



OKLAHOMA TAX COMMISSION

TAX POLICY DIVISION
DAWN CASH, DIRECTOR

PHONE (405) 521-3133
FACSIMILE (405) 522-0063

May 14, 2007

RE: Our File Number LR-06-135: Taxability of hardware and software maintenance agreements

Dear

This is in response to your request for a written opinion regarding the application of Oklahoma sales and use tax to the transaction in your correspondence. I have scanned your fact situation and questions into this letter, followed by our response.

Background

The Company is a wholesaler and retailer of video transmission equipment and prewritten (canned) software. The canned software is only sold electronically. That is, the customer downloads the software from the Company's server and does not receive a copy of it in tangible form. The Company also offers an optional maintenance agreement ("Agreement") that provides for both hardware and software maintenance and support. The Company does not offer components of the Agreement separately and it is unable to allocate a separate price to each component. The following services and functions are provided during the term of the Agreement:

- 24 hour, 7 days a week, 365 days a year support.
- Email and phone support as well as remote diagnostic services.
- Software support for covered canned software program which includes maintenance and both minor and major releases. Maintenance updates, patches, and updates may be provided in tangible form, via electronic download or by "load and leave."
- Product repair and advance replacement of hardware parts.

The Agreement is sold for one single price and no allocation is made internally for any components of the Agreement.

Analysis

As explained above, the Company offers the Agreement for a single price. As such, the Company seeks guidance with respect to the application of Oklahoma sales and use tax with respect to its sale of the Agreement. Based on our findings below, the hardware maintenance portion of the Agreement is nontaxable while the software maintenance portion appears to be taxable.

Oklahoma Regulation Rule 710:65- I 9-365 provides that separately stated charges for an optional extended maintenance agreement or warranty is not taxable.

Oklahoma Regulation Rule 710: 65-19-52 provides that separately stated charges for an optional software maintenance agreement are taxable if the agreement provides only upgrades or enhancements or if it provides upgrades or enhancements and support services and the fee for the support services is not separately stated.

Due to the bundled nature of the Agreement, we would appreciate your response to the questions below.

Issues

1. What is the application of sales and use tax to the sales price of the Agreement?

Our Response: In situations where taxable and exempt personal property or services have been bundled together and sold by the seller as a single product, the total gross receipts from the bundled transaction are subject to sales tax. Therefore, the sale of the agreement would become taxable as part of "gross receipts, "gross proceeds" or "sales price". See Commission Rule 710:65-1-9 (b).

2. Does the Company have any sales or use tax liability with respect to providing any of the services pursuant to the Agreement?

Our Response: Any tangible personal property used in connection with the labor services performed under the contract which are not covered under the contract and which are billed/sold to the customer are subject to sales tax. Tangible personal property purchased by the person providing the maintenance service is taxable to the service provider. See Commission Rules 710:65-19-365 and 710:65-19-371.

This response applies only to the circumstances set out in your request of August 18, 2006. 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


Brenda J. Sullivan
Tax Policy Analyst