

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

TSB-A-91 (70)S  
Sales Tax  
November 8, 1991

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S910808B

On August 8, 1991, a Petition for Advisory Opinion was received from Arthur Andersen and Co., Spear Street Tower, Suite 3500, One Market Plaza, San Francisco, CA 94105.

The issue raised by Petitioner, Arthur Andersen and Co., is whether its client's charge for an optional maintenance agreement on computer software is subject to New York State and local sales and use tax.

Petitioner's client designs, publishes, and retails computer software application development tools ("the Software Product"). The Software Product provides a complete range of interactive facilities to design, generate, document and maintain application software. It generates the source code in RPG or COBOL needed to perform a wide range of interactive, batch and report functions. It also contains a set of administrative and support tools which enable development of menus, manipulation of objects and automatic documentation of existing systems. The Software Product has made the process of developing custom software on midrange computers more efficient than conventional programming methods.

Petitioner's client analyzes the customer's requirements and makes the necessary program adaptations to facilitate the customer's use of the program on their specific CPU. In addition, the software license is evidenced by a written agreement which restricts the customer's duplication, licensing, sublicensing or transferring of the Software Product to a third party. Charges for the canned portion of the program are not separately stated from the charges for the modified portion of the program. Petitioner's client will provide another copy at minimal charge if the customer loses or damages the software and the Software Product is destroyed or returned upon termination of the license period.

Petitioner's client sells the Software Product to customers under a perpetual licensing agreement. This licensing agreement provides for an optional maintenance agreement which may be cancelled at any time. The maintenance agreement covers the canned portion as well as the modified portions of the program. The cost for the maintenance agreement is stated separately within the licensing agreement and is dependent upon the particular computer hardware to which the Software Product is adapted. The fee is assessed on an annual basis. Charges for the maintenance agreement are not separately stated between the canned portion or the modified portion of the program, nor are they broken down between the four services provided under the agreement.

The four service features provided under the maintenance agreement are:

- (1) Telephone support service;
- (2) User group conference attendance;
- (3) Software upgrades, and;
- (4) Program Temporary Fix (PTF) service.

Software upgrades represent the advancement and improvement in products which are available upon request. The releases must be individually coded to facilitate each customer's use on their specific CPU. The PTF service represents Petitioner's support and assistance to clients in instances where the Software Product experiences difficulties, i.e., "bug" removal.

Technical Services Bureau Bulletin 1978-1 defines software as:

"Instructions and routines (programs) which, after an analysis of the customer's specific data processing requirements, are determined necessary to program the customer's electronic data processing equipment to enable the customer to accomplish specific functions with his EDP system." To be considered exempt "software" for purposes of this bulletin, one of the following elements must be present:

A. Preparation or selection of the program for the customer's use requires an analysis of the customer's requirements by the vendor.

or

B. The program requires adaptation, by the vendor, to be used in a specific environment, i.e., a particular make and model of computer utilizing a specified output device. For example, a software vendor offers for sale a pre-written sort program which can be used in several computer models. Prior to operation, instructions must be added by the vendor which specify the particular computer model in which the program will be utilized.

In Computer Language Research, Inc., Adv Op Comm T & F, June 7, 1989, TSB-A-89(13)S, the Commissioner advised that computer programs (software) developed by Petitioner which required an analysis of the customer's requirements and modification of the actual program for use by such customer was considered intangible personal property and therefore not subject to New York State and local sales and use taxes.

Section 1105(c) of the Tax Law imposes tax upon the receipts from every sale, except for resale, of certain enumerated services. The maintaining and servicing of an intangible is not a service enumerated under Section 1105(c) of the Tax Law and, therefore, the fee paid for such service is not subject to sales or use tax.

Effective September 1, 1991, Section 1101(b) of the Tax Law was amended to add the following:

(14) 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.

Moreover, Section 1115 of the Tax Law was amended effective September 1, 1991, to add the following:

(o) 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. . .

Pursuant to Computer Language Research, Inc., supra., the sale of computer programs developed by Petitioner's client and modified to meet the customer's requirement prior to September 1, 1991, is considered the sale of an intangible and, therefore, the sale of such program is not subject to sales and use tax. Accordingly, Petitioner's clients sales of maintenance agreements prior to September 1, 1991, are not subject to sales and use tax since the fees paid are for the maintaining and servicing of an intangible, a service not enumerated under Section 1105(c) of the Tax Law as subject to sales and use tax.

As for Petitioner's clients sale of maintenance agreements on or after September 1, 1991, pursuant to Section 1101(b)(14) of the Tax Law the sale of pre-written software or a pre-written portion thereof that is modified or enhanced to any degree to meet the specifications of a specific purchaser constitutes the sale of tangible personal property unless charges for the pre-written portion and the modifications are separately stated on an invoice or other statement given to the purchaser. Moreover, pursuant to Section 1115(o) of the Tax Law the entire charge for services performed

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under the maintenance agreement is subject to sales tax unless the charge is separately stated between the taxable and exempt services provided under the agreement. Accordingly, since Petitioner's client does not separately state the charges for the pre-written portion and the modified portion and does not separately state the charges for the four services it provides under the maintenance agreement as mandated pursuant to Sections 1115(o) of the Tax Law, the entire charge received from the sale of the maintenance agreement is subject to sales and use tax pursuant to Sections 1101(b)(14) and 1115(o) of the Tax Law.

DATED: November 8, 1991

s/PAUL B. COBURN  
Deputy Director  
Taxpayer Services Division

NOTE: The opinions expressed in Advisory Opinions  
are limited to the facts set forth therein.