

TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 23-05

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This ruling is based on the particular facts and circumstances presented and is an interpretation of the law at a specific point in time. The law may have changed since this ruling was issued, possibly rendering it obsolete. The presentation of this ruling in a redacted form is provided solely for informational purposes and is not intended as a statement of Departmental policy. Taxpayers should consult with a tax professional before relying on any aspect of this ruling.

SUBJECT

The application of the Tennessee sales and use tax to staff augmentation and payment processing services accessed through a digital platform.

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

[REDACTED] (the "Taxpayer") is a technology company headquartered in [STATE]. Its business is to match companies that have short term labor needs (the "Customers") with workers, i.e., it provides staff augmentation services. The Taxpayer also processes payments from the Customers to the

workers. To facilitate these connections and payments, the Taxpayer provides a proprietary digital platform (the "Platform") to match Customers with workers.

The Customers and workers access the Platform through a downloadable app. The Taxpayer solicits Customers who use the Platform by posting a job request containing a general job description seeking one or more workers, proposing the compensation related to that job request, and inviting qualified workers to accept such request. The job requests are short-term by nature and can cover a single day or multiple days. Customers may create templates for posting future job requests on the Platform, and Customers can use the Platform to create lists of favored workers to contact in the future. Customers negotiate a fee for this service, which is typically a percentage of the amounts paid to workers.

Customers provide the Taxpayer with criteria and preferences for the Customers' job requests. To the extent permitted by law, the Taxpayer ensures that any worker who accepts a job request from a Customer may only perform the contracted services if the worker has undergone and successfully completed a post-offer background check. The Taxpayer tailors the background check process to meet Customer preferences and criteria.

The workers use the Platform to sort through job requests, accept a job, and report their time worked for the Customers. If a worker agrees to the job request, a contractual agreement is formed between the Customer and the worker. If a job request requires a background check, the Taxpayer will initiate that background check with the assistance of a third-party provider. Through the platform, Customers review and approve completion of the applicable job and the time reported. The Taxpayer uses this information to prepare invoices for its Customers. Workers and Customers also have the ability to use a messaging feature on the app to communicate with one another about job details and logistics.

In exchange for the Taxpayer's role in facilitating job placement and payments between Customers and workers, the Customers pay the Taxpayer the following amounts: a) an amount equal to the hourly rate bid by the Customers multiplied by the number of hours worked by any workers in connection with services rendered by such workers to the Customers, b) compensation to the Taxpayer of a negotiated additional percentage of the amount paid by the Customers to the workers, c) any cancellation fees, if applicable, and d) any hiring fees, if the Customers ever hire any workers as their own employees. The Taxpayer sends the workers payments via direct deposit to the workers' accounts on record.

On its invoices to Customers, the Taxpayer provides a lump-sum amount for all services a) through d) that is due for the cycle period. The Customers also receive a detailed breakdown backup sheet that itemizes the fees and the hours logged by each individual worker.

The Taxpayer books revenue on a "net basis," meaning it only books its fees into gross receipts. The Taxpayer does not book revenue in connection with the funds that flow to the workers, both for accounting purposes and for income tax purposes. The Taxpayer has the responsibility to issue federal Form 1099 each year to any worker that exceeds the reporting requirement threshold.

RULINGS

1. Are the Taxpayer's fees subject to Tennessee Sales and Use tax?

Ruling: No. Providing staff augmentation and payment processing services through a digital platform is not subject to Tennessee sales and use tax.

ANALYSIS

The fees charged by the Taxpayer to the Customers are not subject to Tennessee sales and use tax because staff augmentation and payment processing are not taxable services. Services are not subject to Tennessee sales and use tax unless specifically enumerated as taxable.¹ The provision of temporary workers is generally not an enumerated taxable service.² Additionally, payment processing is not an enumerated taxable service, and payment processing services have been specifically identified in TENN. CODE ANN. § 67-6-231(b) (2022) as services that are not subject to Tennessee sales and use tax.

Customers use the Taxpayer's Platform to connect with workers to fill the Customers' short-term labor needs, and workers use the Platform to earn money performing short-term jobs. The Taxpayer's Platform is analogous to a labor hall, hiring hall, or employment agency in that it brings together workers seeking jobs and those that need workers for short-term projects. Labor halls are central gathering areas where workers present themselves, showing that they are present, ready, and willing to work for the day.³ Merriam-Webster defines employment agency as "an agency whose business is to find jobs for people seeking them or to find people to fill jobs that are open."⁴ Similar to an employment agency, the Customers pay the Taxpayer a percentage of the amount paid to the workers, plus any hiring fees if the workers are hired as employees by the Customers.

Notably, labor halls, hiring halls, and employment agencies are generally not subject to the Tennessee sales and use tax for the services that they provide connecting workers with job offers.⁵ Those types

¹ TENN. CODE ANN. § 67-6-205 (2022); see *Ryder Truck Rental, Inc. v. Huddleston*, No. 91-3382-III, 1994 WL 420911, at *3 (Tenn. Ct. App. Aug. 12, 1994) (stating that the sales tax does not apply to all services; it applies only to those services specifically enumerated by the statute).

² Repairing tangible personal property or computer software is subject to Tennessee sales and use tax pursuant to TENN. CODE ANN. § 67-6-205(c)(4); laundering or dry cleaning any kind of tangible personal property is subject to Tennessee sales and use tax pursuant to TENN. CODE ANN. § 67-6-205(c)(6); installing tangible personal property that remains tangible personal property after installation and the installation of computer software is subject to Tennessee sales and use tax pursuant to TENN. CODE ANN. § 67-6-205(c)(6); see also Tenn. Dept. Rev. Ltr. Rul. 14-11 (2014) (stating that the provision of temporary workers is not a taxable service, but repairing tangible personal property is a taxable service; a court would have to determine the true object of a transaction involving the provision of temporary workers to repair tangible personal property).

³ See Miriam A. Cherry *Working for (Virtually) Minimum Wage: Applying the Fair Labor Standards Act in Cyberspace*, Alabama Law Review, 60 ALLR 1077, 1083 (2009) (citing Jennifer Gordon, *Suburban Sweatshops: The Fight for Immigrant Rights*, Belknap Press: An Imprint of Harvard University Press (2005). Hiring halls can be either formal facilities designated by communities, governments, and religious organizations or informal sites such as unregulated locations where workers gather outside of businesses, parking lots of home-improvement stores, popular street corners, or gas stations. Analiz Deleon-Vargas *The Plight of Immigrant Day Laborers: Why They Deserve Protection Under the Law*, St. Mary's Law Review on Minority Issues, 10 SCHOLAR 241, 244-45 (2008).

⁴ "Employment agency," *Merriam-Webster.com Dictionary*, Merriam-Webster, <https://www.merriam-webster.com/dictionary/employment%20agency> (last updated Aug. 16, 2022).

⁵ When independent contractors are hired to fabricate software, Tennessee sales tax on fees for their services may apply. The fabrication of computer software is a sale subject to Tennessee sales and use tax. See TENN. CODE ANN. § 67-6-102(86)(A). Tangible personal property includes prewritten computer software. TENN. CODE ANN. § 67-6-102(97)(A). Prewritten computer software that is modified or enhanced to any degree, where the modification or enhancement is designed and developed to the specifications of a specific purchaser, remains prewritten computer software. See *Creasy Sys. Consultants, Inc. v. Olsen*, 716 S.W.

of services are generally not included as an enumerated taxable service under TENN. CODE ANN. § 67-6-205 (2022). Thus, the Taxpayer's Platform is not subject to Tennessee sales and use tax for providing essentially the same service through a downloadable app.

The Taxpayer also provides payment processing services when the Customer pays the Taxpayer for the number of hours that the workers complete, and the Taxpayer then transfers that payment to the workers' accounts. As stated above, payment processing services are specifically identified as not being subject to Tennessee sales and use tax, therefore the Taxpayer's payment processing services do not subject the Taxpayer to Tennessee sales and use tax.

Notwithstanding the above, the Taxpayer's Platform is accessed through an app, which is arguably subject to Tennessee sales and use tax as the use of computer software.⁶ The app also provides Customers with some functions that can be considered the use of computer software, including the generation of templates for future job requests and a means of creating lists of favored workers to contact in the future. Thus, the Taxpayer's fees comprise taxable and non-taxable items.

Under the true object test that is used to determine the taxability of a transaction that involves taxable and non-taxable items, when the non-taxable components are the true object, and the taxable components are merely incidental, the transaction is not subject to sales and use tax.⁷ Customers use the app to find workers and to send them payments for their work. In order to have a broad selection of work opportunities, the Taxpayer promotes its service to Customers. These job opportunities, in turn, attract workers. The software itself would have little value to any one Customer or worker if there were not numerous businesses and workers participating and interacting on the platform. The Taxpayer's activities include soliciting Customers as well as promoting and hosting the platform. These activities are what makes the platform a desirable product: a place where businesses can find workers and workers can find jobs. Connecting businesses and workers for purposes of arranging short-term employment is the true object of the transaction.

In light of the following, use of the app to gain access to the Platform is merely incidental to the non-taxable services: (1) there is no charge for the Customer to download the app, (2) the app is primarily being used to gain access to the non-taxable services, and (3) the app, along with the limited functionality of providing templates and creating lists of favored workers, would be worthless without the non-taxable services. Because the true object of the transaction is the provision of non-taxable services, and the software components are merely incidental to those services, the Taxpayer's Platform is not subject to Tennessee sales and use tax.

2d 35,36 (Tenn. 1986)(stating that the fabrication of, or customized modification or enhancement to, computer software is considered a taxable sale of computer software.). Repairing tangible personal property or computer software is subject to Tennessee sales and use tax pursuant to TENN. CODE ANN. § 67-6-205(c)(4); laundering or dry cleaning any kind of tangible personal property is subject to Tennessee sales and use tax pursuant to TENN. CODE ANN. § 67-6-205(c)(6); installing tangible personal property that remains tangible personal property after installation and the installation of computer software is subject to Tennessee sales and use tax pursuant to TENN. CODE ANN. § 67-6-205(c)(6).

⁶ Computer software is a set of coded instructions designed to cause a computer to perform a task, and it is subject to Tennessee sales and use tax even when the software is accessed remotely. TENN. CODE ANN. §§ 67-6-102(18) (2022) and -231(b) (2022).

⁷ See *generally* Tenn. Dept. of Rev. Ltr. Rul. 14-10 (Oct. 14, 2014) for an application and full analysis of the true object test.

It should be noted that although the Taxpayer provides the means for Customers and workers to communicate through the app regarding job details and logistics, the Taxpayer is not furnishing telecommunication services that would be subject to sales and use tax.⁸ The Customers are not provided with the means to contact other persons other than the workers who they have contracted with, and the communication is limited to details of the job and logistics. As such, the communication feature is also merely incidental to the non-taxable true objects of the transaction, which are staff augmentation and payment processing services.⁹

APPROVED: David Gerregano
Commissioner of Revenue

DATE: June 30, 2023

⁸ See TENN. CODE ANN. §§ 67-6-205(c)(3) and 67-6-102(98)(A) (2022).

⁹ See, e.g., *Equifax Check Services, Inc. v. Johnson*, No. M1999-00782-COA-R3-CV, 2000 WL 827963 (Tenn. Ct. App. June 27, 2000) (employing the true object/primary purpose test to determine if the transfer of information during a check guarantee service was a telecommunications service within the meaning of the Retailer's Sales Tax Act).