

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. See 86 Ill. Adm. Code 130.1935. (This is a GIL.)

March 16, 2009

Dear Xxxxx:

This letter is in response to your letter dated September 27, 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](http://www.tax.illinois.gov) to review regulations, letter rulings and other types of information relevant to your inquiry.

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

ABC is an out-of-state vendor that provides Back office and Point of Sale Software to customers located in North America (State of Illinois). Alternatively to providing a software license, ABC provides Software as a Service (SaaS) in a hosted Infrastructure located in CITY.

SaaS is an agreement between ABC and their client which allows the client to obtain access to ABC's hosted applications (Connected Retailer Solutions consisting of Merchandising, Sales Audit, CRM and POS with an additional option for a Planning Module and Great Plains Dynamics software) and receive POS equipment support and maintenance services for the in-store solution.

The client transmits data to ABC from the in-store POS solution which is stored on ABC's servers. The client's head office users connect to the hosted infrastructure via Remote Desktop Software and have the right to export and save data, and print reports locally. Ownership of the material data for the SaaS solution remains with the client.

ABC charges the client:

1. A Hosting fee, which means a charge for the right to use the Connected Retailer Software in the Hosted environment and at the Point of Sale locations and obtain support services. The client has no right of ownership of the software or any component thereof.

2. A Network Connectivity fee to those clients who opt to purchase the service. This is a high speed broadband connection established between the client's store and/or head office locations to the ABC hosting facility.

The Hosting and Connectivity fees are billed separately.

I would like to know if Sales/Use taxes apply to the Hosting and Network Connectivity fees. If taxes do apply please provide the applicable State ruling.

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

We apologize for the lengthy delay in responding to your inquiry. The Department has been holding information requests regarding computer software hosting to determine the appropriate taxation of these types of arrangements. After review of these issues and the continuing evolution of the different types of transactions involving computer software applications, we believe that the proper forum for providing this type of guidance is through a formal administrative rulemaking process rather than through individual inquiries.

We hope the following general information may be 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.

Please note that it is very common for software to be licensed over the internet and the customer to check a box that states that they accept 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.

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

Very truly yours,

Terry D. Charlton  
Senior Counsel, Sales & Excise Taxes

TDC:msk