

State of Rhode Island and Providence Plantations

Rhode Island Department of Revenue
Division of Taxation

Public Notice of Proposed Rule-Making

Pursuant to the provisions of 42-35-3(a)(1) of the General Laws of Rhode Island, and in accordance with the Administrative Procedures Act (Chapter 42-35 of the General Laws), the Division of Taxation hereby gives notice of its intent to issue a regulation on computers and related systems.

The purpose of this regulation is to implement Chapters 44-18 and 44-19 of the Rhode Island General Laws. These Chapters provide for Sales and Use Taxes Liability and Computation and Sales and Use Taxes Enforcement and Collection in regard to computers and related systems. This regulation amends and supercedes regulation SU 94-25 promulgated January 1, 1994.

The proposed regulation and concise summary of non-technical requirements and proposed new rules are available for public inspection at www.tax.ri.gov, in person at The Rhode Island Division of Taxation, or requested by e-mail at mcanole@tax.ri.gov or by calling Michael Canole at (401) 574-8729.

In the development of the proposed regulation, consideration was given to: (1) alternative approaches; (2) overlap or duplication with other statutory and regulatory provisions; and (3) significant economic impact on small business. No alternative approach, duplication, or overlap was identified based upon available information.

All interested parties are invited to submit written or oral comments concerning the proposed regulations by November 9, 2009 to Michael Canole, Rhode Island Division of Taxation, One Capitol Hill, Providence, RI – telephone number (401) 574-8729 or via, e-mail at mcanole@tax.ri.gov. A public hearing to consider the proposed regulation will be held on November 9, 2009 at the Rhode Island Division of Taxation, One Capitol Hill, Providence, RI, at which time and place all persons interested therein will be heard. The room is accessible to the disabled and interpreter services for the hearing impaired will be provided if requested 48 hours prior to the hearing. Requests for this service can be made in writing to Michael Canole at Rhode Island Division of Taxation, One Capitol Hill, Providence, RI 02908 or by calling 401 574-8729.

Rhode Island Department of Revenue

Division of Taxation

**Concise Summary of ALL Non-technical requirements pursuant to
RIGL Section 42-35-3(a)(1)**

Rules and Regulation on Computers and Related Systems – SU 09-25

The purpose of this regulation is to implement Chapters 44-18 and 44-19 of the Rhode Island General Laws. These Chapters provide for Sales and Use Taxes Liability and Computation and Sales and Use Taxes Enforcement and Collection in regards to computers and related systems.

This regulation amends and supercedes regulation SU 94-25 promulgated January 1, 1994.

~~State of Rhode Island -- Division of Taxation~~

~~Sales and Use Tax~~

~~Regulation SU-94-25~~

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~~Computers and Related Systems~~

~~1. Computer "hardware" is defined as the machine and all of its components. Computer "software" is the programming needed to make computers operate.~~

~~2. The sale to a consumer of a computer and its related components is taxable when delivered to a customer in this state. The rental of a computer and its related components, including terminal equipment (hardware) which is physically located in this state, is taxable.~~

~~3. When computers are accessed by customers through terminal devices which are connected to the computer, each customer is in effect using a portion of the computer. A customer is able to compile programs, provide a variety of computations, have computational results printed out on a terminal and keep data stored within the computer file for future use. This produces basically the same results as if the customer had processed the same data on the customer's own computer; i.e., the customer performs the tasks of entering data into the computer and all processing is accomplished under his/her control. The charge for such use of the computer may include, among other things:~~

- ~~a. average amount of computer storage used,~~
- ~~b. computations performed by the computer,~~
- ~~c. time connected to the computer.~~

~~The above is sometimes referred to as "Time-Sharing Plan" and such charges are the rental of the computer, not service charges, and are taxable when the computer is physically located in this state. When the computer is located outside this state, the rental of the computer is not taxable. The charge made for any terminal device located in this state is taxable.~~

~~4. Canned programs are programs prepared, held, or existing for general or repeated use, including programs developed for in-house use and subsequently held or offered for sale or lease.~~

~~Canned programs which include such items as instructional material, prepunched cards or programmed tapes are tangible personal property and the entire charge is taxable, including the services of a technician to assist the customer in the use of the package whether or not his services are separately stated on the billing.~~

~~The licensing of canned software is a lease or rental and is subject to tax along with any services pertaining thereto. (Cross Reference Regulation SU-92-62)~~

~~5. Custom programs are programs created specifically for one user and prepared to the special order of that user. Such programs are exempt including any services incidental thereto and any modifications made to said programs for a particular user. Custom programs are not subject to tax regardless of the manner or mode of transfer to the customer since the charge for the custom program is a charge for professional services and the manner or mode of transfer is considered incidental to the sale of the service.~~

~~6. When a Service Bureau performs a bookkeeping service for a client, such as keeping a set of records and the furnishing of financial statements, payrolls, tax reports, accounts receivable and accounts payable statements, etc., the charge is for a professional service and is exempt.~~

~~7. Equipment, materials and supplies purchased, leased or rented for use in providing nontaxable services are taxable to the person providing the service. The tax exempt status of the customer is not passed through to the person providing the services.~~

~~8. Data entry cards, tapes and disks are tangible personal property and the entire selling price including any services that are a part of the sale is taxable. The charge made for data entry on such media furnished by the customer is a processing charge and is taxable.~~

~~9. Subleasing receipts are taxable without any deduction or credit for tax paid by the original lessee to his lessor, if the original lessee uses the property in addition to subleasing it. A resale certificate for a portion of a lease or rental period may not be given if the person who is leasing such equipment makes a taxable use thereof during such period.~~

~~R. GARY CLARK
TAX ADMINISTRATOR~~

~~DATE: JANUARY 1, 1994~~

~~THIS REGULATION AMENDS AND SUPERCEDES REGULATION SU 92-25 PROMULGATED
JANUARY 1, 1993.~~

State of Rhode Island - Division of Taxation

Sales and Use Tax

Regulation SU 94-25 09-25

Computers and Related Systems

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RULE I. PURPOSE:

This regulation implements Chapter 44-18 and 44-19 of the Rhode Island General Laws. These Chapters provide for Sales and Use Taxes Liability and Computation and Sales and Use Taxes Enforcement and Collection in regard to computers and related systems.

RULE 2 AUTHORITY

This regulation is promulgated pursuant to RIGL Chapter 44-18 and 44-19 as amended. These rules have been prepared in accordance with the requirements of RIGL Chapter 44-1-1 et. seq. and 44-19-33.

RULE 3 APPLICATION

The terms and provisions of these rules and regulations shall be liberally construed to permit the Department of Revenue to effectuate the purposes of RIGL Chapter 44-18 and 44-19 and other applicable state laws and regulations.

RULE 4. SEVERABILITY

If any provision of these rules and regulations, or the application thereof to any person or circumstances, is held invalid by a court of competent jurisdiction, the validity of the remainder of the rules and regulations shall not be affected thereby.

RULE 5. DEFINITIONS:

“Canned software” – See Prewritten computer software.

“Computer” means an electronic device that accepts information in digital or similar form and manipulates it for a result based on a sequence of instructions.

“Computer hardware” means the physical components of a computer system.

“Computer software” means a set of coded instructions designed to cause a computer or automatic data processing equipment to perform a task.

“Computer software maintenance contract” means a contract that obligates a vendor of computer software to provide a customer with future updates or upgrades to computer software, support services with respect to prewritten computer software, or both.

“Custom software” means a program created specifically for one user and prepared to the special order of that user.

“Delivered electronically” means delivered to the purchaser by means other than tangible storage media.

“Electronic” means relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.

“License” means the right to use, copy or access software.

“Load and leave” means delivery to the purchaser by use of a tangible storage media where the tangible storage media is not physically transferred to the purchaser.

“Prewritten computer software” means computer software, including prewritten upgrades, which is not designed and developed by the author or other creator to the specifications of a specific purchaser. The combining of two or more prewritten computer software programs or prewritten portions thereof does not cause the combination to be other than prewritten computer software. Prewritten computer software 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 the specific purchaser. Where a person modifies or enhances computer software of which the person is not the author or creator, the person shall be deemed to be the author or creator only of such person's modifications or enhancements. Prewritten computer software or a prewritten 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 prewritten computer 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 "prewritten computer software."

RULE 6. COMPUTER HARDWARE

The sale to a consumer of a computer and its related components is taxable when delivered to a customer in this state. The rental of a computer and its related components, including terminal equipment (hardware) which is physically located in this state, is taxable.

RULE 7. COMPUTER SOFTWARE

(1) Prewritten computer software - The sale of prewritten computer software ("canned") delivered in tangible form is taxable *including any services (training, maintenance consultation etc) pertaining to the sale.* However, installation labor separately stated is not subject to tax.

Modifications to prewritten computer software that are designed to make the software conform to a purchaser's specifications are not subject to tax, provided the charges are separately stated.

Prewritten computer software delivered electronically or by load and leave is not subject to tax because it is not considered a sale of tangible personal property.

(2) Custom Software – The sale of custom software as defined above is not subject to tax. This includes any services incidental thereto and any modifications.

If custom software sold to a single purchaser is later sold to others, the later sales are considered sales of prewritten software and are subject to tax.

RULE 8. MAINTENANCE AGREEMENTS

Taxability as it pertains to a prewritten computer software maintenance contract is based on both tangible personal property, and how the updates/upgrades/services per the agreement are received. A computer software maintenance contract in which updates/upgrades are delivered in tangible form is taxable. Updates/upgrades delivered electronically with respect to prewritten software also received electronically are not subject to tax. Updates/upgrades delivered electronically with respect to prewritten software received in tangible format (ex: disk or CD) are subject to tax.

The total sale price of tangible prewritten computer software including separately stated charges for computer software maintenance contracts whether received electronically or in tangible format is subject to tax.

Example #1

A software company has the following charges to a customer:

<u>Prewritten computer software (tangible)</u>	<u>\$5,000</u>
<u>Software maintenance agreement (\$100 per year for five years, paid upfront as part of purchase agreement included with software)</u>	<u>500</u>
<u>Sales Tax</u>	<u>385</u>
<u>Total</u>	<u>\$5,885</u>

Example #2

A software company has the following charges to a customer:

<u>Prewritten computer software (tangible)</u>	<u>\$5,000</u>
<u>Software maintenance agreement (\$100 paid at time of software purchase, and \$100 per year for next 4 years per purchase agreement)</u>	<u>100</u>
<u>Sales Tax</u>	<u>357</u>
<u>Total</u>	<u>\$5,457</u>

Remaining annual payments of \$100 per the computer software maintenance contract delivered electronically or in tangible format are subject to tax, as these charges are related to prewritten computer software received in tangible format and purchased as part of the original purchase agreement.

Example #3

A software company has the following charges to a customer:

<u>Prewritten computer software (tangible)</u>	<u>\$5,000</u>
<u>Sales Tax</u>	<u>350</u>
<u>Total</u>	<u>\$5,350</u>

A computer software maintenance contract delivered electronically and purchased after the original purchase agreement for software - \$500 for 5 years \$500

Since delivered electronically and is a separate charge for a computer software maintenance contract purchased after the original purchase of software, it is not subject to tax.

Example #4

A software company has the following charges to a customer:

<u>Custom computer software (tangible)</u>	<u>\$5,000</u>
<u>Computer software maintenance contract (\$100 per year for five years, paid upfront as part of purchase agreement included with software)</u>	<u>500</u>
<u>Sales Tax</u>	<u>-0-</u>
<u>Total</u>	<u>\$5,500</u>

Custom software and related services are not subject to tax.

RULE 9. EFFECTIVE DATE: This regulation shall takes effect on January 1, 2010 and shall amend and supercede regulation SU 94-25 promulgated January 1, 1994.

RULE 10. CROSS REFERENCES:

CROSS REFERENCE: SU 00-126 "Optional Service, Maintenance and Extended Warranty Contracts"

DAVID SULLIVAN
TAX ADMINISTRATOR