CONFERENCE COMMITTEE MEMO

To: House and Senate Transportation Committee Conferees

From: Christopher R. Anderson, President

Date: May 30, 2013

Re: **Negative effects from expanding the state sales tax to custom software/design services; High Tech Council recommendation on language to ensure legislative intent and limit overreach by the Department of Revenue**

As you work to finalize language within transportation financing legislation (H.3415, S.1766) currently before you, the Massachusetts High Tech Council respectfully asks you to carefully consider a matter of pressing interest to high tech companies here: the proposal to expand the state sales tax to include custom software and design services.

As Massachusetts high tech employers continue to study the impacts of this new tax, they have voiced a variety of concerns that the increased costs and other factors will make it harder for them to compete and win business. Employers are likely to make decisions about where to retain or add employees based on their further analysis of the impact of the new tax. The feedback we have received is broad-based and not just from one particular sector. **The Council is convinced of the negative impacts this new tax will impose on a wide range of businesses across our state's technology ecosystem**.

We are all well aware of our state's economic leadership in science and technology. The Milken Institute's State Technology and Science Index has ranked Massachusetts #1 in this area five times since 2002. At the same time, there are many signs that this edge is being blunted by areas in which we lag behind our competitor states. For example, a recent survey of the most innovative states by *Fast Company* magazine ranked Massachusetts at a disappointing 42nd place overall. A 2013 Tax Foundation survey found that we are 49th in terms of payroll tax competitiveness, which places a major brake on hiring. **Massachusetts should not enact changes that further erode the competitive advantages that we currently enjoy**.

Although the provision to tax custom software/design services offered by the Senate is more narrowly crafted than the House's version, both create a new cost-competitive disadvantage for Massachusetts where none existed before. **Of the 15 peer states that the High Tech Council has identified as Massachusetts' most direct competitors for high tech jobs, only one – Texas – taxes custom software/design services.**

From a Conference perspective, we therefore urge the House to adopt the Senate version and include language limiting the discretion of the Department of Revenue to expand application of the new tax to transactions beyond the Legislature's intent.

We recommend that sourcing language should be added for computer services such as "computer system design services, and the modification, integration, enhancement, installation, or configuration of standardized software, should be sourced for sales and use tax purposes in the same manner as the sale of prewritten computer software."

The High Tech Council respectfully asks you to consider adopting the language that mirrors the following existing provisions (830 Mass. Code Regs. 64H.1.3(15)), which describes the current sourcing methodology for prewritten computer software.

830CMR64H.1.3(15)

Multiple Points of Use Certificates.

830CMR64H.1.3(15)(a)

General Rule. A business purchaser that is not a holder of a direct pay permit that knows at the time of its purchase of prewritten computer software that the software will be concurrently available for use in more than one jurisdiction shall deliver to the seller in conjunction with its purchase an exemption certificate claiming multiple points of use, Form ST-12. Prewritten computer software, for purposes of this section includes, but is not limited to, computer software delivered or accessed electronically, regardless of the location of the server where the software is installed, software delivered by load and leave, or in tangible form. Computer software received in-person by a business purchaser at a retail business location of the seller is not included. Computer software for personal use is not included.

830CMR64H.1.3(15)(a)1.

Upon receipt of an exemption certificate claiming multiple points of use, the seller is relieved of all obligation to collect, pay, or remit the applicable tax and the purchaser shall be obligated to collect, pay, or remit the applicable tax on a direct pay basis. Except as provided in 830 CMR 64H.1.3(15)(a) 7, a certificate claiming multiple points of use must be received by the seller no later than the time the transaction is reported for sales or use tax purposes.

830CMR64H.1.3(15)(a)2.

A purchaser delivering an exemption certificate claiming multiple points of use may use any reasonable, but consistent and uniform, method of apportionment that is supported by the purchaser's books and records as they exist at the time the transaction is reported for sales or use tax purposes.

830CMR64H.1.3(15)(a)3.

A reasonable, but consistent and uniform, method of apportionment includes, but is not limited to, methods based on number of computer terminals or licensed users in each jurisdiction where the software will be used. A reasonable, but consistent and uniform method of apportionment may not be based on the location of the servers where the software is installed.

830CMR64H.1.3(15)(a)4.

A purchaser delivering an exemption certificate claiming multiple points of use shall report and pay the appropriate tax to each jurisdiction where concurrent use occurs. The tax due will be calculated as if the apportioned amount of the prewritten computer software had been delivered to each jurisdiction to which the sale is apportioned pursuant to 830 CMR 64H.1.3(15)(a)2.

830CMR64H.1.3(15)(a)5.

A Multiple Points of Use Certificate may not be used for software received in person by a business purchaser at a retail store.

830CMR64H.1.3(15)(a)6.

A Multiple Points of Use Certificate may not be used for software that is loaded on computer hardware prior to sale. In that situation, the sales tax sourcing rules for computer hardware determine the taxability of the transaction, regardless of whether the price for the prewritten software is separately stated.

830CMR64H.1.3(15)(a)7.

The exemption certificate claiming multiple points of use will remain in effect for all future sales eligible for apportionment under 830 CMR 64H.1.3(15) by the seller to the purchaser, except as to the subsequent sale's specific apportionment that is governed by 830 CMR 64H.1.3(15)(a)2, until it is revoked in writing.

830CMR64H.1.3(15)(a)8.

The purchase of software loaded onto a server located in a single state that will be available for access by a purchaser's employees in multiple jurisdictions is concurrently available for use in more than one jurisdiction within the meaning of 830 CMR 64H.1.3(15) if the purchaser knows at the time of its purchase that the software will be concurrently available for use in multiple jurisdictions.

830CMR64H.1.3(15)(a)9.

Delivery of a copy of the software is not necessary for the software to be "concurrently available for use in more than one jurisdiction" within the meaning of 830 CMR 64H.1.3(15).

830CMR64H.1.3(15)(a)10.

The purchase of a license that allows the licensee/customer to make copies of software that will be used in more than one jurisdiction by the customer is concurrently available for use in more than one jurisdiction within the meaning 830 CMR 64H.1.3(15) if the

purchaser knows at the time of its purchase that the software will be concurrently available for use in multiple jurisdictions.

830CMR64H.1.3(15)(a)11.

Examples:

Example 1: Prewritten software is installed on a server located in another state but concurrently available for use by purchaser's employees in Massachusetts as well as other states. The purchaser gives the seller a properly completed MPU form. Part of the sales price of the software will be apportioned to Massachusetts for sales/use tax purposes.

Example 2: Prewritten software is installed on a server located in Massachusetts but concurrently available for use by purchaser's employees in other states as well as Massachusetts. The purchaser gives the seller a properly completed MPU form. Part of the sales price will be apportioned to those other states for sales/use tax purposes.

Example 3: A business in Massachusetts purchases an enterprise license that allows the purchaser to make copies of software (either from a master disk or downloaded copy) and those copies will be concurrently available for use at the purchaser's business locations in various jurisdictions. The purchaser gives the seller a properly completed MPU form. For sales/use tax purposes, part of the sales price will be apportioned to the other states where the purchaser is using copies of the software.

Example 4: A sale of software eligible for MPU treatment includes a separately stated charge for a maintenance contract including upgrades and telephone support. The charges for upgrades and services provided under the maintenance contract are not separately stated. Both the sales price of the software and the taxable sales price of the service contract, determined under 830 CMR 64H.1.3(7)(c)1 are subject to MPU apportionment.

Example 5: Prewritten software concurrently available for use by the purchaser's employees in other states as well as Massachusetts is delivered in a tangible medium to the purchaser's offices in New Hampshire. New Hampshire does not impose a sales tax and the purchaser does not give the seller a properly completed MPU form. Apportioned use tax is due to Massachusetts.

Example 6: Prewritten software concurrently available for use by the purchaser's employees in other states as well as Massachusetts is delivered via a master copy in tangible medium to the purchaser's offices in Connecticut. The vendor collects and remits Connecticut sales tax. Providing that the conditions of 830 CMR 64H.1.3(3)(c) are met, no additional use tax may be due to Massachusetts.

830CMR64H.1.3(15)(b)

Seller Remittance of Apportioned Tax. Notwithstanding 830 CMR 64H.1.3(15)(a), when the seller knows that the prewritten software will be concurrently available for use in more than one jurisdiction, but the purchaser does not provide an exemption certificate claiming multiple points of use, the seller may work with the purchaser to produce the

correct apportionment. The purchaser and seller may use any reasonable, but consistent and uniform, method of apportionment that is supported by the seller's and purchaser's business records as they exist at the time the transaction is reported for sales or use tax purposes. If the purchaser certifies to the accuracy of the apportionment and the seller accepts the certification, the seller shall collect and remit the tax to the appropriate jurisdictions as provided in 830 CMR 64H1.3(15)(a)4. In the absence of bad faith, the seller is relieved of any further obligation to collect tax on any transaction where the seller has collected and remitted tax pursuant to the information certified by the purchaser, provided that the seller retains records of the methodology used to apportion the tax in addition to the purchaser's written certification.

830CMR64H.1.3(15)(c)

When the seller knows that the prewritten software will be concurrently available for use in more than one jurisdiction and the purchaser does not have a direct pay permit and does not provide the seller with an exemption certificate claiming multiple points of use exemption as required by 830 CMR 64H.1.3(15)(a) or the certification required by 830 CMR 64H.1.3(15)(b), the seller shall collect and remit the tax as provided by 830 CMR 64H.6.7, unless the purchaser is otherwise exempt.

830CMR64H.1.3(15)(d)

A holder of a direct pay permit shall not be required to deliver an exemption certificate claiming multiple points of use to the seller. A direct pay permit holder shall follow the provisions of 830 CMR 64H.1.3(15)(a)2 in apportioning the tax due on prewritten computer software that will be concurrently available for use in more than one jurisdiction.

830CMR64H.1.3(15)(e)

Nothing in 830 CMR 64H.1.3(15) shall limit a person's obligation for sales or use tax to any state in which the qualifying purchases are concurrently available for use, nor limit a person's ability under state, federal, or constitutional law, to claim a credit for sales or use taxes legally due and paid to other jurisdictions.