


STD 96/5A - Addendum - Calculation of tax payable on goods containing tax-advantaged computer programs

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This Document forms part of Sales Tax Determination STD 96/5; it is a Ruling for the purposes of section 77 of the *Sales Tax Assessment Act 1992* and may be relied upon by any person to whom it applies.

Addendum to Sales Tax Determination

**Title: Calculation of tax payable on goods containing
tax-advantaged computer programs**

This Addendum amends Sales Tax Determination STD 96/5 as follows:

Before the heading 'Communication of the Decision' (page 8)

Insert the following heading and section:

**Questions and
answers on tax-
advantaged
computer
programs**

These Questions and Answers were released as part of the minutes of the National Sales Tax Liaison Committee (NSTLC) meeting on 2 October 1996.

Following the issue of Sales Tax Determination STD 96/5: *Calculation of tax payable on goods containing tax-advantaged computer programs*, the professional bodies represented on the NSTLC approached the ATO for clarification of some aspects of the Determination. A Sub-Committee of practitioners and ATO officers have resolved to clarify those issues by way of the following questions and answers.

In this section, 'the Determination' means Sales Tax Determination STD 96/5.

Question 1

Question: Where a taxpayer has established a separate 'off-the-shelf' wholesale selling price for software sold with hardware for one inclusive price, can that price be used as the value of the tax advantaged computer programs ('TACPs')?

Answer: While the off-the-shelf price will often be a good starting point, the ATO has not endorsed its use as a general rule, because packages of software and hardware are normally sold at a price that is discounted below the separate price of the components. Where a hardware and software package is discounted, the ATO expects to see the discount applied to both the hardware and software in proportion to the discount allowed for the package. For example, if hardware with a wholesale price of \$2,000 and TACPs with a wholesale price of \$500 are sold in a package for \$2,000, the discount from the sum of the individual prices is 20%. This discount is applied to both articles to produce a wholesale taxable value of \$1,600 for the hardware.

Furthermore, some off-the-shelf prices are based on very limited sales and, in other cases, the bundled software is not identical to that on which the off-the-shelf price is based. However, where:

- the off-the-shelf prices are based on a significant number of sales, and
- the bundled software is identical to the software sold off-the-shelf,

the off-the-shelf price can be used to determine the value of the tax advantaged computer program in packages of hardware and software not sold at a discount.

The methodology for determining the value of Original Equipment Manufacturer ('OEM') software (as described at page 7 of the Determination) is addressed separately in the answer to Question 3.

Question 2

Question: Where a taxpayer has not established separate wholesale selling prices for either the hardware or the software, but can determine the costs applicable to each of these, can they value the TACP using an equivalent markup between the hardware and TACPs?

Answer: Yes. A similar principle is endorsed in Sales Tax Ruling SST 6.

For example:

Total wholesale selling price		\$2000
hardware cost	\$1000	
TACPs cost	<u>\$200</u>	
Total cost	<u>\$1200</u>	

Therefore,

hardware taxable value	$1000/1200 \times$	$2000 =$	\$1667
TACPs value	$200/1200 \times$	$2000 =$	\$333

In preparing the Determination, costing information was provided by industry members and other experts in valuing TACPs. Cost calculations were made for a range of goods and these calculations showed that, as a general rule, less than 10% of the value of the total package was attributable to TACPs. Thus, 10% was used as the basis for the Safe Harbour provided for in the Determination.

Question 3

Question: Can a taxpayer use the Safe Harbour or any other method for OEM software?

Answer: OEM software is described at page 7 of the Determination. It is usually supplied under international agreements between software suppliers and hardware manufacturers at a heavily discounted price.

The Determination says that OEM software can be valued at its wholesale replacement cost or, if none is available, by using the Safe Harbour. In practice, the ATO will always accept the Safe Harbour figure, as the actual cost per unit of OEM software is generally determined on a settling day at some future date, even though taxpayers may know the (interim) agreed royalty rate set out in their licensing agreement.

Taxpayers can also use the valuation methodology outlined in Question 2, although the ATO believes that this will rarely be better than the Safe Harbour figure.

The valuation methodology in Question 1 cannot be used to value OEM software because it has certain restrictions that the off-the-shelf software does not have. These restrictions are reflected in lower acquisition and distribution costs for the OEM software compared to the otherwise equivalent off-the-shelf software product.

Question 4

Question: Where a taxpayer has not established wholesale selling prices or costs for either the hardware or TACPs, can they use competitors' equivalent prices?

Answer: No. In these circumstances the ATO accepts that TACPs may be valued using the applicable Safe Harbour methodology contained in the Determination. The figures obtained in drafting the Determination demonstrate that, on average, less than 10% of the total package of any goods is attributable to TACPs. Where taxpayers do not have access to such information they can still use the applicable Safe Harbour and, in most cases, this should still adequately cover the cost, plus wholesale markup.

Question 5

Question: Where a taxpayer's supplier has a TACP value approved by the ATO, can the taxpayer rely on that value when determining the value of the TACP component of the same goods sold by them by wholesale?

Answer: Where a taxpayer is aware that a supplier has a TACP value approved by the ATO, the taxpayer may apply to the ATO for a private ruling that relates to their trading circumstances. Having examined the original ruling, the ATO will be in a position to determine whether the circumstances surrounding the original ruling and those which apply to the taxpayer are equivalent. If so, a taxpayer could generally expect that a similar value will be approved by way of a private ruling to them based on their specific circumstances.

Taxpayers should also be aware that the reflection of a value for TACPs on a supplier's price list does not necessarily mean that that value has been approved by the ATO. In some cases it may be necessary for the ATO to make enquiries of the supplier in order to determine the basis for a particular valuation.

Question 6

Question: In the Determination, does *replacement cost* allow for a mark-up on cost?

Answer: The replacement cost valuation method referred to in the Determination refers to the amount that a wholesaler would charge a retailer for the TACPs, rather than the cost to the manufacturer, thus allowing a mark-up on cost. This is indicated in the following example provided in the Determination:

The replacement cost should be determined taking into account the terms of the agreement under which the particular TACP is supplied, for example, a wholesaler of goods who supplies a customer with a replacement TACP may use the arm's length wholesale replacement value for those particular goods.

The Safe Harbours provided in the Determination are based on the actual cost of the TACPs to a manufacturer or wholesaler, plus an average markup based upon an equivalent basket of goods in the same market at the same time of generally 100%.

Question 7

Question: If a taxpayer believes that they have exceptional circumstances and neither the Determination nor these questions and answers clarify their situation, what can they do?

Answer: While the Determination was intended to deal with the bulk of taxpayers' difficulties in relation to TACPs, exceptional circumstances, for example unique goods or high cost low demand technology goods, will still need to be dealt with on an individual basis. Taxpayers who sell these types of goods may seek a private ruling from the ATO, by completing the *Application for Private Ruling on Sales Tax*. Any ruling by the ATO will have protection for the purposes of *section 77* of the Act and may be relied upon by the person to whom it applies.

Commissioner of Taxation12 February 1997

Related Determinations: STD 95/2

Related Rulings: SST 6

Subject Ref: taxable value; the calculation of tax payable on goods containing tax-advantaged computer programs

Legislative Ref: STAA 77

ATO Ref: NAT 96/2606-9

ISSN 1323 - 7209