

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition

of

ECONOMIC INFORMATION SYSTEMS, INC.

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 June 1, 1978  
through February 28, 1982.

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DECISION

In the Matter of the Petition

of

CONTROL DATA CORPORATION

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 June 1, 1978  
through February 28, 1982.

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Petitioner, Economic Information Systems, Inc., 310 Madison Avenue, New York, New York 10017, 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 June 1, 1978 through February 28, 1982 (File No. 39438).

Petitioner, Control Data Corporation, 8100 34th Avenue South, Box 0, Minneapolis, Minnesota 55440, 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 June 1, 1978 through February 28, 1982 (File No. 43195).

A consolidated hearing was held before Jean Corigliano, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on January 16, 1986 at 10:30 A.M., with all briefs to be submitted by July 9, 1986. Petitioners appeared by Arnold B. Panzer, Esq. The Audit

Division appeared by John P. Dugan, Esq. (Joseph W. Pinto, Jr., Esq., of counsel).

ISSUE

Whether a database and software, sold in connection with the bulk sale of a business which provided information services, were each subject to the sales tax imposed upon the sale of tangible personal property.

FINDINGS OF FACT

1. On January 8, 1982, Control Data Corporation ("CDC") purchased all of the assets of Economic Information Systems, Inc. ("EIS") in a bulk sale transaction. The total purchase price was approximately \$9,200,000.00. On or about January 5, 1982, CDC filed with the Audit Division a Notification of Sale, Transfer or Assignment in Bulk containing a schedule of assets being purchased as follows:

<u>Description</u>	<u>Amount</u>
Cash and accounts receivable	\$ 236,000.00
Software and database	8,600,000.00
Leasehold interests	194,000.00
Furniture, fixtures and equipment	160,000.00
Other intangibles	10,000.00
	<u>\$9,200,000.00</u>

2. On March 29, 1982, as the result of a field audit, the Audit Division issued against EIS a Notice of Determination and Demand for Payment of Sales and Use Taxes Due in the amount of \$644,065.48 plus minimum statutory interest for the period December 1, 1981 through February 28, 1982. An identical notice was sent to CDC on the same date, representing its liability as purchaser in the bulk sale transaction. At hearing, the Audit Division conceded that petitioners had satisfied a portion of the assessment, leaving a disputed tax

liability of \$623,500.00 plus interest.<sup>1</sup> The remaining portion of the assessment was based upon the Audit Division's determination that the receipts from EIS's sale of software and a database to CDC were subject to the sales tax imposed by Tax Law §1105(a) upon the sale of tangible personal property.

3. Prior to the sale of its assets to CDC, EIS operated an information service which provided marketing reports, directories and other reference materials on many aspects of the nation's economy. It was founded by two economists who specialized in methods of estimating the national and local markets for various types of goods consumed by certain industries in the process of production. In 1968, EIS began constructing a database which paralleled U.S. Census Bureau records on business activity known as the Standard Industrial Classification ("SIC"). EIS gathered all available information on United States business establishments and firms, including information found in the classified sections of local telephone directories, state and local industrial directories, annual corporate reports and financial statements, government reports, and statements filed with the Securities Exchange Commission. The U.S. Census Bureau is precluded by law from disclosing the identity of any particular company, but by matching and reconciling its data with statistics published by the Census Bureau, EIS was able to determine the identity and location of the top 500,000 business establishments in the United States and to maintain detailed records on each. Once established, the database was updated regularly using a variety of sources which included published materials and

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1 Notices, in the amount of \$282,056.38 plus interest for the periods June 1, 1978 through November 30, 1981, were also issued against petitioners. This assessment was later reduced to \$30,919.33 plus interest. The Audit Division conceded that this assessment had been fully satisfied; consequently, the determination was not in issue.

information obtained directly from individual businesses by EIS. In addition, EIS obtained certain facts unavailable elsewhere by matching data within its own database.

4. The software which was the subject of the sales transaction under consideration consisted of more than 400 computer programs written by EIS's own staff or private contractors to manage the EIS database. This software fell into two general categories: programs used to generate reports from the database and programs used to maintain and update the database. Of these two, the updating programs were the more valuable. The first phase of the updating process consisted primarily of gathering data from the various sources described in Finding of Fact "3", converting it into machine-readable format and editing it to meet certain specifications as to form and content. In the second phase, a series of matching operations was performed during which records were matched to themselves and to other records in the database. This served several functions. Simple clerical tasks, such as the elimination of duplicative data, were performed in this way. In addition, the matching process allowed EIS to link together facts which did not appear together in any other format and by doing so to actually produce new information not available elsewhere. This new information in turn became a part of the EIS database. Finally, a series of calculations were performed which enabled EIS to obtain a fairly accurate estimate of the volume of sales and purchases of virtually all products and services bought and sold by United States business establishments.

5. Using its software and database, EIS produced many types of individualized reports which it marketed to private companies and government agencies. Some of those reports are described below:

Shipments and Share of Market Reports analyzed any industry requested by the buyer in terms of key producers and ownership structure;

Line of Business Reports analyzed individual companies in terms of sales, market share and diversity of operations;

Market Potential Reports identified establishments and firms that use any industrial product or service, with estimates of the amount each one uses;

Market Penetration Analyses utilized a buyer's customer list to build a profile of the buyer's share of market in each industry in which the buyer operated.

6. EIS also published directories and reference books such as those described below:

The Top 1500 Companies identified the top 1,500 companies by name, address, telephone, sales volume, number of employees, and 2-digit SIC;

Congressional District Business Patterns identified every operating industry in each congressional district in terms of number of establishments, number of employees and payrolls;

Zip Code Business Patterns identified the top 10,000 zip code areas in terms of number of establishments, number of employees and payrolls.

7. EIS customers could also purchase the entire database or a portion of it in machine-readable format. These customers were usually large companies or government agencies capable of producing their own software to analyze the data, manipulate it and format it according to their own needs and specifications. **EIS** provided a record layout which defined the fields on the database and identified the content, location and size of each field. The entire database with quarterly updates for a period of one year was sold for approximately

\$50,000.00. Without the updates, the database would be practicably unusable within several months. In some instances, **EIS** also provided the database customers with programs which would enable them to generate their own reports. These customers did not receive documentation which would allow them to determine how the programs were handling the data itself. Prior to the bulk sale at issue, EIS had never sold its updating programs in any transaction.

8. CDC acquired the assets of EIS in order to expand its own business of providing information services. It continued to operate in much the same way as EIS had been operating, expanding and updating the database, refining the software and selling the same reports. As a condition of sale, **EIS** was required to provide CDC with documentation to back up all programs that made up the EIS software and database and to insure that the documentation met certain standards established by CDC. The EIS computer programming staff worked for several months to fulfill this requirement. In addition to acquiring actual copies of the software and database, CDC purchased proprietary rights to both.

9. As stated in Finding of Fact "1", CDC reported its purchase of the assets of **EIS** to the Audit Division and valued the database and software together at \$8,600,000.00. Petitioners' contract of sale included a financial statement which valued the database alone at \$1,656,856.00 in the year 1980. Testimony by a CDC employee placed the value of the database at \$1,100,000.00. However, it was evident that the true value of the software and database was dependent upon their ability to interact with one another and could not be derived from valuing those assets separately. The software was virtually worthless without the database since it was specifically designed to manage that particular database, and without the software needed to update it, the database would lose all value within a short time.

10. The software and database were embodied upon three to four reels of magnetic tape, each about ten inches in diameter. Because the software needed no modification prior to its sale to and use by CDC, the Audit Division considered it to be pre-written or canned software subject to the tax imposed on tangible personal property. The Audit Division also considered the database to be tangible personal property.

11. Petitioners submitted twenty-five proposed Findings of Fact, all of which have been substantially incorporated into this decision, with the exception of proposed Findings 7, 11, 12, 13, 14 and 15 which were unnecessary for the determination and proposed Findings 1, 22, 23 and 25 which stated facts not supported by the record.

#### CONCLUSIONS OF LAW

A. That tangible personal property transferred in a bulk sale of business assets constitutes a purchase at retail as defined in Tax Law §1101(b)(1) and is subject to the tax imposed under Tax Law §1105(a).

B. That the software sold by EIS to CDC cannot be considered tangible personal property within the meaning and intent of Tax Law §1101(b)(6). Software which is created specifically for one user or which requires modification to be used in a specific environment is deemed to be intangible personal property for sales tax purposes. The EIS software was a unique collection of over 400 computer programs specifically created for **EIS** by EIS employees and private contractors. Its only functions were the updating and managing of the **EIS** database and the generating of reports from that database. Separate from the EIS database, the software had virtually no utility at all. This software cannot be considered to be the equivalent of pre-written or canned programs which may be put to use in multiple situations without modification, and which

may be considered tangible personal property subject to sales tax. In this regard, it is notable that CDC acquired not only the programs themselves, but also extensive documentation enabling CDC to modify, expand or replicate the software as needed. The purchaser of canned programs normally does not acquire such documentation. Moreover, the EIS software cannot be deemed to be canned software simply because it did not require modification prior to its sale and use by CDC. No modification was necessary only because the software was purchased in connection with EIS's database and computers and was used by CDC in exactly the same manner as EIS had used it. That is, the environment in which the software was used remained precisely the same, only its owner changed. The change of ownership was not sufficient by itself to change the character of the software.

C. That Tax Law §1105(c)(1) imposes a tax on the receipts from every sale, except for resale, of the service of "furnishing of information by printed, mimeographed or multigraphed matter or by duplicating written or printed matter in any other manner, including the services of collecting, compiling or analyzing information of any kind or nature and furnishing reports thereof to other persons".

D. That 20 NYCRR 527.3(c)(3) provides as follows:

"The purchase of a service subject to tax under section 1105(c)(1) of the Tax Law by a vendor who will resell that service as such or as a part of a service also subject to tax under section 1105(c)(1) is not a purchase at retail and is exempt from the sales tax."

E. That the sale of the EIS database to CDC is analogous to an example given in the regulation which provides as follows:

"A vendor of an investment advisory service purchases a commodity information service and a stock market information service. Both services purchased by the vendor are incorporated into the service he sells. The vendor may purchase the services he uses for resale without payment of sales tax" (20 NYCRR 527.3[c][3]).




F. That the database was a body of information stored on magnetic tape. Clearly, the information itself was not corporeal (see Tax Law §1101[b][6]) and was not taxable as tangible personal property. However, where information is conveyed by any means other than orally, it can be said that there is an integration of the information and the tangible medium which conveys it, and that the end product is taxable under Tax Law §1105(a). Such an interpretation is consistent with the operation of the Tax Law in some instances. For example, dictionaries, encyclopedias and almanacs are subject to the tax imposed upon tangible personal property. But where customers are paying not for the book or the brochure but for the service of having very particular information furnished to them, the Tax Law imposes a tax upon the receipts from the sale of that service. It must be emphasized that it is the service which is taxed, not the information itself nor the medium which conveys the information. Petitioners and the Audit Division agree that **EIS's** receipts from the sale of reports were receipts from the sale of the service of furnishing information and were subject to tax under Tax Law §1105(c)(1). That was the case whether the medium for conveying information was a booklet or a magnetic tape containing all or a portion of the information. Likewise, the transfer of the database from **EIS** to CDC is deemed a purchase of an information service for resale as such and is exempt from the sales tax.

H. That the petitions of Economic Information Systems, Inc. and Control Data Corporation are granted and the Notices of Determination and Demands for Payment of Sales and Use Taxes Due issued on March 29, 1982 are cancelled.

DATED: Albany, New York

STATE TAX COMMISSION

MAY 26 1987

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER