

If all the criteria listed in subsection (a)(1)(A)-(E) of Section 130.1935 are met, then neither a transaction involving the licensing of software nor the subsequent software updates will be considered a taxable retail sale subject to Retailers' Occupation and Use Tax. See 86 Ill. Adm. Code 130.1935. (This is a GIL.)

August 22, 2008

Dear Xxxxx:

This letter is in response to your letter dated October 30, 2007, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

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

I am writing to request a Private Letter ruling, pursuant to 86 Ill. Admin. Code Sec. 1200.110, on behalf of ABC and its wholly owned subsidiary, XYZ who are sellers of computer software. A statement of the facts is set forth below. We have attached representative copies of the relevant software licenses, contracts and invoices. We are requesting this ruling for all open past periods and for future reliance by the taxpayers. We are not aware of any audit activity by the Department with respect to this issue. To the best of our knowledge, the Department has not ruled on this issue for the taxpayer or any predecessor. We have not previously submitted a request for a ruling on this or any similar issue. We believe that our request for ruling is supported by 86 Ill. Admin. Code, Sec. 130.1935 and GIL-ST 99-429. We know of no authority that is contrary to our requested ruling. A copy of power of attorney is attached.

Facts:

ABC and XYZ are manufactures and sellers of 'canned' computer software. ABC is located in STATE1, and XYZ is primarily located in STATE2. Both ABC and XYZ license software to their customers via either Paid-up/Perpetual License Contracts ('PLK') or Leased License Contracts ('LLK'). Neither company sells computer hardware or maintenance agreements that cover computer hardware.

In a PLK, the customer receives a copy of the software that they can use forever, but they receive no software upgrades, unless they purchase a contract, known as TECS. TECS stands for Technical Enhancement, i.e., software upgrades, and Customer Support, i.e., telephone and/or online support. The 'TE' and 'CS' of TECS are not separately stated on the invoice to the customer .

In the ABC software contract, there are separate charges, one for a PLK and one for a TECS, if the customer orders TECS with the PLK. In the XYZ software contract, the first year of a PLK always includes TECS, which is listed as one amount on the invoice, even though this one amount includes a PLK charge and a TECS charge. 'TE' is never separately stated from 'CS' by either ABC or XYZ.

In an LLK, the customer receives customer support and the latest version of the software from XYZ/ABC during the length of the lease period via software upgrades at no additional charge. The TECS is inherently part of an LLK by definition of an LLK, so a separate contract is not necessary. As such, the invoice would not reflect a separate charge for an LLK and another amount for TECS.

Discussion:

In Illinois canned computer software is taxable under 86 Ill. Adm. Code 130.1935(c). However, the written contracts for XYZ and ABC meet the five criteria listed in 86 Ill. Adm. Code 130.1935(a)(1)(A) through (E) and therefore, the ABC and XYZ software licenses are not taxable.

The issue that we are concerned with is if ABC and XYZ do not separately state the selling price of the TECS on the invoices to the customer would that subject the entire charge for the software license to Illinois ROT notwithstanding the fact that the underlying software license is exempt under the Department's regulations. Under 86 Ill. Adm. Code 130.1935(b) 'charges for updates of canned software are considered to be sales of software,' i.e., taxable, under the aforementioned section (c). Section (b) further states 'charges for training, telephone assistance, installation, and consultation are exempt if they are separately stated from the selling price of canned software.' We do not believe that this section is intended to impose tax when the above charges are not separately stated if the software being sold is an exempt sale.

Requested Ruling:

We are requesting a ruling that states that when computer software, that is exempt from Illinois Retailers' Occupation Tax due to the provisions of 86 Ill. Adm. Code 130.1935(a)(1)(A) through (E), that any concurrent or subsequent sale of technical enhancements or upgrades to that software and all customer support services are also exempt as long as the underlying software continues to meet the provisions of Section 1935, even if the charges for those upgrades and services are not separately stated.

The Department issued ST-99-0429-GIL which discussed part of this issue, stating 'If your software license agreement meets all of these criteria, then neither the transfer of the software or the subsequent software updates will be subject to the Retailers' Occupation Tax.'

We think that this specifically addresses the taxability of the TE, finding that it should not be taxable. With respect to the CS or customer support, this is purely a service transaction that does not involve any transfer of tangible personal property. We do not believe that the sale of a nontaxable service, however invoiced, would subject the underlying exempt computer software transaction to tax.

If you have any questions with respect to this request please call me. I request an opportunity to discuss this issue with you if for any reason you believe that the Department may issue a ruling contrary to our request.

DEPARTMENT'S RESPONSE

The Department's regulation "Public Information, Rulemaking and Organization" provides that "[w]hether to issue a private letter ruling in response to a letter ruling request is within the discretion of the Department. The Department will respond to all requests for private letter rulings either by issuance of a ruling or by a letter explaining that the request for ruling will not be honored." 2 Ill. Adm. Code 1200.110(a)(4). Further, the Department's regulations regarding Private Letter Rulings provide that "[i]f there is case law or there are regulations dispositive of the subject to the request, the Department will decline to issue a letter ruling on the subject." 86 Ill. Adm. Code 1200.110(a)(3)(D).

After reviewing the materials you provided in connection with your request, the Department declines to issue a Private Letter Ruling. It is the Department's position that its regulation at 86 Ill. Adm. Code 130.1935 is dispositive of the subject of your request, as are several PLRs and GILs that the Department has issued which can be found on the Department's website. Therefore, we are responding with a General Information Letter, the information contained therein we hope you find helpful.

Generally, sales of "canned" computer software are taxable retail sales in Illinois. Sales of canned software are taxable regardless of the means of delivery. For instance, the transfer or sale of canned computer software downloaded electronically would be taxable. However, if the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. See 86 Ill. Adm. Code 130.1935(c). Custom computer programs or software must be prepared to the special order of the customer.

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

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

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

Very truly yours,

Debra M. Boggess
Associate Counsel

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