Cases and Rulings in the News States A-M, Illinois Department of Revenue, IL—General Information Letter ST 16-0034-GIL, Illinois, (Aug. 17, 2016)

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ST 16-0034-GIL 08/17/2016 COMPUTER SOFTWARE

A provider of software as a service is acting as a serviceman. If the provider does not the transfer any tangible personal property to the customer, then the transaction generally would not be subject to Retailers' Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax. If the provider transfers to the customer an API, applet, desktop agent, or a remote access agent to enable the customer to access the provider's network and services, it appears the subscriber is receiving computer software that is subject to tax. See 86 Ill. Adm. Code Parts 130 and 140. (This is a GIL.)

August 17, 2016

RE: COMPANY

Dear Xxxxx:

This letter is in response to your letter dated June 13, 2014, and email dated July 9, 2014, 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.

In your letter you have stated and made inquiry as follows:

On behalf of our COMPANY (hereinafter "COMPANY"), we are requesting a Private Letter Ruling ("PLR") regarding the application of Retailers' Occupation Tax and related taxes to their Web collaboration services. An executed Power of Attorney form authorizing FIRM ("FIRM") to represent the COMPANY in this matter is enclosed. To the best of COMPANY and FIRM's knowledge: (1) the Illinois Department of Revenue ("Department") has not previously ruled on the same or similar issue for COMPANY or a predecessor; (2) the same or similar issue was not previously submitted and withdrawn by COMPANY or FIRM prior to the Department's issuance of a PLR; and (3) COMPANY is not under audit by or involved in litigation with the Department for transactions from January 1, 20XX to the present.

Background

COMPANY offers Web collaboration services ("Services") through the COMPANY cloud. No tangible personal property is provided to the customer as part of the Services. Customers utilize their own hardware, software and Internet connectivity to utilize the Services. A description of these Services is as follows:

PRODUCT 1

PRODUCT 1 is an integrated collaboration solution that enables rich online meeting experiences by incorporating audio, video and real-time content sharing. PRODUCT 1 enables people to attend meetings

inside and outside corporate firewalls, on a broad variety of platforms – including mobile devices. PRODUCT 1 helps streamline the meeting process by providing a secure, centralized online space for organizing and sharing all meeting-related activities and information. PRODUCT 1 is a software-as-a-service (SaaS) solution delivered through the COMPANY cloud – a highly available and secure service delivery platform.

PRODUCT 2

PRODUCT 2 is an integrated service designed for interactive online meetings. It enables the sharing of documents, applications and desktops over the Web. PRODUCT 2 can be provisioned without needing information technology professionals. PRODUCT 2 allows users to give presentations, demonstrate software, view and annotate any document electronically, and includes tightly integrated audio and video communications. In addition, PRODUCT 2 has additional features such as *record and playback* and the ability to attend a meeting from select smartphones.

PRODUCT 3

PRODUCT 3 is an integrated service designed for online training and e-learning applications delivered over the Web. It enables users to coordinate training from announcement, to enrollment, to follow-up. PRODUCT 3 allows users to deliver live instruction from a variety of sources directly to learners' desktops and give presentations that include integrated audio, video and interactive multimedia. PRODUCT 3 allows users to administer tests, organize multiple simultaneous breakout sessions, hands-on labs, and record and playback entire sessions for future use.

PRODUCT 4

PRODUCT 4 is an integrated service designed for large online events such as press briefings, product announcements and marketing events delivered over the Web. PRODUCT 4 combines interactive meeting capabilities such as the sharing of documents, applications and desktops with pre-program, post-program and campaign management. PRODUCT 4 includes customized attendee registration, automated email invitations, reminders, audience feedback collection through polling and Q&A, live chat, recording and archiving of seminars for on-demand playback, and lead source tracking enrollment/lead scoring.

PRODUCT 5 is a suite of support services delivered over the Web. The PRODUCT 5 services are each available for purchase individually or in combination, or as follows:

PRODUCT 6

PRODUCT 6 is a service that is designed to provide remote technical support and customer service. It allows users to support remote and end-users through the Web, with no requirement for pre-installed software on either computer. PRODUCT 6 incorporates a custom user interface to simplify support interactions for both the support agent and the end-user. It also provides tools for quick technical support resolution such as viewing system requirements, transferring files, logging on as a System Administrator and rebooting and re-connecting to a remote computer.

PRODUCT 7

PRODUCT 7 service, formerly known as PRODUCT 8, is a service designed to remotely manage and administer a company-wide set of computers using a secure, Web-based tool. PRODUCT 7 allows a user, such as IT or support organization, to access remote computers without needing the computer owner's presence at the machine. It allows functionality to install upgrades, perform maintenance, troubleshoot problems, and engage in proactive support.

PRODUCT 9 by COMPANY 1

PRODUCT 9 by COMPANY 1 is designed to track, route, and manage support tickets from a centralized dashboard over the Web. It has a set of different modules for tracking support activities, document management, incident (ticket) management, knowledge base management, relationship management, report management and a Self-Service portal. Additional modules that can be purchased include product, survey and forum modules.

PRODUCT 10

PRODUCT 10 is a bundle that includes four of COMPANY collaboration services: 1) PRODUCT 1 or PRODUCT 2, 2) PRODUCT 3, 3) PRODUCT 4, and 4) PRODUCT 5 or PRODUCT 6. This bundle of services offers a comprehensive solution for collaboration across four distinct business-specific processes: meetings, training, online events and support.

PRODUCT 11

PRODUCT 11 brings together instant messaging, team spaces and widgets into a single interface. It provides presence, secure instant messaging, one-to-one video, PC-to-PC VoIP calls and desktop share. Team spaces include persistent group discussions, document sharing and out of the box widgets like Address Book, Bookmarks, Browser, Bulletin Board, Calendar, Calendar Dashboard, Debug Viewer, Document Manager, Getting Started, Library Management, Meeting Recording, Profile, RSS Reader, Space Management, Space Member, Table, and What's New.

PRODUCT 12

PRODUCT 12 is a feature designed to capture COMPANY meeting recordings including COMPANY integrated audio or third-party audio to archive or share for future use. PRODUCT 12 recordings can capture all or part of meeting as desired by the meeting host. PRODUCT 12 recordings are stored in the proprietary PRODUCT 13. The following COMPANY 1 services include this functionality: PRODUCT 1, PRODUCT 2, PRODUCT 3, PRODUCT 4 and PRODUCT 5.

PRODUCT 14

PRODUCT 14 recordings accessible in the *My Files* directory or through the Meeting Spaces in PRODUCT 1, and can be played back by a direct stream or through a link. Different packages and subscription models include different amounts of storage. Committed PRODUCT 14 can also be purchased.

PRODUCT 15

PRODUCT 15, formerly known as PRODUCT 16, is a service allowing the user to access a remote computer from any location in the world, where the user only needs a Web browser and an Internet connection and without the user needing to open any ports in a firewall protecting the computer. For example, the PRODUCT 15 user can run any application or access the entire desktop of her remote computer, transfer files to and from the remote computer, or print a document from the remote computer on a printer located at the user's location. PRODUCT 15 has several security features including end-to-end Secure Socket Layer (SSL) encryption, two levels of required authentication and each of the following: (i) the ability to blank the screen of the work or home computer so no one can see what the remotely-located user is doing, (ii) the ability to lock the keyboard and mouse of the remote computer so no one can interrupt the user's use, and (iii) the ability to logout or screen-lock the remote computer after the user's session is complete.

PRODUCT 17

PRODUCT 17 is a service that is designed to create and deliver multimedia content for on-demand access over the Web. With PRODUCT 17, users can create presentations that include, and integrate as desired, audio content, video content and digital presentation software content such as presentations created with Microsoft *PowerPoint* software. Presentations created with PRODUCT 17 can be viewed over the Web or can be downloaded to a laptop or a personal digital assistant.

PRODUCT 18

PRODUCT 18 integrates certain COMPANY asynchronous and real-time collaboration capabilities into one unified suite designed for project teams to work more effectively. PRODUCT 18 provides a collaboration suite including a document manager, group calendar, database manager, task manager and several other collaborative business tools, and is designed to meet the collaboration and web meeting needs of project teams.

The following services are also available as add-ons to purchase with one or more of the services described above:

PRODUCT 19

PRODUCT 19 services are fully integrated with PRODUCT 2. PRODUCT 19 is not offered or available or sold on a stand-alone basis. Options for purchase include:

- *Call-in*: A single conference call-in number is provided to participants to join the PRODUCT 1.
- *Callback*: Participants can join the PRODUCT 1 by having the PRODUCT 1 session call them at the number they specify once they've joined the meeting via the web.
- *Integrated VoIP*: Participants can join a PRODUCT 1 from their computer, using a computer headset with a microphone and speaker.
- *Call Me Back*: Gives customers the option to request a call back when requesting an online support request through PRODUCT 6.

PRODUCT 20

A Web based service for monitoring usage of PRODUCT 1 services such as statistics of active and past COMPANY sessions and the number of attendees in a SERVICE meeting. Reporting options are also included.

PRODUCT 21

PRODUCT 22 provides Tier 1 technical support, .WRF recording and reporting services. Options for purchase include:

- Standard Meeting Conferencing Service: SERVICE Producer joins the host online 30 minutes prior to start time, one-hour in-meeting support, no recording. Additional support hours are available for purchase.
- Premium Meeting Conferencing Service: SERVICE Producer joins the host online 30 minutes prior to start time, one-hour in-meeting support and recording. Recordings are available with 24 hours. Additional support hours are available for purchase.
- Standard Training Conferencing Service: SERVICE Producer joins the host online 30 minutes prior to start time, one-hour in-session support, no recording. Additional support hours are available for purchase.
- Premium Training Conferencing Service: SERVICE Producer joins the host online 30 minutes prior to start time, one-hour in-session support and recording. Recordings are available within 24 hours. Additional support hours are available for purchase.

- Standard Event Conferencing Service: SERVICE Producer joins the host online 30 minutes prior to start time, one hour in-event support and recording. Recording and reports are available within 24 hours. Additional support hours are available for purchase.
- Premium Event Conferencing Service Consultation: Event strategy and creation; *Dry Run*: Event timeline and technical run-through; *Live Event* SERVICE Producer starts online event 30 minutes prior to start time, one-hour in-event support and recording. Recording and reports are available within 24 hours. Additional support hours are available for purchase.

How COMPANY PRODUCT 1 Works

As the predominate source of revenue, we would like to explain how a customer uses PRODUCT 1. As described above, PRODUCT 1 is a cloud-based web conferencing application that permits desktop sharing through a Web browser with audio and video capabilities. PRODUCT 1 operates through a participant's computer or mobile device. Audio functionality is either through the computer, mobile device or telephone. Video functionality is through a webcam or mobile device camera but video is not required to participate in the meeting. All participants provide their own hardware and Internet or telephone connection and no hardware or software is provided by PRODUCT 1. No separate charge is made for these downloads.

PRODUCT 1 is offered on a subscription basis (monthly or annually) with plans based on the number of hosts and participants. Once a potential Subscriber chooses a plan that meets their business needs and agrees to the *Terms & Conditions of Service* they can use the service. As an option, a subscriber may add a SERVICE Producer plan which provides call back functionality as well as a toll-free number for participants to use. The PRODUCT 23 option has several plans which vary based on the number of minutes per month. If a subscriber goes over the allotted number of minutes in their plan, additional minutes are billed on a per minute basis.

To schedule a meeting, a subscriber logs on to the COMPANY website and enters a meeting name, date and time, meeting length as well as the email address of meeting participants. Participants then receive a meeting invitation email with the meeting name, date, time, link to the meeting and a toll dial-in number is provided with a meeting ID and access code. For subscribers with the optional PROCUCT 23 plan, a toll-free dial-in number is provided in the meeting invitation.

To join the meeting, the participant clicks on the link and enters their contact information and either uses their computer's microphone and speakers or calls the dial-in number. Participants with cameras may also project video of themselves to other participants during the meeting. For mobile devices, the COMPANY app allows subscribers to create and start meetings and allows attendees to join meetings. During the meeting, subscribers have the ability to share content from their computer with participants or hand off control to another participant so that they can share their content with other participants of the meeting.

Our Analysis

The Services offered by COMPANY are non-taxable services and does [sic] not constitute the lease or license of software. No hardware or software is provided to the customer.

The Illinois Retailers' Occupation Tax ("ROT") is imposed on persons engaged in the business of selling tangible personal property at retail unless specifically exempted from tax. See 86 Ill. Adm. Code 130.101. However, the ROT and Use Tax does [sic] not apply to sales of service that do not involve the transfer of tangible personal property to customers. However, if tangible personal property is transferred incident to sales of service, the Service Occupation Tax or Use Tax will apply to the serviceman, see 86 Ill. Adm. Code 140.101 through 140.109.

Information or data transferred electronically is not considered tangible personal property, see 86 Ill. Adm. Code 130.2105(a)(3). In this case, the Services offered by the COMPANY do not involve the transfer

of tangible personal property, only information or data electronically through their cloud. As such, the Services are not subject to Illinois sales or use taxes.

Requested Action

We request that the Illinois Department of Revenue review the stated facts to issue a private letter ruling that the Taxpayer's Services are not subject to Illinois sales or use taxes.

Please contact me if you have any questions in the important matter.

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). The Department recently met and determined that it would decline to issue a Private Letter Ruling in response to your request. We hope, however, the following General Information Letter will be helpful in addressing your question.

Sales Tax:

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* 35 ILCS 120/2; 86 Ill. Adm. Code 130.101. In Illinois, Use Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. *See* 35 ILCS 105/3; 86 Ill. Adm. Code 150.101. These taxes comprise what is commonly known as "sales" tax in Illinois. If the purchases occur in Illinois, the purchasers must pay the Use Tax to the retailer at the time of purchase. The retailers are then allowed to retain the amount of Use Tax paid to reimburse themselves for their Retailers' Occupation Tax liability incurred on those sales. If the purchases occur outside Illinois, purchasers must self-assess their Use Tax liability and remit it directly to the Department.

Service Transactions:

Retailers' Occupation Tax and Use Tax do not apply to sales of service. Under the Service Occupation Tax Act, businesses providing services (*i.e*., servicemen) are taxed on tangible personal property transferred as an incident to sales of service. See 86 Ill. Adm. Code 140.101. The purchase of tangible personal property that is transferred to the service customer may result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon his activities. The serviceman's liability may be calculated in one of four ways:

(1) separately-stated selling price of tangible personal property transferred incident to service;
(2) 50% of the serviceman's entire bill;
(3) Service Occupation Tax on the serviceman's cost price if the serviceman is a registered de minimis serviceman; or
(4) Use Tax on the serviceman's cost price if the serviceman is de minimis and is not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

The Department does not consider the viewing, downloading or electronically transmitting of video, text and other data over the internet to be the transfer of tangible personal property. However, if a company provides services that are accompanied with the transfer of tangible personal property, including computer software, such service transactions are generally subject to tax liability under one of the four methods set forth above.

If a transaction does not involve the transfer of any tangible personal property to the customer, then it generally would not be subject to Retailers' Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax.

Computer Software

"'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.

It appears from your letter that the Company is making sales of service and is a serviceman. As a serviceman, the Company does not incur Retailers' Occupation Tax. Service Occupation Tax is imposed upon all persons engaged in the business of making sales of service on all tangible personal property transferred incident to a sale of service, including computer software (35 ILCS 115/3), and is calculated as explained above. Currently, computer software provided through a cloud-based delivery system – a system in which computer software is never downloaded onto a client's computer and is only accessed remotely – is not subject to tax. The Department continues to review cloud-based arrangements. If, after review, the Department determines that these transactions are subject to tax, it will only apply this determination prospectively.

You state in your letter that a customer of the services the Company provides does not receive any tangible personal property as part of the service. You also state that customers "utilize their own hardware, software and Interconnect connectivity to utilize the Services." In your description how the PRODUCT 1 works, you once again state, "All participants provide their own hardware and Internet or telephone connection and no hardware or software is provided by COMPANY" You further state, "No separate charge is made for these downloads." The Terms of Service also state that customer may be required to download and install SERVICE Producer software. The Department does not understand the nature of the software that may be provided by PRODUCT 23 and downloaded by a customer. However, the Department wishes to point out that "computer software" is defined broadly in the Retailers' Occupation Tax Act. Even if a provider of a service only provides to the customer an API, applet, desktop agent, or a remote access agent to enable the customer to access the provider's network and services, it appears the customer is receiving computer software. Although there may not be a separate charge to the customer for the computer software, it is nonetheless subject to tax, unless the transfer qualifies

as a non-taxable license of computer software. If the provider, as a serviceman, is not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act and qualifies as a de minimis serviceman, the provider could elect to pay Use Tax on its cost price of the computer software.

I hope this information is helpful. If you have further questions related to the Illinois sales tax laws, please visit our website at *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