the same Region (i.e. WORDS REMOVED) then a fee may apply.

- Retrieving data – When a customer requests that their data be copied or transferred from [a Company’s] service back to their own origin servers a fee will apply.

## II. Applicable Law

Utah Code Ann. § 59-12-103(1) imposes taxes on the purchaser for certain transactions including the following:

- (1) . . . for amounts paid or charged for . . .
  - (a) retail sales of tangible personal property made within the state;
    - . . . .
    - (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; . . .
- . . . .

Utah Code Ann. § 59-12-102(26)-(27) defines computer and computer software as follows, 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.

Utah Code Ann. § 59-12-211 provides the source of certain transactions, stating in part:

- (1) As used in this section:
  - (a) (i) "Receipt" and "receive" mean:
    - (A) taking possession of tangible personal property;
    - . . . .
- (2) Except as provided in Subsections (8) and (14), if tangible personal property, a product transferred electronically, or a service that is subject to taxation under

this chapter is received by a purchaser at a business location of a seller, the location of the transaction is the business location of the seller.

- (3) Subject to Subsection (10), and except as provided in Subsections (7), (8), (9), (11), and (14), if tangible personal property, a product transferred electronically, or a service that is subject to taxation under this chapter is not received by a purchaser at a business location of a seller, the location of the transaction is the location where the purchaser takes receipt of the tangible personal property or service.
- (4) Subject to Subsection (10), and except as provided in Subsections (7), (8), (9), (11), and (14), if Subsection (2) or (3) does not apply, the location of the transaction is the location indicated by an address for or other information on the purchaser if:
  - (a) the address or other information is available from the seller's business records; and
  - (b) use of the address or other information from the seller's records does not constitute bad faith.
- (5) (a) Subject to Subsection (10), and except as provided in Subsections (7), (8), (9), (11), and (14), if Subsection (2), (3), or (4) does not apply, the location of the transaction is the location indicated by an address for the purchaser if:
  - (i) the address is obtained during the consummation of the transaction; and
  - (ii) use of the address described in Subsection (5)(a)(i) does not constitute bad faith.
- (b) An address used under Subsection (5)(a) includes the address of a purchaser's payment instrument if no other address is available.

....

- (12) (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).

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### III. Analysis

Your issues are as follows:

1. Is the Company's Storage Item subject to Utah sales and use taxes?
2. Is the Company's Computing Item with an Open Source Instance subject to Utah sales and use taxes?
3. Is the Company's Computing Item with a Third Party Instance subject to Utah sales and use taxes?

4. Is the usage fee charged in conjunction with the purchase of the Computing Item or the Storage Item subject to Utah sales and use taxes?

This private letter ruling concludes that these items are not subject to Utah sales and use taxes because the Company's computer hardware is located outside of Utah. Each of your issues is analyzed separately below.

**A. The Company's Sale of the Storage Item is Not Subject to Utah Sales and Use Taxes.**

The taxability of the sale of the Storage Item depends on whether the essence, or primary object, of the transaction is for a service, for the use of the Company's computer software, or for the use of the Company's computer hardware.

If the essence of the transaction is for a service not listed as taxable in § 59-12-103(1), the Company's sale of the Storage Item would not be subject to Utah sales and use taxes.

If the essence of the transaction is for use of the computer software, the Company's sale of the Storage Item would be subject to sales and use taxes under § 59-12-103(1)(a) if the transaction is within Utah.<sup>1</sup> The source of the use of the computer software would be the purchaser's location as determined by § 59-12-211(4), (5), and (12). Thus, if the purchaser is located in Utah and the essence of the transaction is the use of the computer software, the sale of the Storage Item would be subject to Utah sales and use taxes.

If the essence of the transaction is for the use of the computer hardware, the Company's sale of the Storage Item would be subject to sales and use taxes under § 59-12-103(1)(a), (k), or (l) if the transaction is within Utah. Under § 59-12-211(2)-(3), a transaction for the use of computer hardware is sourced to the place a purchaser receives or takes possession of the computer hardware. The purchaser of the Storage Item remotely uses and manipulates the computer hardware at the location where the computer hardware physically exists. Because all of your data centers and small clusters of servers are located outside of Utah, the sale would be sourced outside of Utah and would not be subject to Utah sales and use taxes under § 59-12-103(1)(a), (k), or (l) if the essence of the transaction of the sale of the Storage Item is the use of the computer hardware.

The Utah Supreme Court explained the essence of the transaction as follows:

[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 one for services or for tangible personal property. The analysis typically requires a determination either that the services provided are merely

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<sup>1</sup> Under § 59-12-102(110)(b)(v), "sale" includes "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). Under § 59-12-102(125)(b)(v), "tangible personal property" includes "prewritten computer software."

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) (internal citations removed).

To decide whether the essence of the transaction is one for a service provided by the Company, for the use of the Company's software, or for the use of the Company's hardware, one must consider the nature and extent of the services provided by the Company's personnel, the use of the software, and the use of the hardware.

Based on the facts you presented, a purchaser primarily seeks to acquire the use of the computer hardware. Your facts concerning the hardware are as follows. A purchaser of the Storage Item receives "**remote access to computer equipment** so [the purchaser] can store and retrieve large amounts of data at any time and from any location via the internet" (emphasis added). A purchaser will "generally utilize the remote storage services to backup and store data **in lieu of setting up their own on-premises electronic storage infrastructure**" (emphasis added). The Company "merely provides **access to the infrastructure** necessary for customers to store their own digital content" (emphasis added). A purchaser "must **select a specific data center** to provide the [Storage Item]" (emphasis added). Overall, a purchaser wants to use the Company's computer equipment instead of using his or her own.

Some software is involved in the Storage Item; however, use of this software is incidental to the use of the computer hardware. According to your facts, the software includes a management console and certain software development kits. You explained the management console "is a simple . . . web interface that allows users to create . . . storage 'buckets' and then upload or delete objects contained in those buckets. [The free tool] allow[s] customers to manage and make efficient use of the storage service." Based on these facts, the management console software only supports a purchaser's use of the Company's computer hardware. Thus, the software's use is incidental to the use of the computer hardware. The software development kit ("SDK") is text files of sample computer code. The SDK is not computer software as defined in § 59-12-102(27). The text files of sample computer code cannot cause "a computer to perform a task" as required by § 59-12-102(27). Furthermore, these samples of computer code are available free of charge to any user of the web. Based on these facts, the SDK is incidental to the use of the computer hardware. Thus, both the management console and the SDK are not the essence of the transaction.

You characterized the Storage Item as a service; however, the essence of the transaction is not one involving a non-taxable service for purposes of § 59-12-103(1). No facts suggest the services of the Company's personnel are the essence of the transaction. If the Company's personnel provide services that generally support the computer hardware, those services would be incidental to a purchaser's use of that computer hardware. Thus, the services of the Company's personnel are not the essence of the transaction.

In summary, the essence of the transaction of the Storage Item is the sale of the use of the computer hardware. This transaction is not taxable because it does not meet § 59-12-103(1)(a), (k), or (l), which require the transaction to be within Utah. Under § 59-12-211(2)-(3), the

transaction is sourced outside of Utah. Thus, the sale of the Storage Item is not subject to Utah sales and use taxes because the computer hardware is located outside of Utah.

**B. The Company's Sale of the Computing Item with an Open Source Instance is not Subject to Utah Sales and Use Taxes.**

The analysis for the Computing Item with an Open Source Instance is similar to the previous analysis for the Storage Item in that both items require analysis of the essence of the transaction. If the essence of the transaction is for the use of the Company's computer software, the Company's sale of the Computing Item with an Open Source Instance would be subject to Utah sales and use taxes if the purchaser is located in Utah. If the essence of the transaction is for use of the Company's computer hardware, the Company's sale of the Computing Item with an Open Source Instance would not be subject to Utah sales and use taxes because the Company's computer hardware is located outside of Utah.

To decide whether the essence of the transaction is the use of the Company's software or the use of the Company's hardware, one must consider the nature and extent of the use of the software and the use of the hardware.

Based on the facts you presented, a purchaser primarily seeks to acquire the use of the computer hardware. Your facts concerning the computer hardware are as follows. With the Computing Item, a purchaser "can procure computing resources." A purchaser can do with the Computing Item "essentially anything computer equipment, especially a computer server, can do" if the purchaser were to own the computer equipment directly. With the Computing Item, a purchaser has "remote access to computing capacity and control of their computing resources without significant information technology investment (e.g., customers no longer have to buy their own servers or set up their own on-premises data centers)." A purchaser can upload his or her own software to the Company's network. A purchaser "must select a specific data center to provide [the] computing services." Overall, a purchaser wants to use the Company's computer equipment to act as his or her computer server instead of the purchaser using his or her own equipment.

Some software is involved in the use of the Computing Item; however, the use of this software is incidental to the use of the Company's computer hardware. The software includes operating system software, application programming interfaces, and the SDK.

Your facts concerning the operating system software are as follows. The operating system is part of an Instance, which is a configuration of memory, CPU, storage, and operating system. A "basic operating system is required to direct the computing power; therefore, use of an operating system is provided with each Instance." You explained, "[T]he operating system software runs on servers within the [Company's] network to provide the [Computing Item]. . . . A customer's use of this operating system software is only in conjunction with the use of the [Computing Item]." The Company "makes either open source or third party operating system software available with each Instance so customers can make use of the virtual servers." Based on these facts, the operating system software only supports a purchaser's use of the Company's computer hardware. Thus, the operating system software's use is incidental to the use of the Company's computer hardware.

Your facts about the application programming interfaces include the following. The application programming interfaces are “free tools.” They are also “optional and are simply posted on web pages; customers may choose to make use of [the Computing Item] without utilizing these free tools.” A purchaser “can use application programming interfaces to allow their existing systems to communicate to the [Computing Item].” Based on these facts, the application programming interfaces only support a purchaser’s use of the Company’s computer hardware. Thus, the use of the application programming interfaces is incidental to the use of the Company’s computer hardware.

The analysis of the SDK for the Computing Item is the same as the analysis of the SDK for the Storage Item. The SDK is not computer software as defined in § 59-12-102(27), and the SDK is incidental to the sale of the use of the Company’s computer hardware.

You characterized the Computing Item as a service that could be described as Infrastructure as a Service. However, the Company’s personnel do not provide personalized services to the purchasers. Regardless of the description of Infrastructure as a Service, based on the facts presented, the essence of the transaction is not one for a service. The essence of the transaction is for the use of the Company’s computer hardware.

In summary, the essence of the transaction of the Computing Item with Open Source Instance is the sale of the use of the Company’s computer hardware. This transaction is not taxable because it does not meet § 59-12-103(1)(a), (k), or (l), which require the transaction to be within Utah. Under § 59-12-211(2)-(3), the transaction is sourced outside of Utah. Thus, the sale of the Computing Item with Open Source Instance is not subject to Utah sales and use taxes because the computer hardware is located outside of Utah.

### **C. The Company’s Sale of the Computing Item with a Third Party Instance is not Subject to Utah Sales and Use Taxes.**

The analysis for the Computing Item with a Third Party Instance is very similar to the analysis for the Computing Item with an Open Source Instance. The essence of the transaction analysis must be applied to determine whether the sale is primarily for the use of the Company’s computer software or for the use of the Company’s computer hardware.

Based on the facts, a purchaser primarily seeks the use of the Company’s computer hardware regardless of whether the purchaser buys the Computing Item with an Open Source Instance or the Computing Item with the Third Party Instance. The facts about both Computing Items are very similar; the only difference is the operating system software that is used.

Third party operating system software is used to the same extent to operate the Company’s computer hardware as open source operating system software. Either operating system software is necessary for the use of the Company’s computer hardware. A purchaser only uses either operating system software in conjunction with the use of the Company’s computer hardware for the Computing Item. Thus, the use of either operating system software is incidental to the use of

the computer hardware regardless of whether that operating system software is open source software or is third party software. The use of the operating system software is incidental regardless of whether the purchase price of a Computing Item with a Third Party Instance is more expensive than a Computing Item with an Open Source Instance.

In summary, the essence of the transaction of the Computing Item with a Third Party Instance is the use of the Company's computer hardware. Thus, the sale of the Computing Item with a Third Party Instance is not subject to Utah sales and use taxes; the transaction is sourced outside of Utah, where the Company's computer hardware is located.

**D. The Usage Charges Sold in Conjunction with the Computing Item or the Storage Item are not Subject to Utah Sales and Use Taxes.**

The usage charges sold in conjunction with the Computing Item or the Storage Item are not subject to Utah sales and use taxes because the Computing Item and the Storage Item are not subject to Utah sales and use taxes.

IV. Conclusion

The Company's sale to a Utah customer of the Storage Item and/or Computing Item is not subject to Utah sales and use taxes. The essence of the transaction for the Storage Item and the Computing Item is the use of the Company's computer hardware. Because that computer hardware is located outside of Utah, the sale of the use of that computer hardware is sourced outside of Utah and the transaction is not subject to Utah sales and use taxes. The taxability of the Computing Item does not vary based on whether an open source or a third party operating system is used. Usage charges incurred in conjunction with the purchase of the Storage Item or the Computing Item are not subject to Utah sales and use taxes because the Storage Item and the Computing Item are not subject to Utah sales and use taxes.

The Tax Commission's conclusions are based on the facts as you described them and the Utah law currently in effect. Should the facts be different or if the law were to change, a different conclusion may be warranted. If you feel we have misunderstood the facts as you have presented them, you have additional facts that may be relevant, or you have any other questions, please feel free to contact the Commission.

Additionally, you may also appeal the private letter ruling in the following two ways.

First, you may file a petition for declaratory order, which would serve to challenge the Commission's interpretation of statutory language or authority under a statute. This petition must be in written form, and submitted within thirty (30) days after the date of this private letter ruling. You may submit your petition by any of the means given below. **Failure to submit your petition within the 30-day time frame could forfeit your appeal rights and will be deemed a failure to exhaust your administrative remedies.** Declaratory orders are discussed in Utah Administrative Code R861-1A-34 C.2., available online

at <http://tax.utah.gov/commission/effective/r861-01a-034.pdf>, and in Utah Administrative Code R861-1A-31, available online at <http://tax.utah.gov/commission/effective/r861-01a-031.pdf>.

Second, you may file a petition for redetermination of agency action if your private letter ruling leads to an audit assessment, a denial of a claim, or some other agency action at a division level. This petition must be written and may use form TC-738, available online at <http://tax.utah.gov/forms/current/tc-738.pdf>. Your petition must be submitted by any of the means given below, within thirty (30) days, generally, of the date of the notice of agency action that describes the agency action you are challenging.

You may access general information about Tax Commission Appeals online at <http://tax.utah.gov/commission-office/appeals>. You may file an appeal through any of the means provided below:

- **Best way**—by email: [taxappeals@utah.gov](mailto:taxappeals@utah.gov)
- By mail: Tax Appeals  
USTC  
210 North 1950 West  
Salt Lake City, UT 84134
- By fax: 801-297-3919

For the Commission,

Rebecca L. Rockwell  
Commissioner

RLR/aln  
16-004