

December 16, 2002

Re: Our File Number LR-02-206; Canned Software

Dear

This is in response to your inquiry concerning the sales, franchise and income tax treatments of transactions arising from the sale of canned software. I have copied your fact situations and questions into this email and each question is followed by our response.

**Fact Situation**

XYZ is a manufacturer of "canned or prewritten" software (in a state other than your state), and sells its software into several states, including your state. XYZ does not maintain a physical location in your state, owns no property, and has no payroll in your state.

XYZ's software is sold by granting customers in your state a license to use the software. The software is shipped to customers in the following manners:

- By mail or common carrier,
- Electronically via the telephone or
- Installed by XYZ employees at a location in your state.

In addition, as part of the installation process, XYZ employees may provide training.

In general, customers are not required to purchase service/maintenance agreements. If customers purchase such an agreement, they are entitled to receive telephone service and minor software updates. XYZ does not specifically allocate charges for its service/maintenance agreements between the service elements and software updates. However, XYZ believes that most of such charges should be allocable to the service elements of the agreements. The agreements are for a term of 12 months and are renewable in increments of 12 months.

**Sales & Use Tax**

1. Is sales & use tax nexus created by XYZ's sale/licensing of its "canned or prewritten" software in your state?

**Response: If XYZ has employees working in the state, that contact is sufficient physical connection with the company for the company to be required to charge and remit sales tax on any sales completed by XYZ employees and use tax on any sales completed by mail, common carrier or telephone. Please refer to Oklahoma Tax Commission Rule 710:65-21-3.**

2. If the answer to question 1 is yes, are XYZ's software installation and training activities subject to sales & use tax? Does the answer change if they are contracted for and billed separately from the software?

**Response: If the installation and training activities are contracted for and billed separately from the software, they are not subject to sales tax. Please refer to Oklahoma Tax Commission Rule 710:65-19-158.**

3. If the answer to question 1 is yes, are XYZ's service/maintenance agreements subject to sales & use tax? Does the answer change if charges for the service elements and software updates of the agreements are separately stated?

**Response: Since the service/maintenance agreements provide for software updates, they are subject to sales or use tax depending on which tax is due. Please see Oklahoma Tax Commission Rule 710:65-19-52.**

### **Income/Franchise Tax**

1. Is income/franchise tax nexus created by XYZ's sale/licensing of its "canned or prewritten" software in your state?

**Response: Yes. Please refer to Oklahoma Tax Commission Rule 710:50-17-3(9)**

2. Is income/franchise tax nexus created by XYZ's software installation and training activities?

**Response: Yes. Please refer to Oklahoma Tax Commission Rule 710:50-17-3(11)**

3. If the answer to either question 1 or 2 is yes, does the XYZ's sale/licensing of its "canned or prewritten" software constitute a sale of tangible property for the purposes of apportioning XYZ's income?

**Response: Yes.**

4. If the answer to either question 1 or 2 is yes, how are XYZ's service/maintenance agreements treated for the purposes of apportioning XYZ's income?

**Response: They are considered to be Oklahoma Sales and included in the sales apportionment factor.**

This response applies only to the circumstances set out in your request of November 8, 2002. Pursuant to Commission Rule 710:1-3-73(e), this Letter Ruling may be generally relied upon **only** by the entity to whom it is issued, assuming that all pertinent facts have been accurately and completely stated, and that there has been no change in applicable law.

If I can be of further assistance, please feel free to contact me.

Sincerely,  
OKLAHOMA TAX COMMISSION

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