ST 24-0003-PLR 09/26/2024 COMPUTER SOFTWARE

A provider of software as a service is acting as a serviceman. If the provider does not transfer any tangible personal property to the customer, then the transaction generally would not be subject to Retailers' Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax. If the provider transfers to the customer an API, applet, desktop agent, or a remote access agent to enable the customer to access the provider's network and services, it appears the subscriber is receiving computer software that is subject to tax. See 86 Ill. Adm. Code Parts 130 and 140. (This is a PLR.)

September 26, 2024

NAME
COMPANY
ADDRESS

Dear NAME:

This letter is in response to your letter dated April 16, 2024, 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 https://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 COMPANY1 (d/b/a COMPANY2, 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 COMPANY1, 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:

We are requesting a private letter ruling on behalf of COMPANY1 (d/b/a COMPANY2) (the "Taxpayer" or "COMPANY2"), a STATE corporation,

pursuant to Ill. Admin. Code tit. 2, § 1200.110. (A copy of Form IL-2848, *Power of Attorney,* authorizing this Firm to represent the Taxpayer was filed with the Illinois Department of Revenue on April 16, 2024, via facsimile transmission to PHONE and is attached hereto as *Exhibit "A."*)

The Taxpayer remotely provides connectivity solutions to facilitate the process of
laboratory testing, as well as obtaining and sharing laboratory results for laboratories located across the country, including laboratories in Illinois. The essence of the Taxpayer's services is best characterized as data processing, data translation and data exchange services. Recently, the Taxpayer's gross receipts from sales of services into Illinois have exceeded the $100,000 threshold, which threshold is sufficient for the Taxpayer to create a substantial economic nexus with Illinois. However, the Taxpayer believes that none of the services it provides to Illinois customers are subject to either *(i)* the Illinois retailers' occupation and use tax; or *(ii)* the Illinois service occupation and service use tax. Thus, we respectfully request, on behalf of the Taxpayer, that the Illinois Department of Revenue (the "Department") rule on whether the Taxpayer's services, which services process and translate laboratory test results and that allow various customers' software systems to communicate with each other, are services that are exempt from Illinois retailers' occupation and use tax and Illinois service occupation and service use taxes.

A. TAXPAYER INFORMATION AND STATEMENTS RELATED TO REQUEST

1. TAXPAYER INFORMATION

The Taxpayer interested in this matter is set forth below, along with its mailing address, telephone number, taxpayer identification number, and state of incorporation. The Taxpayer reports on a calendar year basis, and it uses the accrual method of accounting.

Taxpayer:
COMPANY1
(d/b/a COMPANY2)
c/o NAME
COMPANY
STATEADDRESS
Telephone: PHONE1
EIN: NUMBER
State of Incorporation: STATE

2. Ill. Admin. Code tit. 2, § I200.l l0(b)(3) requires that the Taxpayer identify the tax period at issue. The Taxpayer is not currently registered for Illinois sales and use tax purposes because it believes that none of its product offerings remotely provided to Illinois customers is subject to Illinois sales or use taxes. Given that this Private Letter Ruling Request pertains to the taxability of the Taxpayer's product offerings in general, there is no specific tax period at issue.

3. In accordance with Ill. Admin. Code tit. 2, § 1200.110(b)(3), the Taxpayer and its representatives hereby represent that, the Taxpayer has not been contacted by the State of Illinois, the Multistate Tax Commission or any other agent thereof for purposes of an audit concerning any Illinois state tax obligation. As such, at the time of this Private Letter Ruling Request, ***no*** identical issue is involved in the Taxpayer's return for an earlier period, and that ***no*** issue is being examined as a part of any Department audit or is pending in litigation in a case involving the Taxpayer or a person related to the Taxpayer in which the Department is named as a plaintiff or defendant.

4. In accordance with Ill. Admin. Code tit. 2, § 1200. l 10(b)(4), the Taxpayer and its representatives hereby represent that, to the best of the knowledge of the Taxpayer and its representatives: *(i)* the Department has not previously ruled on the same or a similar issue for the Taxpayer or its predecessor; and *(ii)* neither the Taxpayer nor any of its representatives previously submitted the same or a similar issue to the Department but withdrew it before a letter ruling was issued.

5. In accordance with Ill. Admin. Code tit. 2, § 1200.110(a)(3)(D), the Taxpayer and its representatives hereby represent that they have reviewed all relevant Illinois tax statutes, regulations and administrative opinions issued by the Department, but were unable to locate authority that is dispositive of the subject of this Private Letter Ruling Request and that directly addresses the taxation of offerings furnished by the Taxpayer to its Illinois customers.

6. In accordance with Ill. Admin. Code tit. 2, § 1200.110(b)(6), the Taxpayer and its representatives hereby represent that they have reviewed all relevant Illinois tax statutes, regulations, and administrative opinions issued by the Department, but were unable to locate authority claiming that the types of offerings furnished by the Taxpayer to its Illinois customers are subject to taxation.

B. STATEMENT OF FACTS

The Taxpayer is a STATE-based service corporation (copies of the Taxpayer's Certificate of Incorporation, By-laws, and Certificate of Renewal of Alternate Name are attached hereto as ***Exhibits "B," "C", and "D"***) that has developed proprietary software to facilitate the process of laboratory ("lab") testing, obtaining lab results and sharing the lab results with physician practices and patients. The proprietary software furnishes a connectivity solution to order and collect lab tests from laboratories ("Labs"), to timely and securely receive such test results by physician practices, and to quickly and securely share such results with the practices' patients. The software is capable of electronic interconnectivity, and the essence of the Taxpayer's services is the combination of data processing, data translation, data hosting and data exchange services (sometimes collectively referred to as the "Data Processing Services").

The Taxpayer's proprietary software and other software are stored in the Taxpayer's data centers located exclusively in STATE. STATE is the place in which the Taxpayer hosts and maintains its own infrastructure to provide the Data Processing Services. This infrastructure includes hardware *(e.g.,* multiple servers) and multiple types of other software necessary to support, manage and process lab test results and dataflow from Labs to the Labs' customers, which customers are generally physician practices and physicians. Depending on the software that the physician practices use to manage and store patient healthcare records, the Taxpayer's Data Processing Services are provided via the following two types of connections: *(i)* the Electronic Medical Record ("EMR") connections; and *(ii)* the COMPANY2Portal connections. A detailed dataflow spreadsheet (the "Dataflow Spreadsheet") describing each step of the dataflow is attached hereto as ***Exhibit "E."***

1. DATAFLOW SUMMARY. The dataflow includes the following participants, in addition to the Taxpayer: *(i)* Labs; *(ii)* physician practices; *(iii)* patients; and *(iv)* in the case of the EMR connections, EMR vendors (the "Dataflow Participants"[1], and can be briefly summarized as follows:

Step #1: Each Lab collects lab tests via its own laboratory information software ("LIS").

Step #2: The collected data is conveyed to the Taxpayer's STATE servers where the data is processed, combined with proprietary codes ("translated") in order to be readable by other software systems,

[1] Although the Taxpayer is also a participant of the dataflow, for purposes of this Private Letter Ruling Request, the term "Dataflow Participants" does not include the Taxpayer.

and hosted for further delivery to the end users. Note that the above-described Step #1 and Step #2 are similar for both types of connections, the EMR connections and the COMPANY2 Portal connections.

Step #3: The processed data is delivered to either EMR vendors (in the case of the EMR connections) or physician practices, and, in some cases, to patients themselves (in the case of the COMPANY2 Portal connections). As described below, the essence of the Taxpayer's services rendered via the EMR connections and the COMPANY2 Portal connections is the same. However, there is a slight difference as to how the lab test results are ultimately displayed to the physician practices and patients.

(i) EMR Connections. As noted *supra,* the delivery of the processed lab test results to the Lab's customers *(i.e.,* physician practices) for display depends upon the software that the physician practices use to manage and store patient lab test results. Some physician practices use EMR software, which they separately purchase from various EMR vendors. Generally, an EMR system purchased by a physician practice is not immediately compatible with the relevant Lab's LIS. Thus, the Taxpayer has to map or configure each Lab's LIS to the respective physician practice's EMR system.

The Taxpayer deals with hundreds of physician practices across the country. Accordingly, each physician practice could have a different EMR system. Also, there are hundreds of EMR vendors located throughout the U.S. Thus, in order to deliver the required lab test results from a Lab's system *(i.e.,* LIS) to a physician practice in the most expedient and secure manner, the Taxpayer must "translate" or manipulate the Lab's test codes and results (data) such that they can be read by that physician practice's EMR system. Once "translated," the data is then pushed to the relevant EMR software, and the EMR vendor (not the Taxpayer) transfers it to the physician practice. Simply stated, the essence of the Taxpayer's services via the EMR connections is to: *(i)* process data received from its customers via "translation" and other data manipulation so that the physician practice's EMR system can read and understand it; and *(ii)* electronically transfer, or push, the lab test results between two systems, the Lab's LIS and the EMR vendor's system.

The Subscriber Data Processing Agreement (the "Subscriber Agreement") between the Taxpayer and each Lab (a sample of which is attached hereto as *Exhibit "F")* does not authorize the retail sale of software. Under the Subscriber Agreement, the Taxpayer does not issue a license to the software. Notably, none of the Dataflow Participants can have any access or rights to use or control the Taxpayer's software

system. Consequently, none of the Dataflow Participants can install, download or transfer any of the Taxpayer's software or applications to their computers. In fact, each Dataflow Participant has its own software and applications purchased from third-party vendors: each Lab uses its own LIS system, while each physician practice uses its own EMR software supplied by its respective EMR vendor. The Taxpayer owns, operates, and maintains the software applications, as well as the servers (all located in STATE) that support the application software. Thus, none of the Dataflow Participants has any control over the network, servers, operating systems, storage or application capabilities of the Taxpayer. In essence, the Taxpayer's personnel and the Taxpayer's system only process the data and push the processed data between the Lab's LIS and the EMR vendor's software.

(ii) COMPANY2 Portal Connections. Some physician practices use the COMPANY2 Portal, a cloud-based platform housed in the Taxpayer's STATE data center, to access lab test result data. For physician practices, such access is accomplished via the COMPANY2 Provider Portal to securely access for display the remotely stored lab test results via the internet using HTTPS (Hyper Text Transfer Protocol Secure) or SSL (Secure Sockets Layer). Physician practices can also remotely place Lab orders (in a preset format) to the COMPANY2 Portal. Also, the COMPANY2 Portal permits the patients to remotely access for display their lab test results via a HIPAA and CLIA compliant Patient Access Portal, which is simply a separate feature of the COMPANY2 Portal. The Patient Access Portal can be remotely accessed via the internet (using HTTPS/SSL).

Furthermore, the Taxpayer developed: *(i)* a mobile physician application (the "Physician App"); and ***(ii)*** a mobile patient application (the "Patient App," or collectively the "Apps"), which Apps function as the COMPANY2 Provider Portal and the Patient Access Portal, respectively. Although the Taxpayer so far has ***not*** had any customers in Illinois utilizing the Apps, physician practices and patients have an option to download their respective Apps to a personal device, such as a phone, table, *etc.* The Apps are hosted on the Taxpayer's servers located in STATE and are publicly available for download, free of charge, via the COMPANY2 Portal or Apple's "App Store." The Taxpayer does not provide any of its Dataflow Participants with a personal device ***(****i.e.,* tablet or cell phone) for use with the Apps; nor does it provide any other tangible personal property. Both the Physician Apps and the Patient Apps merely provide an alternative means of accessing Lab test results for the sole purpose of viewing them, and in the case with the Physician Apps, to order Lab test results by completing pre-coded fields. The Apps have no function or purpose other than to display lab test results (and, as

applicable, completing the Lab orders) and therefore have no separate value apart from the Apps' relationship to COMPANY2's Data Processing Services. Importantly, Labs do not use the COMPANY2 Portal or any of the Apps, as they have their own software, *i.e.,* LIS.

As is the case with the Taxpayer's services via the EMR connections, the Subscriber Agreement with Labs does not authorize the retail sale of the COMPANY2 Portal software. Under the Agreement, the Taxpayer does not issue a license to the COMPANY2 Portal software to any of the Dataflow Participants. Although physician practices and patients can download the Apps, they cannot acquire any control over the Taxpayer's software, manipulate or otherwise change the data, as the Apps' use is strictly limited to the viewing of Lab test results and, as applicable, inputting Lab orders information into pre-coded fields. The Taxpayer owns, operates, and maintains the software applications, as well as the servers that support the application software.

Thus, none of the Dataflow Participants has any control over the network, servers, operating systems, storage or application capabilities of the Taxpayer. Thus, the essence of the Taxpayer's services rendered via the COMPANY2 Portal connections remains the same as it does via the EMR connections: *(i)* to provide data processing services so that various software used by the Taxpayer can read and understand it; and *(ii)* electronically transfer, or push, the lab test results between two systems: the Lab's LIS and the COMPANY2 Portal. The only difference is that the lab test results in the case of the COMPANY2 Portal connections can be viewed directly by the physician practices and patients via the Taxpayer's platform and Apps hosted in STATE, not via the EMR vendor's software.

Finally, in order to facilitate the transfer of the processed lab test results, the COMPANY2 Portal offers an automated, cloud-based printing module "PRINT," which allows a physician practice to print paper copies (using the practice's own paper) of the electronically received lab test results to a designated computer in the physician's office ***(****i.e.,* physician's own computer). The PRINT module is a built-in function of the COMPANY2 Portal and therefore does not require separate downloading of additional software or applications.

2. CUSTOM PROGRAMMING & SUBSTANTIAL HUMAN INVOLVEMENT. The cloud-based software that the Taxpayer utilizes in the provision of its Data Processing Services, or more specifically, Software as a Service ("SaaS")[2], cannot be categorized as prewritten

[2] For purposes of this Private Letter Ruling Request, the terms "cloud-based software" and "SaaS" shall be used interchangeably.

software, irrespective of how broadly the phrase "prewritten software" is defined. In contrast to other cloud-based software that can be used immediately by populating fields, a Lab ***cannot*** simply login to the Taxpayer's system or any of the Taxpayer cloud-based software at Step #2 (as described *supra*, at p. 4) and start uploading its lab test results for subsequent delivery to the physician practices and patients (via the above-described EMR and COMPANY2 Portal connections). Before this can happen, the Taxpayer is required to perform substantial customization of its software, and as applicable, the EMR software, which process requires many hours of human labor.

Specifically, there are over five hundred (500) types of LIS and equipment testing software vendors (who sell software to Labs), with each such software having a unique data structure. Consequently, every Lab has its own unique combination of various vendors and unique data structures. Thus, in order to enable the processing of data of any given Lab, or more specifically, in order for such Lab to start conveying its lab test results to the Taxpayer's system for data processing, the Taxpayer's personnel must: (*i*) create interfaces to such Lab's LIS; and (*ii*) perform substantial programming customizations of its own software (***e.g.***, writing and validating new codes, connection setups, troubleshooting and making additional changes) to accommodate the specifications of the data coming from the Lab's LIS.

The foregoing custom programming of the Taxpayer's system and software to enable data processing and "translation" requires many hours of labor. For example, in order to start processing lab test results from any given Lab, the Taxpayer's personnel must perform over one hundred (100) hours of custom programming to customize its system and software for such particular Lab, and this is just a basic minimum. A hospital system or a Lab with multiple testing locations generally requires between two hundred (200) and five hundred (500) hours of custom programming. Absent any specific reasons and given associated administrative costs, the Taxpayer has not tracked the exact number of hours its personnel spends [sic] on ongoing custom programming for each project. However, according to the Taxpayer's analysis of other relevant data for 2023, its personnel devotes [sic] approximately 61% of working hours to ongoing custom programming (as opposed to 39% of its working hours devoted to initial custom programming).

Furthermore, in the case of the EMR connection, the Taxpayer has to map or configure each Lab's LIS to the respective physician practice's EMR system owned by each of the physician practices to make it compatible with the relevant Lab's LIS.

The above-described custom initial and ongoing custom programming that require substantial involvement of the Taxpayer's personnel are an integral part of the data processing and "translation" services. It is important to note that none of the Taxpayer's system (*i.e.*, cloud-based software), or its COMPANY2 Portal and Apps have any separate value for Labs, physician practices or patients, other than as the mode for viewing lab test results.

Finally, in addition to the initial and ongoing custom programming, the provision of the Data Processing Services (*e.g.*, the "translation" and manipulation of the received lab test results) requires substantial personal and professional services from the Taxpayer's personnel on a daily basis. Overall, the human labor component in the provision of the data processing services exceeds seventy (70%) percent, by value, of all of the Taxpayer's expenses.

3. REVENUE FLOW. Despite the many Dataflow Participants, the Taxpayer receives fees only from Labs. Specifically, each Lab signs a contract with the Taxpayer. The Taxpayer renders the Data Processing Services, and in exchange for such services, each Lab pays the Taxpayer a monthly fee for processing and hosting the data (the "Monthly Data Processing Fee"). This is the main source of revenue for the Taxpayer. (Two samples of the Taxpayer's invoices are attached hereto as ***Exhibits "G" and "H***."). Generally, the amount of the Monthly Processing Fee is determined based on the following factors: (*1*) the number of physician practices for which the Lab performs lab tests; and (*2*) the size of each physician practice. In essence, the Taxpayer's pricing is based on the volume of the data to be processed and hosted for each Lab (as opposed to the value of the cloud-based software/SaaS to be utilized by each Lab or such Lab's customers).

Given that before the provision of the Taxpayer's Data Processing Services to each Lab and such Lab's customers the Taxpayer must substantially modify and customize its software, the Taxpayer separately charges initial customization and set up fees (the "Initial Setup Fees") to at least ***partially*** reimburse some of the costs associated with human labor.

As indicated above, the Patient and Physician Apps are free of charge and can be downloaded via the Taxpayer's website or Apple's "App Store." In the event that a Lab desires that its customers (*i.e.*, physician practices and patients) have an option to use the Apps, the Taxpayer charges a Lab a one-time setup fee (at a flat rate irrespective of the number of downloads) to cover human labor for the initial customization that enables the delivery of the lab tests to the Apps (the "Setup App Fees"). In addition, Labs are separately charged an additional

monthly fee for additional processing (*e.g.*, code modifications and manipulations) of the data to be delivered to such Apps (the "Monthly App Fees").

4. NEXUS WITH ILLINOIS. The Taxpayer does not maintain an office in Illinois. Neither does the Taxpayer engage in taxable sales of property and services via persons, acting on its behalf, such as employees, independent contractors, agents, or other sales representatives. Furthermore, the Taxpayer does not regularly solicit orders from Illinois customers via the website of an entity or individual physically located in Illinois.

However, recently, the Taxpayer's gross receipts generated from sales of services to its customers located in Illinois exceeded $100,000 during the preceding 12-month period.

C. RULINGS REQUESTED

RULING #I: All of the Taxpayer's offerings to Illinois customers are non-taxable services, and are not taxable sales, leases, licenses or other transfers of software, SaaS or other tangible personal property in Illinois.

RULING #2: None of the Taxpayer's services provided to Illinois customers constitute taxable telecommunication services.

RULING #3: The Taxpayer is not required to collect any of: (i) retailers' occupational tax; (ii) use tax; (iii) service occupation tax; or (iv) service use tax in Illinois or to register with the Department to collect the foregoing taxes.

D. STATEMENT OF LAW AND ANALYSIS

RULING #I: All of the Taxpayer's offerings to Illinois customers are non-taxable services, and are not taxable sales, leases, licenses or other transfers of software, SaaS or other tangible personal property in Illinois.

1. GENERAL SALES AND USE TAXATION IN ILLINOIS

The Illinois sales and use tax system operates with the following four separate taxes: (*i*) retailers' occupation tax; (*ii*) service occupation tax; (*iii*) use tax; and (*iv*) service use tax (from time to time collectively referred to as the "Illinois Sales and Use Taxes"). 35 ILCS §§ 120/14, 115/1, 105/1

and 110/l. All of these taxes have the same tax rate of 6.25%. 35 ILCS § 105/3-10.

Retailers' occupation tax is imposed upon persons engaged in the business of selling tangible personal property at retail, and its complementary tax is the use tax. 35 ILCS §§ 120/2 and 105/3. "Sale at retail" means "any transfer of the ownership of or title to tangible personal property to a purchaser, for the purpose of use or consumption." 35 ILCS 120/1. Since January 1, 2021, retail sales by out-of-state retailers have been sourced to Illinois where the tangible personal property is shipped or delivered or where the purchaser takes possession. 35 ILCS 120/2-12(6).

Service occupation tax is imposed upon all persons engaged in the business of rendering services (referred to as "servicemen"), and its complementary privilege tax is the service use tax. 35 ILCS §§ 115/3 and 110/3. Service occupation tax is only applicable to tangible personal property transferred as an incident of a sale of a service, including computer software, as opposed to property sold and purchased at retail. 35 ILCS § 115/3. The serviceman's liability may be calculated in one of the four (4) following ways: (*i*) separately stated selling price of tangible personal property transferred incident to the service; (*ii*) 50% of the serviceman's entire bill; (*iii*) service occupation tax on the serviceman's cost price if the serviceman is a registered *de minimis* serviceman; or (iv) use tax on the serviceman's cost price if the serviceman is *de minimis* and is not otherwise required to be registered under 35 ILCS 120/2(a). Ill. Admin. Code tit. 86, § 130.2115(b); Illinois General Information Letter ST 14-0009-GIL (March 10, 2014) (attached hereto as ***Exhibit "I"***).

In view of the foregoing, if a service provider transfers no tangible personal property as part of its services, the transaction is not subject to the service occupation and service use taxes. Illinois General Information Letter ST 17-0018-GIL (June 2, 2017) (service transactions not involving transfer of tangible personal property to a customer are exempt from taxation) (attached hereto as ***Exhibit "J"***).

2. PREWRITTEN SOFTWARE AND CERTAIN SAAS ARE TAXABLE BY ILLINOIS AS TANGIBLE PERSONAL PROPERTY.

Illinois considers prewritten software to be tangible personal property and subjects it to taxation regardless of the method of its delivery. Ill. Admin. Code tit. 86, § 130.1935(a). However, charges for installation and implementation of prewritten software are exempt if they are separately stated from the selling price of prewritten software. Ill. Admin. Code tit. 86, § 130. l 935(b).

"Prewritten software" means prewritten computer programs held for general or repeated sale or lease. Ill. Admin. Code tit. 86, § 130.1935. Modification of an existing prewritten program to meet the customer's needs is custom software. Ill. Admin. Code tit. 86, § 130. I 935(c)(2). If modified software is sold to other customers without further real and substantial modifications to the operational coding, it is "taxable canned software," and is treated as repeated sales of such modified software. *Id*

The selection of pre-written or canned programs or program modules assembled by the vendor into a software package does not constitute custom software unless real and substantial changes are made to the programs or the creation of program interfacing logic. If the pre-written program or module was previously marketed, the new program would qualify as a custom program if the price of the pre-written program was 50% or less of the price of the new program. If the pre-written program was not previously marketed, the new program would qualify as a custom program if the charge made to the customer for custom programming services, as evidenced by the records of the seller, was more than 50% of the contract price to the consumer. Ill. Admin. Code tit. 86, § 130.1935(c)(3).

Generally, Illinois does not impose tax on SaaS or software furnished via a cloud-based delivery system and is only accessed remotely, provided that the transaction does not include a transfer of tangible personal property. Illinois General Information Letter ST 20-0018-GIL (Sept. 28, 2020) (attached hereto as *Exhibit "K"*); Illinois General Information Letter 17-0024- GIL (June 28, 2017) (attached hereto as *Exhibit "L"*).

However, if the provider of such SaaS provides to the customer an ***API (Application Programming Interface), applet,*** desktop agent, or remote access agent to enable the customer to access the provider's network and services, the customer is considered to ***have received computer software*** from the provider. *Id*. This transaction is subject to tax (and the provider of SaaS acts as a serviceman rather than a retailer), even if there is no separate charge to the customer for the computer software, unless the transaction qualifies as a ***non-taxable license of computer software***. *Id*.

A license of prewritten software is not a taxable sale if the transaction meets all of the following criteria: (*i*) it is evidenced by a written agreement signed by the licensor and the customer; (*ii*) it restricts the customer's duplication and use of the software; (*iii*) 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; (*iv*) 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 (*v*) the customer must destroy or return all copies of the software to the licensor at the end of the license period (the "License Exception"). Ill. Admin. Code tit. 86, § 130.1935(a)(l). A license agreement in which the customer electronically accepts the terms of the license by clicking "I agree" does not comply with the requirement of a written agreement set forth in Ill. Admin. Code tit. 86, § 130.l 935(a)(l). *Id*.

Notwithstanding the foregoing, the Department has held in a number of General Information Letters and at least in one Private Letter Ruling that if an Illinois customer downloads computer software for ***free*** from an ***out-of-state retailer's website or server*** that is also located out-of-state, the retailer, even though it is donating tangible personal property to the customer, ***has exercised no power or control over the property in Illinois***. In this instance, the donor would not have made any taxable use of the property in Illinois. The customer, the donee, would incur no use tax liability for the retailer to collect and remit to Illinois. Illinois does not tax subscriptions. Illinois General Information Letter ST 21-0001-GIL (Jan. 15, 2021) (attached hereto as *Exhibit "M"*); Illinois General Information Letter ST 20-0018-GIL (Sept. 28, 2020) (see *Exhibit "K*," supra); Illinois Private Letter Ruling ST 20-0004-PLR (June 10, 2020) (attached hereto as *Exhibit "N*"); Illinois General Information Letter ST 19-002 I-GIL (Dec. 4, 2019) (attached hereto as *Exhibit "O*").

3. DATA PROCESSING SERVICES AND INFORMATION SERVICES ARE NON-TAXABLE SERVICES.

In Illinois, electronically transferred or downloaded data or information is not deemed to be a transfer of tangible personal property. Ill. Adm. Code tit. 86, § 130.2105(a)(3). The Department does not consider the viewing, downloading or electronically transmitting of information and other data over the internet to be a transfer of tangible personal property. Illinois General Information Letter ST 20-0018-GIL (Sept. 28, 2020) (*see Exhibit "K," supra*). Thus, if no tangible property is transferred as part of the services, the transaction is not subject to any of the Illinois Sales and Use Taxes.

Illinois does not separately define either "information services" or "data processing services."

4. APPLICATION OF ILLINOIS LAW TO THE TAXPAYER'S OFFERINGS.

(a) <u>None of the Taxpayer's offerings rendered via the EMR connections can be deemed as a taxable SaaS. Although the Taxpayer's customers gain temporary access to its cloud-based software/SaaS when the Taxpayer renders its Data Processing Services via the COMPANY2 Portal connections, such limited access does not render the Taxpayer's offerings taxable.</u>

Given that the Taxpayer's cloud-based software/SaaS has no separate or ascertainable value apart from the Taxpayer's Data Processing Services (due to such users' limited access, if any, to generally view lab test results), it is not clear whether such software/SaaS is prewritten software or custom software. Absent any separate value for the customers, the Taxpayer's cloud-based software/SaaS was not prepared to the special order of any specific customer. Rather, it was developed by the Taxpayer to facilitate the Taxpayer's provision of the Data Processing Services to multiple Labs and their customers. Such multiple-customer utilization of the software/SaaS could conceivably bring it within the purview of Illinois' broad definition of prewritten software set forth in Ill. Admin. Code tit. 86, § 130.1935.

However, as described above, before such software/SaaS can be utilized for the provision of the Data Processing Services to a certain Lab and such Lab's customers, it requires a substantial level of customization and modification, which should exempt such software/SaaS from taxation pursuant to Ill. Admin. Code tit. 86, § 130.1935(c)(2). Nonetheless, Ill. Admin. Code tit. 86, § 130.1935(c)(3) appears to require that in order to be substantial, the modified product's price should exceed the price of the prior version of the software by 50%. Given that the Taxpayer's pricing for its offerings is generally determined based on the volume of the processed information that is processed for each Lab (not based on the value of the software utilized by the Taxpayer or accessed, if any, by the Dataflow Participants), the foregoing 50% threshold does not appear to be applicable to the Taxpayer.

Setting aside the aforesaid substantial customization argument and assuming, *arguendo*, that the cloud-based software/SaaS utilized by the Taxpayer as part of the provision of its data processing services is prewritten cloud-based software/SaaS, the main question is whether such software/SaaS constitutes ***taxable*** SaaS. As stated *supra* at pp. 10-11, a taxpayer's cloud-based computer software/SaaS becomes taxable in Illinois only if the taxpayer both: (*i*) provides to its customers ***remote access*** to the SaaS; and (*ii*) as part of such access, the taxpayer also

provides to its customers an ***API, applet, desktop agent, or remote access agent*** to enable the customers to access the provider's network and services. In the event that (*i*) the taxpayer's customers have no access to the taxpayer's network; or (*ii*) they do have the access, but such access does not include the furnishing of any of the API, applet, desktop agent, or remote access agent, the taxpayer's SaaS is not subject to the Illinois Sales and Use Taxes.

In the case of the Taxpayer's offerings provided via the EMR connections, at no point do any of the Dataflow Participants (*i.e.,* Labs, EMR vendors, physician practices or patients) gain access, electronically or by any other means, to the Taxpayer's network or the Taxpayer's cloud-based software. Specifically, each Dataflow Participant has its own software: each Lab uses its own LIS system, while each physician practice uses its own EMR software supplied by its respective EMR vendor. Simply stated, in this case, the Taxpayer's software and personnel process and translate the received data and push such data between the Lab's LIS and the EMR vendor's software, and none of the Dataflow Participants may access COMPANY2's system (even temporarily) via the usage of their prewritten software. Thus, absent ***any*** access to the Taxpayer's system by its customers (including such customers' customers), none of the Taxpayer's offerings provided via the EMR connections should be taxed as cloud-based software/SaaS.

In view of the foregoing, absent any access to the Taxpayer's network and SaaS, none of the Monthly Data Processing Fees charged by the Taxpayer for its offerings via the EMR connections is subject to any of the Illinois Sales and Use Taxes. Furthermore, given that the separately stated charges for installation and implementation of prewritten software are tax-exempt services under Ill. Admin. Code tit. 86, § 130. l 935(b), the Initial Setup Fees charged by the Taxpayer as part of its services rendered via the EMR connections are also exempt from the Illinois Sales and Use Taxes.

With respect to the cases with the COMPANY2 Portal connections, in which cases the processed data is pulled for display via the COMPANY2 Portal software, the Labs, as the actual customers of the Taxpayer (*i.e*., the customers who pay for the Taxpayer's Data Processing Services), use their own LIS software to manage and create lab test results. Each Lab's use of the Taxpayer's cloud-based software is limited to temporary logins to the COMPANY2 Portal to turn on, or more specifically initiate, the automatic transfer of LIS data to the Taxpayer's data center. The physician practices do gain some temporary access to the Taxpayer's system for the following limited purposes, such as: (*i*) to order lab test results by completing pre-coded fields; and (*ii*) to view the

processed lab tests via the COMPANY2 Portal or the Physician Apps (with the latter being publicly available for download, free of charge). Finally, the patients' temporary access to the Taxpayer's system is strictly limited to viewing the processed lab tests either via the COMPANY2 Portal or the Patient Apps (with the latter being publicly available for download, free of charge).

In order to gain the foregoing temporary access to the COMPANY2 Portal, all of the Dataflow Participants (*i.e*., Labs, physician practices and patients) can only use a secure URL/HTTPS. Importantly, however, such access to the COMPANY2 Portal does not include the furnishing of any API, desktop agent, or remote access agent by the Taxpayer. Regarding the Physician Apps and the Patient Apps, although the Taxpayer so far has not had any customers in Illinois utilizing this option, the physician practices and patients can ***optionally*** download, free of charge, the Physician Apps and the Patients Apps, respectively, hosted by the Taxpayer on its out-of-state servers. This is just an alternative mode to temporarily access the Taxpayer's cloud-based system/SaaS.

As applicable to the App downloads, Illinois has a well-established position that such Apps should not be subject to the Illinois Sales and Use Taxes (or, more specifically, to the use tax) because they are downloaded for ***free*** from the Taxpayer's ***out-of-state web site and/or server***. Furthermore, the separately stated one-time Setup App Fee and Monthly App Fees that the Labs pay the Taxpayer in connection with the downloaded Apps should not be subject to any of the Illinois Sales and Use Taxes. Specifically, the one-time App Setup Fees should be tax-exempt as separately stated charges for installation and/or implementation of prewritten software pursuant to Ill. Admin. Code tit. 86, § 130.1935(b). The App Monthly Fees should also be tax-free because they constitute nontaxable data processing services, or more specifically, the services (*e.g.,* additional code writing and combining) that enable the delivery of the processed lab test results to the end users (*i.e*., physician practices and patients). As described *supra* at p. 11, Illinois does not tax subscriptions.

Regarding the Taxpayer's customers' temporary access to the COMPANY2 Portal, as noted *supra*, such customers can only use a secure URL/HTTPS. Given that the Taxpayer does not furnish to any of its customers any API, desktop agent, or remote access agent, the Taxpayer does not believe that such access includes any transfer of tangible personal property. Even if we assume, *arguendo*, that some SaaS were transferred as part of such temporary logins, its limited functionality in the hands of the Taxpayer's customers is strictly confined to: (*i*) initiating the transfer of data to the Taxpayer for processing; (*ii*) populating pre-written templates for lab test orders; and (*iii*) viewing the processed data

output (*i.e.*, lab test results), without any right to manipulate or otherwise utilize it, such transferred SaaS, if any, has no separate value to the Taxpayer's customers to warrant its taxation.

Absent any ***separate value*** to the Taxpayer's customers apart from the Data Processing Services rendered to them, it is impossible for the Taxpayer to determine which SaaS is actually being transferred to its customers and therefore to quantify the cost associated with such transfer. In view of this, the cost methods for calculating the Taxpayer's liability set forth in the above-cited Ill. Admin. Code tit. 86, § 130.2115(b) and Illinois General Information Letter ST 14-0009-GIL (March 10, 2014) cannot be utilized by the Taxpayer to determine the cost of the transferred SaaS; the usage of the other methods (*e.g.*, 50% of the entire bill) would unfairly cause over-taxation of the Taxpayer's services.

Absent any specific guidance from Illinois regarding the taxation of SaaS that is combined with tax-exempt data processing services, the Taxpayer analyzed sales tax laws of other states that tax such SaaS in a manner similar to Illinois (the "Surveyed States"). The Taxpayer understands that such state law analyses are not binding upon Illinois. Nonetheless, such analyses are persuasive inasmuch, as they illustrate the legal soundness of the Taxpayer's arguments advanced in this Private Letter Ruling Request.

According to our analysis (attached hereto as *Exhibit "P"*), the Surveyed States subject to taxation a combination of the cloud-based prewritten computer software and services as SaaS, only when the cloud-based software allows the taxpayer's customers ***multi-functional utilization***. In such an event, such software constitutes a valuable component of the transaction, thereby rendering the taxpayer's SaaS taxable by the Surveyed States.

Specifically, in order to be taxable in the Surveyed States, the access to the taxpayer's cloud-based software must allow the taxpayer's customers: (*i*) to have some meaningful control over the data entry (importantly, however, data entry into templates created by the service provider does not rise to the level of control that renders transactions taxable); (*ii*) to manipulate, analyze and otherwise process such data and/or combine such data with some other data obtained from third parties; and (*iii*) to create various types of reports that can be furnished to others. To this end, mere retrieval and creation of reports that contain personal or individual information (such as lab tests or other patient results) that is not or may not be substantially incorporated into reports furnished to others is not a taxable transaction.

In contrast to the above-described wide-range functionality of SaaS that renders it taxable in the Surveyed States, the Taxpayer's customers cannot have any meaningful control over the data entry (as noted *supra*, placing lab test orders in a pre-set format is disregarded for such purposes). Furthermore, the Taxpayer's customers cannot manipulate, analyze and otherwise process such data; this function is performed by the Taxpayer. Finally, the Taxpayer's customers cannot create various types of reports to be furnished to others, as lab test results represent personal information. To be more specific, the Taxpayer's SaaS has a ***very limited functionality*** in the hands of the Taxpayer's customers, as they can only utilize the SaaS to transfer their raw data to the Taxpayer for processing and view the final output. To this effect, the true object of the Taxpayer's offerings is the data processing services, and the Taxpayer's software merely facilitates the provision of such data processing services.

Generally, nontaxable computer data processing services are confined to the following ***three*** steps: (*i*) the taxpayer receives data from its customers; (*ii*) the taxpayer (not the taxpayer's customers) processes such customer-supplied data utilizing its software; and (*iii*) the taxpayer distributes the processed output in the form of a screen display, a report or in some other forms. The customers are only allowed to transfer the data for processing (including completing orders) and view the final output. This invariably limits the cloud-based software's functionality for the customers to the extent that they can only access the software to transfer their data to the taxpayer for processing and to view the final output processed by the taxpayer. In view of such limited functionality, the states that subject SaaS to sales and use tax ***exempt*** from taxation the offerings that combine/bundle data processing services with cloud-based software. The main rationale for this is that although certain SaaS is being transferred as part of the data processing services, the SaaS's limited functionality in the hands of the customers has no independent or ascertainable value apart from its relationship to the taxpayer's data processing services.

Thus, the purpose for using cloud-based software as part of data processing transactions for any customer is the ability to transfer the data for processing and to access the final processed output, not the customer's ability to utilize the taxpayer's software to compare, manipulate and analyze data or create various types of output by utilizing various aspects of the software's functionality. Once a taxpayer's customers are allowed to have control over the data entry and to manipulate and otherwise process the data, the object of the transaction is no longer data processing services; rather, the object is the taxable SaaS which can be best described as either taxable access to database services or information retrieval products, or some combination thereof. As noted

above, such services are generally subject to the sales tax by the Surveyed States.

The Taxpayer's offerings are data processing services in their purest form. As described above, (i) Labs electronically supply test results (originated from physician practices) to the Taxpayer; (ii) the test results supplied by the Labs are then automatically manipulated and processed by the Taxpayer and its cloud-based software (not by the Labs, physician practices or patients); and (iii) the processed data is then transferred back to the physician practices and patients. Consequently, the ***functionality*** of the Taxpayer's cloud-based software/SaaS for the Taxpayer's direct and indirect customers (*i.e.,* the Labs and the Lab's customers) is ***strictly limited*** to such customers' ability to transfer the data to the Taxpayer (by logging into the COMPANY2 Portal to initiate the automatic transfer of LIS data to the Taxpayer's data center or by completing pre-coded fields to order lab tests) and to view the processed lab tests either via the COMPANY2 Portal or the Apps. Given such limited functionality for the Taxpayer's customers, neither the COMPANY2 Portal nor the Apps can have any separate or ascertainable value for the Taxpayer's customers apart from its relationship to the Taxpayer's Data Processing Services.

In view of the foregoing, insofar as the Taxpayer's customers are given the right to access the COMPANY2 Portal for the sole purpose of transferring the data to the Taxpayer for data processing and viewing the final output, such limited access should not subject the Taxpayer's offering to the Illinois Sales and Use Taxes. Consequently, none of the Monthly Data Processing Fees charged by the Taxpayer for its offerings via the COMPANY2 Portal connections should be subject to any of the Illinois Sales and Use Taxes. Furthermore, given that the separately stated charges for installation and implementation of prewritten software are tax-exempt services under Ill. Admin. Code tit. 86, § 130. I 935(b), the Initial Setup Fees charged by the Taxpayer as part of its services rendered via the COMPANY2 Portal connections should also be exempt from the Illinois Sales and Use Taxes.

(b) Even if, as part of its Data Processing Services, the Taxpayer is deemed to be transferring taxable cloud-based prewritten software/SaaS, it should be exempt from the Illinois Sales and Use Taxes because it meets the License Exception.

As noted above, a license of prewritten software is not a taxable sale if the transaction meets all of the following five criteria of the License Exception:

(i) it is evidenced by a written agreement signed by the licensor and the customer;

(ii) it restricts the customer's duplication and use of the software;

(iii) 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;

(iv) 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

(v) the customer must destroy or return all copies of the software to the licensor at the end of the license period.

Although the Taxpayer believes that none of its offerings is subject to the Illinois Sales and Use Taxes, any cloud-based software/SaaS that could be deemed to be received and used by Illinois customers meets all five (5) requirements of the License Exemption.

(i) The access to the Taxpayer's cloud-based software/SaaS as part of the Taxpayer's Data Processing Services is evidenced by a written agreement *(see a sample of the Subscriber Agreement attached hereto as Exhibit "F");*

(ii) The Subscriber Agreement restricts the customer's duplication and use of the Taxpayer's cloud-based software/SaaS. Specifically, Section 9.A. of the Subscriber Agreement provides in relevant part that *"all of COMPANY2's software, Proprietary Material ... and the COMPANY2 System shall remain the sole and exclusive property of COMPANY2. "*

Furthermore, Section 9.B. of the Subscriber Agreement states that *"Subscriber acknowledges and agrees that Subscriber and Subscriber's end-user customers shall have no right to control or direct the use of COMPANY2's software or the COMPANY2 System, and that Subscriber's and its end-user customers' use of COMPANY2 's software and the COMPANY2 System shall be limited to viewing the processed laboratory test results, using the COMPANY2 System's modules to print such results on Subscriber's and its end-user customers' 'printers, and, if applicable,*

placing test orders (as fully described in Exhibit A attached hereto), subject to additional restrictions set forth in Section 11 hereof"

Finally, Section 11 of the Subscriber Agreements expressly provides that *"Subscriber may not under any circumstances attempt, or knowingly permit or encourage others to attempt to de-compile, decipher, disassemble, reverse engineer, or otherwise decrypt or discover the source code of all or any portion of the COMPANY2 System, including any third-party portions of the system embedded within the COMPANY2 System. Use of the COMPANY2 System is restricted solely to viewing the processed data and using limited functions and features available through screens provided to Subscriber."*

(iii) The Taxpayer's Subscriber Agreement prohibits the Taxpayer's customers from licensing, sub licensing or transferring the software to a third party. Section 9.A. of the Subscriber Agreement provides in its pertinent part that *"Subscriber further agrees that COMPANY2 grants no license to use any of COMPANY2's software, Proprietary Material or the COMPANY2 System, and that Subscriber shall have no right to sell, license, sublicense or otherwise dispose of any of such items."*

(iv) The Taxpayer has a policy of providing another copy at no charge if the customer loses or damages the software. To this end, it should be noted that the Taxpayer's customers do not receive any software from the Taxpayer (other than the Apps). Furthermore, given the customers' very limited access to the Taxpayer's cloud-based software (restricted to mere ordering and viewing of lab tests), the Taxpayer's customers cannot damage the Taxpayer's cloud-based software. The only software that can be damaged or destroyed is the App. The Apps are publicly available for download, free of charge, via the COMPANY2 Portal or Apple's "App Store."

(v) The Taxpayer's Subscriber Agreement provides that the customer must destroy or return all copies of the software to the licensor at the end of the license period. Pursuant to Section 6.D. of the Subscriber Agreement, *"[u]pon termination of the Agreement, the Subscriber's access to the COMPANY2 System shall be terminated and Subscriber shall return to COMPANY2 all of the items and documentation related to the COMPANY2 System and/or COMPANY2 Proprietary Materials."* In addition to this as this relates to COMPANY2's software, Section 9.A. of the Subscriber Agreement provides that, *"[u]pon the termination of this Agreement, [software] items not returned to COMPANY2 pursuant to Section 6.D. hereof shall be completely destroyed by Subscriber."*

In view of the foregoing, the Taxpayer's cloud-based prewritten software and the Apps clearly meet the five-part test of the License Exception. Thus, even if, as part of its Data Processing Services the Taxpayer is deemed to be transferring a taxable cloud-based prewritten software/SaaS to its customers, it should be exempt from the Illinois Sales and Use Taxes because it meets the License Exception.

RULING#2: None of the Taxpayer's services provided to Illinois customers constitute taxable telecommunication services.

Telecommunication services in Illinois are not subject to any of the Illinois Sales and Use Taxes. Rather, Illinois subjects telecommunication services to telecommunications excise tax on the act or privilege of originating or receiving intrastate or interstate telecommunications by persons in Illinois at the rate of 7% of the gross charges for such telecommunications purchased at retail from retailers by such persons. 35 ILCS § 630/3; 35 ILCS § 630/4.

The term "telecommunications" is broadly defined to include messages and information transmitted through the use of computer exchange services and any other transmission of messages or information by electronic or similar means. 35 ILCS § 630/2(c). However, "gross charges" do not include the charges for storing data or information for subsequent retrieval or for processing data or information intended to change its form or content. 35 ILCS § 630/2(a)(3). Finally, persons who provide services and who do not, as part of those services, charge customers for the line or other transmission charges that are used to obtain these services are not considered to be telecommunications retailers by virtue of those activities. Illinois General Information Letter ST 19-0021-GIL (Dec. 4, 2019) (attached hereto as *Exhibit "O").*

For the reasons stated in the analysis for Ruling #1, the true object of the Taxpayer's offerings to Illinois customers is data processing services, and the Taxpayer's gross charges related to data transmittance represent the charges for: (*i*) processing lab tests, which processing changes its digital form and content (*e.g.,* code modifications and other code and data manipulations); and (*ii*) subsequent storing of the processed lab tests in the Taxpayer's services for subsequent retrieval by the Taxpayer's customers. Specifically, for such services the Taxpayer charges the Monthly Data Processing Fees and Monthly App Fees.[3] Finally, the Taxpayer does not, as part of its data processing services,

[3] The Taxpayer also charges the Initial Setup Fees and Setup App Fees. However, such fees are charged for human labor associated with initial customization of the Taxpayer's software, and therefore they are unrelated to any possible electronic transmittance of data.

charge customers for the line or other telecommunication transmission charges that are used to obtain these services.

In view of the foregoing, none of the Taxpayer's services provided to Illinois customers constitute taxable telecommunication services and the Taxpayer should not be considered to be a telecommunications retailer by virtue of the provision of its Data Processing Services.

RULING #3: The Taxpayer is not required to collect any of: (i) retailers' occupational tax; (ii) use tax; (iii) service occupation tax; or (iv) service use tax in Illinois or to register with the Department to collect the foregoing taxes.

The Taxpayer does not maintain an office in Illinois or engage in taxable sales of property and services via persons, acting on its behalf, such as subsidiaries, employees, independent contractors, agents, or other sales representatives in Illinois. Neither does the Taxpayer maintain any inventory in Illinois. Thus, the Taxpayer has not established either a physical nexus or an affiliate nexus with Illinois. 35 ILCS 105/2. Furthermore, the Taxpayer does not have any contracts with persons located in Illinois for the referral of customers through the use of a promotional code or other mechanism that would allow the Taxpayer to track purchases of customers referred by such in-state persons. 35 ILCS 105/2(1.2).

Effective October 1, 2018, remote service providers who render services to purchasers in Illinois from outside Illinois are subject to the Illinois Sales and Use Taxes if gross receipts from such sales are at least $100,000 or involve at least 200 separate transactions in the preceding 12- month period (the "Wayfair Nexus"). 35 ILCS § 110/2(9). Remote sellers who meet either threshold must register with the Department to collect the Illinois Sales and Use Taxes.

Recently, the Taxpayer's gross receipts from sales in Illinois exceeded $100,000 for the preceding 12-month period. However, pursuant to Ill. Admin. Code tit. 86, § 150.803(e)(2), in the event that an out-of-state retailer's only activities are non-taxable sales (*i.e.,* 100% of their sales to Illinois purchasers are exempt), such out-of-state retailer is not required to register with the Department.

For the reasons stated in the analysis for Rulings #1 and #2, the Taxpayer does not engage in taxable sales of tangible personal property, prewritten computer software, cloud-based prewritten computer software, or any taxable services delivered into Illinois. The Taxpayer provides only non-taxable services to Illinois customers. As such, the Taxpayer is not

required to be registered as a remote seller with the Department or collect any of the Illinois Sales and Use Taxes.

E. CONCLUSION

RULING #I: Although Illinois generally subjects to the Illinois Sales and Use Taxes sales of cloud-based prewritten computer software (*i.e.*, SaaS) and apps as tangible personal property if the user is located in Illinois, none of the Taxpayer's offerings to Illinois customers constitute a taxable sale, lease, license or other transfer of cloud-based computer software or other tangible personal property in Illinois.

This is because the true object of the Taxpayer's transactions in Illinois is non-taxable data processing services, not the use of the underlying cloud-based software/SaaS, Apps (which are publicly available via a free download) or the network that the Taxpayer hosts in STATE and utilizes to render such services. The sole purpose for which the Taxpayer's customers engage in transactions with the Taxpayer is the Taxpayer's Data Processing Services. Specifically, the scope of the Taxpayer's services is confined to the following three steps: (*i*) the Taxpayer receives data for processing from its customers; (*ii*) the Taxpayer (not its customers) processes and stores such customer-supplied data utilizing its software; and (*iii*) the Taxpayer delivers the output (*i.e.*, processed data) by an electronic transfer for retrieval in the form of a screen display. The Taxpayer's cloud-based software/SaaS, Apps and network merely facilitate the provision of such Data Processing Services.

Generally, Illinois subjects to taxation cloud-based software (*i.e.*, SaaS) ***only if*** the provider of such SaaS provides to customers an API, applet, desktop agent, or remote access agent to enable such customers to access the provider's network and services. In such case, Illinois treats the customers as if they have received cloud-based software/SaaS from the provider as part of the rendered services.

In the case of the Taxpayer's offerings provided via the EMR connections, at no point do any of the Taxpayer's customers gain access, electronically or by any other means, to the Taxpayer's network or the Taxpayer's cloud-based software. Thus, absent any access to the Taxpayer's cloud-based software/SaaS and network, none of the Taxpayer's offerings provided via the EMR connections should be taxed as SaaS.

With respect to the cases with the COMPANY2 Portal connections, the Taxpayer's customers can temporarily access the COMPANY2 Portal

via a secure URL/HTTPS for the following limited purposes: (*i*) initiating the transfer of data to the Taxpayer for processing; (*ii*) populating pre-written templates for lab test orders; and (*iii*) viewing the processed data output (*i.e*., lab test results). Although the Taxpayer so far has not had any customers in Illinois utilizing the Apps, the Taxpayer may provide its customers the Apps (with the latter being publicly available for download, free of charge), which is an ***alternative*** mode to ***temporarily*** access the Taxpayer's cloud-based system/SaaS.

As applicable to the App downloads, Illinois has a well-established position that such Apps should not be subject to the Illinois Sales and Use Taxes (or more specifically to the Use Tax) because they are downloaded for free from the Taxpayer's ***out-of-state website and/or server***. Regarding the Taxpayer's customers' temporary access to the COMPANY2 Portal via a secure URL/HTTPS, since the Taxpayer does not furnish to any of its customers any API, desktop agent, or remote access agent, the Taxpayer does believe that such access includes any transfer of tangible personal property. Even if we assume, for purposes of this Private Letter Ruling Request, that, as part of the above-described temporary logins, some cloud-based software/SaaS were transferred, the Taxpayer believes that given the ***very limited functionality*** of such cloud-based software/SaaS in the hands of the Taxpayer's customers, such cloud-based software/SaaS should not be subject to the Illinois Sales and Use Taxes. This is because such SaaS is merely a means to deliver data for processing and to view the processed output. Furthermore, the SaaS ***cannot*** function ***independently*** of the Taxpayer's system. Neither the SaaS nor the furnished data can be ***altered*** or ***manipulated*** by the Taxpayer's customers. As such, the Taxpayer's SaaS, has ***no value*** for the Taxpayer's customers other than as a mere facilitator for the provision of the Taxpayer's non-taxable services. Finally, even if, despite the foregoing arguments, the Department were to conclude that as part of its Data Processing Services the Taxpayer is deemed to be transferring taxable cloud-based prewritten software/SaaS, it should be exempt from the Illinois Sales and Use Taxes because it meets the License Exception.

In view of the foregoing, insofar as the Taxpayer's customers are given the right to access the COMPANY2 Portal for the sole purpose of transferring the data to the Taxpayer for data processing and viewing the final output, such limited access should not subject the Taxpayer's offerings to the Illinois Sales and Use Taxes. Thus, all of the Taxpayer's offerings to Illinois customers are non-taxable services, and are not taxable sales, leases, licenses or other transfers of software, SaaS, the Apps or other tangible personal property in Illinois.

RULING #2: Even though Illinois broadly defines the term "taxable telecommunications services," it expressly excludes from taxation charges for storing data or information for subsequent retrieval or for processing data or information intended to change its form or content. Furthermore, a service provider who does not, as part of that service, charge customers for the line or other transmission charges that are used to obtain these services is not considered to be a telecommunications retailer.

Given that the true object of the Taxpayer's offerings to Illinois customers is data processing services, all of the Taxpayer's gross charges related to data transmittance represent charges for processing lab tests, which processing changes its digital form and content (*e.g.*, code modifications and other code and data manipulations) and subsequent storage in the Taxpayer's servers for subsequent retrieval by the Taxpayer's customers. Finally, the Taxpayer does not, as part of its Data Processing Services, charge its customers for the line or other telecommunication transmission charges that are used to obtain these services.

In view of the foregoing, none of the Taxpayer's services provided to Illinois customers constitute taxable telecommunication services and the Taxpayer cannot be considered to be a telecommunications retailer by virtue of the provision of its Data Processing Services.

RULING #3: The Taxpayer's only nexus with Illinois is its gross receipts from the sales in Illinois that have recently exceeded the $100,000 threshold, which threshold is sufficient for an out-of-state retailer to create the Wayfair Nexus with Illinois. However, the Taxpayer does not engage in taxable sales of tangible personal property, prewritten computer software, cloud-based prewritten computer software/SaaS, or any taxable services delivered into Illinois. The Taxpayer provides only non-taxable services to Illinois customers. As such, the Taxpayer is not required to register with the Department or collect any of the Illinois Sales and Use Taxes.

Please contact the undersigned at PHONE1 if you have any questions about this request.

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.

Please note that it is very common for software to be licensed over the internet and for the customer to check a box that states that the customer accepts the license terms. Acceptance in this manner does not constitute a written agreement signed by the licensor and the customer for purposes of subsection (a)(1)(A) of Section 130.1935. To meet the signature requirement for an exempt software license, the agreement must contain the written signature of the licensor and customer. An electronic agreement in which the customer accepts the license by means of an electronic signature that is verifiable and can be authenticated and is attached to or made part of the license will comply with this requirement. 86 Ill. Adm. Code 130.1935(a)(1)(A).

A provider of software as a service is acting as a serviceman. As a serviceman, the seller does not incur Retailers' Occupation Tax. Service Occupation Tax is imposed upon all persons engaged in the business of making sales of service on all tangible personal property transferred incident to a sale of service, including computer software (35 ILCS 115/3). Computer software provided through a cloud-based delivery system – a system in which computer software is never downloaded onto a client's computer and is only accessed remotely – is not subject to tax.

If a provider of a service provides to the subscriber an API, applet, desktop agent, or a remote access agent to enable the subscriber to access the provider's network and services, the subscriber may be receiving computer software. Although there may not be a separate charge to the subscriber for the computer software, it is nonetheless subject to tax, unless the transfer qualifies as a non-taxable license of computer software.

Under the Service Occupation Tax Act, a serviceman is taxed on tangible personal property transferred incident to a sale of service. The transfer of tangible personal property to service customers may result in either Service Occupation Tax liability or Use Tax liability for servicemen, depending upon which tax base they choose to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or (4) Use Tax on cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

If the provider, as a serviceman, is not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act and qualifies as a de minimis serviceman, the provider could elect to pay Use Tax on its cost price of the computer software.

If an Illinois customer downloads computer software for free from an out-of-State retailer's web site or server that is also located out-of-State, the retailer, even though it is donating tangible personal property to the customer, has exercised no power or control over the property in Illinois. In this instance, the donor would not have made any taxable use of the property in Illinois. The customer, the donee, would incur no Use Tax liability for the retailer to collect and remit to Illinois. Illinois generally does not tax subscriptions of software-as-a-service.

Telecommunications

The Illinois Telecommunications Excise Tax Act imposes a tax on the act or privilege of originating or receiving intrastate or interstate telecommunications by persons in Illinois at the rate of 7% of the gross charges for such telecommunications purchased at retail from retailers by such persons. 35 ILCS 630/3 and 4. The Simplified Municipal Telecommunications Tax Act allows municipalities to impose a tax on the act or privilege of originating in such municipality or receiving in such municipality intrastate or interstate telecommunications by persons in Illinois at a rate not to exceed 6% for municipalities with a population of less than 500,000, and at a rate not to exceed 7% for municipalities with a population of 500,000 or more, of the gross charges for such telecommunications purchased at retail from retailers by such persons. 35 ILCS 636/5-10 and 5-15.

The Act defines gross charges as including the amount paid for the act or privilege of originating or receiving telecommunications in this State and for all services and equipment provided in connection therewith by a retailer. 35 ILCS 630/2(a). The Act does exclude charges for customer equipment, including equipment that is leased or rented by the customer from any source, when those charges are disaggregated and separately identified from other charges. 35 ILCS 630/2(a)(4).

"Gross charges" does not include charges for the storage of data or information for subsequent retrieval or charges for the processing of data or information intended to change its form or content. 35 ILCS 630/2(a)(3). Charges for automated data storage, retrieval and processing services or for the use of computer time or other equipment are not included in gross charges. Automated information retrieval or data processing charges are not included in gross charges. For example, a customer who accesses an on-line computer database is not subject to tax on the charge for the data processing or inquiry but would be subject to tax on any charge for the transmission of the data. 86 Ill. Adm. Code 495.100(c).

Ruling

According to the Company, the Company

> "has developed proprietary software to facilitate the process of laboratory ("lab") testing, obtaining lab results and sharing the lab results with physician practices and patients. The proprietary software furnishes a connectivity solution to order and collect lab tests from laboratories ("Labs"), to timely and securely receive such test results by physician practices, and to quickly and securely share such results with the practices' patients. The software is capable of electronic interconnectivity, and the essence of the Taxpayer's services is the combination of data processing, data translation, data hosting and data exchange services (sometimes collectively referred to as the "Data Processing Services")."

The Company enters into agreements with Labs to provide the Data Processing Services. The following parties are involved: (i) Labs; (ii) physician practices; (iii) patients; and (iv*)* in the case of the EMR connections, EMR vendors ("Dataflow Participants"). The Company describes a three step process: (i) each Lab collects lab tests from physician practices via the Lab's laboratory information software or "LIS"; (ii) the collected data is conveyed by the Labs to the Company's servers located in STATE where the data is processed, combined with proprietary codes ("translated") in order to be readable by other software systems, and stored on the Company's servers for future delivery; (iii) the processed data is delivered to either EMR vendors (in the case of the electronic medical record ("EMR") connections), who transmit the data to the physician practice or physician practices.

If the physician has purchased EMR software from an EMR vendor, the Company must "translate" the Lab's test codes and results so that the results can be read by the physician's EMR system. The results are then transferred to the EMR vendor, and the EMR vendor transfers the data to the physician. In other cases, physicians use the Company's COMPANY2 Portal, a cloud-based platform housed in the Company's STATE data center to access lab test results. Physician practices using the COMPANY2 Portal may use a cloud-based printing module called "PRINT" to print paper copies of the electronically received lab results. PRINT does not require the downloading of software or applications.

The Company must expend considerable time and money to create interfaces to the multitude of LIS systems and perform substantial customization to its own systems to accept lab results from all the different Labs' LISs. The Company must also map and configure each Lab's LIS to the physicians EMR systems. According to the information received from the Company by email dated May 8, 2024, "COMPANY1 never makes any changes to either a Lab's LIS or an EMR vendor's software. … All changes associated with the initial set-up connections and any future changes are done only to COMPANY1's own software and systems to enable them to interface and communicate

with each Lab's LIS and EMR vendor's software. Thus, all initial and ongoing programming is done only on COMPANY1's side."

None of the Dataflow Participants can install, download, or transfer any of the Company's software or applications on their computers, nor do any of the parties have "any control over the network, servers, operating systems, storage, or application capabilities" of the Company.

The Company charges Labs a Monthly Data Processing Fee for processing and hosting the data based on the number of physician practices for which the Lab performs lab tests and the size of each physician practice. The Company also charges the Labs an Initial Setup Fee to recover some the costs incurred by the Company to modify the Company's software to communicate with EMR vendors.

The Company has developed: (i) a mobile physician application and **(**ii) a mobile patient application (collectively the "Apps"), which Apps function as the COMPANY2 Provider Portal and the Patient Access Portal, respectively. Physician practices and patients have an option to download their respective Apps to a personal device, such as a phone, tablet, *etc.* The Apps are hosted on the Taxpayer's servers located in STATE and are publicly available for download, free of charge, via the COMPANY2 Portal or Apple's "App Store." If a Lab desires that its customers (*i.e*., physician practices and patients) have an option to use the Apps, the Taxpayer charges a Lab a one-time setup fee (at a flat rate irrespective of the number of downloads) to cover The Company's human labor for the initial customization that enables the delivery of the lab tests to the Apps. In addition, Labs are separately charged an additional monthly fee for additional processing (*e.g*., code modifications and manipulations) of the data to be delivered to such Apps.

The Company is making sales of service and is a serviceman. The services the Company provides, collectively the Data Processing Services (except for the Patient and Physician Apps), are not subject to Retailers' Occupation Tax or Service Occupation Tax because the Company does not transfer any computer software to the Data Flow Participants. The Company provides the Data Processing Services using a cloud-based delivery system – a system in which computer software is never downloaded onto a client's computer and is only accessed remotely. It is our understanding the ability of a client to print lab results on a client's device does not involve the transfer of any computer software to the client, and the Company does not incur any tax liability on this option.

The Labs pay a Monthly Processing Fee for the Company's services. The Company states that no tangible personal property is transferred in consideration of the Fee. The Fee is not subject to Retailers' Occupation Tax or Service Occupation Tax. The Initial Setup Fee is charged by the Company to Labs for customization of the Company's computer software. Once again, no tangible personal property is

transferred in consideration of the Fee, and it is not subject to Retailers' Occupation Tax or Service Occupation Tax.

In two situations the client does download computer software: when a patient or physician downloads an App on a mobile device. Computer software is defined broadly in the Retailers' Occupation Tax Act. Although there may not be a separate charge to the clients for the downloaded Apps, apps are subject to tax under one of the four methods discussed above, unless the transfer of the software qualifies as a non-taxable license of computer software, or the Apps are downloaded for free from an out-of-State web site or server that is located out of State. If the Apps are downloaded from the Company's server in STATE, the Company does not incur any Retailers' Occupation Tax or Service Occupation Tax liability. The Company also does not incur any Retailers' Occupation Tax or Service Occupation Tax liability on the one-time setup fee to cover the cost of the Company's labor for the initial customization that enables the delivery of lab tests to the Apps or on the additional monthly fee the Company charges Labs for additional processing (*e.g.*, code modifications and manipulations) of the data to be delivered to such Apps.

Lastly, the Data Processing Services the Company provides do not fall withing the definition of "telecommunications" and are not subject to Telecommunications Excise Tax. 35 ILCS 630/2(c). Moreover, "gross charges" does not include charges for the storage of data or information for subsequent retrieval or charges for the processing of data or information intended to change its form or content. 35 ILCS 630/2(a)(3).

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules or in the factual representations recited in this ruling.

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 https://tax.illinois.gov/ or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Samuel J. Moore
Chairman – Private Letter Ruling Committee

SJM:RSW:slc