ST 20-0002-PLR 03/03/2020 SALE FOR RESALE

This letter discusses certificates of resale. *See* 86 Ill. Adm. Code 130.1405. (This is a PLR.)

March 3, 2020

Dear Xxxx:

This letter is in response to your letter dated September 20, 2019, in which you requested 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.

Review of your request disclosed that all the information described in paragraphs 1 through 8 of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY, for the issue or issues presented in this ruling, and is subject to the provisions of subsection (e) of Section 1200.110 governing expiration of Private Letter Rulings. Issuance of this ruling is conditioned upon the understanding that neither COMPANY, nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request. In your letter you have stated and made inquiry as follows:

> As counsel for, and on behalf of COMPANY, pursuant to 2 Ill. Admin. Code §1200.110, we hereby formally request a Private Letter Ruling ("PLR") from the Illinois Department of Revenue ("Department"), confirming that, based upon the representations below.
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> COMPANY is not currently under audit by the Department regarding this issue. COMPANY is not aware of any authority contrary to the views expressed in this PLR request. Furthermore, we ask that COMPANY's name, address, and any contracts which are attached or subsequently provided to the Department be kept confidential and deleted from the publicly disseminated version of a PLR issued in response to this request. A power of attorney authorizing my and NAME's representation of COMPANY before the Department in connection with this PLR is attached as Exhibit A.
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> **I. Facts**
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> Pursuant to Ill. Admin. Code §1200.110(b), COMPANY makes the following representations:
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> - COMPANY is a STATE corporation.

- COMPANY focuses on the integration of business insight and technical invention. COMPANY creates business value for clients and solves business problems through integrated solutions that leverage information technology with knowledge of business processes.

- COMPANY also has an ecosystem of Business Partners with the capabilities and capacity to deliver high value solutions to end customers. COMPANY utilizes its channel of Business Partners to resell COMPANY products and services and in the case of COMPANY programs, Business Partners may acquire the right to remarket COMPANY licensed programs to end user customers. Business Partners establish their own prices to the end user customer.

- COMPANY enters into agreements with various distributors and unrelated third parties ("Business Partners") who are thereby enabled to remarket COMPANY Products and Services.

    - An COMPANY Service is defined as a performance of a task, provision of advice and counsel, assistance, support or access to a resource (such as an information database) that COMPANY may approve its remarketers to market.

    - An COMPANY Product is defined as a machine or program. A "Program" is defined as: "the following including the original and all whole or partial copies: a. machine-readable instructions and data; b. components; c. audio-visual content; and d. related licensed materials. The term "Program' includes any COMPANY Program, or non- COMPANY Program that COMPANY may approve its remarketer to market.

    - This letter ruling request only addresses the tax treatment of "Programs" (i.e. COMPANY software).

- In general, the Business Partner Agreement grants authority to the Business Partner – Distributor to remarket Programs to remarketers. The Business Partner Agreement identifies the specific Programs that a Business Partner – Distributor can remarket.

- The Program is obtained by the end user primarily by electronic delivery.

- The Programs marketed by the Business Partners require COMPANY license agreements to be agreed to by the end user. In those instances, the possessor of the Program, e.g. the end user, will be granted a license. (hereinafter referred to as "Licensee").

- The COMPANY license agreements are direct terms between COMPANY and the License.

- Specific Facts:

- COMPANY has Business Partners who are authorized to remarket the Programs to other remarketers who in turn remarket the Programs to Licensees who are located in Illinois.

- For purposes of this PLR, the Business Partner – Distributor is referred to as ABC.

- ABC is headquartered outside of Illinois.

- COMPANY enters into a Business Partner Agreement ("BPA") with ABC which grants ABC the right to actively remarket Programs as a COMPANY Business Partner – Distributor.

- ABC is not approved to remarket to the end user. Instead, ABC is permitted to remarket Programs to other remarketers who in turn remarket to end users.

- ABC sets the price of the Program to be remarketed to their remarketers.

- The remarketer then remarkets the Program to the end user. COMPANY licenses the Program to the end user directly using a license agreement between COMPANY and the end user. The Program is subject to the AGREEMENT ("AGREEMENT") and its applicable DOCUMETNS. A Program may be subject to additional program license acquisition terms.

- The AGREEMENT is the license agreement which governs the Licensee's permitted use of the Program.

- ABC never enters into a license agreement with COMPANY, nor does COMPANY give ABC authorization to enter into sublicense agreement with COMPANY, nor does COMPANY give ABC authorization to enter into sublicense agreements with remarketers or end users under the Business Partner Agreement.

- ABC remarkets Programs to other remarketers who remarket the Programs to Licensees located in Illinois, including CITY.

- COMPANY does not receive payment directly from the Licensee (end user). Instead, COMPANY invoices ABC, ABC then invoices the remarketer, and the remarketer invoices the end user.

- COMPANY receives payment from ABC.

- Pertinent provisions of the Business Partner Agreements, related Attachments, and applicable license agreements are the following:

  - ABC remarkets COMPANY Programs to remarketers on an equitable basis.

- ABC is free to set its own prices regarding COMPANY Programs that it remarkets.

- ABC does not license the Programs from COMPANY.

- ABC "fulfills" valid Program orders from remarketers. Practically, this means that ABC provides the end user's data to COMPANY so that COMPANY can provide the COMPANY license for the relevant Program to Licensee (end user).

- In the event of an eligible refund, ABC and remarketer are responsible to process the refund to the Licensee under certain terms.

- COMPANY's and ABC's Business Partner current agreement is evidenced by a wet ink signature. However, as previously stated above, the Business Partner Agreement does not contain a license for ABC's use of Programs.

- The Licensee enters into the AGREEMENT license agreement and any applicable LI documents with COMPANY and is subject to the terms and conditions.

- The AGREEMENT and any applicable LI documents that are entered into between COMPANY and the Licensee are not evidenced by a wet ink signature of the Licensee. Rather, the Licensee agrees to the license terms and conditions by "clicking to accept" or "clicking to acknowledge."

II. Question Presented

Does COMPANY's licensing agreement with the end user satisfy the first prong of the Illinois five-part test as prescribed by 86 Ill. Admin. Code 130.1935(a)(1)(A)? If not, is the transaction a taxable sale subject to the Illinois retailer's occupation tax?

III. Illinois Law

Computer software is statutorily defined as tangible personal property and its sale or use is taxable in Illinois. 35 ILCS 120/2. "Computer software" is defined as:

> A set of statements, data, or instructions to be used directly or indirectly in a computer in order to bring about a certain result in any form in which those statements, data, or instructions may be embodied, transmitted, or fixed, by any method now known or hereafter developed, regardless of whether the statements, data, or instructions are capable of being perceived by or communicated to humans, and includes prewritten or canned software that is held for repeated sale or lease, and all associated documentation and materials, if any, whether contained on magnetic tapes, discs, cards, or other devices or media…

35 ILCS 120/2-25. "Computer software" includes all types of software including operational, applicational, utilities, compliers, templates, shells and all other forms. 86 Ill. Admin. Code § 130.1935(a).

A license of computer 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 of 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.

86 Ill. Admin. Code § 130.1935(a)(1). If a transfer of software meets the five-part test, the transfer is not a sale subject to the Retailers' Occupation Tax.

While it is very common for software to be licensed over the internet and for the customer to check a box that states that he or she accepts the license terms, it is the Illinois Department of Revenue's position that such an acceptance does not constitute an acceptance for purposes of 86 Ill. Admin. Code § 130.1935(a)(1)(A). Illinois Gen. Info. Letter No. ST 12-0011-GIL, 2/29/12. To meet the signature requirement for an exempt software license, the agreement must contain the written signature of the licensor and customer. The signature must be an ink signature or an electronic signature. If a transfer of software does not meet the signature requirement, the transfer is a sale subject to the Retailers' Occupation Tax. *Id*.

IV. Authorities

We have reviewed all relevant Illinois tax status, regulations and administrative opinions issued by the Department but were unable to locate authority directly on point. However, the cited authority supports the position advocated by COMPANY and we did not locate any authority contrary to the position advocated by COMPANY.

V. Discussion/Analysis

The Department has stated on numerous occasions that software licenses over the internet requiring the customer to check a box that states he or she accepts the license

terms does not constitute a written agreement signed by the licensor and the customer for purposes of 86 Ill. Admin. Code 130.1935(a)(1)(A). The Department has previously indicated that to meet the signature requirement for an exempt software license, the agreement must contain the written signature of the licensor and customer. Ill. Gen Info. Letter No. ST 12-0011-GIL (2/29/12). However, the Department has more recently determined that an electronic license agreement in which the customer accepts the license by means of a signature in electronic form that is attached to or is part of the license, is verifiable, and can be authenticated will comply with the requirement of a written agreement signed by the licensor and customer. Ill. Gen. Info. Letter No. ST 18-0003 (2/28/18). A license agreement in which the customer electronically accepts the terms by clicking "I agree" does not satisfy the first prong of the five-part test.

Here, the AGREEMENT and related LI documents contain the license terms and conditions which governs the Licensee's permitted use of the COMPANY Program. While ABC provides the end user's data to COMPANY which enables COMPANY to provide the relevant Program license to the Licensee, ABC never enters into, or signs a license agreement with COMPANY. Conversely, the Licensee accepts the terms and conditions of the AGREEMENT and any applicable LI documents with COMPANY by "clicking to accept" or clicking to acknowledge" the terms and conditions of the applicable license agreement. Notably, the AGREEMENT and any applicable LI documents which are entered into between COMPANY and Licensee are not evidenced by a wet signature of the Licensee.

The Department recently examined the issue of whether multiple documents could be considered together to meet the signature requirement. *See* Ill. Private Letter ST 18-0003 (2/28/18). In that ruling, the company provided its customers with two documents, an order form and a licensing agreement. Read together the document contained the full licensing contract, however only the order form had a wet signature. The company argued that the two documents should satisfy 86 Ill. Admin. Code § 130.1935(a)(1)(A) because of the operation of the doctrine of incorporation by reference and because the signed order form creates the contract. Applying the legal doctrine "incorporation by reference", the Department ruled that "[w]henever an order form incorporates terms and conditions from another document, the Department will review the order form and the document that is incorporated by the order form to determine if all the requirements of Section 130.1935(a)(1) have been met."

In this instance, however, the AGREEMENT and LI documents containing the applicable licensing terms and conditions is exclusively entered into between COMPANY and the end user Licensee. ABC and the end user are unrelated third parties and COMPANY does not enter into any licensing agreement with ABC. Any agreement between COMPANY and ABC, even though evidenced by a wet signature, cannot be incorporated by reference into the AGREEMENT and any applicable LI documents entered into between COMPANY and the Licensee to satisfy the requirements of Section 130.1935(a)(1). Accordingly, the relations between COMPANY and ABC and the Licensee is distinguishable from the parties' relationship in PLR ST18-0003 because there, the party who accepted the purchase order with a wet signature was the same party who entered into the license agreement with a "click to accept." Conversely here, there are at least three parties involved in the relevant transaction, and ABC, the Business Partner, does not enter into the AGREEMENTS or any LI

document with COMPANY. Instead, the Business Partner Agreement permits ABC the right to actively market Programs to third parties. Because the licensing agreement between COMPANY and the end user is electronically accepted or acknowledged by clicking a box, the agreement does not constitute a written agreement signed by the licensor and customer as required under Section 130.1935(a)(1)(A).

Additionally, while COMPANY enters into the AGREEMENT and DOCUMENTS documents with the Licensee, it never receives payment directly from the Licensee for its use of the COMPANY Program. Instead, COMPANY invoices ABC, ABC invoices any applicable remarketers, and the remarketers invoice the Licensee. In accordance with this payment structure, ABC and the applicable remarketers are free to set their own prices of the Programs which are marketed. This is relevant because COMPANY is unaware of the remarketer's selling price of the COMPANY Programs to the Licensee. Accordingly, COMPANY only receives compensation for the sale of its Programs from ABC. Thus, because part one of the five-part test is not met, the sale of COMPANY Programs is subject to Illinois retailers' occupation tax, and the measurable tax base is COMPANY's selling price of the COMPANY Program to ABC.

VI. Conclusion

In conclusion, COMPANY's license agreement with the Licensee does not constitute a written agreement signed by the licensor (COMPANY) and the customer (ABC) under 86 Ill. Admin. Code 130.1935(a)(1)(A) and the transaction is therefore a taxable sale subject to the Illinois retailers' occupation tax. COMPANY should collect Illinois retailer's occupation tax from ABC based on the selling price of the COMPANY Program to ABC, or if applicable, collect a properly completed ABC Illinois resale certificate. Copies of the relevant referenced agreements are available upon the Department's request. Finally, should the Department not be able to issue the PLR as requested, we request a meeting to discuss the matter.

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. 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. If the purchases occur in Illinois, the purchasers must pay the Use Tax to the retailer at the time of purchase. The retailers are then allowed to reduce the amount of Use Tax they must remit by the amount of Retailers' Occupation Tax liability which they are required to and do pay to the Department with respect to the same sales. See 86 Ill. Adm. Code 150.130.

Computer Software

"'Computer software' means a set of statements, data, or instructions to be used directly or indirectly in a computer in order to bring about a certain result in any form in which those statements, data, or instructions may be embodied, transmitted, or fixed, by any method now known or hereafter developed, regardless of whether the statements, data, or instructions are capable of being perceived

by or communicated to humans, and includes prewritten or canned software." 35 ILCS 120/2-25. Generally, sales of "canned" computer software are taxable retail sales in Illinois. Canned computer software is considered to be tangible personal property regardless of the form in which it is transferred or transmitted, including tape, disc, card, electronic means, or other media. 86 Ill. Adm. Code 130.1935. However, if the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. 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 86 Ill. Adm. Code 130.1935(c)(3). Computer software that is not custom software is considered to be canned computer software.

If transactions for the licensing of computer software meet all of the criteria provided in subsection (a)(1) of Section 130.1935, 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.

If a license of canned computer software does not meet all the criteria the software is taxable.

In order to comply with the requirements as set out in Section 130.1935(a)(1), there must be a written "signed" agreement. A license agreement in which the customer electronically accepts the terms by clicking "I agree" does not comply with the requirement of a written agreement signed by the licensor and customer. The Department previously held that an electronic signature did not comply with the requirement of Section 130.1935(a)(1)(A) that the license be evidenced by a written agreement signed by the licensor and the customer. ST 06-0005-PLR (December 16, 2006). In ST 18-0003-PLR (February 8, 2018), the Department decided that an electronic license agreement in which the customer accepts the license by means of a signature in electronic form that is attached to or is part of the license, is verifiable, and can be authenticated will comply with the requirement of a written agreement signed by the licensor and customer. See ST 18-0010-PLR (September 26, 2018) for examples of acceptable written signatures. A license agreement in which the customer electronically accepts the terms by clicking "I agree" remains unacceptable.

Sales for Resale

In order to document the fact that its sale to Purchaser is a sale for resale, Company is obligated by Illinois to obtain a valid Certificate of Resale from Purchaser. See 86 Ill. Adm. Code 130.1405. A Certificate of Resale is a statement signed by the purchaser that the property purchased by him is purchased for purposes of resale. In addition to the statement that the property is being purchased for resale, a Certificate of Resale must contain:

1) The seller's name and address;

2) The purchaser's name and address;

3) A description of the items being purchased for resale;

4) Purchaser's signature, or the signature of an authorized employee or agent of the purchaser, and date of signing; and

5) Registration Number, Resale Number, or a statement that the purchaser is an out-of-State purchaser who will sell only to purchasers located outside the State of Illinois.

The Department provides a standard form for documenting sales for resale (Form CRT-61 Certificate of Resale). This form can be obtained from the Department's website.

The obligations of a seller with respect to accepting a Certificate of Resale were addressed in *Rock Island Tobacco and Specialty Company v. Illinois Department of Revenue*, 87 Ill.App.3d 476, 409 N.E.2d 136, 42 Ill. Dec. 641 (3rd Dist. 1980). The *Rock Island* court held that when a retailer obtains a proper Certificate of Resale that contains a registration or resale number that is valid on the date it is given, the retailer's liability is at an end. If the purchaser uses that item himself or herself (i.e., it was not purchased for resale), the Department will proceed against the purchaser, not the retailer, provided the above stated conditions are met. The purchaser's registration or reseller number can be verified at the Department's website by clicking on the "Tax registration inquiry" box.

Failure to present an active registration number or resale number and a certification to the seller that a sale is for resale creates a presumption that a sale is not for resale. This presumption may be rebutted by other evidence that all of the seller's sales are sales for resale or that a particular sale is a sale for resale. For example, other evidence that might be used to document a sale for resale, when a registration number or resale number and certification to the seller are not provided, could include an invoice from the purchaser to his customer showing that the item was actually resold, along with a statement from the purchaser explaining why it had not obtained a resale number and certifying that the purchase was a purchase for resale in Illinois. The risk run by a retailer in accepting such other documentation and the risk run by purchasers in providing such other documentation is that an Illinois auditor is more likely to require that more information be provided as evidence that the particular sale was, in fact, a sale for resale.

It is the Department's understanding that COMPANY sells canned computer software to ABC, and the agreement between COMPANY and ABC does not meet the license requirements of Section 130.1935(a)(1). COMPANY must pay Retailers' Occupation Tax and collect Use Tax on its sales of computer software to ABC unless COMPANY receives a resale certificate from ABC.

I hope this information is helpful. If you have further questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters
Chairman, Private Letter Ruling Committee

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