North Carolina Department of Revenue

Pat McCrory
Governor

Lyons Gray
Secretary

July 29, 2014

FEIN: [redacted]
Account #: [redacted]

[redacted]

Re: Private Letter Ruling

Dear Ms. [redacted]

We have completed our review of your letter dated July 16, 2012, in which you requested a private letter ruling regarding the application of North Carolina State and local sales and use tax to business transactions of [redacted] ("[redacted]"). Please accept our apology for the delay in providing a response.

It is our understanding that [redacted] licenses several electronic health information products: [redacted] and [redacted] requests guidance on the taxability of the [redacted] ("[redacted]") product. [redacted] did not request a private letter ruling on the taxability of [redacted] and [redacted] products for North Carolina State, local and transit sales & use taxes and the Department does not express an opinion on them. The private letter ruling request states, '[redacted] has determined that the first three products in the list (i.e. [redacted] and [redacted] are non-taxable information services."

N.C. Gen Stat. § 105-164.3(14a) defines "information service" as "[a] service that generates, acquires, stores, processes, or retrieves data and information and delivers it electronically to or allows electronic access by a consumer whose primary purpose of using the service is to obtain the processed data or information"

The [redacted] product at issue for purposes of the ruling response is described as follows:

"The [redacted] product includes an intelligent engine that retrieves specific audio, graphic, text, and animation information (contained within the product) based on input and responses from the user and delivers it electronically or displays it, allowing for electronic access to such information by the user."

'[redacted] are web-based multimedia interactive tools that help people learn about a specific health topic and develop a plan of action to deal with a health issue relating to that topic. [redacted]. Each [redacted] is a 10-15 minute interactive multimedia online conversation that speaks directly to a user with text, a human voice, images, illustrations, animations, and a series of questions that require input from the user. In response to the user's input, the [redacted] provide information specifically for that individual, using text, voice, animation, and multimedia effects. As a result, the [redacted] provide each user only with the information the user wants or needs, based on the user's input, thereby making the experience one that is unique and custom tailored."

"[redacted] licenses these products to [redacted]."

"The [redacted] product is licensed to clients for an annual fee [redacted]). At no time do clients take ownership of or title to the [redacted] product. Upon termination of the license, clients are required to cease usage and delete all copies of the product residing on their servers, if applicable."

"[redacted] licenses and makes the [redacted] product available to clients using one of the following two delivery methods:

1. [redacted]**hosted**. The [redacted] product resides on [redacted]owned computers located in [redacted] The client provides access to the user through its website, portal or a patient's electronic health record, which links to the [redacted] product residing on the [redacted] computers in [redacted] The client does not take possession of the product on their own computers.
2. **Client-hosted**. [redacted] places the [redacted] product on an FTP site on the internet and the client downloads the entire product from the FTP site to its own computers. The client provides access to the user through its website portal or a patient's electronic personal health record, which links to the [redacted] product residing on the client's computers."

Question 1:
Is the [redacted] product exempt for North Carolina State and local sales and use tax purposes as an information service?

Response 1:
The sale (license) of [redacted] product to its clients would not be classified as information services for North Carolina State and local sales and use tax purposes.

When the [redacted] product is hosted by [redacted] ("[redacted]hosted"), the [redacted] product resides on [redacted]owned computers located in [redacted] The North Carolina client does not receive any tangible personal property, as defined in N.C. Gen. Stat § 105-164.3(46), which includes prewritten computer software; therefore the tax levied on tangible personal property by N.C. Gen. Stat. § 105-164.4(a)(1) does not apply to the [redacted]hosted [redacted] product. Currently, the State does not impose a tax on remote access to prewritten computer software.

The [redacted] product sold to a customer where the product is downloaded to a client's computer from an FTP internet site ("client-Hosted"), meets the definition of tangible personal property, as defined in N.C. Gen. Stat § 105-164.3(46), which includes prewritten computer software. The sale of [redacted] where the product is downloaded and such sale is sourced to North Carolina in accordance with N.C. Gen. Stat. § 105-164.4B is subject to the tax levied on tangible personal property at the 4.75% general State and applicable local and transit rates of sales and use tax.

N.C. Gen. Stat. § 105-164.13(43a)a affords an exemption for computer software purchased to run on an enterprise server operating system. The exemption includes a purchase or license of application software for high-volume, simultaneous use on multiple computers. A customer purchasing the "client-hosted" [redacted] product to run on an enterprise server operating system who claims an exemption per N.C. Gen. Stat. § 105-164.13(43a)a must provide a certificate of exemption in accordance with N.C. Gen. Stat. § 105-164.28.

Question 2:
If the [redacted] product is not exempt for North Carolina State and local sales and use tax purposes, what is the taxability of [redacted] product sold (or licensed) together with non-taxable products for one nonitemized price?

Response 2:
The sale (license) of the "[redacted]hosted" or the "client-hosted" [redacted] product together with one or more other non-taxable product(s) for one nonitemized price may constitute the sale of a bundled transaction.

> N.C. Gen. Stat. § 105-164.3(1j) defines "bundled transaction" as:
> "[a] retail sale of two or more distinct and identifiable products, at least one of which is taxable and one of which is exempt, for one nonitemized price. Products are not sold for one nonitemized price if an invoice or another sales document made available to the purchaser separately identifies the price of each product. A bundled transaction does not include the retail sale of any of the following:
>
> a. A product and any packaging item that accompanies the product and is exempt under G.S. 105-164.13(23).
> b. A sale of two or more products whose combined price varies, or is negotiable, depending on the products the purchaser selects.
> c. A sale of a product accompanied by a transfer of another product with no additional consideration.
> d. A product and the delivery or installation of the product.
> e. A product and any service necessary to complete the sale."

N.C. Gen. Stat. § 105-164.4D details the application of North Carolina State and local tax to bundled transactions. If the "client-hosted" [redacted] product is sold (licensed) as a bundled transaction that includes a service, and [redacted] determines an allocated price for each product in the bundle, based on a reasonable allocation of revenue that is supported by [redacted] business records kept in the ordinary course of business, tax applies to the allocated price of the taxable [redacted] product and each additional taxable item included in the bundled transaction. If the price of all taxable items included in the bundled transaction does not exceed 10% of the price of the bundle, North Carolina State, and local and transit sales and use tax do not apply.

A retailer of a bundled transaction subject to the provisions of N.C. Gen. Stat. § 105-164.4D may use either the retailer's cost price or the retailer's sales price to determine if the transaction meets . . . the ten percent (10%) test set out in subdivision. . . (a)(3) of N.C. Gen. Stat. § 105-164.4D. A retailer may not use a combination of cost price and sales price to make this determination. If a bundled transaction subject to subdivision (a)(3) of N.C. Gen. Stat. § 105-164.4D includes a service contract, the retailer must use the full term of the contract in determining whether the transaction meets the threshold set in N.C. Gen. Stat. § 105-164.4D(a)(3).

This ruling is based solely on the facts submitted to the Department of Revenue for consideration of the transactions described. If the facts and circumstances given are not accurate, or if they change, then the taxpayer requesting this ruling may not rely on it. If a taxpayer relies on this letter ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material aspect from the facts and circumstances given in this letter ruling, the letter ruling will not afford the taxpayer any protection. It should be noted that this letter ruling is not to be cited as precedent and that a change in statute, a regulation, or case law could void this ruling.

If we may be of additional assistance, you may contact the Sales and Use Tax Division at the phone number listed on page one.

Very truly yours,

[redacted]
Administration Officer
Sales and Use Tax Division

[redacted]

cc: [redacted], Director of Sales and Use Tax Division