

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
VOICEMATE.COM, INC. : SMALL CLAIMS
 : DETERMINATION
 : DTA NO. 819864
for Revision of a Determination or for Refund of Sales and :
Use Taxes under Articles 28 and 29 of the Tax Law for the :
Period September 1, 1998 through August 31, 2001. :

Petitioner, Voicemate.com, Inc., One Penn Plaza, Suite 2212, New York, New York 10119, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1998 through August 31, 2001.

A small claims hearing was held before James Hoefer, Presiding Officer, at the offices of the Division of Tax Appeals, 90 South Ridge Street, Rye Brook, New York, on December 16, 2004 at 10:45 A.M. Petitioner appeared by Michael J. Buxbaum, CPA. The Division of Taxation appeared by Christopher C. O'Brien, Esq. (Michael J. Miller).

The final brief in this matter was due by March 4, 2005 and it is this date that commences the three-month period for the issuance of this determination.

ISSUES

I. Whether computer system hardware purchased by petitioner was used directly and predominantly in the design and development of computer software for sale and was thus exempt from sales and use tax pursuant to Tax Law § 1115(a)(35).

II. If it is determined that petitioner is producing computer software for sale, whether all of the computer equipment at issue herein represents computer system hardware eligible for the exemption set forth in Tax Law § 1115(a)(35).

FINDINGS OF FACT

1. On November 18, 2001, petitioner, Voicemate.com, Inc., filed with the Division of Taxation (“Division”) Form AU-11, Application for Credit or Refund of Sales and Use Tax. The application encompassed the period September 1, 1998 to August 31, 2001, requested a refund in the sum of \$16,576.72 and contained the following explanation:

Voicemate.com is a computer software company that is applying for a refund for the overpayment of Sales and Use tax for computer hardware (servers and computers) that is used predominantly (more than 50% of the time) in designing and developing custom computer software for sale (Section 1115[a][35] and TSB-M-98[5][S]).

Voicemate.com is a computer software company that sells custom computer software to specific industries. The purchase of the servers and computers are [sic] used to develop this software for customers so that they can manage information with voice (including wireless) or keystroke commands.

2. Pursuant to a letter dated April 19, 2002, the Division effectively¹ denied petitioner’s application for refund on the basis that, although the computer hardware at issue herein was used directly and predominantly in the design and development of computer software, petitioner did not sell the computer software it designed, and therefore the computer hardware did not qualify for the exemption set forth in Tax Law § 1115(a)(35). Petitioner disagreed with the Division’s determination that it did not sell the computer software it designed and this small claims proceeding ultimately ensued.

¹ By Order dated April 28, 2003, Administrative Law Judge Timothy J. Alston concluded that petitioner’s application for credit or refund was in processible form; that the Division’s letter dated April 19, 2002 was a denial of the application; and that the Division of Tax Appeals had proper jurisdiction in this matter.

3. Voicemate.com, Inc., located at One Penn Plaza, Suite 2212, New York, New York, was established in 1999 as a start-up computer software company. From October 6, 1999 to February 6, 2001, petitioner made numerous purchases of computer equipment totaling \$200,928.73. Sales tax of \$16,576.72 was paid by petitioner on these purchases and in this proceeding petitioner seeks a refund of the sales tax it paid on this equipment.

4. In a sales/informational brochure, petitioner provides the following company overview:

Voicemate provides the end-to-end services that help businesses instantly publish, manage and deliver branded, personalized knowledge to their customers over a mobile phone, PC, or hand-held device in the most trusted medium - the human voice. With a robust platform and state-of-the-art services for creating and hosting voice sites rapidly, Voicemate helps businesses enhance their brands and strengthen relationships with customers in an increasingly mobile world.

Only Voicemate offers all the applications and services needed to deliver content to the widest possible audience, without requiring enterprises to purchase, configure or maintain any additional hardware, software or hosting bandwidth.

5. As of the date petitioner filed its application for refund it had only one customer. The contract which petitioner entered into with this customer is identified as a "Service Agreement" which provides for a "Hoot-Holler Network.Enhancement." The service agreement, in relevant part, contains the following provisions:

Existing Service Description

[The customer] currently utilizes a hoot-holler system for allowing its financial professionals (e.g., traders) to participate into an open voice forum from multiple locations across the globe. The system is built on a proprietary network and has a multi-level hub-and-spoke architecture. At the center, there is a conference bridge ("hub"). Emanating from this hub are connections ("spokes") over a proprietary network to various locations around the globe (one connection per location). At each location, the audio feed is further distributed to multiple professionals, who can listen to the feed and / or speak using special devices on their desks. . . .

Voicemate Service Description

Voicemate's service allows corporations to publish, manage and deliver knowledge across all devices (wireless/wireline phones, WAP phones, desktop PC's, laptops, handhelds, MP3 players) using the most natural medium, the human voice. Voicemate's service can integrate content from multiple sources, both internal and external to a corporation, and can deliver both live and pre-recorded voice content. Voicemate's service can use the hoot-holler network as a knowledge feed and distribute this feed to all devices mentioned above, not just the special devices on the traders' desks. Thus, [the customer's] professionals will be able to access the hoot-and-holler knowledge from anywhere, not just their desks. Furthermore, when users dial into Voicemate's service from their phones, they will be able to select the channel of their choice and switch between channels using Voicemate's speech-enabled, hands-free interface.

Service Implementation

To implement the service, Voicemate will need an audio feed from the bridge for each of the channels. This can be achieved by running a dedicated line (e.g., fractional T1) between [the customer's] facility. . . and one of the collocation hosting facilities where Voicemate's infrastructure is deployed. . . . Voicemate's platform has the ability to take these live feeds and redistribute them over the web (to users accessing the web site of the service) as well as over the public phone network (to users dialing into the Voicemate platform). . . .

Fee Structure

The fee structure is based on two parameters: 1) Voice site set-up and 2) Voice site maintenance, hosting and delivery fees. . . .

Service Content

Voicemate shall not be held responsible for any delays that result from the failure of [the customer] to deliver content in time. [The customer] is responsible for providing in audio form the content to be delivered on the channels.

Service Exceptions

The fees do not cover the cost of delivering the audio feeds from [the customer] to Voicemate's facilities; [the customer] will be responsible for providing the necessary connections. The fees do not cover the cost of connecting to the Voicemate service. . . .

Intellectual Property

No license is granted herein, either by implication, estoppel or otherwise to any Voicemate product or service or any copyright, patent, trademark or other legally protectible right incorporated in such product or service.

6. The service agreement was for a period of six months and the capacity which petitioner made available to the customer consisted of a total of 40 ports, 14 of which were identified as “simultaneous content publishing ports dedicated” and the remaining 26 were listed as “simultaneous content delivery ports dedicated.” The service agreement further provided that the one-time setup fee was waived. This fee would normally include the “creation and customization of the voice site for delivery over both the telephone network (through gateways) and the web, the definition of channels, the creation of the default profiles and the configuration of the administrative interface.” Petitioner charged the customer \$30,000.00 per month for “voice site maintenance & delivery fees (account maintenance, content maintenance, content archival, support. . . .)”

7. Petitioner employs the Application Service Provider (“ASP”) business model and in this model the software which it develops is placed on a server. Petitioner’s customer’s access to the ASP interface occurs through a variety of media that are connected to the Internet.

8. The numerous pieces of computer equipment purchased by petitioner and at issue in this proceeding are disclosed on 27 separate purchase invoices. Of the 27 purchase invoices, 25 reveal that, in addition to computer system hardware, petitioner also purchased such items as extended warranties, operating system software and/or application software. The 25 invoices which show the purchase of extended warranties, operating system software and/or application software all contain a lump sum purchase price with no breakdown or allocation of the purchase price between computer system hardware and the extended warranties, operating system software and/or application software.

SUMMARY OF THE PARTIES' POSITIONS

9. Petitioner maintains that the custom computer software which it develops is leased to its customer through the ASP business model, and since it is undisputed that a lease constitutes a sale, the computer system hardware it purchased to develop the custom software clearly falls within the exemption set forth in Tax Law § 1115(a)(35).

10. The Division asserts that the computer system hardware at issue does not qualify for the exemption contained in Tax Law § 1115(a)(35) since the software which petitioner develops is not sold or leased. The Division argues that petitioner's contract with its only customer at the time the refund application was made clearly shows that petitioner was providing a service and that the contract also contains a specific clause which indicates that no license was granted to the customer for any of Voicemate's product. The Division postulates in its brief that:

Voicemate's use of its proprietary software to provide a service of whatever nature does not constitute a sale, lease or license to use such software. The essence of the transaction(s) is the provision of the service(s) described in Voicemate's contract(s) with its customer(s), Voicemate's Internet advertising and its advertising brochures (rather than a sale, lease or license to use Voicemate's proprietary software), whether or not access to such services is provided through Voicemate's proprietary software.

11. Petitioner counters the Division's position by asserting that its customers "are purchasing software that provides a service. This 'service' is used by the taxpayer to indicate a 'benefit' or 'utility' being provided by the custom computer software." Petitioner further argues that the advertising brochures relied upon by the Division are merely marketing tools to:

advertise an economic incentive for companies to purchase expensive software at a manageable price. The service level approach spreads the cost of the expensive software over time. This revenue model measures the sale of the software to a function of the customer's use. The lower initial cost of investment allows businesses to afford the purchase of this innovative and expensive software.

12. Petitioner also maintains that the “Intellectual Property” paragraph of the contract should be accorded little or no weight since it was “written by Intellectual Property lawyers and is not relevant to the definition of ‘Sale’ or ‘Use’ as described in Tax Law 1101.”

13. Alternatively, the Division asserts that if it is determined that the software developed by petitioner is “for sale,” no refund can be granted with respect to the 25 purchase invoices which show the purchase of extended warranties and/or prewritten software. The Division points out that the exemption provided for in Tax Law § 1115(a)(35) applies only to computer hardware and not extended warranties and computer software. Relying on its memorandum TSB-M-98(5)S, dated June 8, 1998, the Division argues that when a computer software program developer purchases hardware, extended warranties and software for one price, the seller must reasonably allocate the purchase price among the items purchased. TSB-M-98(5)S provides that the entire sales price is subject to tax if the seller does not reasonably allocate the sales price between the taxable and nontaxable components of the sale. Since there is no allocation of the sales price on the 25 purchase invoices which contain both taxable and nontaxable components, the Division maintains that no refund can be granted with respect to the sales tax paid on said 25 purchase invoices.

14. Petitioner argues that no allocation of the sales price is required since all 27 purchase invoices reflect only the purchase of computer hardware. Any prewritten software is, in petitioner’s view, de minimis.

CONCLUSIONS OF LAW

A. Effective June 1, 1998, section 97 of chapter 56 of the Laws of 1998 added paragraph 35 to Tax Law § 1115(a). This amendment provided that “computer system hardware used or

consumed directly and predominately in designing and developing computer software for sale” was exempt from the sales and use taxes imposed by Articles 28 and 29 the Tax Law.

B. In the instant matter, the parties do not dispute that the computer system hardware purchased by petitioner, and at issue herein, was used directly and predominately to design or develop computer software. The primary issue to address in this controversy is whether the software produced by petitioner’s computer system hardware was “for sale.”

C. Sale, selling or purchase is broadly defined in Tax Law § 1105(b)(5) as:

Any transfer of title or possession or both, exchange or barter, rental, lease or license to use or consume (including, with respect to computer software, merely the right to reproduce), conditional or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement therefor, including the rendering of any service, taxable under this article, for a consideration or any agreement therefor.

D. On this record, I conclude that the weight of the evidence does not support a conclusion that petitioner sold or leased the computer software which it designed and developed. Examination of the sole executed contract in the record reveals, in my view, that petitioner is using the software which it develops in the performance of a service and that the software is not being sold or leased to the customer. It must be noted that the software is loaded onto a server that is owned and controlled solely by petitioner and thus there is clearly no transfer of title or possession of the software. Furthermore, the contract specifically provides that no license is granted to Voicemate’s customer for any of its product or service. While petitioner attempts to downplay the significance of this provision, I believe this clause has serious implications. There is no ambiguity in the “Intellectual Property” clause of the contract in which petitioner unequivocally states that no license is granted “either by implication, estoppel or otherwise to any Voicemate product or service. . . .” Since there is no license to use the software, it cannot be found that petitioner’s customer was leasing said software. Without a transfer of title or

possession, lease or a license to use or consume there can be no sale of the software within the definition of “sale” as contained in Tax Law § 1105(b)(5).

This conclusion is consistent with the contract insofar as it suggests that the software is being used or consumed by petitioner and not its customers. The customer’s data, content or knowledge, apparently in audio form, is already contained on the customer’s proprietary hoot-holler system and this data, content or knowledge is then fed by a dedicated line to Voicemate’s infrastructure. It is here that Voicemate, using its server and its software, takes the live or prerecorded feeds and redistributes them for access via the web site of the service and over the public phone network for users dialing into Voicemate’s platform. The software at issue herein cannot be accessed by the customer and it is not loaded onto the customer’s server or computer. Voicemate designed the software to allow it to perform the service of redistributing its customer’s data, content or knowledge for easier access via the Internet or by phone. The form and substance of this transaction is one of a service and not the sale, lease or license to use software. It is noted that none of the principals of petitioner appeared at the hearing to offer their testimony and the one-page affidavit of petitioner’s CEO submitted post-hearing contained insufficient detail to change the impressions which are drawn from the contract.

E. The second issue raised in this controversy is rendered moot by the conclusion that the software which petitioner designs and develops is not for sale within the meaning and intent of Tax Law § 1105(b)(5). Accordingly, no conclusions are made in this determination with respect to this second issue.

F. The petition of Voicemate.com, Inc. is denied and the Division's refund denial dated April 19, 2002 is sustained.

DATED: Troy, New York
June 2, 2005

/s/ James Hoefler
PRESIDING OFFICER