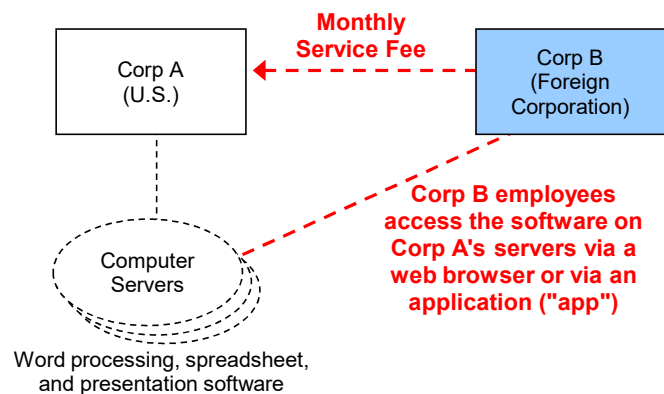


**Prop. Reg. 1.861-19(d),
Example 6**

**Online Word Processing, Etc. Via
Browser or App: Provision of Services**

Copyright © 2019 Andrew Mitchell LLC
International Tax Services
www.andrewmitchel.com

Corp A provides Corp B word processing, spreadsheet, and presentation software and allows employees of Corp B to access the software over the internet through a web browser or an application (“app”). In order to access the software from a mobile device, Corp B’s employees usually download Corp A’s app onto their devices. To access the full functionality of the app, the device must be connected to the internet. Only a limited number of features on the app are available without an internet connection. Corp B has no ability to alter the software code. The software is hosted on servers owned by Corp A and located at Corp A’s facilities and is used concurrently by other Corp A customers. Corp A is solely responsible for maintaining and repairing the servers and software, and ensuring continued functionality and compatibility with Corp B’s employees’ devices and providing updates and fixes to the software (including the app) for the duration of the contract with Corp B. Corp B pays a monthly fee based on the number of employees with access to the software. Upon termination of the arrangement, Corp A activates an electronic lock preventing Corp B’s employees from further utilizing the app, and Corp B’s employees are no longer able to access the software via a web browser.



This is a cloud transaction because Corp B obtains a non-de minimis right to on-demand network access.

The download of the app is a transfer of a computer program (suggesting that 1.861-18 could apply), but the app is de minimis in the context of the overall arrangement.

(A) Corp A's provision to Corp B of a non-de minimis right to on-demand network access to Corp A's computer hardware and software resources for the purpose of fully utilizing Corp A's software is a cloud transaction described in Reg. 1.861-19(b).

(B) Corp B has neither physical possession of nor control over Corp A's word processing, spreadsheet, and presentation software or computer hardware. Additionally, the servers and software are part of an integrated operation in which Corp A maintains the servers and updates the software. Corp A makes available its word processing, spreadsheet, and presentation software and servers to Corp B and other customers concurrently. Corp A's compensation, though based in part on the passage of time, is also determined by reference to Corp B's level of use (that is, the number of Corp B employees with access to the software). Taking into account all of the factors, the transaction between Corp A and Corp B is classified as the provision of services under Reg. 1.861-19(c).

(C) The provision of the app to Corp B's employees by download onto their devices would be a transfer of a computer program rather than a cloud transaction subject to Reg. 1.861-19(b). However, under Reg. 1.861-19(c)(3), it is necessary to consider whether that transfer is de minimis in the context of the overall arrangement and in light of the surrounding facts and circumstances. Here, the significance of the download of the app by Corp B's employees is limited by the fact that the device running the app must be connected to Corp A's servers via the internet to enable most of the app's core functions. The software that enables such functionality remains on Corp A's servers and is accessed through an on-demand network by Corp B's employees. Therefore, the download of the app is de minimis, and under Reg. 1.861-19(c)(3), the entire arrangement is classified as a service.