

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.)

January 8, 2009

Dear Xxxxx:

This letter is in response to your letter dated June 25, 2008, in which you requested a Private Letter Ruling. 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:

This letter is being sent to request a private letter ruling regarding the taxability for Illinois Retailers' Occupation Tax purposes of the subscription fees received from the Illinois customers of COMPANY is a STATE1 corporation with one marketing employee based in Illinois.

The Company provides 'on-demand' marketing solutions to small businesses, associations and non-profits. The Company's revenue consists primarily of subscription fees paid by customers in order to gain access and use of the Company's email marketing and survey tools via the internet. The Company's customers use the email marketing tool to create, send and track permission-based email marketing campaigns. The Company's customers use the online survey tool to create, send, and host surveys and to tabulate and analyze responses. Both tools are accessed using a personal computer's standard web browser and an internet connection. To become a customer, a person navigates to the Company's website, creates an account, agrees to a 'Terms of Use' and selects a login ID and password used to access their account. Once logged in, a customer may choose to activate their subscription by providing a credit card or other means of payment and thereby obtain full functionality to either or both the email marketing and online survey tools. No tangible personal property is delivered to customers related to their purchase of the subscription and no software is ever installed

on customers' computers. During their subscription period, customers are given unlimited access to their accounts.

Customers use the email marketing tool to design email newsletters, promotions, or other communications by choosing from a group of pre-designed html email templates. Customers use the tool to manipulate and customize an on-line template and to add relevant content and images. They also enter email addresses for the prospective recipients of the email newsletter or promotion. The Company does not sell, rent or otherwise provide email addresses to its customers. Once customers have completed their designs of an email, they then use the email marketing tool to select which email addresses will receive the email and instruct the email to be sent. The Company then sends the email to the recipients via its email servers. After the email has been sent, customers may use their account to view reports on certain success metrics, such as the number of people who opened the email or the number of emails forwarded to others. A link is provided at the bottom of each email that allows an email recipient to opt out of receiving further emails from the sender. If that link is used by the recipient, the Company's email marketing tool prohibits further emails from being sent to that email address. All data input and output is transported via the internet and all processing and data storage is completed by the Company's proprietary software application that is hosted on computer equipment located entirely in STATE2.

Customers use the online survey tool in a nearly identical manner as the email marketing tool. The primary difference is that instead of creating an email that the company sends, customers create a survey questionnaire that the Company hosts as a webpage. Customers use their online survey account to analyze the responses.

The use of both tools is supported by access to telephone, email and online chat support from customer service representatives. The company provides compliance services to monitor its customers' compliance with email laws and regulations. Both of these services are provided at no additional fee by a combination of the Company's proprietary software and the Company's employees located in STATE2. The Company also maintains the hosting environment and monitors technical environment of the Company's tools.

Included with this letter is a copy of the Company's 'Terms of Use' which customers must agree to. Also included is a copy the Company's most recent annual report and recent stock offering documents. These documents are intended to provide the Department with a further overview of the Company's business and products. A demonstration account of the Company's marketing tools has been activated for the Department's review which may be assessed by web browser using the login 'illinoisdor' and password 'ILtaxes'.

The Company believes its marketing solutions constitute a combination of access to hosted software via the internet and services provided by the Company. The Company considers itself to be part of an industry referred to as 'Software-as-a-Service', which reflects that combination of services and software. The Company believes that though its marketing solutions involve the combination of software and services, the essential element of the sale is the use of the Company's hosted software. Therefore, the Company applied the guidance in Regulation Section 130.1935 of Title 86 of the Department of Revenue Regulations as follows:

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 - ***Customers must agree to a 'Terms of Use' by checking a box within the Company's marketing tool. The Company does not require an actual signature on a written agreement, but it does make its 'Terms of Use' available for its customers to print for their records and does believe the acknowledgement is legally binding.***
- B. It restricts the customer's duplication and use of the software - ***Section 6.1 of the Company's 'Terms of Use' restricts customers from duplication and Section 6.2 restricts use.***
- C. It prohibits the customer from licensing, sublicensing, or transmitting the software to a third party without the permission and continued control of the licensor - ***Section 6.1 of the Company's 'Terms of Use' prohibits Customer from licensing, etc. to a third party.***
- D. The licensor has a policy of providing another copy at minimal or no charge if the customer loses or damages the software, or of 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 - ***The Company provides access to a hosted software application therefore, it would not be applicable for the Company to provide additional copies. If Customers misplace login credentials, they may obtain this information through a customer support request and will again be able to access the marketing tool.***
- 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 - ***The Company does not provide copies of software to its customers; therefore, there is no provision for return or destruction of software copies. Section 7 of the Company's 'Terms of Use' does provide the Company the right to disable access to the Company's tools at the end of the paid subscription term.***

The Company does not believe it fulfills all requirements of Section 130.1935 paragraphs A. through E. Therefore, when the Company commenced business in Illinois, it concluded that its subscription fees were subject to Illinois Retailers' Occupation Tax.

On two separate occasions the Company has been contacted by the Illinois Department of Revenue as a result of complaints to the Department from customers stating that they did not believe the Company should be collecting Illinois Retailers' Occupation Tax on its subscription fees. In both cases, the Department employee agreed with the customer that the Company's marketing solutions constitute services and are not taxable in Illinois. In the most recent instance, the Company was contacted by PERSON who consulted with her supervisor and concluded that they did not believe the Company should be collecting tax on its subscription fees. They further recommended the Company seek a private letter ruling from the Department.

The Company has been paying sales taxes on subscription fees from Illinois customers since April 30, 2007. There is no audit or litigation pending with the Illinois Department of Revenue. To the best of our knowledge, the Illinois Department of Revenue has not previously ruled on the same or a similar issue for COMPANY, any related subsidiary or any predecessor. Additionally, neither COMPANY nor any duly appointed representatives have previously submitted the same or similar issue to the Illinois Department of Revenue and withdrew it before a letter ruling was issued.

Thank you for your consideration of this request. If the Department requires further information please contact me directly.

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).

The Private Letter Ruling Committee recently determined that it will no longer issue Private Letter Rulings regarding whether a specific license of prewritten (canned) computer software meets the requirements of subsection (a)(1) of 86 Ill. Adm. Code 130.1935. It is the Private Letter Ruling Committee'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.

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 or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Terry D. Charlton
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