



AICPA®

December 23, 2024

The Honorable Glenn Hegar
Texas Comptroller of Public Accounts
Lyndon B. Johnson State Office Building
111 East 17th Street
Austin, Texas 78774

RE: Recommendation to include current rule tax return preparation and all financial statements preparation exceptions in proposed rule amendments to 34 TAC § 3.330 data processing services

Dear Comptroller Hegar:

The American Institute of Certified Public Accountants (AICPA) recommends that the [proposed rule amendments to Texas Administrative Code \(TAC\), Title 34, Part 1, Chapter 3, Subchapter O, Rule § 3.330\(a\)\(1\)](#) (dated Aug. 30, 2024) be modified as in the attached AICPA recommended legislative language fixes to the proposed amendments to include and not delete the current rule exception for tax return preparation and all financial statements preparation in the definition of “data processing services.”

Specifically, the [current 34 TAC § 3.330\(a\)\(1\)](#) provides that preparing federal income tax, state franchise or sales tax returns and all financial statements preparation are not “data processing.” Current 34 TAC § 3.330(a)(1) states, “Data processing does not include the use of a computer by a provider of other services when the computer is used to facilitate the performance of the service or the application of the knowledge of the physical sciences, accounting principles, and tax laws, e.g., the use of a computer to provide interpretive or enhancement geophysical services or the use of a computer by a CPA firm, enrolled agent, or bookkeeping firm to produce a financial report, prepare federal income tax, state franchise or sales tax returns, or charges for temporary secretarial personnel who as part of their function use word processing equipment.”

We suggest keeping (with a slight modification to delete “income” between “federal” and “tax” and delete “franchise or sales” between “state” and “tax”) this language in proposed rule § 3.330(a)(1) or including it (with a slight modification to delete “income” between “federal” and “tax” and delete “franchise or sales” between “state” and “tax”) as new proposed rule § 3.330(a)(1)(B)(v) and renumbering prior proposed rule § 3.330(a)(1)(B)(v) instead to proposed rule § 3.330(a)(1)(B)(vi) and providing new proposed rule § 3.330(a)(1)(B)(v) to read as: “the use of a computer by a provider of other services when the computer is used to facilitate the performance of the service or the application of the knowledge of the physical sciences, accounting principles, and tax laws, e.g., the use of a computer to provide interpretive or enhancement geophysical services or the use of a computer by a CPA firm, enrolled agent, or bookkeeping firm to produce a financial report, prepare federal tax returns, state tax returns, or charges for temporary secretarial personnel who as part of their function use word processing equipment.” In addition, we suggest adding as an example under § 3.330(b) as new (4) and renumber the prior proposed (4)-(12) as (5)-(13) and provide new proposed § 3.330(b)(4) to read as “The preparation of federal tax returns and state tax returns is not included in taxable data processing because the result is solitary and depends upon the skills of a tax professional.”

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In addition, we note that the proposed rule new language in § 3.330(b)(3) includes an example excluding the preparation of financial statements *under Generally Accepted Accounting Principles (GAAP)*, but not tax returns - or financial statements prepared on another basis. Specifically, proposed § 3.330(b)(3) states, “The preparation of financial statements kept in accordance with generally accepted accounting principles, is not included in taxable data processing, even though it has elements of data processing, because the categorization and characterization of the data is variable and depends upon the discretion and certified opinion of an accounting professional.” We think the “ancillary exclusion” should apply, but it is less clear than it is in the current rule exception for tax preparation in the definition of data processing services. We suggest that proposed § 3.330(b)(3) be modified to cover all financial statements so it should say, “The preparation of financial statements is not included in taxable data processing, even though it has elements of data processing, because the categorization and characterization of the data is variable and depends upon the discretion and certified opinion of an accounting professional.”

The proposed rule should retain the current tax return preparation and all financial statements preparation exceptions. If the tax return and all financial statements preparation exceptions language is stricken, and the above recommended modifications to the proposed rule are not included, the accounting profession may be impacted as it would not be clear if tax return preparation and non-GAAP financial statements preparation are still excepted from the data processing service.

We recommend the above modifications to the proposal so that the current rule exceptions to the definition of data processing services for tax return preparation and all financial statements preparation are retained and included in the proposed rule amendments to 34 TAC § 3.330. Thank you for your consideration of our comments.

The AICPA is the world's largest member association representing the CPA profession, with more than 400,000 members in the United States and worldwide, and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

We appreciate your consideration of our request and welcome the opportunity to discuss this request further. If you have any questions, please contact Marta Zaniewski, AICPA Vice President of State Regulatory and Legislative Affairs, at (202) 591-0908, or Marta.Zaniewski@aicpa-cima.com; or me at (830) 372-9692 or [bvickers@alamo-group.com](mailto: bvickers@alamo-group.com).

Sincerely,



Blake Vickers, CPA (licensed in Texas), CGMA
Chair, AICPA Tax Executive Committee

Encl: AICPA Recommended Legislative Language Fixes to Proposed Amendments to 34 TAC
§ 3.330 Data Processing Services

**AICPA Recommended Legislative Language Fixes to Proposed Amendments to 34 TAC
§3.330 Data Processing Services (in redline)**

TITLE 34. PUBLIC FINANCE

PART 1. COMPTROLLER OF PUBLIC ACCOUNTS

CHAPTER 3. TAX ADMINISTRATION

SUBCHAPTER O. STATE AND LOCAL SALES AND USE TAXES

34 TAC §3.330. DATA PROCESSING SERVICES

The Comptroller of Public Accounts proposes amendments to §3.330, concerning data processing services. The comptroller amends this section to clarify existing definitions; to add new definitions; to list examples of services that are included in and excluded from taxable data processing services; to describe data processing that is not taxable; to explain the incidence of the tax; and to update provisions related to the collection of local sales and use taxes on data processing services. The amendments implement language in Senate Bill 153, 87th Legislature, 2021 regarding payment processing. Other revisions improve the clarity and readability of the section.

Subsection (a) provides definitions. The comptroller amends the general definition of "data processing service" in paragraph (1) to list the operative words included as examples of "data processing service" in Tax Code, §151.0035(a)(1) ("Data Processing Service"). The comptroller moves and amends existing language regarding examples to subsection (b). The comptroller deletes existing language regarding internet access services as they are no longer taxable.

The comptroller adds new subparagraph (A) listing services that are specifically included in data processing service under Tax Code, §151.0035.

The comptroller adds new subparagraph (B) listing services that are specifically excluded from data processing service under Tax Code, §151.0035, including services added by Senate Bill 153.

The comptroller adds new subparagraph (C) to exclude some data processing that might otherwise be included in "data processing service" as described in Tax Code, §151.0035. The comptroller adds subparagraph (C) under its exclusive jurisdiction to interpret taxable services, as provided in Tax Code, §151.0101(b) ("Taxable Services").

Subparagraph (C) provides that a data processing service will not be taxable if it is sold for a single charge with another service, the data processing service does not have a separate value, and the data processing service is ancillary to the other service.

New subparagraph (C)(i) provides that if the data processing service is sold for a single charge with another service that does not have a separate value, and the other service is ancillary to the data processing service, the entire charge will be taxable as a data processing service.

New subparagraph (C)(ii) provides that if the data processing service has a separate value and is sold or purchased for a single charge with a nontaxable related service, subsection (e) applies.

New subparagraph (C)(iii) identifies factors that the comptroller may consider in determining whether the data processing service has a "separate value." The "separate value" requirement is drawn from *Rylander v. San Antonio SMSA Ltd. P'ship*. 11 S.W.3d 484, 488 (Tex. App.--Austin 2000, no pet.). The opinion uses the "separate value" concept in evaluating whether services could be segregated for taxation purposes.

The "separate value" requirement of subparagraph (C)(iii) is also consistent with the comptroller's longstanding rule, retained in subsection (e)(3), which provides for the segregation of nontaxable and taxable services sold or purchased for a single charge.

The comptroller explains the "ancillary" requirement in new subparagraph (C)(iv). The requirement is similar to the current provision that excludes data processing service if it "facilitates the performance" of another service. But subparagraph (C)(iv) identifies specific factors, which are not in the current rule.

The test for determining whether a data processing service is "ancillary" to a nontaxable service is not an essence of the transaction test. The essence of the transaction test attempts to determine what the buyer ultimately wants. *Combs v. Chevron, Inc.*, 319 S.W.3d 836, 843 (Tex. App.--Austin 2010, pet. denied) ("underlying goal"). The buyer will never want the manipulation of data for its own sake. The buyer will always want the manipulation of data as the means to achieve an end. Therefore, the identification of the "underlying goal" of the buyer, or the essence of the transaction, is not the appropriate test for data processing services. See also, Hellerstein & Hellerstein, *State Taxation* §12.08 (3rd ed. 2020) (the primary purpose test is "folly").

In determining whether a data processing service is "ancillary" to a nontaxable service, the comptroller will focus on what the seller is doing, and not what the buyer wants. The repetitive or routine manipulation of data by the seller is a factor suggesting that the activity is not ancillary and should be taxable as a data processing service, while the manipulation of data that depends on the external knowledge and discretionary judgment of the service provider suggests that the activity is ancillary and should not be taxable as a data processing service.

For example, the insertion of data into form title or loan documents for a client would ordinarily be a taxable data processing service. The primary service is the compilation, retrieval, and accurate manipulation of the data into the forms, even though there may be an element of independent judgement in correctly entering the data. However, the preparation of a title opinion would not ordinarily be a taxable data processing service. The primary service is the application of legal knowledge and judgement to a set of facts, even though there may be elements of data processing. The "ultimate goal" of the preparation of loan documents and the preparation of title opinions may be the same - to close a real estate deal. But one service is a taxable data processing service because it requires the repeated application of the same process to different data, albeit with skill and expertise; and the other service is not a taxable data processing service because it produces a solitary result based on legal principles. These examples are illustrated in the recent opinion in *Hegar v. Black, Mann, & Graham, L.L.P.*, No. 03-20-00391-CV, 2022 WL 567853 (Tex. App.--Austin Feb. 25, 2022, no pet.).

The comptroller amends current paragraph (2) to delete the definition of "internet" as that term is already defined in Tax Code, §151.00393 (Internet). The comptroller adds a new definition of "downstream payment processor" based on the language in Senate Bill 153 that incorporates the definition in 7 TAC §33.4(c) (Payment Processors) as that provision existed on January 1, 2021.

The comptroller amends paragraph (3) to delete the definition of "internet access services" as the statutory reference to that definition is now listed in subsection (a)(1)(B)(i) and a separate definition is no longer necessary. The comptroller adds a new definition of "point of sale payment processor" based on the language in Senate Bill 153 that incorporates the definition in 7 TAC §33.4(d) as that provision existed on January 1, 2021.

The comptroller adds new paragraph (4) to add a definition of "settling of an electronic payment transaction" based on the language in Senate Bill 153.

The comptroller moves the existing text of current subsection (b) to amended subsection (c)(2), with changes. Amended subsection (b) text provides examples that apply the definition of "data processing service."

The comptroller adds new paragraphs (1)-(3) to restate text from current subsection (a)(1) that payroll services, business accounting, and the preparation of financial statements are data processing services.

The comptroller adds new paragraph (4) based on the holding in *Hegar v. Black, Mann, & Graham, L.L.P.*, No. 03-20-00391-CV, 2022 WL 567853 (Tex. App.--Austin Feb. 25, 2022, no

pet.), which held the preparation of form title or loan documents is taxable data processing.

The comptroller adds new paragraph (5) to clarify that marketplace providers may provide data processing services to their customers if they enter, retrieve, search, manipulate, and store data or information in the course of their business.

The comptroller adds new paragraph (6) to clarify that internet hosting as defined by Tax Code, §151.108 (Internet Hosting) is taxable data processing.

The comptroller adds new paragraph (7) to clarify that video streaming subscriptions are taxable cable television services under Tax Code, §151.0033 ("Cable Television Service"). See also §3.313 of this title (relating to Cable Television Service and Bundle Cable Service).

The comptroller adds new paragraph (8) to clarify that streaming video gaming subscriptions are taxable amusement services as set forth in Tax Code, §151.0028 ("Amusement Services") and in STAR Accession No. 201405957L (May 28, 2014), and are not taxable data processing services.

The comptroller adds new paragraph (9) to provide that the compilation of nontaxable opinion polls and survey information as described by §3.342 of this title (relating to Information Services), is not taxable data processing if the data processing is ancillary to the acquisition of the information and the service provider's expertise is not managing data, such as in an inventory management service.

The comptroller adds new paragraph (10) to provide that the compilation of nontaxable information derived from laboratory, medical, or exploratory testing or experimentation as described by §3.342 of this title is not taxable data processing if the data processing is ancillary to the provision of the information.

The comptroller adds new paragraphs (11) and (12) to add examples from Comptroller's Decision No. 116,834 (2022) regarding the taxability of computerized three-dimensional rendering, website design, website development, search engine optimization, social media marketing, and lead generation.

The comptroller moves current subsection (c) to amended subsection (d), with changes. New subsection (c) is titled "Imposition of tax, permits."

The comptroller adds new paragraph (1) to provide that the use of data processing service is subject to state sales and use tax and that local sales and use tax may also be imposed.

The comptroller adds new paragraph (2) that contains language moved from current subsection (b) and restates that providers of data processing services must obtain a Texas

sales and use tax permit. The paragraph includes the permitting safe harbor for small remote sellers as set forth in §3.286(b)(2) of this title (relating to Seller's and Purchaser's Responsibilities).

The comptroller adds new paragraph (3) that contains language moved from current subsection (a)(1) stating that a data processing service is taxable regardless of the ownership of the computer or whether that data is provided by the customer or the customer's authorized designee.

The comptroller adds new paragraph (4) to restate the language from current subsection (b) which exempts 20% of the amount charged for data processing services from sales and use tax based on Tax Code, §151.351 (Information Services and Data Processing Services).

The comptroller amends relettered subsection (d), formerly subsection (c), to update the storage medium used in the example from a magnetic tape to a Universal Serial Bus (USB) drive.

The comptroller amends relettered subsection (e), formerly subsection (d). The substantive effect of subsection (e) is the same as former subsection (d). However, the term "unrelated service" is replaced by the term "nontaxable related service" to conform to the ordinary usage of the terms. Subsection (e) applies when multiple services are sold or purchased for a single charge. Because the services are sold or purchased for a single charge, the services are in some manner going to be "related," as that term is ordinarily used, even if they are also distinct. When services are related by a common charge, and the services are each also commonly provided on a stand-alone basis, and the performances are distinct and identifiable, then the single charge may be segregated under the conditions described in subsection (e).

The comptroller reletters subsection (f), formerly subsection (e).

The comptroller amends relettered subsection (g), formerly subsection (f) and retitles it "Determining the incidence of the tax (service benefit rule)". The comptroller moves current text in subsection (g) regarding local taxes to relettered subsection (h), with changes.

The comptroller amends paragraph (1) to restate the statutory definition of "use" in Tax Code, §151.011 ("Use" and "Storage"). The comptroller deletes the current presumption language in paragraph (1) regarding a separate, identifiable segment of a customer's business. The current presumption language is replaced by the presumption in paragraph (2) that more closely follows the statutory presumption in Tax Code, §151.104(a) (Sale for Storage, Use, or Consumption Presumed).

The comptroller amends paragraph (2) to restate statutory language in Tax Code, §151.104(a) regarding presumption of use in Texas. The comptroller moves language in current paragraph (2) regarding business conducted both inside and outside the state to amended paragraph (3) and moves language regarding multi-state customers' method of allocation to new paragraph (6).

The comptroller amends paragraph (3) and adds clauses (i)-(ii) to restate statutory language in Tax Code, §151.104 and §151.330 (Interstate Shipments, Common Carriers, and Services Across State Lines). The comptroller moves language in current paragraph (3) regarding a multi-state customer providing an exemption certificate to new paragraph (6).

The comptroller amends paragraph (4) to restate statutory language in Tax Code, §151.101 (Imposition of Use Tax) and to be consistent with the interpretation of statute in Comptroller's Decision No. 116,293 (2022). The comptroller deletes language in current paragraph (4) regarding identifiable segments of a business as the revised subsection follows the statutory guidelines more closely.

The comptroller amends paragraph (5) to restate statutory language in Tax Code, §151.303(c) (Previously Taxed Items: Use Tax Exemption or Credit) and §3.338 of this title (relating to Multistate Tax Credit and Allowance of Credit for Tax Paid to Suppliers). The comptroller deletes language in current paragraph (5) regarding services that cannot be assigned to an identifiable segment of a business, as the revised subsection follows the statutory guidelines more closely.

The comptroller adds new paragraph (6) to restate moved language from current paragraph (3) regarding multi-state customers issuing exemption certificates, with non-substantive changes to improve readability.

The comptroller adds new paragraph (7) to restate language from paragraph (2) regarding a multistate customer's use of any reasonable method for allocation which is supported by business records.

The comptroller adds new clause (i) to restate moved language from current paragraph (2) regarding the method used for business records to allocate a data processing service used both within and outside Texas.

The comptroller adds new clause (ii) to add language regarding the good faith acceptance of an exemption certificate as set forth in §3.287 of this title (relating to Exemption Certificates).

The comptroller amends relettered subsection (h), formerly (g) regarding Local Taxes.

The comptroller amends paragraph (1) to provide general guidance on the consummation of sale for local sales tax and directs taxpayers to §3.334 of this title (relating to Local Sales and Use Taxes) and deletes the existing language.

The comptroller amends paragraph (2) to provide general guidance on determining local use tax and directs taxpayers to §3.334 of this title and to delete language that is now located in §3.334 of this title.

Language in former subparagraph (A) remains as new paragraph (3). The comptroller deletes subparagraph (B) as that language is now located in new subsection (g)(6).

The comptroller adds subsection (i) to restate former subsection (h) and to make minor changes for readability.

The comptroller adds new paragraphs (1) and (2) to clarify when a customer is responsible to report use tax due on the purchase of taxable data processing services under Tax Code, §151.101.

Tetyana Melnyk, Director of Revenue Estimating Division, has determined that during the first five years that the proposed amended rule is in effect, the rule: will not create or eliminate a government program; will not require the creation or elimination of employee positions; will not require an increase or decrease in future legislative appropriations to the agency; will not require an increase or decrease in fees paid to the agency; will not increase or decrease the number of individuals subject to the rule's applicability; and will not positively or adversely affect this state's economy.

Ms. Melnyk also has determined that the proposed amended rule would benefit the public by conforming the rule to current statute and improving readability. This rule is proposed under Tax Code, Title 2, and does not require a statement of fiscal implications for small businesses or rural communities. The proposed amended rule would have no significant fiscal impact on the state government, units of local government, or individuals. There would be no anticipated significant anticipated economic cost to the public.

You may submit comments on the proposal to Jenny Burleson, Director, Tax Policy Division, P.O. Box 13528, Austin, Texas 78711-3528 or to the email address: tp.rule.comments@cpa.texas.gov. The comptroller must receive your comments no later than 30 days from the date of publication of the proposal in the *Texas Register*.

The comptroller proposes the amendments under Tax Code, §111.002 (Comptroller's Rules; Compliance; Forfeiture), which provide the comptroller with the authority to prescribe, adopt, and enforce rules relating to the administration and enforcement of

provisions of Tax Code, Title 2 (State Taxation), and taxes, fees, or other charges or refunds which the comptroller administers under other law.

The amendments implement Tax Code, §§151.0035 ("Data Processing Services"), 151.0101 (Taxable Services), 151.105 (Importation for Storage, Use, or Consumption Presumed), 151.330 (Interstate Shipments, Common Carriers, and Services Across State Lines), 151.351 (Information Services and Data Processing Services), 321.203 (Consummation of Sale), and 321.205 (Use Tax).

§3.330. Data Processing Services.

(a) Definitions. The following words and terms, when used in this section, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Data processing service--the computerized entry, retrieval, search, compilation, manipulation, or storage of data or information. [services--~~the processing of information for the purpose of compiling and producing records of transactions, maintaining information, and entering and retrieving information. It specifically includes word processing, payroll and business accounting, and computerized data and information storage or manipulation. The charge for data processing services is taxable regardless of the ownership of the computer. Examples of data processing services include entering inventory control data for a company, maintaining records of employee work time, filing payroll tax returns, preparing W-2 forms, and computing and preparing payroll checks. Data processing does not include the use of a computer by a provider of other services when the computer is used to facilitate the performance of the service or the application of the knowledge of the physical sciences, accounting principles, and tax laws, e.g., the use of a computer to provide interpretive or enhancement geophysical services or the use of a computer by a CPA firm, enrolled agent, or bookkeeping firm to produce a financial report, prepare federal income tax, state franchise or sales tax returns, or charges for temporary secretarial personnel who as part of their function use word processing equipment. Data processing services does not include Internet access services or data processing services provided in conjunction with and incidental to the provision of Internet access service when billed as a single charge.]~~

(A) Data processing service includes:

- (i) word processing;
- (ii) payroll and business accounting data production;
- (iii) the performance of a totalizator service with the use of computational equipment required by Occupations Code, Subtitle A-1, Title 13, (Texas Racing Act); and

(iv) the use of a computer or computer time for data processing whether the processing is performed by the provider of the computer or computer time or by the purchaser or other beneficiary of the service.

(B) Data processing services do not include:

(i) Internet access service as defined by Tax Code, §151.00394 (Internet access service);

(ii) the transcription of medical dictation by a medical transcriptionist;

(iii) the display of a classified advertisement, banner advertisement, vertical advertisement, or link on an Internet website owned by another person;

(iv) services exclusively to encrypt electronic payment information for acceptance onto a payment card network that allows a person to accept a specific brand of debit or credit card by routing information and data to settle an electronic payment transaction, in order to comply with standards set by the Payment Card Industry Security Standards Council; or

(v) the use of a computer by a provider of other services when the computer is used to facilitate the performance of the service or the application of the knowledge of the physical sciences, accounting principles, and tax laws, e.g., the use of a computer to provide interpretive or enhancement geophysical services or the use of a computer by a CPA firm, enrolled agent, or bookkeeping firm to produce a financial report, prepare federal tax returns, state tax returns, or charges for temporary secretarial personnel who as part of their function use word processing equipment.

(vi) settling of an electronic payment transaction by:

(I) a downstream payment processor or point of sale payment processor or point of sale payment processor that routes electronic payment information to an entity described in subclause (II) or (III) of this clause;

(II) a federally insured financial institution, as defined by Finance Code, §201.101 (Definitions), that is organized under the laws of Texas, another state, or the United States, or an affiliate of the institution;

(III) a payment card network that allows a person to accept a specific brand of debit or credit card by routing information and data to settle an electronic payment transaction;

(IV) a person who has entered into a sponsorship agreement with an entity described in subclause (II) for the purpose of processing that entity's electronic payment transactions through a payment card network; or

(V) a person who is engaged in the business of money transmission and required to obtain a license under Finance Code, §152.101 (Money Transmission License Required).

(C) Under its exclusive jurisdiction to interpret taxable services, the comptroller excludes from the definition of "data processing service" data processing that is sold for a single charge with another service if the data processing service does not have a separate value, and the data processing service is ancillary to the other service. The burden is on the taxpayer to demonstrate that the data processing service does not have a separate value and is ancillary to the other service.

(i) If the data processing service is sold for a single charge with another service that does not have a separate value, and the other service is ancillary to the data processing service, the entire charge will be taxable as a data processing service.

(ii) If the data processing service is sold for a single charge with another service that has a separate value, subsection (e) of this section applies.

(iii) In determining whether the data processing service and the other service have separate values, the comptroller will consider whether the services are distinct and identifiable and whether each service is of a type that is commonly provided on a stand-alone basis or commonly provided as an additional service for a greater single charge.

(iv) In determining whether the data processing service is ancillary to another service, or conversely, whether the other service is ancillary to the data processing service, the comptroller may consider the extent to which the service provider exercises discretion or judgment in individual applications of the processed data based on knowledge of the physical sciences, accounting principles, law, or other fields of study. The repetitive or routine manipulation of data by the seller is a factor suggesting that the data processing activity is not ancillary to another service and should be taxable as a data processing service. The manipulation of data that depends on the external knowledge and discretionary judgment of the service provider in individual applications suggests that the data processing activity is ancillary to another service and should not be taxable as a data processing service. The provider's skill, experience, or expertise, in processing data or information is not a factor. Other factors may be considered, and the weight of the factors may vary from case to case. The evaluation is based on what the service provider is doing, not on what the customer wants.

(2) Downstream payment processor--A payment processor that acts as an intermediary between a consumer-facing entity that has incurred an outstanding money transmission obligation to a consumer, and the consumer's designated recipient. [Internet - collectively the myriad of computer and telecommunications facilities, including equipment and

operating software, that comprise the interconnected worldwide network of networks that employ the Transmission Control Protocol/Internet Protocol, or any predecessor or successor protocols to the protocol, to communicate information of all kinds by wire or radio.]

(3) Point of sale payment processor--A payment processor that receives funds from a consumer on behalf of a consumer-facing entity that either sells goods or services other than money services or accepts charitable donations. [Internet access service - a service that enables users to access content, information, electronic mail, or other services offered over the Internet and may also include access to proprietary content, information, and other services as part of a package of services offered to consumers. Internet access service does not include any other taxable service, unless the taxable service is provided in conjunction with and is merely incidental to the provision of Internet access service. Individuals providing Internet access should refer to §3.366 of this title (relating to Internet Access Services).]

(4) Settling of an electronic payment transaction--The authorization, clearing, or funding of a payment made by credit card, debit card, gift card, stored value card, electronic check, virtual currency, loyalty program currency such as points or miles, or a similar method. The term does not include charges by a marketplace provider, as that term is defined by Tax Code, §151.0242 (Marketplace Providers and Marketplace Sellers).

(b) Examples of services that are and are not taxable data processing services. [Hold permits. All providers of data processing services must obtain Texas sales and use tax permits and collect tax on charges for data processing services, or accept properly completed resale, exemption, or direct pay permit certificates in lieu of collecting tax. See §3.285 of this title (relating to Resale Certificate; Sales for Resale); §3.287 of this title (relating to Exemption Certificates); §3.288 of this title (relating to Direct Payment Procedures and Qualifications). Effective October 1, 1999, 20% of the total amount charged for data processing services is exempted from tax. The exemption applies to services performed on or after October 1, 1999. The exemption does not apply to services performed before the effective date and billed or paid for after the effective date of the exemption.]

(1) Payroll services, such as maintaining records of employee work time, computing and preparing payroll checks, filing payroll tax returns, and completing pre-printed employee-related forms such as W-2s, are taxable data processing because they involve the routine and repeated simultaneous application of the same process to different data. The service provider's skill, experience, or expertise with payroll documents is not determinative.

(2) The production of business accounting data, such as inventory reports, is taxable data processing because it involves the routine and repeated simultaneous application of the same process to different data. The service provider's skill, experience, or expertise with business reports is not determinative.

(3) The preparation of financial statements kept in accordance with generally accepted accounting principles, is not included in taxable data processing, even though it has elements of data processing, because the categorization and characterization of the data is variable and depends upon the discretion and certified opinion of an accounting professional.

(4) The preparation of federal tax returns and state tax returns is not included in taxable data processing because the result is solitary and depends upon the skills of a tax professional.

(54) The insertion of data into form title or loan documents for a client is taxable data processing because it involves the repeated application of the same process to different data. The service provider's skill or experience with title or loan documents is not determinative. The preparation of a title opinion is not included in taxable data processing, even though it has elements of data processing, because the result is solitary and depends upon the opinion or skills of a legal professional.

(65) Marketplace provider services may be included in taxable data processing services when they involve the computerized entry, retrieval, search, compilation, manipulation, or storage of data or information provided by the purchaser or the purchaser's designee. For example, services to store product listings and photographs, maintain records of transactions, and to compile analytics are taxable data processing services.

(76) Internet hosting, as defined by Tax Code, §151.108 (Internet Hosting), is included in taxable data processing services when the user stores data on the service provider's hardware, or processes data on software that is owned, licensed, or leased by the user or provider. An example is the provision of servers and operating systems that are used by a customer to store software applications and content that can be accessed by the customer's customers.

(87) Streaming video subscriptions are taxable as a cable television service but not as data processing services. See also §3.313 of this title (relating to Cable Television Service and Bundle Cable Service).

(98) Streaming video game subscriptions are taxable as an amusement service but not as data processing services. See also §3.298 of this title (relating to Amusement Services).

(109) The compilation of information that the service provider acquires from unrelated third parties through nontaxable opinion polls and surveys as described by §3.342 of this title (relating to Information Services) is not a taxable data processing service if the data processing is ancillary to the main service of data acquisition and the data processing does not have a separate value. However, if the service provider acquires and compiles data from the customer or the customer's designees, and the service provider's expertise is in managing the data, such as in inventory management, the main service is data processing and the service is taxable.

(110) The compilation of nontaxable information primarily derived from the service provider's laboratory, medical, or exploratory testing or experimentation or any similar method of direct scientific observation of physical phenomena as described by §3.342 of this title (relating to Information Services) is not a taxable data processing service if the data processing is ancillary to the main service and the data processing does not have a separate value. Examples may be geophysical surveys, polygraph tests, and the recording and tracking of vital signs in a medical treatment.

(111) Computerized three-dimensional rendering that is created using customer provided data is taxable data processing as it requires the computerized entry, retrieval, search, compilation, manipulation, or storage of data or information.

(112) Website design, website development, search engine optimization, social media marketing, and lead generation are taxable data processing when they involve the storage, manipulation, compilation, and entry of data.

(c) Imposition of tax, permits.

(1) State sales and use tax and any applicable local sales and use tax are imposed on each sale or use of a data processing service in Texas.

(2) Except for small remote sellers described in §3.286(b)(2)(B) of this title (relating to Seller's and Purchaser's Responsibilities), a seller of data processing services must obtain a Texas sales and use tax permit and collect and remit tax on charges for data processing services, or accept properly completed resale, exemption, or direct pay permit certificates in lieu of collecting tax. See §3.285 of this title (relating to Resale Certificate; Sales for Resale); §3.287 of this title (relating to Exemption Certificates); §3.288 of this title (relating to Direct Payment Procedures and Qualifications).

(3) A charge for data processing services is taxable regardless of the ownership of the computer or whether the data is provided by the customer or the customer's authorized designee.

(4) Twenty percent of the total amount charged for data processing services is exempted from tax. If the data processing service is also taxable as another type of taxable service other than an information service, the twenty percent exemption does not apply.

(d) [e] Resale certificates.

(1) Providers of data processing services may issue a resale certificate in lieu of tax to suppliers of tangible personal property only if care, custody, and control of the property is transferred to the client. For example, a service provider purchases a Universal Serial Bus (USB) drive [magnetic tape] to transfer the results of data processing services to customers. The USB drive [tape] is transferred to the customer, and the customer owns and uses the USB drive [tape] to review the results of the data processing service. The service provider may purchase the USB drive [tape] tax free by issuing a resale certificate. Tax is due on the total amount charged the customer, including amounts for the USB drive [tape] and for the services.

(2) A resale certificate may be issued for a service if the buyer intends to transfer the service as an integral part of taxable services. A service will be considered an integral part of a taxable service if the service purchased is essential to the performance of the taxable service and without which the taxable service could not be rendered.

(3) A resale certificate may be issued for a taxable service if the buyer intends to incorporate the service into tangible personal property which will be resold. If the entire service is not incorporated into the tangible personal property, it will be presumed the service is subject to tax and the service will only be exempt to the extent the buyer can establish the portion of the service actually incorporated into the tangible personal property. If the buyer does not intend to incorporate the entire service into the tangible personal property, no resale certificate may be issued, but credit may be claimed at the time of sale of the tangible personal property to the extent the service was actually incorporated into the tangible personal property.

(e) [d] Nontaxable related [Unrelated] services.

(1) A service will be considered as a nontaxable related service [unrelated] if:

- (A) it is neither a data processing service, nor a service taxed under other provisions of the Tax Code, Chapter 151;
- (B) each of the services provided are [it is] of a type which are [is] commonly provided on a stand-alone basis; and

(C) the performance of the service is distinct and identifiable. Examples of such a service would be consultation, development of and preparation of feasibility studies, design and development, or training.

(2) Where nontaxable related [~~unrelated~~] services and taxable services are sold or purchased for a single charge and the portion relating to taxable services represents more than 5.0% of the total charge, the total charge is presumed to be taxable. The presumption may be overcome by the data processing service provider at the time the transaction occurs by separately stating to the customer a reasonable charge for the taxable services. However, if the charge for the taxable portion of the services is not separately stated at the time of the transaction, the service provider or the purchaser may later establish for the comptroller, through documentary evidence, the percentage of the total charge that relates to nontaxable related [~~unrelated~~] services. The service provider's books must support the apportionment between exempt and nonexempt activities based on the cost of providing the service or on a comparison to the normal charge for each service when [~~if~~] provided alone. If the charge for exempt services is unreasonable when the overall transaction is reviewed considering the cost of providing the service or a comparable charge made in the industry for each service, the comptroller will adjust the charges and assess additional tax, penalty, and interest on the taxable services.

(3) Charges for services or expenses directly related to and incurred while providing the taxable service are taxable and may not be separated for the purpose of excluding these charges from the tax base. Examples would be charges for meals, telephone calls, hotel rooms, or airplane tickets.

~~(f) [(e) Service benefit location.] If both the data processing service provider and the customer are located in Texas, Texas tax is due.~~

~~[(f) Service benefit location--multi-state customer.]~~

(g) Determining the incidence of the tax.

(1) With respect to a taxable service, "use" means the derivation in Texas of direct or indirect benefit from the service. [To the extent a data processing service is used to support a separate, identifiable segment of a customer's business (other than general administration or operation of the business) the service is presumed to be used at the location where that part of the business is conducted.]

(2) The sale of a data processing service that is delivered in Texas is presumed to be a sale for storage, use, or consumption in Texas until the contrary is established. [If that part of the business is conducted at locations both within and outside the state, the service is not

~~taxable to the extent it is used outside Texas. A multi-state customer may use any reasonable method for allocation which is supported by business records.]~~

(3) A data processing service performed in Texas is subject to Texas sales tax unless an exemption applies. [A multi-state customer purchasing data processing services for the benefit of both in-state and out-of-state locations is responsible for issuing to the data processing service provider an exemption certificate asserting a multi-state benefit, and for reporting and paying the tax on that portion of the data processing charge which will benefit the Texas location. A data processing service provider that accepts such a certificate in good faith is relieved of responsibility for collecting and remitting tax on transactions to which the certificate relates.]

(A) A data processing service performed in Texas for use entirely outside of Texas is exempt from sales tax.

(B) A data processing service performed in Texas for use both within and outside of Texas is exempt to the extent that the service is used outside Texas.

(4) A data processing service performed outside of Texas is subject to Texas use tax to the extent that the service is for use in Texas, unless an exemption applies. [The customer's books must support the assignment of the service to an identifiable segment of the business, the determination of the location or locations of the use of the service, and the allocation of the taxable charge to Texas.]

(5) A purchaser of a data processing service performed outside of Texas for use in Texas may claim a credit for a similar tax paid in another state if that state provides a similar credit for a taxpayer in Texas. [To the extent the use of the service cannot be assigned to an identifiable segment of a customer's business, the service is presumed to be used to support the administration or operation of the customer's business generally. The service is presumed to be used at the customer's principal place of business. The principal place of business means the place from which the trade or business is directed or managed.]

(6) A purchaser asserting the use of a data processing service at business locations in multiple states may issue to the service provider a form promulgated by the comptroller, or a substantially similar document that asserts a concurrent multi-state business use and represents that the purchaser will report and pay the state and local tax on the portion that is taxable and is not exempt.

(A) The multi-state purchaser may use a reasonable and consistent method supported by its business records to allocate the service between jurisdictions.

(B) A service provider that accepts a multi-state use certificate in good faith is relieved of responsibility for collecting and remitting Texas state and local sales and use taxes on transactions subject to the certificate.

(h) [({g})] Local taxes.

(1) Local sales tax is due in a local jurisdiction where the sale is consummated. The sale may be consummated at a place of business of the seller where the order is received, a place of business of the seller where the order is fulfilled, or at the location to which the service is delivered. See §3.334 of this title (relating to Local Sales and Use Taxes). [For local sales tax purposes, city, county, transit authority, and/or special purpose district sales taxes are due if the data processing service provider has only one place of business (the location where clients request service) within the boundaries of a local taxing entity. Local sales tax must be collected based upon the tax rate at that location, except that no MTA or CTD sales tax is due on services provided at a location outside the boundaries of the transit area. In the case of multiple locations, if an order for service is placed at one location but the service is provided at another location, the place of business from which the service is provided will determine to which local taxing entity the tax is allocated.]

(2) Local use tax may also be due in a local jurisdiction where a direct or indirect benefit from the service is derived if the 2.0% local tax cap has not been exceeded. See also §3.334 of this title. [For the purposes of the local use tax, if a place of business is outside the boundaries of a local taxing entity, the data processing service provider will be required to collect local use tax if the client is within the local taxing entity and the service provider has representation in the local taxing entity as outlined in §3.286 of this title (relating to Seller's and Purchaser's Responsibilities). Even if the service provider is not required to collect local use tax, the client is still liable for the tax if the service is performed or a benefit is derived from the service within the boundaries of a local taxing entity.]

(3) [({A})] An in-state customer purchasing data processing services for the benefit of locations in more than one local taxing entity is responsible for issuing to the data processing service provider an exemption certificate claiming a multi-city benefit and for determining the extent of benefit for each entity. The local use tax for each entity must be reported, allocated, and paid by the customer. A data processing service provider that accepts in good faith an exemption certificate claiming a multi-city benefit is relieved of responsibility for collecting and remitting local tax on transactions to which the certificate relates.

[(B) A multi-state customer purchasing data processing services for the benefit of both in-state and out-of-state locations is responsible for issuing an exemption certificate and for reporting and paying local tax as provided by subsection (f)(3) and (4) of this section.]

(i) [(h)] Use tax. The customer is responsible to report and pay use tax if the service provider: [If a provider of a data processing service is not doing business in Texas or in a specific local taxing jurisdiction and is not required to collect Texas tax, it is the Texas customer's responsibility to report and pay the state and local use tax directly to this office.]

- (1) is not required to collect and remit the sales or use tax; or
- (2) does not collect the correct amount of sales or use tax.

The agency certifies that legal counsel has reviewed the proposal and found it to be within the state agency's legal authority to adopt.

Filed with the Office of the Secretary of State on August 30, 2024.

TRD-202404132

Jenny Burleson

Director, Tax Policy

Comptroller of Public Accounts

Earliest possible date of adoption: October 13, 2024

For further information, please call: (512) 475-2220

<https://www.sos.texas.gov/texreg/archive/September132024/Proposed%20Rules/34.PUBLIC%20FINANCE.html>