

A license of canned software is subject to Retailers' Occupation Tax liability if all of the criteria for an exempt license of canned software set out in 86 Ill. Adm. Code 130.1935(a)(1) are not met. See 86 Ill. Adm. Code 130.1935. (This is a GIL.)

April 2, 2009

Dear Xxxxx:

This letter is in response to your letter dated September 29, 2008, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

We are seeking a ruling on the taxability of our computer software and related services in relation to your ruling 130.1935 which we have read. We have called for clarification and received conflicting answers to the taxability of our particular software products and therefore at the suggestion of your tax specialist, seek a letter ruling from your department.

A. Our Financial Compass Software

This computer software was developed specifically for Banks. We have a written agreement with them that they will not copy or transfer this to a third party. We set up this software for them and deliver it to them electronically. Throughout the duration of the licensing agreement, we maintain the functionality of the 'Financial Compass System', train their representatives who will operate the system and give continuing support to explain the methods and meaning of the simulations and analyses and use of the system. Should they discontinue the licensing agreement, the software will no longer function.

Please rule on the taxability of th [sic] this system including the Monthly Licensing and support fees (p1), and the installation charge (p2) relating to this regulation 130.1935.

It is further our assumption that the supplementary ancillary products and module enhancements available (see attached agreement) will follow the taxability of the main items mentioned above. Please advise [sic] if this is not the case.

I have attached a copy of our licensing agreement for your review.

We are also seeking a ruling in relation to ruling 130.1935 on our non tangible web based products shown below and discussed further in detail on the attached agreement and attached supplementary product briefs.

- B. PRODUCT A. This is a web based management tools [sic] that draws on the Financial Compass database for a graphic presentation of the banks [sic] position, trend and projections. Details on this are also included in the attached agreement (p4).
- C. PRODUCT B - This web based program allows the customer to create a report establishing a reasonable estimate of margin and equity risk based on analyses using historical PRODUCT. Please see the attached product brief (p7) for further details.

If you have any questions, please feel free to call our office. Thank you for your assistance in this matter.

#### **DEPARTMENT'S RESPONSE:**

The Private Letter Ruling Committee recently determined that it will no longer issue Private Letter Rulings regarding whether a specific license of prewritten (canned) computer software meets the requirements of subsection (a)(1) of 86 Ill. Adm. Code 130.1935. It is the Private Letter Ruling Committee's position that its regulation at 86 Ill. Adm. Code 130.1935 is sufficiently clear for a licensee or licensor to determine whether a specific license of prewritten computer software meets the requirements of subsection (a)(1) of that rule.

The Illinois Retailers' Occupation Tax Act imposes a tax upon persons engaged in this State in the business of selling tangible personal property to purchasers for use or consumption. See 86 Ill. Adm. Code 130.101. In Illinois, Use Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. See 86 Ill. Adm. Code 150.101. These taxes comprise what is commonly known as "sales" tax in Illinois.

Illinois Retailers' Occupation and Use Taxes do not apply to sales of service that do not involve the transfer of tangible personal property to customers. However, if tangible personal property is transferred incident to sales of service, this will result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon his activities. For your general information see 86 Ill. Adm. Code 140.101 through 140.109 regarding sales of service and Service Occupation Tax. Services that involve the transfer of tangible personal property (such as, for example, written reports, other tangible media and training manuals) incident to a sale of service may be subject to either Service Occupation Tax liability or Use Tax liability.

Information or data that is electronically transferred or downloaded is not considered the transfer of tangible personal property in this State. See 86 Ill. Adm. Code 130.2105(a)(3). However, canned computer software is considered taxable tangible personal property regardless of the form in

which it is transferred or transmitted, including tape, disc, card, electronic means or other media. See 86 Ill. Adm. Code 130.1935. If the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. See Section 130.1935(c).

Custom computer programs or software are prepared to the special order of the customer. The selection of pre-written or canned programs assembled by vendors into software packages does not constitute custom software unless real and substantial changes are made to the programs or creation of program interfacing logic. See Section 130.1935(c)(3).

If transactions for the licensing of computer software meet all of the criteria provided in Section 130.1935(a)(1), neither the transfer of the software or the subsequent software updates will be subject to Retailers' Occupation Tax. A license of software is not a taxable retail sale if:

- A) It is evidenced by a written agreement signed by the licensor and the customer;
- B) It restricts the customer's duplication and use of the software;
- C) It prohibits the customer from licensing, sublicensing or transferring the software to a third party (except to a related party) without the permission and continued control of the licensor;
- D) The licensor has a policy of providing another copy at minimal or no charge if the customer loses or damages the software, or permitting the licensee to make and keep an archival copy, and such policy is either stated in the license agreement, supported by the licensor's books and records, or supported by a notarized statement made under penalties of perjury by the licensor; and
- E) The customer must destroy or return all copies of the software to the licensor at the end of the license period. This provision is deemed to be met, in the case of a perpetual license, without being set forth in the license agreement.

Please note that acceptance of a software license agreement by clicking "accept" while online is not considered "acceptance" sufficient enough to constitute a written agreement signed by the licensor and the customer for purposes of subsection (a)(1)(A) of Section 130.1935.

Charges for updates of canned software are fully taxable pursuant to Section 130.1935. If the updates qualify as custom software under Section 130.1935(c), they may not be taxable. But, if maintenance agreements provide for updates of canned software, and the charges for those updates are not separately stated and taxed, then the whole agreement would be taxable as sales of canned software.

Assuming that any services provided, such as installation, phone support, training, and seminars, do not require the transfer of tangible personal property to the recipients of those services, charges for such services are exempt if they are separately stated from the selling price of canned software. See Section 130.1935(b). If computer software training or other support services are provided in conjunction with a sale of custom computer software or a license of computer software, the charges for that training are not subject to tax.

Please note that the Department had been holding letter ruling requests that may involve computer software Application Service Providers (ASPs), software hosting and web-based software products. We have determined that the proper forum to determine the appropriate taxation of these types of arrangements is through a formal administrative rulemaking process rather than on a case-by-case basis through individual inquiries.

I hope this information is helpful. If you require additional information, please visit our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters  
Associate Counsel

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