



**Revenue Ruling  
No. 04- 001  
Sales and Use Tax  
March 17, 2004**

**State Sales Taxability of Charges for Computer Software Maintenance Agreements**

The purpose of this Revenue Ruling is to discuss the department's position concerning the sales taxability of charges for computer software maintenance agreements in view of:

- The 1994 decision of the Louisiana Supreme Court in *South Central Bell Telephone Company v. Sidney J. Barthelemy, et al.*, 94-0499 (La. 10/17/94), 643 So. 2d 1240, in which the court held that either "canned" or custom software constitutes "tangible personal property," as the term is defined by La. Rev. Stat. Ann §47:301(16);
- An amendment by Acts 1998, No. 46 to the definition of "tangible personal property" for sales tax purposes, adding an exclusion from this term for the work products (other than work products consisting of the creation, modification, updating, or licensing of computer software) of persons licensed or regulated by Title 37 of the Louisiana Revised Statutes;
- The 2003 decision of the Louisiana First Circuit Court of Appeal in *Shaw Group, Inc. v. Kennedy*, 02 0655 (La.App. 1 Cir, 07/02/03), in which the court held that state sales tax was not due on Shaw's purchases of certain enhancements for its existing software for periods before the effective date of Acts 1998, No. 46; and
- The phased-in exclusion of custom computer software from the definition of the term "tangible personal property", as provided for by La. Rev. Stat. Ann. §47:301(16)(h)(i-iv) as enacted by Acts 2002, No. 7. This exclusion is discussed in detail in Revenue Ruling No. 02-008, which can be viewed from the department's web site at <http://www.rev.state.la.us/forms/lawspolicies/RR02008.pdf>.

**What Is Software Maintenance?**

When a person purchases software, the person receives a license to use the version of the software that is current at the time of purchase. Software maintenance agreements, which are provided at additional cost, usually include combinations of several types of services:

- Maintenance releases, sometimes called bug fixes, enable purchasers to correct problems with software that the developers have detected after the release of the purchaser's version of the software. Maintenance releases do not add capabilities to software beyond those included in the version of the software that was purchased.
- Software upgrades are priced for each release or are provided without additional charge to persons who have paid annual or other periodic fees to the software developers. Typically, software upgrades will enhance software beyond the capabilities of earlier versions of the software.
- Consultation Support enables software licensees to address user-specific problems to software developers.

Very often, there is no question of sales taxability associated with the furnishing of maintenance releases because the releases are furnished to identified purchasers without charge. Charges to a software licensee that provides the licensee only with the right of personal consultation with the software development company are likewise not taxable. Whether packages that include other services are taxable in full or in part, will depend upon:

1. the meaning ascribed by the vendor and the customer to term “maintenance services”;
2. whether any new or enhanced software is included within a “maintenance service” package;
3. whether the software included is “canned” or customized;
4. whether the “maintenance service” package includes any updating, enhancing and reformatting of software; and
5. on what dates those services are provided.

The *South Central Bell* case involved a dispute between the City of New Orleans and South Central Bell over the sales and use taxability of computer software. The court upheld the assessments that the city made on South Central Bell’s purchases of customized software used in the operation of the company’s central office switching equipment. The court ruled that computer software, either “canned” or custom, constitutes taxable tangible personal property regardless of whether transmitted on media such as diskettes, by telephone lines, or by other means.

In its *South Central Bell* ruling, the court also discussed the taxability of software maintenance services that, in the facts before the court, consisted of technical support by South Central Bell’s vendor, including updating, enhancing, and reformatting the software, and advising South Central Bell with respect to certain usages of the software. The City of New Orleans had sought to tax these so-called maintenance services under the provision of the city sales tax code that levied that tax on the furnishing of repairs to tangible personal property. The court held that the services in question were not taxable as repair services. The court held that a repair is replacing a part, putting together what is torn or broken, or restoring a thing to the condition in which it originally existed.

In concluding that the Shaw Group’s purchases of certain enhancements for its existing software were not taxable during the period January 1994 through December 1996, the First Circuit Court of Appeals in *Shaw Group v. Kennedy* cited the language of *South Central Bell* regarding the taxability of maintenance services. The court noted, however, that Acts 1998, No. 46 changed the law governing the sales taxability of some software maintenance services, effective June 24, 1998. This act added § 47:301(16)(e) to the sales tax law to provide an exclusion from the definition of the term “tangible personal property,” and made an exception from that exclusion, as follows:

- (e) The term “tangible personal property” shall not include work products which are written on paper, stored on magnetic or optical media, or transmitted by electronic device, when such work products are created in the normal course of business by any person licensed or regulated by the provisions of Title 37 of the

Louisiana Revised Statutes of 1950, unless such work products are duplicated without modification for sale to multiple purchasers. This exclusion shall not apply to work products which consist of the creation, modification, updating, or licensing of computer software.

In *Shaw Group v. Kennedy*, the court said that it would have determined the software modification and update transactions in that case to have been taxable, had the above language been in the sales tax law during the periods covering the transactions. Since the transactions then in question occurred during the years 1994 through 1996, and the above language was not added to the law until 1998, the court determined that the transactions were not taxable, in accord with the Louisiana Supreme Court decision in *South Central Bell*.

Following the interpretation provided by *Shaw Group v. Kennedy*, transactions occurring after June 24, 1998, in which updates, modifications, or enhancements of software are provided are considered to be the equivalent of sales of new software. For periods between June 24, 1998, and June 30, 2002, all such transactions will be state sales or use taxable at 4 percent, regardless of whether the updates, modifications, or enhancements constitute “canned” software or custom software. Beginning July 1, 2002, updates, modifications, and enhancements that constitute “canned” software will remain taxable at 4 percent, but those that constitute custom software will be taxable at the percentages of their sales prices provided by §47:301(16)(h)(i-iv), as follows:

July 1, 2002 through June 30, 2003 .....	25 percent excluded—75 percent taxed
July 1, 2003 through June 30, 2004 .....	50 percent excluded—50 percent taxed
July 1, 2004 through June 30, 2005 .....	75 percent excluded—25 percent taxed
July 1, 2005 and thereafter.....	100 percent excluded—Not taxable

More recently, software “maintenance services” packages have included a variety of products and services. While some of the software-related services within the packages may not be taxable as repairs, some services or products included within “maintenance services” packages might constitute sales of new or enhanced software. If a package of products and services consists of both taxable and non-taxable components, the entire package is taxable at the highest rate applicable to any component of the package, unless the non-taxable or lower-percentage taxable components can be purchased separately from those that are taxable at higher rates, and are separately priced.

Questions concerning this matter can be directed to the Taxpayer Services Division at (225) 219-7356.

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