

Taxing the Cloud

Vinay Kumar Singh

email: vinay.kumar.ak1907@gmail.com

Student, School of computing science and engineering, Galgotias University, Greater noida, Uttar Pradesh.

Abstract

Nowadays consumers are more liking to download a software file from the internet then to purchase it from the market. Due to which we can see that the sales of the computer softwares CDs are declining at a very fast rate. Consumers are downloading software files and storing them in cloud, so the government is looking towards the "cloud". As they think that it can be new source for Tax revenues.

Today the sales of the USB drive is declining as consumers are preferring to store data in the cloud, which in turn caused decrement in the sales tax revenue as the sale of the physical goods have decreased, but as the government is looking forward to tax the cloud there are many questions that is arising for the taxing of the cloud. In order to impose a tax, the government must have some jurisdiction over the entity they are taxing.

keywords- taxing, tax revenues, jurisdiction, consumers

Introduction

Cloud computing is provision of IT resources in a virtual environment.

In this recent year we have witnessed the shift of the multinational businesses from the classical model where they had fixed investments and real property to the economy model where there is intangible property. In the multinational businesses (MNB) the major thing is the transaction and the transaction over the "cloud" have gained most importance and popularity in very short period of time. It is recognised as the new methods for providing resources. The cloud computing technology have released a lot of financial pressure from the multinational businesses. As earlier the MNB have to invest a lot for purchasing, updating and downloading the softwares but nowadays they don't have to invest a lot as by the use of cloud computing they can make use of the software that they require which is located on remote computers. These transactions

in the cloud offers the MNB lower operational costs, more improved reliability and more increased scalability.

This features of cloud computing is attracting many MNB towards itself as the MNB are switching towards the cloud computing the governments are under pressure. The laws that are present does not provide proper and sufficient guidance on the tax implications of business in the cloud.

We can further say that the cloud can be a "public cloud" or a "private cloud". The end result of both the cloud are the same but there is a difference between the two clouds. The "public cloud" provides cloud computing techniques publicly which means that anyone who have access to the internet can make the use of this cloud by paying a small or no cost. Where as the "private cloud" does not provides the cloud computing techniques publicly it is a private datacenter. Only limited

numbers of user a allowed to use this services by paying certain costs.

The "cloud" is used due to the services it provides. The nature of the services that the "cloud" delivers is also known as cloud delivery model. Based on the services cloud delivery model is divided into three major categories.

- IaaS: Infrastructure as a Service
- SaaS: Software as a Service
- PaaS: Platform as a Service

IaaS: Infrastructure as a Service

Earlier the MNB has to invest a lot for purchasing large and costly infrastructure which included the data centres, equipments, network infrastructure. This investment in infrastructure area was giving financial pressure

to the MNB.

This delivery model of the cloud helped the MNB in releasing some of the financial pressure as in this model the MNB can make use of the infrastructure in their business as a service that is provides by some other party located in remote place. In this delivery model the MNB had to pay "as per its usage" there is no extra costing.

IaaS (Infrastructure as a service) is also called as Hardware cloud. In this hardware cloud the users are allowed to expand as well as contract their requirements as per his business needs.

SaaS: Software as a Service

This cloud delivery model requires an infrastructure/hardware cloud to run. In this delivery model of the cloud the software application is made available by the service providers which is located in remote place for its user to use them. This delivery model make the user free from installing and then running the software application on the user computer. The maintenance cost of the software is also

reduced. This service is made available through internet and the user can access the service easily and from anywhere.

SaaS (Software as a Service) is also called as software cloud. This features of the software cloud attracts the MNB toward itself as earlier the companies had to pay a lot in updation of their softwares, maintenance of the software. Sometimes the MNB had to switch to another software which in turn gave extra financial pressure on the companies as they had to install the new software in each and every system their workers worked on. This service solved a great problems for the MNB and now they don't require to pay such a lot for the software they can easily avail this cloud delivery service.

PaaS: Platform as a Service

PaaS (Platform as a service) is also known as the Desktop cloud as it provides a platform for the software developers where the developers can deploy various application and softwares that he had created by the use of coding or some other methods. This cloud delivery service make the developer free from installing and keeping the tools that is required in the software maintenance in developers computers.

Once the software developed by the developer is deployed in this cloud service then the software can be accessed from anywhere and can be used. Many MNB companies are making use of this services in order to expand their business like Facebook.

Advantages Of Cloud Computing

In present scenario many MNB is moving towards the cloud computing because there are many advantages of cloud computing that attracts the MNB towards itself.

1. Flexible Costs

The costs of cloud computing is much more flexible then that of traditional method. In cloud

computing more server and infrastructure capacity can be provisioned at the peak time and can be de-provisioned when they are no longer needed whereas in the traditional method computing requires buying server and infrastructure capacity sufficient for peak times and allowing them to sit idle for the rest of the time.

2.Always-On Availability

In cloud computing most of the cloud providers are extremely reliable in providing their services.In this the connection is always on and as long as workers have an Internet connection, they can get to the applications that they need. Some applications even work off-line.

3.Fresh Software

With SaaS(Software as a service), the latest versions of the applications that is needed to run the business are made available to all it's customers as soon as they are released.All the older softwares are Immediately upgraded and with the new features and functionality they are put into their customers hands to make their business more productive. software enhancements are typically released quite frequently. This is in contrast to home grown or purchased software that might have major new releases only once a year or so and take significant time to roll out.

4.Cost Effective

By making the use of the cloud computing technology companies don't have to purchase equipment or build and operate a data center, they even don't have to spend significant amount of money on hardware, facilities, utilities and other aspects of operations. With traditional computing, a company had to spend millions before they gets any value from their investment in the data center.

5.Improved Mobility

This means that the data and applications are easily available to their employees irrespective of their location in the world.Their employees can

take their work anywhere via smart phones and tablets—i.e roaming through a retail store to check the status of customers out, customers who had visited their homes or offices, working in the field or at a plant, etc.

6.Less Environmental Impact

With fewer data centers present worldwide and with more efficient operations, companies are collectively having less impact on the environment. Companies those who are using the shared resources are improving their 'green' credentials.

Taxing

Nowadays the states are moving forward towards the taxation of digital products, the technology has evolved a lot and left states racing to catch up. Cloud computing is predicated to be the borderless global networks. As different state might have different laws for tax.If the location of the server cannot be pinpointed then it would be difficult to apply the state's laws in taxing the cloud. If a state taxes at the point of use, and services are free at the point of use then the state cannot tax it. If the process of taxing is based on the location of the servers or on the office from where the cloud computing provider provides their services then the questions arises that will service providers simply move to the lowest-tax jurisdiction?Similarly there are many more questions that is providing hindrance in cloud taxation.

Though lagging far behind, states indeed are chasing the clouds as they find it a new source for generation of the tax revenues.States have update their statutes, in order to cope with the fast changing technology, some states are including languages that are aimed at SaaS, a logical first step, as SaaS(software as a service) platforms are often referred to as application service providers, that have been around the longest. For example, Washington State updated its statutes in 2009 to specifically tax SaaS providers for purposes of

both sales and use tax and business and occupancy tax.

Other states are handling the issue through private letter rulings. For example, the Missouri Department of Revenue (DOR) made a rule that the sale of software which are hosted on out-of-state servers is not subject to sales tax when accessed or used from an in-state location. In contrast, the New York Department of Taxation and Finance made a rule that the SaaS services hosted on out-of-state servers are subject to tax in New York if the related software is accessed or used from a New York location. The department of Taxation and Finance (New York) also believes that SaaS software falls within the state's definition of tangible personal property, the use of which occurs when accessed in New York, and that access constitutes a taxable —transfer of possession of the software, as the customers gain constructive possession of the software and gain the right to use, control or direct use of the software. However, the department of taxation and finance (New York) has ruled that separately stated hosting services are exempt in New York if those services can be purchased separately from software licenses.

The major challenges that states are facing in taxing the cloud offerings is in the tax classification of cloud services themselves. Some questions that arise while taxing the cloud are: Is the offering a taxable or nontaxable service? Is it a data processing or information service? Is it the sale or lease of tangible personal property? Significant number of states have addressed cloud services from a SaaS point of view, but there are very few states that have addressed tax classification from an IaaS or PaaS standpoint, and in that there are very few states who have updated their statutes and regulations to address this emerging use of technology.

Effect Of Taxing The Cloud

The very first reaction to the question of taxing the cloud was a big deal, many users thought that the cost of the cloud would increase and they will have to pay extra in the form of the tax.

The very important question that came up was where, exactly, do the states tax the cloud? As we know that the location of the cloud is nebulous. Do the states tax the cloud in the place where the services are consumed? or The place where the data centre is located? In the former the main issue comes up with the mobile users who are consuming services across many geographies. And in the latter the cloud providers just shift as much of their infrastructures as to data centres in tax advantageous areas—especially to the areas where legislators give it's full support to make cloud computing tax free. The taxation of the cloud on the other hand has discouraged technology advancement. Some of the specific jurisdiction with the underdeveloped tax codes creates risks that drive companies to invest in innovation in other geographies.

In the international picture. According to a recent Ernst & Young report, the local tax laws have not evolved sufficiently that can specifically address the taxation of the cloud computing services. The present law often predate that the emergence and rise of popularity of cloud computing technologies. At last we can say that till now the tax codes haven't caught up with cloud technology anywhere in the world.

Steps To Determine If Cloud Computing Is Taxable

1. Do I have a nexus in that state?

This is the first step that a company should take into consideration.

2. Is this considered as a service or a taxable product?

In some cases the states often consider the downloadable software as a taxable product, but

not always. In some cases, states consider the process in which the client uses the software in order to claim it as a taxable product.

3. Who controls the end product?

This issue is very much trickier for the customer who are using the SaaS that whether the sales tax is charged or not.

4. If it's considered a product, does the state tax SaaS or downloadable software?

It is important to determine whether the state taxes downloaded or SaaS software.

5. If it's a service, is it taxable?

Different states have different and specific rules for different services. Whereas other states allow exemptions for certain services.

Treasury Regulation [1.861-18]

The discussions that were reported in the tax press have noted the possible applications. At least by analogy, of section 1.861-18 of the regulations. This section of the regulation deals mainly with the transactions involving the transfer of the computer program. This regulation divides the transaction involving the transfer of a computer program into four main categories.

- Transfer of a copyright right in the program.
- Transfer of a copy of the program.
- The provision of services for developing or modifying the program.
- The provision of know-how relating to programming techniques.

One of the important questions that came up was: How might these categories of treasury regulation of international transfer be applied to cloud

services? Some of the state tax authorities have extended the rules of the computer program to access the program in the cloud. The IRS (Internal Revenue Service) recognized that there is no actual "transfer" occurring when the software is used through the cloud. The views which were expressed at an ABA meeting by a senior counsel in the IRS office of associate chief counsel (International) were reported as:

"The reg [1.861-18] does require a transfer," Shelburne said, adding that because a transfer is presumed, the reg has limited services application."

This approach sticks closer to the text than some of the state decisions. If the cloud services are not taxed by analogy to the section 1.861-18 regulation, on the basis that they involve no "transfer," they surely can't be ignored.

Conclusion

As day by day the sales of the softwares in the physical form is going down. The MNB are getting much benefits from the cloud services. So, all the MNB are shifting towards the cloud due to which the tax revenue of the government is also going down. Thus finding the proper way in which the government can tax the cloud easily without any difficulties has become an important issue and they are trying to catch up the fast moving cloud technology. If the government successfully finds a way from which they can easily tax the cloud then once again they can collect the targeted revenue that they have lost due to not taxing the cloud.

References

1. Taxing the cloud/www.pewtrusts.org
2. Cloud computing taxation-an analysis from Indian perspective/www.taxsutra.com
3. Taxing the cloud-Berkeley law scholarship repository/scholarship.law.berkeley.edu

4. Cloud computing risks/challenges-legal & tax issues/www.nishithdesai.com

5. Advantages of cloud computing/www.skyhighnetworks.com

6. How does one tax the cloud/www.pwc.com/us/en/state-local-tax

7. States taxing the cloud/www.wired.com/insights

8. Are cloud computing services taxable/www.accuratetax.com ›

9. The taxation of cloud computing and digital content/scholarship.law.upenn.edu/faculty_scholarship/475/