

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 11-38**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

The application of the Tennessee sales and use tax to document management services.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[TAXPAYER] is a [BUSINESS ENTITY TYPE] that provides a wide range of traditional and technology-driven services to [TYPE OF BUSINESSES].

The Taxpayer provides a service (the “Data Service”) by which it obtains a collection of electronic data from the client. [REDACTED]. The Taxpayer sends a [REDACTED] team to the client’s location to collect all relevant electronic information contained on the client’s computer hard drives, servers, telephone systems, and so on. Once the Taxpayer has retrieved the relevant information, the Taxpayer loads the data into a software program housed on the Taxpayer’s servers. The software program eliminates duplicate data and applies data filters and key word searches to “cull” any irrelevant information. The Taxpayer then loads the resulting data and information into a database on its servers. The client may review the database and tag the particular items that the client wishes to have produced as .pdf or .tiff files.

The Taxpayer then loads the processed files into a secondary database, which the Taxpayer hosts on a monthly basis (the “Hosting Service”). The client is able to access the database throughout the term of the Hosting Service. No physical media are delivered to the client in conjunction with the Data Service or the Hosting Service.

After the term of the Hosting Service ends, the Taxpayer will remove the database from its servers unless the client requests otherwise. In the event the client requests that the Taxpayer not delete the database, the Taxpayer will maintain the data files on its servers (the “Storage Service”). The Taxpayer does not transfer a copy of the documents to the client as part of the Storage Service.

Upon completion of the particular [REDACTED] project, the client may choose to have the Taxpayer deliver certain files to it via a physical medium (*i.e.*, an external hard drive, printed paper, etc.) Alternatively, the client may choose to have the Taxpayer deliver a copy of the final selected documents to it electronically (for example, as an ftp download). In some cases, the client does not wish to receive copies of documents at all. The Taxpayer bills the client separately for any transfer of files via tangible medium.

The Taxpayer may also charge the client a separate project management fee, which is billed on an hourly basis for consulting help and assistance in setting up and searching the information database (the “Project Management Service”).

The Taxpayer invoices and charges separately for each of the services described above.

QUESTIONS

1. Is the Taxpayer’s Data Service subject to the Tennessee sales and use tax?
2. Is the Taxpayer’s Hosting Service subject to the Tennessee sales and use tax?
3. Is the Taxpayer’s Storage Service subject to the Tennessee sales and use tax?
4. Is the fee for the Taxpayer’s Project Management Service subject to the Tennessee sales and use tax?
5. Is Taxpayer’s transfer of copies of documents via electronic means at the completion of the Hosting Service subject to the Tennessee sales and use tax?

6. Is the Taxpayer's transfer of copies of data and/or documents via a tangible medium at the completion of the Hosting Service subject to the Tennessee sales and use tax?

RULINGS

1. No. The Taxpayer's Data Service is not subject to the Tennessee sales and use tax.
2. No. The Taxpayer's Hosting Service is not subject to the Tennessee sales and use tax.
3. No. The Taxpayer's Storage Service is not subject to the Tennessee sales and use tax.
4. No. The fee for the Taxpayer's Project Management Service is not subject to the Tennessee sales and use tax.
5. No. The Taxpayer's transfer of copies of documents via electronic means at the completion of the Hosting Service is not subject to the Tennessee sales and use tax.
6. Yes. The Taxpayer's transfer of copies of data and/or documents via a tangible medium at the completion of the Hosting Service is subject to the Tennessee sales and use tax.

ANALYSIS

Under the Retailers' Sales Tax Act, TENN. CODE ANN. § 67-6-101 *et seq.*, the retail sale in Tennessee of tangible personal property is subject to the sales and use tax. TENN. CODE ANN. § 67-6-102(79) (Supp. 2010) provides that the term "retail sale" means "any sale, lease, or rental for any purpose other than for resale, sublease, or subrent." TENN. CODE ANN. § 67-6-102(81)(A) defines the term "sale" in pertinent part to mean "any transfer of title or possession, or both, exchange, barter, lease or rental, conditional or otherwise, in any manner or by any means whatsoever of tangible personal property for a consideration."¹

Additionally, TENN. CODE ANN. § 67-6-102(81)(D) defines the term "sale" to include "the furnishing of any of the things or services taxable" under the Retailers' Sales Tax Act. The sales tax does not apply to all services; rather, it only applies to retail sales of those services specifically enumerated by the statute. *Ryder Truck Rental, Inc. v. Huddleston*, 1994 WL 420911 (Tenn. Ct. App. Aug. 12, 1994). Even if a service is not specifically enumerated by the statute, however, the service may be subject to the sales tax where charges for the service are included in the sales price of a taxable good or service. Specifically, TENN. CODE ANN. § 67-6-102(82)(A) provides that the sales price of a good or service equals the "total amount of consideration . . . for which personal property or services are sold," with no deduction for the seller's costs or charges by the seller for services necessary to complete the sale. Thus, when the sale of a non-enumerated service is part of the sale of a taxable good or service, the charges for the non-enumerated service are included in the sales price of the taxable good or service and as such are subject to taxation.

¹ TENN. CODE ANN. § 67-6-102(92)(A) defines "tangible personal property" to include prewritten computer software.

Accordingly, the transactions described herein will be subject to the Tennessee sales and use tax if the particular transaction constitutes 1) the sale of tangible personal property in Tennessee; 2) the furnishing of a taxable service; and/or 3) the furnishing of an otherwise nontaxable service that is sold as part of the sale of a taxable good or service.

1-3. Data Service, Hosting Service, and Storage Service

Charges for the Taxpayer's Data Service, Hosting Service, and Storage Service are not subject to the Tennessee sales and use tax.

As noted above, the Taxpayer's Data Service, Hosting Service, and Storage Service will be subject to the Tennessee sales and use tax if the particular transaction constitutes 1) the sale of tangible personal property in Tennessee; 2) the furnishing of a taxable service; and/or 3) the furnishing of an otherwise nontaxable service that is sold as part of the sale of a taxable good or service.

First, no sale or transfer of tangible personal property, including prewritten software, occurs in conjunction with the Taxpayer's furnishing of the Data Service, Hosting Service, or Storage Service. Additionally, the Taxpayer does not sell, lease, license, or otherwise provide the use of computer software to its client in conjunction with these services.²

Second, the Taxpayer's Data Service, Hosting Service, and Storage Service do not constitute taxable services for Tennessee sales and use tax purposes. As noted above, only specifically enumerated services are subject to the Tennessee sales and use tax. The Taxpayer's Data Service, Hosting Service, and Storage Service are most properly characterized as document management services that involve the capture, sorting, hosting, and storage of data related to [REDACTED]; such services are not among the services enumerated under the Retailers' Sales Tax Act.³

Third, because the Taxpayer does not make sales of tangible personal property in conjunction with the Data Service, Hosting Service, or Storage Service, and does not provide a taxable service, no part of the transaction can be described as the furnishing of an otherwise nontaxable service that is sold as part of the sale of a taxable good or service.

² While software may be used by the Taxpayer to sort data for the client, the Taxpayer's client does not itself use the software.

³ Note that the facts indicate that the Taxpayer is not providing a telecommunications service, which is subject to taxation under TENN. CODE ANN. § 67-6-205(c)(3). The term "telecommunications service" is defined under TENN. CODE ANN. § 67-6-102(93)(A) in pertinent part as the "electronic transmission, conveyance, or routing of voice, data, audio, video, or any other information or signals to a point, or between or among points." Apart from the fact that the Taxpayer does not sell a service by which it routes data from one point to another, TENN. CODE ANN. § 67-6-102(93)(B)(i) specifically excludes from the definition of "telecommunications service" data processing and information services "that allow data to be generated, acquired, stored, processed, or retrieved and delivered by electronic transmission to a purchaser, where such purchaser's primary purpose for the underlying transaction is the processed data or information." Here, the client's primary purpose is to obtain the underlying processed data and information.

Accordingly, charges for the Taxpayer's Data Service, Hosting Service, and Storage Service are not subject to the Tennessee sales and use tax.⁴

4. *Project Management Service*

The fee for the Taxpayer's Project Management Service is not subject to the Tennessee sales and use tax.

As noted above, the Project Management Service will be subject to the Tennessee sales and use tax if the particular transaction constitutes 1) the sale of tangible personal property in Tennessee; 2) the furnishing of a taxable service; and/or 3) the furnishing of an otherwise nontaxable service that is sold as part of the sale of a taxable good or service.

First, no sale or transfer of tangible personal property, including prewritten software, occurs in conjunction with the Taxpayer's furnishing of the Project Management Service. Additionally, the Taxpayer does not sell, lease, license, or otherwise provide the use of computer software to its client in conjunction with this service.

Second, the Taxpayer's Project Management Service is not properly considered a taxable service for Tennessee sales and use tax purposes. As noted above, only specifically enumerated services are subject to the Tennessee sales and use tax. The Taxpayer's Project Management Service involves the furnishing of consulting help and assistance in setting up and searching an information database; consulting services are not among the services enumerated under the Retailers' Sales Tax Act.

Third, because the Taxpayer does not make sales of tangible personal property and does not provide a taxable service, no part of the transaction can be described as the furnishing of an otherwise nontaxable service that is sold as part of the sale of a taxable good or service.

Accordingly, the fee for the Taxpayer's Project Management Service is not subject to the Tennessee sales and use tax.

5. *Transfer of documents by electronic means*

The Taxpayer's transfer of copies of documents via electronic means at the completion of the Hosting Service is not subject to the Tennessee sales and use tax.

As noted above, the Tennessee sales and use tax is imposed on the retail sale of tangible personal property in Tennessee. TENN. CODE ANN. § 67-6-102(81)(A) (Supp. 2010) defines the term "sale" in part as "any *transfer* of title or possession, or both, exchange, barter, lease or rental, conditional or otherwise, in any manner or by any means whatsoever *of tangible personal*

⁴ Note that the Retailer's Sales Tax Act does not require that the Taxpayer maintain specific documentation with respect to its sales of nontaxable services. However, there is a general requirement that each dealer keep records of its sales and purchases. TENN. CODE ANN. § 67-6-523 (2006) generally requires all taxpayers to establish and maintain records that are adequate for auditors to use in determining the correct amount of the taxpayer's tax liability. The Taxpayer should therefore keep records of its sales and purchases, including copies of invoices and purchase orders. Records of business transactions must be retained for a minimum of three years from December 31 of the year in which the associated Tennessee sales and use tax return was filed.

property for a consideration.” (Emphasis added.) In the case of the electronic transmission of documents or data,⁵ no transfer of tangible personal property occurs between the Taxpayer and its client. Additionally, no transfer of tangible personal property takes place when the client subsequently prints out or otherwise creates tangible copies of the transferred documents for its own use.

Accordingly, no taxable sale takes place for purposes of the Tennessee sales and use tax when the Taxpayer transfers documents or data via electronic means.

6. *Transfer of documents via physical medium*

The Taxpayer’s transfer of copies of data and/or documents via a tangible medium at the completion of the Hosting Service is subject to the Tennessee sales and use tax.

Under the Retailers’ Sales Tax Act, TENN. CODE ANN. § 67-6-101 *et seq.*, retail sales of tangible personal property in Tennessee are subject to sales and use tax. TENN. CODE ANN. § 67-6-102(79) (Supp. 2010) defines a “retail sale” as a “sale, lease, or rental for any purpose other than for resale, sublease, or subrent.” The term “sale” is defined under the Tennessee sales and use tax laws in pertinent part as “any *transfer* of title or possession, or both ... of *tangible personal property* for a consideration.” TENN. CODE ANN. § 67-6-102(81)(A) (emphasis added).

At the end of the Hosting Service, the client may choose to have the Taxpayer deliver selected files to it via a tangible medium (*i.e.*, an external hard drive, printed paper, and so on) for a fee. Such activity constitutes the transfer of title or possession of tangible personal property for a consideration. Accordingly, Taxpayer’s transfer of copies of data and/or documents via a tangible medium at the completion of the Hosting Service is subject to the Tennessee sales and use tax.

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APPROVED: Richard H. Roberts
Commissioner of Revenue

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⁵ Note that the transfer of certain items via electronic means is subject to the sales and use tax. For example, the “retail sale, lease, licensing or use of specified digital products transferred to or accessed by subscribers or consumers” in Tennessee is subject to the sales and use tax. TENN. CODE ANN. § 67-6-233(a) (Supp. 2010). “Specified digital products” is defined as “electronically transferred digital audio-visual works, digital audio works and digital books.” TENN. CODE ANN. § 67-6-102(89). Additionally, TENN. CODE ANN. § 67-6-231(a) (Supp. 2010) provides that the retail sale, lease, licensing or use of computer software in Tennessee is subject to the sales and use tax, regardless of whether the software is delivered electronically or via a tangible storage medium.

