

This letter concerns the taxation of computer software transactions. See 86 Ill. Adm. Code 130.1935. (This is a GIL.)

August 22, 2011

Dear Xxxxx:

This letter is in response to your letter dated November 23, 2010, 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 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:

I am requesting your help to determine the sales taxability of services my company furnishes to our clients. The following services are described below:

BILLABLE SERVICE CALL. A service that is outside of the client's original support contract. When a client calls in and needs assistance outside of the parameters outlined in their support contract, COMPANY bills the client per hour of support. There are no tangible materials exchanged during this process.

CUSTOM PROGRAMMING. A service that provides new features/functionality, reporting, or interfaces that are unique to a business and/or specifically requested by a business using software development to address the need. The solution is generally developed for a single customer, designed to their specifications. There is no tangible material exchanged during this process as any software updates are provided to the client via [sic] or ftp site.

INTEGRATION. A service that involves the development of process to allow two or more applications to function together, exchanging information and taking appropriate actions based on the exchange. There is no tangible material exchanged during this process.

CONSULTATION. The service whereby an analyst or subject matter expert reviews an operation or need and provides feedback as to alternative approaches to achieve either improvement or a solution to the need. There are no tangible materials exchanged during this process as any reports provided to the client are sent electronically through email or ftp site.

SOFTWARE. A canned product that has already been developed and is resold by COMPANY. The product is designed to perform all of the tasks needed to collect money. There are no tangible materials exchanged during this process as any reports provided to the client are sent electronically through email or ftp site.

SUPPORT. An additional service that is offered to the client and is not tied to the software or the original contract. A Support Agreement is designed to provide answers to the most commonly asked questions from end users of the software or provide resolutions that exist in a knowledge base to those of a more complex nature. There is no tangible material exchanged during this process.

TRAINING. A service that allows users to gain the knowledge, skills, and competencies they need to excel at their position. This is as a result of the teaching of vocational or practical skills and knowledge that relate to specific useful competencies. Training is provided through three facets. First is Online Training (E-Learning) where the client is located at their office and a COMPANY trainer is connected remotely. On-Site education involves the COMPANY trainer traveling to the client's location and training in-person. The third is training at COMPANY where the client travels to COMPANY's offices to train in-person. In each instance, the trainer provides a tangible training guide for the client's reference.

We would appreciate your time and effort to respond to our taxability questions. If you need further clarification as to the products and services described above, please do not hesitate to contact me.

DEPARTMENT'S RESPONSE:

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 nor 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 nontaxable custom computer software or a nontaxable license of computer software, the charges for that training are not subject to tax, regardless of whether they are separately.

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

Sincerely,

Samuel J. Moore
Associate Counsel

SJM:msk