

ST 13-0075-GIL 11/26/2013 COMPUTER SOFTWARE

This letter discusses the taxability of computer software licenses. See 86 Ill. Adm. Code 130.1935. (This is a GIL.)

November 26, 2013

Dear Xxxxx:

This letter is in response to your letter received in this office on September 26, 2013, 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:

COMPANY 1 claims exemption from Illinois Sales and Use Tax for purposes of the NAME entered into between COMPANY 2 and COMPANY 1 under authority of Illinois Administrative Code 86 Section 130.1935(a), which categorizes certain software licensing agreements as not subject to Illinois sales and use tax.

We have agreed that COMPANY 2 will not invoice, collect and remit Illinois sales or use tax from COMPANY 1 due to the applicability of this provision.

We have also agreed that if the Illinois Department of Revenue reviews the exempt status of the subject NAME, COMPANY 2 will immediately notify COMPANY 1 of such and provide full cooperation with COMPANY 1 to the extent that COMPANY 1 (at its expense) chooses to defend the exempt position on this agreement.

We have further agreed that if the Illinois Department of Revenue, upon reviewing this position with COMPANY 1, determines that sales or use tax should have been collected and remitted on the Enterprises Agreement, COMPANY 2 may invoice and collect from COMPANY 1 any sales or use tax, plus any applicable interest and penalties, which it is required to remit to the state as a result of determination.

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. The tax is measured by the seller's gross receipts from retail sales made in the course of such business. "Gross receipts" means the total selling price or the amount of such sales. The retailer must pay Retailers' Occupation Tax to the Department based upon its gross receipts, or actual amount received, from the sale of the tangible personal property.

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. However, if the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. 86 Ill. Adm. Code 130.1935. Computer software that is not custom software is considered to be canned computer software, whether it is "stand-alone" or not. Custom computer programs or software are prepared to the special order of the customer. The selection of pre-written or canned programs assembled by vendors into software packages does not constitute custom software unless real and substantial changes are made to the programs or creation of program interfacing logic. *See* Section 130.1935(c)(3).

If transactions for the licensing of computer software meet all of the criteria provided in 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. We cannot determine from the

limited information provided in your letter whether the software license is subject to Retailers' Occupation Tax liability. It appears that you have attached a form provided by the licensor in which you claim that your COMPANY 1 does not owe excise tax on the licensing agreement. However, software licenses are subject to tax unless all of the criteria set out in 86 Ill. Adm. Code 130.1935(a)(1) are met. Based on the limited information provided in your letter, we cannot say whether the license meets all of the criteria in the regulation. Therefore, we cannot say whether the license is subject to tax.

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,

Cara Bishop
Associate Counsel