

TO: Alabama Tax Tribunal

FROM: Legal Division

DATE: January 8, 2016

AGILE CONSULTING GROUP, INC.
5255 Triangle Parkway, Suite 150
Norcross, GA 30092

Taxpayer,

v.

Docket No. S. 15-1683

STATE OF ALABAMA
DEPARTMENT OF REVENUE.

ANSWER

Facts:

This case concerns the Department's denial of a sales tax refund requested by Agile Consulting Group, Inc. ("Taxpayer") for February 2012 through August 2014.

Issue:

Whether the Department correctly denied Taxpayer's requested sales tax refund for February 2012 through August 2014.

Department's position:

The Taxpayer petitioned for refund amount of \$17, 907.39. The Department has determined that Taxpayer is not due a refund because the software contained canned software that was customized and the non-taxable customized portion was not separated from the taxable canned portion on the invoice, the full sales price is to be included in the gross proceeds of sales. Sales and Use Tax Rule 810-6-1-.37 explains this process.

Therefore, the Department correctly denied Taxpayer's requested refund.

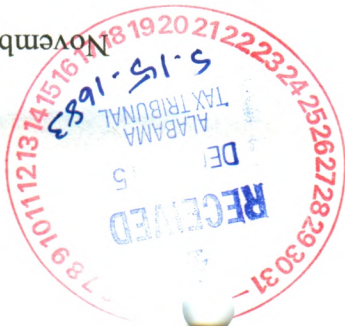


/s/ Margaret Johnson McNeill
MARGARET JOHNSON MCNEILL
Assistant Counsel
State of Alabama Department of Revenue
P.O. Box 320001
Montgomery, AL 36132-0001
(334) 242-9690

sm



Agile Consulting Group, Inc.
5255 Triangle Pkwy., Suite 150
Norcross, GA 30092
(888) 350-4TAX (4829)



November 24, 2015

To Whom It May Concern,

Alabama Tax Tribunal
P.O. Box 327130
Montgomery, AL 36132-7130

We would like to request a formal hearing with the Alabama Tax Tribunal over the denial of \$17,907.39 of sales tax paid to Medhost of Tennessee Inc. DBA Healthcare Management Systems (Account #SLS-6800 50160) by Russell County Community Hospital LLC (Account #SLS-R000798981). The refund period covered by this denial is February 2012 through August 2014.

We are requesting a formal hearing for the denial of \$17,907.39 because the software in question is customized software, which was adapted specifically for Russell County Community Hospital. Russell County Community Hospital purchased a patient flow management software, physician documentation software, and radiology imaging software implementation solution from Medhost. This implementation consisted of a 5 step process that allowed Medhost to customize the software to Russell County Community Hospital's unique workflow and environment. I have attached an email from Medhost Account Executive Chris Thomas which explains the 5 step implementation process.

This customized software implementation was denied on the basis of Alabama Department of Revenue Sales & Use Tax Rule 810-6-1-.37, which discusses the taxability of computer hardware and software. Specifically, the request for refund was denied because the auditor reviewing the refund believed customized software implementation is only exempt if the charges for the customized portion are separately stated from charges for canned software.

However, his denial of this refund is incorrect. Section 5 of this rule defines custom software programming as, "software programs created specifically for one user and prepared to the special order of that user." The rule also states that custom software programming "includes programs that contain pre-existing routines, utilities, or other program components that are integrated in a unique way to the specifications of a specific purchaser." Furthermore, this situation was addressed in AL HealthSouth Corporation v. State of AL Dept. of Rev., Docket # S. 06-243, 8/10/2006. In this case, HealthSouth Corporation purchased canned software that was adjusted to fit their specific needs. The canned software purchased was determined to be custom software because it was modified exclusively for HealthSouth Corporation. I have attached a copy of this rule and court case.

Since Russell County Community Hospital purchased software that was modified exclusively for their own use, this fits the criteria of custom software programming. Therefore, the software implementation purchased from Medhost should not be subject to sales tax and the refund denial totaling \$17,907.39 be granted in its entirety. If necessary, we are happy to provide additional information, such as invoice copies, or answer any specific questions pertaining to this formal



Agile Consulting Group, Inc.
5255 Triangle Pkwy., Suite 150
Norcross, GA 30092
(888) 350-4TAX (4829)

hearing request. If you have any questions, I can be reached at (248) 854-2583. Thank you for your assistance in this matter.

Sincerely,

A handwritten signature in black ink, appearing to read "Mathew E. Soifer". The signature is fluid and cursive, with a long horizontal line extending to the left.

Mathew E. Soifer
Principal
Agile Consulting Group, Inc.
5255 Triangle Pkwy., Suite 150
Norcross, GA 30092
Cell: (248) 854-2583
Fax: (770) 206-2548

Changlan Li
Revenue Examiner

Sincerely,
Changlan Li

If you are not in agreement and wish to pursue this matter further, you may request a formal hearing before the Alabama Tax Tribunal within two years from November 9, 2015 or you may appeal directly to circuit court. If you desire a hearing before the Tax Tribunal you must file an appeal with the Alabama Tax Tribunal, P. O. Box 327130, Montgomery, Alabama 36132-7130.

convenience. The refund request is denied.

This is further explained in Sales & Use Tax Rule 810-6-1-.37, a copy of which is enclosed for you. The taxable portion on the invoice, the full sales price is to be included in the gross proceeds of sales. contained canned software that was customized and the nontaxable customized portion was not separated from petitioned for refund of sales tax on software claimed was custom. The refund is not due because the software contained canned software that was customized and the nontaxable customized portion was not separated from

A review of your refund claim by our audit section revealed that Russell County Community Hospital On March 11, 2015, the Alabama Department of Revenue received the above referenced petition for refund.

Re: Joint Petition for Refund
&
Medhost of Tennessee Inc.
Russell County Community Hospital
Alabama Sales Tax account: 6800 50160
Period Covered: 2/12-8/14
Attention: Matthew Soifer, POA
Agile Consulting Group, Inc.
5255 Triangle Pkwy., Suite 150
Norcross, GA 30092

November 9, 2015

State of Alabama
Department of Revenue
(www.revenue.alabama.gov)
50 North Ripley Street
Montgomery, Alabama 36132



JULIE P. MACEE
Commissioner

MICHAEL E. MASON
Assistant Commissioner
JOE W. GARRETT, JR.
Deputy Commissioner
CURTIS E. STEWART
Deputy Commissioner

810-6-1-.37. Computer Hardware and Software.

(1) Computers and related equipment, also known as computer hardware, consist of components and accessories that make up the physical computer assembly. The retail sale of computer hardware is subject to sales or use tax. The rental of computer hardware is subject to rental tax.

(2) The term "computer software" as used in this regulation shall mean a sequence of automatic data-processing equipment instructions necessary to solve a problem, and includes both system and application programs and subdivisions, such as assemblers, compilers, routines, generators and utilities.

(3) The term "canned computer software" as used in this regulation shall mean software programs prepared, held, or existing for general or repeated use, including software programs developed in-house and subsequently held or offered for sale or lease. Canned computer software includes all software, except custom software programming, regardless of its function and regardless of whether it is transferred to the purchaser in physical form, via telephone lines, or by another alternative form of transmission.

(4) Canned computer software is tangible personal property; and, on and after March 1, 1997, the retail sale or rental of canned computer software is subject to the sales, use, or rental tax, whether such transaction was affected by a transfer of title, or of possession or of both, or a license to use or consume. Unless specifically stated otherwise, the licensing of canned computer software is considered a retail sale, and not a rental, and is subject to sales or use tax. The measure of tax upon which the sales, use, or rental tax is to be computed is the total amount received from the sale or rental of canned computer software to the customer. Wal-Mart Stores, Inc. v. City of Mobile and County of Mobile, Alabama Supreme Court, decided September 13, 1996, substitute opinion released November 27, 1996.

(5) The term "custom software programming" as used in this regulation shall mean software programs created specifically for one user and prepared to the special order of that user. The term "custom software programming" also includes programs that contain pre-existing routines, utilities, or other program components that are integrated in a unique way to the specifications of a specific purchaser. Custom software programming also includes those services represented by separately stated charges for modifications to a canned computer software program when such modifications are prepared to the special order of the customer. Modification to a canned computer software program to meet the customer's needs is custom software programming only to the extent of the modification. Custom software programming is not subject to tax regardless of the manner or medium of transfer to the customer since the charge for the custom software programming is a charge for professional services and the manner or medium of transfer is considered incidental to the sale of the service.

(6) The provider of custom software programming would owe sales or use tax on the cost of the tangible medium for transferring the custom software programming to the

(Continued)

810-6-1-.37. (Continued)

customer. Such tangible mediums would include tapes, cards, discs, compact discs, and any other tangible personal property used in transferring custom software, programming to the customer.

(7) The term "software maintenance agreement/contract" as used in this regulation shall mean contracts sold in connection with the sale or rental of canned software and can include any, all, or a combination of the following: technical consultation (support) services either by telephone or on-site visits, corrections of errors or malfunctions (bugs) in the canned software, provisions for enhancements (software upgrades) to the canned software, revisions to operating manuals for the canned software, and training services. If the maintenance contract is required as a condition of the sale or rental of canned software, the gross sales price or gross rental price is subject to tax whether or not the charge for the maintenance contract is separately stated from the charge for the canned software. If the maintenance contract is optional to the purchaser of the canned software, then only the portion of the contract fee representing enhancements or upgrades and new operating manuals is subject to tax provided the fees for consultation or support services, error corrections, and training services are separately stated and such separate statement is not used as a means of avoiding imposition of tax upon the actual gross receipts from the furnishing of upgrades or manuals. If these fees are not separately stated, the entire charge for the maintenance contract is subject to tax. If the maintenance contract is optional to the lessee of the canned software, the rental tax will not apply to the gross receipts derived therefrom.

(8) Maintenance contracts sold in connection with custom software programming, whether required or optional, or whether or not separately stated, are not subject to tax. The provider of the custom software programming is the consumer of any tangible personal property used in producing operating manuals and would owe sales or use tax on the cost of these items. (Section 40-23-2(1)) (Adopted July 2, 1975, amended June 12, 1978, February 21, 1997, amended August 21, 1997) readopted through APA effective October 1, 1982, amended January 29, 1990, amended

This item involves approximately 5,500 magazines purchased by the Taxpayer. The magazines were shipped to the Taxpayer's headquarters in Birmingham, and, according to the Taxpayer's representative, some were distributed in Alabama and some were shipped to the Taxpayer's inpatient hospitals outside of Alabama. The Department examiner did not allow the temporary storage exemption provided in Reg. 810-6-5-.23 because he saw no evidence as to when and where the magazines were shipped out-of-state, if at all.

(2) Stratum 2, Line 6, Item 366.

I cannot determine from the invoice whether the items purchased were tangible property or nontaxable intangible services. The final assessment is *prima facie* correct, and the burden was on the Taxpayer to establish that the items were nontaxable. Code of Ala. 1975, § 40-2A-7(b)(5)c. It failed to do so. Consequently, this invoice was correctly included as taxable.

(1) Stratum 1, Line 96, Item 9271.

This disputed invoice is for "201 print clippings." The Department examiner taxed the items because he understood the items were tangible property. The Taxpayer contends that the invoice involved nontaxable information.

The Department audited the Taxpayer and determined that the Taxpayer owed additional Alabama use tax. The Taxpayer raised various objections to the Department's audit. The Department responded to the Taxpayer's objections by either requesting additional information concerning an objection, or explaining why it did not agree with the objection. The Department thereafter made some adjustments based on additional information provided by the Taxpayer. It then entered the final assessment in issue.

The items in issue in this case are identified in the Department's June 13, 2005 response to the Taxpayer's objections, Department Ex. B. Those disputed adjustments were addressed at the July 11 hearing, and are discussed below.

The Revenue Department assessed HealthSouth Corporation ("Taxpayer") for State use tax for October 1999 through September 2002. The Taxpayer appealed to the Administrative Law Division pursuant to Code of Ala. 1975, § 40-2A-7(b)(5)a. A hearing was conducted on July 11, 2006. Michael Martin represented the Taxpayer. Assistant Counsel Margaret McNeill represented the Department.

OPINION AND PRELIMINARY ORDER

OPINION

Tax Type(s): Sales and Use Tax

Date Issued: 08/10/2006

Docket/Court: DOCKET NO. S. 06-243, Alabama Department of Revenue, Administrative Law Division

Case Information:

HEALTHSOUTH CORPORATION HEALTHSOUTH COMPANY STORE P.O. BOX 380546 BIRMINGHAM, AL 35238-0546, Taxpayer, v. STATE OF ALABAMA DEPARTMENT OF REVENUE.

AL HEALTHSOUTH CORPORATION HEALTHSOUTH COMPANY STORE P.O. BOX 380546 BIRMINGHAM, AL 35238-0546, Taxpayer, v. STATE OF ALABAMA DEPARTMENT OF REVENUE, DOCKET NO. S. 06-243, 08/10/2006

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Again, the burden was on the Taxpayer to maintain records showing that some of the magazines were shipped out of Alabama. Without such records, or other evidence establishing the number of magazines that were shipped out of Alabama, the magazines must be taxed in full.

(3) Stratum 2, Line 23, Item 127.

This involves an invoice from CLA Architecture, Inc. The Department taxed the invoice because the invoice did not identify what was being purchased. The Taxpayer's representative claims that the Taxpayer was purchasing nontaxable architectural services. He indicated at the July 11 hearing that he could contact the vendor and determine exactly what the invoice was for. As explained below, the representative will be allowed time to do so.

(4) Stratum 3, Line 52, Item 23.

This is one of several invoices from Ingenix Publishing Group. The Department taxed the invoices because there was no indication that the items sold — "workers comp fee sch plus — ren" — were not tangible property, and thus taxable.

The Taxpayer's representative conceded that he was not sure what the invoices involved, but that the company's website indicated that it was an information services provider. However, without some evidence that the invoices were for nontaxable services, the Department correctly included the invoices as *prima facie* taxable.

(5) Stratum 3, Line 64, Item 92.

These invoices were for "PeopleSoft Upgrade Training" from PeopleSoft USA, Inc. The "training units" purchased by the Taxpayer were primarily for software training. The Department concedes that if the units were used for training, the cost was nontaxable. However, the contracts also provided that if the items or credits were not redeemed for training, they may be used to obtain tangible items. Because there was no evidence indicating which units were redeemed for training versus tangible property, the Department taxed the entire amounts. Again, without some evidence showing the separate amounts spent for nontaxable training and taxable property, the examiner correctly taxed the entire amount. *State v. Ludlum*, 384 So.2d 1089 (Ala. Civ. App.), cert. denied, 384 So.2d 1094 (Ala. 1980).

(6) Stratum 3, Line 74, Item 248.

It is not disputed that this invoice involved the taxable sale of tangible property. The Department also initially taxed a separately stated freight charge, which it later deleted from the taxable measure. The Taxpayer also claims that it should be allowed a credit for a \$3,000 charge for training on the invoice on which it had erroneously accrued and paid tax. The Department apparently agrees.

(7) Stratum 3, Line 91, Item 1.

This invoice involves a software package the Department deemed to be canned software, and thus taxable. The Taxpayer contends that the software was nontaxable custom software because it was developed exclusively for the Taxpayer.

The Alabama Supreme Court has held that "canned" or generic computer software constitutes tangible property subject to sales, use, or lease tax. *Wal-Mart Stores v. City of Mobile*, 690 So.2d 290 (Ala. 1996). However, the Department still considers the gross proceeds from custom or special-designed software to be nontaxable as a charge for professional services. See, Dept. Reg. 810-6-1-37.

The Taxpayer's representative testified that he understood that the software was developed exclusively for the Taxpayer. The Department examiner explained that the software was taken off the shelf, i.e., was canned, but that "they took it and made adjustments for it." (T. 23) By adjusting the software to fit the Taxpayer's needs, the software became custom software, and thus was not taxable per Reg. 810-6-1-37.

(8) \$100,000 + Stratum, Line 9, Item 58.

This is another canned versus custom software issue. The item is not taxable for the reasons explained above, see (7).

(9) \$100,000 + Stratum, Line 18, Item 34.

This involves an invoice for approximately \$160,000 from M. J. Harrison, a large construction company. The Department taxed the invoice because there was no indication on the invoice was not for taxable property versus a nontaxable construction service. The Taxpayer claims that the invoice was for building improvements to real property, and thus not taxable. The Taxpayer's representative indicated at the July 11 hearing that he would contact the vendor and verify what the invoice was for. Without evidence that the invoice was nontaxable, it

must be included as taxable.

(10) \$100,000 + Stratum, Line 21, Items 19 an 20; Line 23, Item 21.

These invoices involve purchases from Peoplesoft. The Department does not dispute that the Taxpayer paid sales tax to Peoplesoft. The problem is that the Department has no evidence that Peoplesoft remitted the tax to the State. Peoplesoft is located in another State, and does not have an Alabama sales tax account. The Taxpayer's representative indicated at the July 11 hearing that he would contact Peoplesoft and find out if they remitted the tax to Alabama. Otherwise, the invoices must be included as taxable.

(11) \$100,000 + Stratum, Line 24, Item 14.

This item involves a purchase of nontaxable information services the Department did not assess. The Taxpayer claims that it may have improperly accrued tax, and if so, it should be allowed a credit. I agree. However, there is no evidence that the Taxpayer did, in fact, accrue and pay tax on the amount. Without such proof, no credit can be allowed.

(12) \$100,000 + Stratum, Line 26, Item 6.

This invoice involves tangible property that was shipped to Georgia. The Department taxed the amount because it was suspected that the property may have subsequently been shipped into and used at the Taxpayer's headquarters in Alabama. There is no evidence, however, that the property was used anywhere other than in Georgia. This item should be excluded from the audit.

The taxability of many of the disputed items discussed above turns on whether the Taxpayer can provide records or other sufficient evidence showing that the items were not taxable. The Taxpayer is allowed until September 29, 2006 to provide additional evidence concerning the items. The evidence should be submitted to the Administrative Law Division, and will be forwarded to the Department for review and response. An appropriate Order will then be entered.

This Opinion and Preliminary Order is not an appealable Order. The Final Order, when entered, may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, § 40-2A-9(g).

Entered August 10, 2006.

BILL THOMPSON

Chief Administrative Law Judge

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