



Sales Tax Division *Tax Compliance Guide*

SOFTWARE

The Breckenridge Town Code imposes sales tax on the purchase price or charge for data processing equipment and data processing programs.

DATA PROCESSING EQUIPMENT

Data processing equipment is taxable as tangible personal property when the equipment is sold in Breckenridge or physically in Breckenridge. Data processing equipment is taxable as a service, whether or not the equipment is physically in Breckenridge, when a charge for the equipment is related to a charge for the use of a data processing program.

DATA PROCESSING PROGRAMS

A. Definitions

1. Data Processing Program: A data processing program is a set of statements or instructions in machine readable format that is capable of causing a machine or device having information processing capabilities to indicate, perform, or achieve a particular function, task, or result, and includes, but is not limited to, software.
2. “Custom” Data Processing Program: Includes data processing programs designed, created and/or modified to meet the needs of a specific user or set of users.
3. “Pre-Written” Data Processing Program: Includes, but is not limited to, “canned”, “shrink-wrapped”, “off-the-shelf” or any other data processing program developed for sale or license to multiple users. Pre-written data processing programs include data processing program modules or components that are designed to be integrated into a larger data processing package.

B. Taxable Sales: The DRMC imposes sales tax on the sale, storage, use, distribution, or consumption of data processing programs, no matter how defined including “custom” and “pre-written” data processing programs, regardless of the method of delivery and whether purchased in tangible or intangible form. The data processing program is taxed as a service since the true essence of the transaction is the purchase or use of the intangible data processing program, not the purchase or use of the medium.

C. Taxable Portion: The taxable portion of a data processing program is the aggregate of all amounts associated with the creation of the data processing program, including, but not limited to, the following:

1. Conceptualizing and designing the program;
2. Planning program requirements;
3. Project management;

4. Writing the code of the program;
5. Testing and evaluating the program;
6. Implementing the program;
7. Creating or writing manuals, instructions, and any other documentation; and
8. Any customer support or maintenance agreement that is required by the purchase contract or that includes the

D. Separately Stated Non-taxable Charges: Non-taxable charges, when separately stated, that relate to a data processing program would include the following:

1. Separately stated labor for training charges; and
2. Follow-up customer support that is not required by the purchase contract for the software, and which does not include the right to program updates or modifications.

E. Taxable Data Processing Programs vs. Non-Taxable Services

A distinction exists between the sale of data processing programs, including “custom” data processing programs, which are taxable, and the sale of other certain personal services, which are not taxable. Data processing programs are taxable services which are generally the culmination of a programmer’s logic and knowledge. The personal services to design, write, test, implement, and otherwise create data processing programs are subject to sales tax.

1. Examples of “custom” data processing programs which are subject to sales tax include, but are not limited to, the following:

- a. A new module or new stand alone instruction set is created;
- b. An instruction set or module is created that adds functionality or new features to an existing data processing program or module;
- c. A new data processing program is created. This would not only include the creation of a completely new data processing program, but also combining prewritten procedures from a “library” to create a new data processing program;
- d. Modifications are made to existing “pre-written” or custom data processing programs to upgrade to the desired specifications of the customer;
- e. Modifications are made related to an initial data processing program purchase to meet the purchase requirements of the customer; and/or
- f. Programmer owns the work in progress, including “works made for hire.”

2. Examples of other personal services, which are not subject to sales tax when separately stated, include the following:

- a. A correction to an instruction set that the customer already owns, which does not add functionality or new features to the data processing program. An example of a personal service correction is changing the date field in a program from a two-digit year to a four-digit year;

b. Changing the configuration or “settings” of a data processing program when not in conjunction with the purchase of the data processing program, which do not allow rights to use new functions or features of the data processing program, and when the source code is not modified. An example of a personal service change of configuration is changing the default file location setting, or the security settings assigned to a particular user; and

c. Data retrieval by a programmer, where a programmer writes the code to “query” the customer’s database and produce an output for the customer, but the customer has no right to re-run or re-use the query language, nor does the customer obtain ownership rights to the query language.

F. Taxable Right or License to Use: Breckenridge’s sales tax is also imposed on the right to use or license to use a data processing program or data processing equipment in the Town of Breckenridge. The use of a data processing program or equipment in Breckenridge is defined as any action that controls, directs, runs, or operates the data processing program or equipment as directed by a person, computer, or business in Breckenridge. This is generally limited to real-time or interactive control of the data processing program or equipment. In other words, when the user in Breckenridge enters a command, directive, or data, the data processing program or equipment operates on that command, directive, or data once received from the user. The data processing program or equipment itself does not have to be located in Breckenridge to be used in Breckenridge. Indications that the data processing program or equipment is used in Breckenridge would include having the inputs to the data processing program or equipment coming directly from Breckenridge, or the outputs of the data processing program or equipment coming directly into Breckenridge. The taxable purchase price will include the charge for the software usage, hardware usage, time usage, and any other charges that are related to the usage or operation of the data processing program or equipment. *See also* , Maintenance Agreements, Section H of this Guide, below.

G. Batch Processing:

1. A data processing program or data processing equipment is not considered to be used by a customer in Breckenridge, and as such is not subject to sales or use tax, if all of the following conditions occur: the customer transmits its records electronically in a “batch” format to a computer processor; the customer’s records are stored by the computer processor until the computer processor processes them at a later time in a separate action; the customer has no control over the “run time” or processing of its records, other than a general expectation of when its records will be processed; the computer processor uses a data processing program that they (and not their customers) own, have a right to use, or a license to use; and the output produced is based solely upon the data in the customer’s records and is in the nature of reports, hard-copy outputs, or third-party directives.

2. When a computer processor located in Breckenridge uses a data processing program to provide non-taxable batch processing services (see Section G.1. of this Guide), sales tax would not be due on the processing charges charged to the customer. Nevertheless, if the data processing program is used by the computer processor in Breckenridge, the computer processor would owe sales tax on the purchase, right to use, or license of the data processing program.

H. Maintenance Agreements: Data processing programs are sometimes sold, or are licensed for use, with an additional periodic fee, generally called a maintenance fee. If the periodic fee is mandatory to maintain the right to use the data processing program, then the periodic fee is subject to sales tax. If the periodic fee is not mandatory to maintain the right to use the data processing program, then the substance of what the fee entitles the customer to receive must be considered. If the periodic fee includes updates to the data processing program, or the rights to updates and modifications if they occur, then that fee is part of the charge for a data processing program and is subject to tax. If the periodic fee is only for technical support, and does not entitle the customer to updates and modifications, then it is not subject to tax.

I. Taxable Downloads or Taxable Access: The method of delivery of, or access to, a data processing program does not affect the taxability of the program for purposes of Breckenridge's sales tax. Taxable delivery methods or taxable access to data processing programs include, but are not limited to, a vendor, owner, or other distributor: (a) selling or licensing a disk, CD or other software medium to a customer; (b) electronically downloading the software to a customer's system using a telecommunications or similar medium including the Internet, or where the customer so downloads; (c) utilizing "load and leave" or "load and return" distribution methods wherein the vendor owner, or other distributor visits the customer's site, installs the software, and then takes its physical medium; (d) providing access to software through a third party, such as an Application Service Provider ("ASP"), who offers users access to software, which is located on the third party's system, over the Internet; including, but not limited to, when the customer does not download the data processing program, but instead uses or accesses it over the Internet; (e) a vendor, owner, or other distributor creating or programming software directly on the customer's computer system either on or off site; and (f) the right to "unlock" software or the sale of a digital code that unlocks or allows a data programming program to operate; and such methods and access shall be taxable regardless of whether billed as "subscription fee", "license fee", "service", or otherwise.

EXAMPLES

A. Deluxe Accommodations, which operates a hotel in Breckenridge, is a franchisee of a national hotel chain. As part of its franchise agreement, Deluxe pays for the right to use the franchisor's electronic reservation system. Deluxe's electronic reservation system automatically uploads and downloads information pertaining to room availability, reservations, price information, and reports to and from the franchisor's reservation system. The full amount paid by Deluxe for the right to access the franchisor's reservation system is taxed by Breckenridge.

B. GMO Oil Exploration Company, which has their administrative and engineering offices in Breckenridge, develops oil wells throughout the world. In order to determine where to profitably drill their wells, GMO uses the proprietary software program "DrillFinder" from HT Software in Houston, TX. DrillFinder is loaded on HT Software's server located in Houston, and, for a flat fee per month, varying telecommunication charges, and a "hardware usage charge" for actual time used on HT Software's servers, GMO has the right to use the software. To use the software, GMO's engineers open up a web browser, access the website of HT Software, and, after entering a user ID and password, are able to enter in their seismic and other data and obtain the results of the analysis. The full amount charged by HT software or paid by GMO is taxed by Breckenridge.

C. GMO also contracts with PRU Payroll to provide payroll services to their employees worldwide. GMO collates all the time and pay information for each pay cycle, assembles the information in a batch file, and transmits the batch file to PRU, which is located in Phoenix, AZ. PRU Payroll contractually guarantees that if the batch file is received by 5:00 pm the Tuesday after the pay cycle, that they will process the file and have all reports, direct deposits, checks and withholding payments completed and issued by 7:00 am the Friday following the pay cycle. GMO has no direct access to the software programs used by PRU nor do they have any “real time” right or expectation to have their data processed. The charge by PRU to GMO for this service is not taxed by Breckenridge.

D. After years of paying exorbitant fees to HT Software for the rights to use the DrillFinder data processing program, GMO decides to develop their own version of the software. GMO contracts with Software Solutions of Atlanta, GA to design, program, and implement a data processing program that will perform the same tasks as DrillFinder. Software Solutions has never done a project this specialized before, but they hire programmers, petroleum engineers, and subcontractors to conceptualize the project, develop the specifications and logic, write and test the data processing program, and implement the data processing program for GMO. Most of the software is custom developed by Software Solutions, but to save money, they also included some source code modules that were configured to perform common utilities. The data processing program was developed both at Software Solution’s Atlanta site and GMO’s Breckenridge site. The majority of the work was covered under the development contract which called for fixed payments based on a milestone schedule. However, some of the specialized petroleum engineer consulting costs and some of the change order programming costs were billed at an hourly rate for the services involved. All the above amounts paid by GMO are for the ultimate creation of a data processing program and is taxed by Breckenridge.

RELATED TOPICS

Information Services

Maintenance Agreements

Breckenridge Town Code 3-1

THE ABOVE INFORMATION IS A SUMMARY IN LAYMEN'S TERMS OF RELEVANT BRECKENRIDGE TAX LAW FOR THIS TOPIC, INDUSTRY, OR BUSINESS SEGMENT. IT IS NOT INTENDED FOR LEGAL PURPOSES TO BE SUBSTITUTED FOR THE FULL TEXT OF THE BRECKENRIDGE TOWN CODE AND APPLICABLE RULES AND REGULATIONS. THIS GUIDE DOES NOT CONSTITUTE A TOWN TAX POLICY.

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