

This letter discusses the requirements for a license of computer software. See 86 Ill. Adm. Code 130.1935. (This is a GIL.)

July 17, 2017

**Interpretation of Regulation Title 86 130 section 130.1935: Computer Software**

Dear Xxxxx:

This letter is in response to your letter dated June 19, 2017, in which you requested information. The Department issues two types of letter rulings. Private Letter Rulings (“PLRs”) are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department’s regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter (“GIL”) is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at [www.tax.illinois.gov](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:

I am writing in reference to subsection B) of the above published regulation which states:

B) it restricts the customer’s duplication and use of the software

We believe that our company’s technology offering qualify for sale tax exemption under the above-mentioned tax regulation but wish to confirm your interpretation before claiming the benefit.

We offer an artificial intelligence technology that automates labor intensive business functions. Our software is delivered via a URL that our clients download upon service activation. While our written contracts dictate the specific application including site deployments, number of service incidents that can be resolved, and end of usage dates, we allow

customers unlimited downloads and duplication of the software from the URL provided.

It is comparable to a Microsoft Windows license. Upon purchase, the user can download multiple instances of the software but the company ensures that the user can only use on limited devices by requiring a unique license key before activation. In the same vein, we allow our customers to download and duplicate our software but we control and manage how and where the software is used.

We believe that this restriction on usage satisfies subsection B of the regulation.

I anticipate your written agreement or explanation as to how your interpretation differs.

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

“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.

By your own admission you allow unlimited downloads and duplication. You state that the Company controls and manages how and where the software may be used but you do not provide an explanation of the nature and extent of that control and management. From the limited information you have provided it does not appear your agreement would meet paragraph B of the Department's licensing requirements contained subsection (a)(1) of Section 130.1935.

The Department generally does not issue Private Letter Rulings on licensing of computer software. However, your letter raises a novel issue that the Department would be willing to consider should you submit a request conforming with 2 Ill. Adm. Code 1200.110.

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,

Richard S. Wolters  
Associate Counsel

RSW:bkl