

1 Department of Revenue

2

3 Adopted Permanent Rules Relating to Computer Software

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5 Rules as Adopted

6 8130.9910 COMPUTER SOFTWARE.

7 Subpart 1. Definitions. For purposes of this part, the  
8 following words and phrases have the meanings given them in  
9 items A to H I.

10 A. A "sale" and a "purchase" has the meaning given it  
11 in Minnesota Statutes, section 297A.01, subdivision 3, clause  
12 (k).

13 B. "Computer program" has the meaning given it in  
14 Minnesota Statutes, section 297A.01, subdivision 18, clause (3).

15 C. "Custom computer program" has the meaning given it  
16 in Minnesota Statutes, section 297A.01, subdivision 18.

17 D. "Canned or prewritten computer program" is defined  
18 in Minnesota Statutes, section 297A.01, subdivision 18, to mean  
19 a "program that is held or existing for general or repeated sale  
20 or lease, even if the prewritten or "canned" program was  
21 initially developed on a custom basis or for in-house use."

22 A computer program is considered to be canned or prewritten  
23 if it meets the following guidelines:

24 (1) the object code of the program is not  
25 modified by the seller. Modification of the program by  
26 inserting file names or formatting data is not changing the  
27 object code;

28 (2) the program, copies of which are  
29 mass-produced by the manufacturer, is inventoried by a vendor,  
30 or otherwise held for repeated sale, license, or lease; and

31 (3) the program is sold, licensed under a written  
32 contract agreement, or leased by means of a shrink-wrapped,  
33 box-top, or tear-open license agreement or bill of sale.

34 E. "Computer" means an electronic device, including  
35 word processing equipment and testing equipment, or combination

1 of components that is programmable and that includes a processor  
 2 (central processing unit or microprocessor), internal memory,  
 3 and input and output connections. An electronic device  
 4 otherwise qualifying as a computer remains a computer even  
 5 though it may be used for information processing, data  
 6 acquisition, process control, or for the control of  
 7 manufacturing machinery or equipment. As provided in Minnesota  
 8 Statutes, section 297A.01, subdivision 18, clause (2),  
 9 "computer" does "not include tape-controlled automatic drilling,  
 10 milling, or other manufacturing machinery or equipment."

11 F. "Maintenance agreements agreement support services"  
 12 means ~~providing error corrections, improvements,~~  
 13 updates received by any means, consultation services, or  
 14 technical support for computer programs.

15 G. "Upgrades or enhancements" means information and  
 16 directions which provide new or significantly improved  
 17 functionality to a computer program. It includes information  
 18 and directions that dictate the function performed by data  
 19 processing equipment. Computer software, in any form which is  
 20 provided under a maintenance agreement, and which does not  
 21 provide new or significantly improved functionality is deemed to  
 22 be a maintenance agreement support service.

23 H. "Computer program" means computer software.

24 ~~H.~~ I. "Storage media" has the meaning given it in  
 25 Minnesota Statutes, section 297A.01, subdivision 18, clause (1).

26 Subp. 2. Tax applications.

27 A. Sales tax is due on the sale, lease, or license of  
 28 a canned or prewritten program that is held or existing for  
 29 general or repeated sale, lease, or license. The sale of canned  
 30 or prewritten programs is the sale of tangible personal  
 31 property. Minnesota Statutes, section 297A.01, subdivision 11,  
 32 defines "tangible personal property" in part to include  
 33 "computer software, whether contained on tape, discs, cards, or  
 34 other devices."

35 B. Sales tax is not due on the sale, lease, or  
 36 license of a custom computer program. The sale of a custom

1 computer program is a service transaction. The purpose of the  
 2 transaction is to obtain personalized service and the expert  
 3 knowledge of the program creator. The transfer of any tangible  
 4 personal property is incidental to the service being performed.

5 C. Charges for computer program maintenance furnished  
 6 for a canned computer program are taxable if the customer is  
 7 entitled to receive or receives canned computer software  
 8 upgrades or enhancements. However, charges for computer program  
 9 maintenance furnished for custom software are not taxable.

10 Maintenance contracts sold in connection with the sale or  
 11 lease of canned software ~~generally~~ may provide that the  
 12 purchaser will be entitled to receive ~~storage-media-on-which~~  
 13 ~~prewritten-program-improvements-have-been-recorded~~ upgrades or  
 14 enhancements. The maintenance contract may also provide that  
 15 the purchaser will be entitled to receive ~~certain-services,~~  
 16 ~~including-error-corrections-and-telephone-or-on-site~~  
 17 ~~consultation~~ maintenance agreement support services.

18 (1) If the maintenance contract is required by  
 19 the vendor as a condition of the sale or rental of canned  
 20 software, it will be considered as part of the sale, or rental  
 21 of the canned software, and the gross sales price is subject to  
 22 tax whether or not the charge for the maintenance contract is  
 23 separately stated from the charge for the software.

24 (2) If the maintenance contract is optional to  
 25 the purchaser of canned software~~;~~:

26 (a) then only the portion of the contract  
 27 fee representing ~~improvements~~ upgrades or enhancements delivered  
 28 on storage media or by any other means is subject to sales tax  
 29 if the fee for ~~other-services,-including-consultation-services~~  
 30 ~~and-error-corrections,~~ any maintenance agreement support  
 31 services is separately stated~~;~~;

32 (b) if the fee for ~~other-services,-including~~  
 33 ~~consultation-services-and-error-corrections,~~ any maintenance  
 34 agreement support services is not separately stated from the fee  
 35 for ~~improvements~~ upgrades or enhancements delivered on storage  
 36 media or by any other means, then 20 percent of the entire

1 charge for the maintenance contract is subject to sales tax;  
 2 (c) if the maintenance contract only  
 3 provides canned computer software upgrades or enhancements, and  
 4 no maintenance agreement support services, then the entire  
 5 contract is taxable;

6 (d) if the maintenance contract only  
 7 provides maintenance agreement support services, and the  
 8 customer is not entitled to or does not receive any canned  
 9 computer software upgrades or enhancements, then the entire  
 10 contract is exempt.

11 D. Separately stated charges for instructions written  
 12 training materials on the use of a canned computer program are  
 13 taxable. Charges for instructions written training materials on  
 14 the use of a custom computer program are not taxable, whether or  
 15 not separately stated. Charges for training services and  
 16 similarly related services are nontaxable.

17 E. When a computer and canned computer programs are  
 18 purchased together, the sales tax is due on the total charge.

19 F. When a computer and custom computer programs are  
 20 purchased together, sales tax is due on the total charge if the  
 21 charge for the custom computer program is not separately stated.

22 G. Master computer programs which are purchased and  
 23 used to make copies for sale or lease are property purchased for  
 24 resale and not subject to sales tax. See Minnesota Statutes,  
 25 section 297A.01, subdivision 4.

26 ~~H. Modification-to-existing-prewritten-software-to~~  
 27 ~~meet-the-customer's-needs-is-custom-computer-programming-only-to~~  
 28 ~~the-extent-of-the-modification-and-only-to-the-extent-that-the~~  
 29 ~~actual-amount-charged-for-the-modification-is-separately~~  
 30 ~~stated.~~ Examples of services that do not result in custom  
 31 software include loading parameters to initialize program  
 32 settings and arranging preprogrammed modules to form a complete  
 33 program.

34 ~~When-the-charges-for-modification-of-a-prewritten-program~~  
 35 ~~are-not-separately-stated, tax-applies-to-the-entire-charge-made~~  
 36 ~~to-the-customer-for-the-modified-program-unless-the-modification~~

~~1 is-so-significant-that-the-new-program-qualifies-as-a-custom  
2 program.--If-the-prewritten-program-before-modification-was  
3 previously-marketed,--the-new-program-will-qualify-as-a-custom  
4 program-if-the-price-of-the-prewritten-program-was-50-percent-or  
5 less-of-the-price-of-the-new-program.--If-the-prewritten-program  
6 was-not-previously-marketed,--the-new-program-will-qualify-as-a  
7 custom-program-if-the-charge-made-to-the-customer-for-custom  
8 programming-services,--as-evidenced-by-the-records-of-the-seller,  
9 was-more-than-50-percent-of-the-contract-price-to-the-customer.~~

10 No tax results when the modifications to existing  
11 prewritten software are required to meet the customers' specific  
12 needs. These modifications are considered to be custom  
13 programming.

14 When the charges for modification are not separately  
15 stated, the records of the transaction may be used to  
16 demonstrate to what extent the program has been modified.

17 The department will use the following records to determine  
18 the extent of modification to prewritten software when there is  
19 not a separate charge for the modification: logbooks,  
20 timesheets, dated documents, source codes, specifications of  
21 work to be done, design of the system, performance requirements,  
22 diagrams of programs, flow diagrams, coding sheets, error  
23 printouts, translation printouts, correction notes, and invoices  
24 or billing notices to the client.

25 If the charges for modification are not separately stated  
26 and the records of the transaction do not adequately document  
27 the extent of the modifications, the entire charge for the  
28 program is taxable.

29 I. Canned or prewritten computer programs may be  
30 transferred to the customer in the form of punched cards, data  
31 on magnetic tape, or by listing the program instructions on  
32 coding sheets. In some cases they are usable as written.  
33 However, in most cases it is necessary that the program be  
34 modified, adapted, and tested to meet the customer's particular  
35 needs. The sale of all property, including coding sheets, cards  
36 or magnetic tape, on which or into which such programs have been

1 coded, punched, or otherwise recorded is subject to tax.

2           J. The temporary transfer of possession of a canned  
3 or prewritten computer program, for a consideration, for the  
4 purpose of direct use or to be recorded by the customer, is a  
5 lease or the granting of a license to use or consume tangible  
6 personal property and the tax does apply. Where the  
7 consideration consists of license fees or royalty payments for  
8 canned or prewritten computer programs, all license fees or  
9 royalty payments, present or future, whether for a minimum use  
10 or for extended periods, are ~~not~~ includable in the measure of  
11 tax.

12           K. Programming changes to a canned or prewritten  
13 computer program to adapt it to a customer's equipment,  
14 including translating a program to a language compatible with a  
15 customer's equipment, are in the nature of fabrication labor and  
16 are taxable.

17           L. Charges for assembler, compiler, utility, and  
18 other canned or prewritten computer programs provided to those  
19 who lease or purchase automatic processing equipment are subject  
20 to tax.