



May 11, 2016

City of Chicago
Rahm Emanuel, Mayor

Department of Law

Stephen R. Patton
Corporation Counsel

Revenue Litigation Division
30 North LaSalle Street
Suite 1020
Chicago, IL 60602-2580

(312) 744-5691
(312) 744-6798 (Fax)

Re: [REDACTED]

Dear [REDACTED]:

I am writing in response to your letter of January 26, 2016 ("Request") (copy enclosed), requesting a private letter ruling ("PLR") concerning the application of the Chicago Personal Property Lease Transaction Tax ("Lease Tax" or "Tax"), Chapter 3-32 of the Municipal Code of Chicago ("Code"), to the charges imposed by [REDACTED] for the use of the products described in the Request ("Products").

Based on the facts set forth in your Request, along with the additional information provided through the on-line demonstration provided by [REDACTED] on April 5, 2016, we are of the opinion that charges imposed for the use of the Products are not subject to the Lease Tax in either the "[REDACTED]" (i.e., nonpossessory) version or the "client-hosted" (i.e., possessory) version. In both cases, a key consideration is your representation that the Products consist almost entirely of materials (such as articles, videos and lessons) that are written by [REDACTED] (through its employees and contractors).

A. [REDACTED] Products

Lease Tax Ruling #12 concerns nonpossessory computer leases. The Ruling includes the following provision:

Access to materials that are primarily proprietary is ... an exempt use of the provider's computer. The customer may pay a subscription fee for the ability to download or otherwise access the desired information or data, and the subscription fee may allow the customer to use a search function to locate the information or data that the customer wishes to download or otherwise access, but the value of the search function is subordinate to the value of the information or data that the customer wishes to download or otherwise access (i.e., the charge is predominantly for the information or data). This will typically apply in the case of a web site or "app" that allows a subscriber to download or otherwise access materials that are primarily proprietary, such as copyrighted newspapers, newsletters or magazines, that the subscriber would have to purchase if the materials were acquired or accessed through other means, such as a purchase at a "bricks and mortar" store. ¶ 11.

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May 11, 2016

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As noted, you have represented that the Products consist almost entirely of materials that are written by ██████████. For example, the ██████████ is essentially an electronic medical encyclopedia, written by ██████████. Other Products consist of proprietary articles, videos and lessons.

B. Client-hosted Products

According to the Illinois Department of Revenue, "Information or data that is downloaded electronically, such as downloaded books, musical recordings, newspapers or magazines, does not constitute the transfer of tangible personal property." See 86 Admin. Code Section 130.2105(a)(3). This is in contrast with software, which is considered tangible personal property. See 35 ILCS 120/2. The client-hosted versions of the Products are more in the nature of e-books than software. Because the Lease Tax does not apply to intangibles such as e-books, it does not apply to the charges imposed for the use of the Products.

This opinion is based on the law as of the date of this letter and the facts as represented in your Request and demonstration being accurate and complete. The opinions contained herein are expressly intended to constitute written advice that may be relied upon pursuant to Section 3-4-325 of the Code.

Sincerely,



Weston W. Hanscom
Deputy Corporation Counsel
(312) 744-9077

cc: Joel Flores, Department of Finance

[REDACTED]

January 26, 2016

Tax Policy Section
City of Chicago
Department of Revenue
Room 300, DePaul Center
333 South State Street
Chicago IL 60604-3977

Re: Request for a Private Letter Ruling – City of Chicago Department of Revenue
In conjunction with a Voluntary Disclosure application

BACKGROUND

We became aware of possible obligations under the Chicago Personal Property Lease Transaction Tax law as a result of the Information Bulletin on Non-Possessory Computer leases issued in November 2015. [REDACTED] has submitted an application for the Voluntary Disclosure Agreement as offered in the Information Bulletin. The City acknowledged our application on December 30, 2015. On January 12, 2016, we submitted a New Account Application and an Initial Taxable Period affidavit and the City was notified that we were preparing this Letter Ruling Request.

[REDACTED] [REDACTED] incorporated and headquartered in the State of [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] creating, licensing and distributing a number of electronic health information and education products. [REDACTED] is registered with the State of Illinois to collect Illinois Use Tax on taxable products sold to non-exempt clients.

We have several questions about how the Chicago Personal Property Lease Transaction Tax applies to the license fees we charge our Chicago clients for use of software and information services, both in the case where clients access products on [REDACTED] servers ([REDACTED]), and in the case where clients take possession of the products on their own servers (client-hosted). In both of these cases, [REDACTED] retains title to the property and charges a monthly or annual license fee to clients for use of the products.

Our specific questions follow below the section of this letter containing the [REDACTED] product descriptions.

[REDACTED]

PRODUCT DESCRIPTIONS OF [REDACTED] PRODUCTS LICENSED TO CHICAGO CUSTOMERS

General Information on [REDACTED] Products

[REDACTED]'s electronic health information and education products are used by health care organizations such as health plans, hospitals, and physician groups. These organizations use the products by making them available to their user groups, who may be health plan members, or hospital and physicians' patients, generally at no cost to the users, with the goal of helping users [REDACTED]. [REDACTED] licenses its products either directly to health care organizations or to distributor and reseller organizations that relicense the products to healthcare organizations.

[REDACTED] charges an annual license fee that is generally invoiced to clients quarterly. The license fee amount is based on the size of the organization's user group, such as the number of members in a health plan or the number of hospital patients with access to the products. Products are updated periodically, ranging from quarterly to bi-annually, depending on the specific product and changes in medical research or medical practice.

[REDACTED] makes its products available to clients using one of the following two electronic delivery methods:

1. [REDACTED]. The product is hosted by [REDACTED] i.e. the product resides on computers maintained by a third-party hosting service that [REDACTED] contracts with to host its products. Clients access the products on these third-party computers. Clients do not take possession of the product on their own computers.

OR

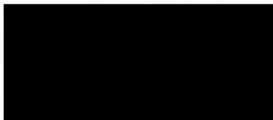
2. Client-hosted. [REDACTED] places the product on an FTP site on the Internet and the client downloads the entire product from the FTP site to its own computers. The client does not access any Healthwise computers or any third-party hosting service computers.

Information on Specific Products

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

[REDACTED]



[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

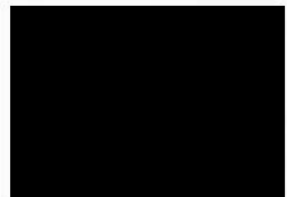
[REDACTED]

[REDACTED]

LIST OF RULING REQUESTS

We are requesting rulings on the following issues:

- A. Questions related to client-hosted products



1. Is the client-hosted [REDACTED] a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?
2. Is the client-hosted [REDACTED] product a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?
3. Is the client-hosted [REDACTED] [REDACTED] bundled product a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?

B. Questions related to [REDACTED] products

4. Is the [REDACTED] database or software as defined under the Municipal Code of Chicago, Section 3-32-020? Does Exemption 11 apply? If tax is due, what is the effective date of the liability?
5. Is the [REDACTED] [REDACTED] a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?
6. Is the [REDACTED] [REDACTED] product a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?

C. Other questions

7. Are the [REDACTED] subject to the Chicago Lease tax?

[REDACTED]

Each of these ruling requests is addressed in detail below.

A. QUESTIONS RELATED TO CLIENT-HOSTED PRODUCTS

Question #1 - Is the client-hosted [REDACTED] a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?

Section 3-32-020.E. of the Chicago Municipal Code defines Computer Software as follows:

“Computer software” or “software” means, but not by way of limitation, data and information that are associated with the hardware of a computer such as a collection of computer programs, routines, compilers, assemblers, translators, manuals, circuit diagrams and operation procedures.”

[REDACTED]

and defines Computer Program as follows:

“Computer program” or “program” means, but not by way of limitation, a series of coded instructions or statements in a form acceptable to a computer and intended for execution on a computer, either directly or indirectly, to bring about a certain result, such as causing the computer to process data and supply the results of the data processing.”

and defines Data or a Database as follows:

“Data” or “database” means, but not by way of limitation, a representation of information, knowledge, facts, concepts or instructions, including program documentation, which is prepared in a formalized manner and is stored or processed in or transmitted by a computer. Data may be in any form including, but not limited to, reports, printouts, magnetic or optical storage media, punch cards or data stored internally in the memory of the computer.”

Based on these definitions, we believe the client-hosted [REDACTED] is a database. The [REDACTED] health content is a representation of information and facts organized into topics (i.e. prepared in a formalized manner). It is stored in a computer and transmitted by computer when the client downloads it to its own computers. The product does contain some software in order for the search and navigation functions to work, and to facilitate the operation of the 3% of the [REDACTED] that contains content that allows interactivity with the user, but the product in itself is not software in that it does not consist solely or even primarily of “a collection of computer programs, routines, compilers, assemblers, translators, manuals, circuit diagrams and operation procedures”. The majority of the product consists of text-based articles and still images that contain the health information.

We were unable to locate any authorities contrary to our view.

Question: Does the City agree that the client-hosted [REDACTED] is a database?

Question: As a database, we believe the [REDACTED] when licensed as a client-hosted product is subject to the Chicago lease tax, and has been subject to the tax since prior to the start of the Voluntary Disclosure look-back period for [REDACTED] which is December 29, 2011. Does the City agree with this conclusion?

Question #2 – is the client-hosted [REDACTED] product a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?

Based on the definitions outlined in Question 1 above, we believe the [REDACTED] product is software. Each [REDACTED] contains information files on the specific health topic as well as computer programs that govern how the information is presented. While it does have elements of a database in that it is a representation of knowledge in a formalized manner, it also has a substantial amount of computer software that allows the product to present the information to the user in a predetermined, timed sequence and to select specific information in response to the user's input. [REDACTED]

We were unable to locate any authorities contrary to our view.

Question: Does the City agree that the client-hosted [REDACTED] product is software?

Question: As software, we believe the [REDACTED] product when licensed as a client-hosted product are subject to the Chicago lease tax. Does the City agree with this conclusion?

Question: Ruling #5 on the "Usage of Computers and Computer Software", effective September 1, 2013 states that "a transfer of software that meets the five-part test set forth in 87 Illinois Administrative Code Section 130.1935 is a lease, subject to the lease tax". We conclude from this that September 1, 2013 is the start date for the liability for Chicago lease tax for licenses for client-hosted software that meet the 5-part test. Does the city agree with this conclusion?

Question #3 – Is the client-hosted [REDACTED] bundled product a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?

Based on the City's definitions outlined in Question 1 above, we believe the [REDACTED] bundled product is software. While the [REDACTED] are largely composed of content with a minimal amount of software, each [REDACTED] contains information files on the specific health topic as well as computer programs that govern how the information is presented. While it does have elements of a database in that it is a representation of knowledge in a formalized manner, it also has a substantial amount of computer software that allows the product to present the information to the user in a predetermined timed sequence and to select specific information in response to the user's input.

We were unable to locate any authorities contrary to our view.

Question: Does the City agree that the client-hosted [REDACTED] product is software?

Question: As software, we believe the [REDACTED] product when licensed as a client-hosted product is subject to the Chicago lease tax. Does the City agree with this conclusion?

Question: Ruling #5 on the "Usage of Computers and Computer Software", effective September 1, 2013 states that "a transfer of software that meets the five-part test set forth in 87 Illinois Administrative Code Section 130.1935 is a lease, subject to the lease tax". We conclude from this that September 1, 2013 is the start date for the liability for Chicago lease tax for licenses for client-hosted software that meet the 5-part test. Does the city agree with this conclusion?

[REDACTED]

B. QUESTIONS RELATED TO [REDACTED] PRODUCTS

Question #4: Is the [REDACTED] [REDACTED] a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? Does Exemption 11 apply? If tax is due, what is the effective date of the liability?

For the same reasons as outlined in Question #1 above, we believe the [REDACTED] [REDACTED] is a database.

We also believe that Exemption 11 applies to the [REDACTED] [REDACTED] for the following reasons.

Code Section 3-32-050(A)(11) ("Exemption 11") provides: Notwithstanding any other provision of this chapter, the following leases, rentals or uses shall be exempt from the taxes imposed by this chapter: Under rules to be prescribed by the department, the nonpossessory lease of a computer in which the customer's use or control of the provider's computer is de minimis and the related charge is predominantly for information transferred to the customer rather than for the customer's use or control of the computer, such as the nonpossessory lease of a computer to receive either current price quotations or other information having a fleeting or transitory character.

Ruling #12 on Nonpossessory Computer Leases – Exemption 11, effective 7/1/15, further clarifies the application of Exemption 11. Paragraph 9 of Ruling 12 states that "As explained below, exempt use may be demonstrated either (a) by access to information or data which is entirely passive (such as streaming data), without interactive use, or, in other cases, (b) by access to materials that are primarily proprietary, such as copyrighted newspapers, newsletters or magazines". In this case, (a) does not apply, but (b) does apply – [REDACTED] content is proprietary, as evidenced by the fact that it is copyrighted. Paragraph 11 of Ruling 12 goes on to describe a situation where a customer pays a subscription fee for the ability to download or otherwise access desired information, and the subscription fee may allow the customer to use a search function to locate the information, but the value of the search function is subordinate to the value of the information. Paragraph 11 states that this is an exempt use. This is precisely the situation with the [REDACTED] – the subscription allows the use of a search function to locate the desired information, but it is the information itself that is the primary value to the client. Clients license the [REDACTED] for the value of the uniquely written health information contained in it. The value of the search function is subordinate to the value of the information; In fact, it is not necessary to use the search function to access the information – a user can use the alphabetical index instead.

Paragraph 11 also states that the value of the search function is subordinate to the value of the information "in the case of a web site or "app" that allows a subscriber to download or otherwise access materials that are primarily proprietary, ... , that the subscriber would have to purchase if the materials were acquired through other means,..." The [REDACTED] contains content that is finely crafted to effect behavior change in the reader, is copyrighted, and must be purchased by our clients. It is not available without being purchased from [REDACTED] or from a licensed distributor. Based on Ruling #12, we believe that the [REDACTED] [REDACTED] is exempt from the Chicago Lease tax under Exemption 11, and, if [REDACTED] is accepted into the Voluntary Disclosure program as offered in the Inform[REDACTED]

November 2015, that no tax or interest or penalties based on those charges are owed for any periods ending before January 1, 2016.

We were unable to locate any authorities contrary to our view.

Question: Does the City agree that the [REDACTED] [REDACTED] [REDACTED] is a database?

Question: Does the city agree that the [REDACTED] [REDACTED] [REDACTED] is exempt from the Chicago Lease tax under Exemption 11?

Question: Does the City agree that no tax or interest or penalties based on those charges are owed for any periods ending before January 1, 2016, in accordance with the offer made in the Information Bulletin of November 2015, as long as [REDACTED] is accepted into the Voluntary Disclosure program and as long as [REDACTED] comes into compliance with the Lease Tax Ordinance and Ruling #12 by January 1, 2016 (or such later date as the Department may agree to for good cause)?

Question: If the City agrees that the [REDACTED] is a database exempt from tax under Exemption 11, does the City agree that no taxes need to be charged from January 1, 2016 onwards?

Question #5: Is the [REDACTED] [REDACTED] a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?

Based on the definitions outlined in Question 1 above, we believe the [REDACTED] product is software. Each [REDACTED] course contains information files on the specific health topic as well as computer programs that govern how the information is presented. While it does have elements of a database in that it is a representation of knowledge in a formalized manner, it also has a substantial amount of computer software that allows the product to present the information to the user depending on the path the user selects, allows the user to select the individual lessons, and allows the user to respond to quizzes, and provides feedback to the user's input. Computer programs also allow the user's progress through the online course to be tracked so that if the user does not complete the course in one sitting, the product will restart them at the point they left off, with all their prior responses retained. The user's progress can also be tracked and reported to the client for use in a variety of ways. We believe that this amount of functionality enabled by computer programs characterizes this product as software rather than as a database.

We were unable to locate any authorities contrary to our view.

Question: Does the City agree that the [REDACTED] product is software?

Question: As software, we believe the [REDACTED] product when licensed as a [REDACTED] product is subject to the Chicago lease tax. Does the City agree with this conclusion?

[REDACTED]

Question: Does the City agree that, if the [REDACTED] [REDACTED] product is software, taxes are owed only for the period of January 1, 2015 through December 31, 2015, with no liability for interest or penalties, in accordance with the offer made in the Information Bulletin of November 2015, as long as [REDACTED] is accepted into the Voluntary Disclosure program and as long as [REDACTED] comes into compliance with the Lease Tax Ordinance and Ruling #12 by January 1, 2016 (or such later date as the Department may agree to for good cause)?

Question #6 - Is the [REDACTED] product a database or software as defined under the Municipal Code of Chicago, Section 3-32-020? If tax is due, what is the effective date of the liability?

Based on the City's definitions outlined in Question #1 above, we believe the [REDACTED] are software as sold to [REDACTED] [REDACTED] [REDACTED] [REDACTED]; an interactive module, and uses computer programs to guide users through a series of questions and answers to evaluate the severity of symptoms and provide a recommendation for seeking health care targeted to the specific user's situation. We believe the relatively large amount of computer programs included with the [REDACTED] product would classify the entire product as software.

We were unable to locate any authorities contrary to our view.

Question: Does the City agree that the [REDACTED] product is software?

Question: As software, we believe the [REDACTED] product when licensed as a [REDACTED] product is subject to the Chicago lease tax. Does the City agree with this conclusion?

Question: Does the City agree that, if the [REDACTED] [REDACTED] [REDACTED] product is software, taxes are owed only for the period of January 1, 2015 through December 31, 2015, with no liability for interest or penalties, in accordance with the offer made in the Information Bulletin of November 2015, as long as [REDACTED] is accepted into the Voluntary Disclosure program and as long as [REDACTED] comes into compliance with the Lease Tax Ordinance and Ruling #12 by January 1, 2016 (or such later date as the Department may agree to for good cause)?

C. OTHER QUESTIONS

Question #7- Are the [REDACTED] subject to the Chicago lease tax?

The fee charged [REDACTED] for the [REDACTED] covers the service for the initial development of the [REDACTED], services for periodic updates as needed, and a license fee for ongoing use. We believe the fee for the development, update, and client use of the [REDACTED] [REDACTED] is exempt from the Chicago Lease Tax.

[REDACTED]

The Information Bulletin of November 2015, in the second to last paragraph in the "General" section, explains there are some specific exclusions that the City has recognized as inherent to the Lease Tax, "for example, payments for services, including software that is custom designed for the customer".

In addition, Paragraph 7 of Ruling #12 states "Charges for services are not subject to lease tax: If a customer pays a provider to write a report, article, or similar document consisting primarily of the provider's own observations, opinion, ideas or analysis (hereafter collectively referred to as a "report"), the charge is for the service of writing the report for the customer and is not subject to the lease tax, even if the report is accessed electronically. Likewise, if a customer pays a provider to create a database, the charge is for the service of creating the database for that customer and is not subject to lease tax, even if the database is accessed electronically."

Although the [REDACTED] are not software, a report, or a database, the fee includes services to custom design and develop the [REDACTED] as well as any services needed to update them for medical changes.

The fee does also include a license fee for ongoing use of the [REDACTED]. The response to FAQ #13 in the November 2015 Information Bulletin states that "where the provider does not separate the taxable and nontaxable charges, the entire fee will be subject to the Lease Tax unless the taxpayer can prove that 50% or more of the charge is for non-taxable items". We would argue that the fees charged for the [REDACTED] can be divided equally between the three types of charge, two of which are a fee for services (the initial development and the periodic updates). This would calculate as 66.7% of the fee for a non-taxable service and 33.3% of the fee is for the usage, so that at least 66.7% of the fees would not be subject to the Lease Tax. Since the Municipal Code of Chicago does not address the issue of fees for usage of a custom developed product, we would assume that this portion of the fee would also not be subject to the Lease Tax.

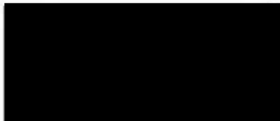
Other than explained in the paragraph above, we were unable to locate any additional authority contrary to our views.

Question: Does the City agree that the fees for the [REDACTED] are not subject to the Chicago Lease Tax?

[REDACTED]

[REDACTED]

[REDACTED]



[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

OTHER ISSUES

We understand that our ruling request may delay the finalization of a Voluntary Disclosure Agreement. [REDACTED]

[REDACTED]

We would like to request that no interest or penalties be charged on any taxes for the period after 1/1/16 and until the date of issuance of the letter ruling, as long as [REDACTED] pays those taxes by the due date indicated by the City when the letter ruling response has been issued. [REDACTED]

[REDACTED]

Please let us know if this is acceptable to the City.

Thank you for your consideration of our ruling request. If you have any questions or need further information, please contact [REDACTED] or by phone at [REDACTED]

Sincerely,

[REDACTED]

[REDACTED]



City of Chicago
January 26, 2016
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cc: [redacted] [redacted]

[redacted]
[redacted]
[redacted] [redacted] [redacted] [redacted]
[redacted]

