New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-96 (27)S
Sales Tax
May 2, 1996

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. S950811A

On August 11, 1995, a Petition for Advisory Opinion was received from ALLTEL Financial Information Services, Inc. (formerly Systematics Financial Services, Inc.), 4001 Rodney Parham Rd., Little Rock, Arkansas 72212.

The issue raised by Petitioner, ALLTEL Financial Information Services, Inc., is whether sales tax should apply to fees billed under a software license and maintenance agreement signed prior to a change in the Tax Law effective September 1, 1991.

Petitioner provides the following facts. Petitioner provides software for the financial industry to meet the data processing needs for all major applications of banks and other financial institutions. The software is often provided in a packaged investment charter agreement which includes a software license, software upgrades, documentation, training courses, corrections, replacements, installation assistance, technical assistance and consultation throughout the life of the contract. All of these services are packaged together and cannot be broken out separately for the client to purchase part of the package and not the whole. Generally, fees are paid partially upon signing of the contract, and then the remainder of the fees are paid annually over the life of the contract. The future services and software upgrades are sometimes referred to as software maintenance.

The software is pre-written software that must be modified to some extent to adapt to the customer's specific environment. An analysis of the customer's needs and the specific computer equipment is required before the software can be licensed.

Prior to a change in the Tax Law, effective September 1, 1991, Petitioner's software was considered custom software (intangible personal property) and exempt from sales tax. Maintenance relating to the intangible software was also exempt from sales tax.

Petitioner now applies sales tax to all fees under investment charter software license agreements signed after September 1, 1991. Under the amendments to the Tax Law effective September 1, 1991, Petitioner's software is considered taxable tangible personal property because it is pre-written software rather than being designed and developed for one specific user. Petitioner states in its Petition that maintenance relating to this pre-written software is taxable under current law. According to Petitioner, the entire charge for the maintenance is taxable because it includes software upgrades and enhancements along with other services.

Petitioner has provided a sample contract and amendment for review. The contract includes a fee payment schedule and a description of the services provided in the package.

The contract was originally entered into on November 7, 1988 for a five (5) year term. The contract was amended April 30, 1991 changing the effective date to November 7, 1996.

Effective September 1, 1991, Chapter 166 of the Laws of 1991 amended the Tax Law relating to pre-written computer software. Section l101(b)(6) of the Tax Law was amended to define tangible personal property, in part, as follows:

> Tangible personal property. Corporeal personal property of any nature .... Such term shall also include pre-written computer software, whether sold as part of a package, as a separate component, or otherwise, and regardless of the medium by means of which such software is conveyed to a purchaser ....

Paragraph (14) was added to section ll01(b) of the Tax Law to read as follows:

> Pre-written computer software. Computer software (including pre-written upgrades thereof) which is not software designed and developed by the author or other creator to the specifications of a specific purchaser. The combining of two or more pre-written computer software programs or pre-written portions thereof does not cause the combination to be other than pre-written computer software. Pre-written software also includes software designed and developed by the author or other creator to the specifications of a specific purchaser when it is sold to a person other than such purchaser. Where a person modifies or enhances computer software of which such person is not the author or creator, such person shall be deemed to be the author or creator only of such person's modifications or enhancements. Pre-written software or a pre-written portion thereof that is modified or enhanced to any degree, where such modification or enhancement is designed and developed to the specifications of a specific purchaser, remains pre-written software; provided, however, that where there is a reasonable, separately stated charge or an invoice or other statement of the price given to the purchaser for such modification or enhancement, such modification or enhancement shall not constitute pre-written computer software.

Subdivision (o) was added to section 1115 of the Tax Law to read as follows:

> Services otherwise taxable under subdivision (c) of section eleven hundred five or under section eleven hundred ten shall be exempt from tax under this article where performed on computer software of any nature;

> provided, however, that where such services are provided to a customer in conjunction with the sale of tangible personal property any charge for such services shall be exempt only when such charge is reasonable and separately stated on an invoice or other statement of the price given to the purchaser.

In addition, section 1105(c)(3) of the Tax Law imposes sales tax on the following:

> (3) Installing tangible personal property, excluding a mobile home, or maintaining, servicing or repairing tangible personal property, including a mobile home, not held for sale in the regular course of business, whether or not the services are performed directly or by means of coin-operated equipment or by any other means, and whether or not any tangible personal property is transferred in conjunction therewith.

Section 406(j) of Chapter 166 of the Laws of 1991, pertaining to the effective date of the above-referenced pre-written computer software provisions, states:

> The provisions of sections one hundred fifty-four through one hundred fifty-nine of this act shall take effect September 1, 1991, and shall apply to all sales or uses made on or after that date although made under a prior contract, except that a delivery or transfer of possession of computer software on or after such date pursuant to an agreement for the sale of such software made before May 1, 1991, shall not be subject to tax if (1) such agreement for the sale of such software was made in writing, (2) the software so sold or agreed to be sold was segregated, before May 1, 1991, from any other similar property in the vendor's possession and identified as having been appropriated to such sale or agreement of sale, and (3) the purchaser, before September 1, 1991, shall have paid to the vendor not less than ten percent of the sale price of such software.

In the case of the sample contract provided by Petitioner the agreement to sell and maintain the software was entered into prior to September 1, 1991, and signed by the purchaser on November 7, 1988. However, the transitional provisions of Section 406(j) of Chapter 166 of the Laws of 1991 provide that the pre-written computer software provisions enacted by Chapter 166 apply to sales or uses of software and related services made on or after September 1, 1991, although made under a prior contract. Accordingly, the software maintenance services furnished by Petitioner on

or after September 1, 1991, which are not exempt from tax under Section 1115(o) of the Tax Law, are subject to tax even though the services are performed under a contract entered into before September 1, 1991.

In addition, Petitioner does not separately state the charges for software maintenance services from the charges for software upgrades and enhancements. According to Petitioner, the software upgrades and enhancements are pre-written software. Accordingly, the software maintenance services furnished by Petitioner after September 1, 1991, are taxable since these services are sold in conjunction with pre-written computer software which, after September 1, 1991, constitutes tangible personal property. Although Section 406(j) of Chapter 166 of the Laws of 1991 provides for special circumstances under which pre-written software sold after September 1, 1991, pursuant to a pre-existing contract, will not be considered tangible personal property, it does not appear that these circumstances apply in this case. There is no indication that the software upgrades and enhancements furnished under Petitioner's contract on or after September 1, 1991, were segregated by Petitioner from other similar property in its possession and identified as having been appropriated to the contract before May 1, 1991. Therefore, to the extent they do not qualify under the transitional provisions of Section 406(j) of Chapter 166, these software upgrades and enhancements, and the software maintenance services provided in conjunction with them, which are sold on or after September 1, 1991, are subject to State and local sales and use taxes. Maintenance services furnished pursuant to Petitioner's contract prior to September 1, 1991, are not subject to tax. See Computer Language Research, Adv. Op. Comm. Of Taxation and Finance, June 7, 1989, TSB-A-89(13)S.

Because Petitioner's maintenance agreement charges under the sample contract are due on an annual basis, Petitioner may pro-rate the annual maintenance charge for the year 1991 by comparing the number of months for the period September 1, 1991 to the annual payment date, to the twelve month annual period (i.e., two twelfths of the Petitioner's total maintenance charge due in November 1991 is subject to the state and local sales and use taxes). The Petitioner's maintenance charges for the remainder of the maintenance agreement after 1991 are also subject to the appropriate state and local sales and use taxes.

/s/

DATED: May 2, 1996

Doris S. Bauman
Director
Technical Services Bureau