



Taxation of Computer Software

Tax Webinar: December 2023

Information is current as of the date presented and may not reflect legislative and other subsequent changes. For the most up-to-date information, please refer to our [published tax manuals](#) and [Revenue Help articles](#). Additionally, you can find legislative summaries by year/tax type [here](#).

Thanks for joining us!

We will begin at 9:00 am (CST)

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- Link to Technical Service Resource Guide <https://www.cisco.com/c/en/us/support/web/tac/technical-services-resource-guide.html>
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tn.gov/revenue > Taxpayer Education > Tax Webinars

<https://www.tn.gov/revenue/taxpayer-education/tax-webinars.html>

The webinar recording will be posted in the "Webinar Video Library" the day after the event.

➤ **Please submit specific account-related questions or any questions that do not get addressed in this webinar to us directly!**

- www.tn.gov/Revenue
- Revenue.support@tn.gov
- 615.253.0600 (M-F 8-4:30 CST)



Overview

The access and use of computer software in TN is subject to sales and use tax regardless of a customer's chosen method of use.

Tenn. Code Ann. §67-6-231

- **LAW & DEFINITIONS**
- **DETERMINING TAXABILITY**
- **EXEMPTIONS**
- **RESOURCES**

Basic Law

The retail sale, lease, licensing, or use of computer software in this state, including prewritten and custom computer software, is subject to sales and use tax if provided/delivered ...

- Via remote access to a customer located in Tennessee;
- On a tangible storage medium, e.g., disks and tapes, to the customer in Tennessee;
- By loading and leaving on the customer's or the customer's designee's computer in Tennessee;
- By electronic delivery, e.g., download, to the customer's or the customer's designee's computer in Tennessee; or
- By programming it into the customer's or the customer's designee's computer in Tennessee.

“Computer Software” Definition:

A set of coded instructions designed to cause a computer or automatic data processing equipment to perform a task.

*INCLUDES
PREWRITTEN &
CUSTOMIZED
COMPUTER
SOFTWARE*

Prewritten Software:

Software, including prewritten upgrades, that is not designed/developed to the specifications of a purchaser. Can include:

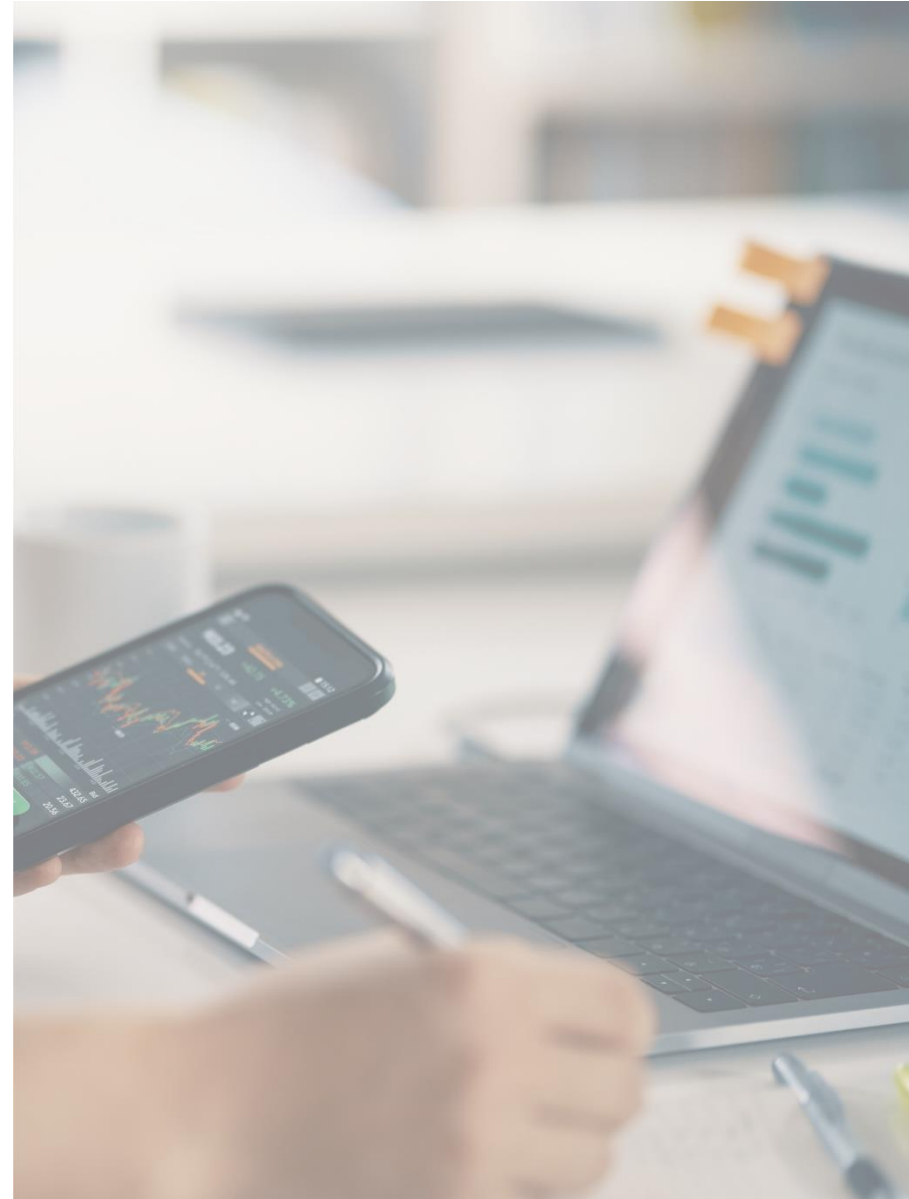
* software that was originally designed as custom but is subsequently sold to a purchaser it was not designed for

* prewritten upgrades designed to modify or enhance previously purchased prewritten computer software

* combination of two or more “prewritten computer software” programs or prewritten portions or modules

Customized Software:

Software designed and developed to the specifications of a specific purchaser.



Remotely Accessed Software (SaaS)

Also known as cloud/
internet-based, providing
remotely accessed software
as a service includes the
access/use of software that
remains in the possession of
the dealer who provides the
software.

TN Department of Revenue
Sales and Use Tax Notice
Notice #15-14 June 2015 (last updated December 2015)

Remotely Accessed Software

Changing Technology Requires Law Change
Computer software has been subject to sales and use tax in Tennessee since 1977. When enacted, and in subsequent amendments, the law addressed the methods by which customers accessed and used computer software at that time. Changing technology, however, has made it possible to use software remotely through the Internet.

To address this change in technology, Public Chapter 514, effective July 1, 2015, says that the taxable use of computer software in Tennessee includes the access and use of software that remains in possession of the seller and is remotely accessed by a customer for use in this state. This provision ensures that software remains subject to sales and use tax regardless of a customer's method of use.

Payment of Tax by the User
If the seller does not collect the tax, purchasers in this state who remotely access and use software must report and pay use tax directly to the Department on the purchase price for the use of the remotely accessed software.

Users in Multiple States¹
If the purchaser pays for access to software that will be used by individuals who are located in this state, and other individuals who are located outside this state (for example, the purchaser's employees), then the price paid by the purchaser may be allocated based on the percentage of users located in Tennessee to determine the amount subject to Tennessee tax. This may be done in one of two ways.

If the purchaser is registered for Tennessee sales and use tax purposes, then it may use the new Remotely Accessed Software Direct Pay Permit form to purchase the software without paying tax to the seller. The purchaser then must directly pay the tax to the Department on the portion of the price that corresponds to the percentage of users located in Tennessee. The form must include the purchaser's Tennessee sales and use tax registration number. See important notice 15-24 for more information about the newly created Remotely Accessed Software Direct Pay Permit that became available for use December 2015.

If the purchaser is not registered for Tennessee sales and use tax purposes, then it may use a fully

Collection of Tax by the Seller
The seller must collect tax at the 7% state tax rate, plus the applicable local tax rate, on the sales price for the use of remotely accessed software during billing periods that begin on or after July 1, 2015. The tax applies to any access and use of the software from a location in Tennessee, and it applies whether the charge for the software is on a per use, per user, per license, subscription, or any other basis. The software is accessed from a location in Tennessee if a customer's residential or primary business address is in this state.

Disclaimer: The information provided here is current as of the date of publication but may change as a result of new statutes, regulations, or court decisions. While this notice is intended to be comprehensive, events and situations unanticipated by this notice may occur. In such cases you should contact the department or your tax professional for further guidance.

¹ This section was updated in December 2015 to detail a new Department form and procedure.

[NOTICE 15-14](https://www.tn.gov/content/dam/tn/revenue/documents/notices/sales/sales15-14.pdf)

<https://www.tn.gov/content/dam/tn/revenue/documents/notices/sales/sales15-14.pdf>

Sales Price & Sourcing

SALES PRICE - The sales price is the total amount for which an item is sold. It includes labor and service costs of the seller as well as charges for services necessary to complete the sale.

SOURCING - Sales of computer software and taxable services are sourced by:

- if a customer uses/accesses the software from a location in this state it is subject to TN sales tax
- if the purchaser has users, e.g., employees, located in the state and outside of the state that access and use the software, the sales price may be allocated to claim an exemption for the out-of-state portion of the sales price.

Webinar: [Nexus for Out-of-State Businesses](#)



Software-Related Services - Taxable

- Charges for **consulting or other services that contribute to the creating, designing, developing, fabricating, programming, altering, or modifying** of computer software are labor/service costs that are necessary to complete the sale of the software are subject to tax when made as a part of the sale of the software, even when the service charges are separately itemized or invoiced by the seller of the computer software.
- **Modifications or enhancements** to customized or prewritten computer software are considered sales of computer software and are subject to sales and use tax.
- Software **Installation and Repair** services are enumerated by law as being subject to sales tax in TN.

Training/Configuration

- Tennessee does not specifically impose sales tax on training or software configuration; however, these services **are taxable if necessary to complete the sale** of the computer software or installation of computer software, regardless of whether they are separately itemized.
- Stand-alone training or software configuration services provided by a third party are not subject to sales tax.

Software configuration is a means of setting pre-defined toggles or switches and/or building tables that give direction or define values of parameters within the software.

Maintenance Contracts

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

COMPUTER SOFTWARE MAINTENANCE CONTRACTS ARE SUBJECT TO BOTH SALES AND USE TAX

- Applies to computer software installed on computers located in TN
- If location of software covered is not known, tax is applicable if the purchaser's residential/primary street address is in TN

TN Department of Revenue
Sales and Use Tax Notice
Notice #15-25 December 2015

Sales of Computer Software Maintenance Contracts

Computer Software Maintenance Contract Is Defined by State Law
Tennessee law specifically defines a computer software maintenance contract. It is a contract that obligates one person to provide to another person future updates, upgrades and/or support services for computer software.

Computer Software Maintenance Contracts Are Subject to Sales and Use Tax
The sale of, use of, or subscription to a computer software maintenance contract in Tennessee is subject to sales and use tax. It does not matter whether the purchase is a mandatory requirement to obtaining the computer software, or the purchase is optional and separately priced and invoiced from the computer software covered by the software maintenance contract. Sales or use tax is due under each of the following circumstances:

- 1) A Computer Software Maintenance Contract Is Taxable If Sold in Conjunction with a Taxable Sale of Computer Software**
A computer software maintenance contract is taxable if it is sold as part of a Tennessee taxable sale of computer software.
Example: A purchaser buys computer software in Tennessee from Tennessee Computer Software Dealer ("TCSD"). At the same time, the purchaser also buys a software maintenance contract that covers repairs of the software he is purchasing. TCSD charges Tennessee sales tax on the sale of the
- 2) A Computer Software Maintenance Contract Is Taxable If the Software Is Installed on a Computer in Tennessee**
A computer software maintenance contract is taxable if the computer software covered by the computer software maintenance contract is installed on a computer in Tennessee.
Example: A purchaser buys a computer software maintenance contract from Software Maintenance Contract Dealer ("SMCD"). The contract covers repairs to software that is installed on the purchaser's Tennessee office computer. The sale of the contract is subject to the Tennessee sales tax, and SMCD would collect and remit the tax. However, if the sales tax was not collected on the purchase, the purchaser would owe Tennessee use tax on the purchase price of the contract.
- 3) A Computer Software Maintenance Contract Is Taxable If the Location of the Software Is Unknown, but the Purchaser Has a Tennessee Address**
A computer software maintenance contract is taxable if the location of the computer software covered by the computer software maintenance contract is unknown, but the purchaser's residential or primary business address is located in Tennessee.
Example: Tennessee Purchaser ("TP") buys a computer software maintenance contract from

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Notice #15-25

<https://www.tn.gov/content/dam/tn/revenue/documents/notices/sales/sales15-25.pdf>

Other Services: **Not Taxable**

- **information or data processing services [including the capability of the customer to analyze such information or data provided by the dealer]**
- **payment or transaction processing services**
- **payroll processing services**
- **billing and collection services**
- **internet access services**
- **the storage of data, digital codes, or computer software**
- **converting, managing, and distributing digital products**

Single Article Application

APPLICABLE

- Prewritten Software

NOT APPLICABLE

- Custom Software
- Computer Software Maintenance Contracts
- Taxable Service when not bundled or not necessary to complete the sale

[Webinar: Single Article Application](#)

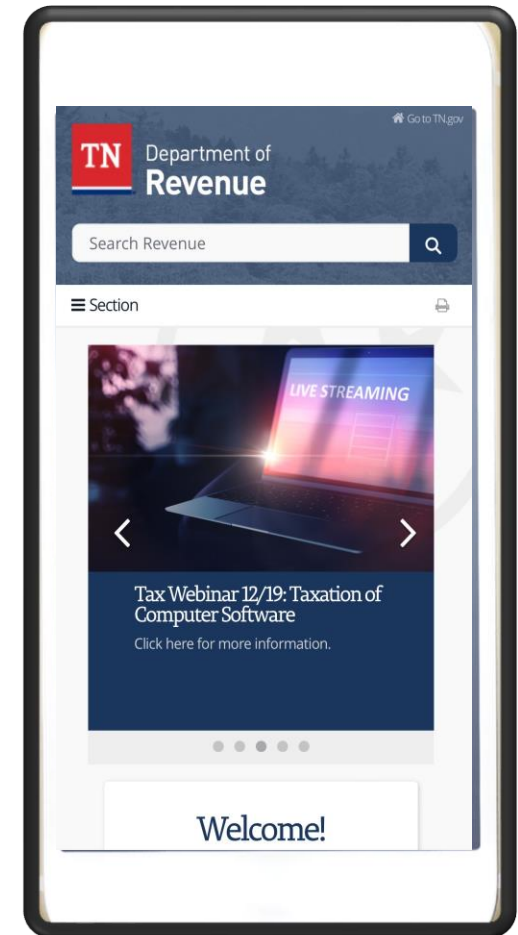
https://www.tn.gov/content/dam/tn/revenue/documents/taxpayer_education/sales/single-article-2022.pdf

Exemptions

- **Personal** - An individual fabricating software for their own personal use is exempt from tax. [NOTICE #22-05](#)
- **Entity-Based** - There are thirteen different based entity exemptions: Agriculture, Common Carrier, Manufacturer, Warehouse or Distribution Facility, Research and Development, Nonprofits/Educations entities, Credit Unions, Qualified Data Centers, Headquarters Centers, Health and Fitness centers, Call Centers, Government exemptions, Foreign missions, Qualified Production and Broadband Communication. Several of these address computer software exemption specifically.
- **Manufacturers and Headquarters Centers**
- **In-house Computer Software**
- **Resale** - If computer software is purchased for the purpose of reselling access/use, a resale certificate may be used to exempt the tax

Resources

- [Sales & Use Tax Manual](#)
- **Important Notices**
 - [#22-05 Computer Software Developed for Personal Use](#)
 - [#15-25 Sales of Computer Software Maintenance Contracts](#)
 - [#15-24 Remotely Accessed Software Direct Pay Permit](#)
 - [#15-14 Remotely Accessed Software](#)
- **Revenue Help**
 - [SUT-61 - Computer Software - Custom Software](#)
 - [SUT-60 - Computer Software - Consulting Services](#)
 - [SUT-59 - Computer Software - Software Installed on Servers in Tennessee](#)
 - [SUT-62 - Computer Software - Maintenance Contracts](#)
 - [Remotely Accessed Software](#)



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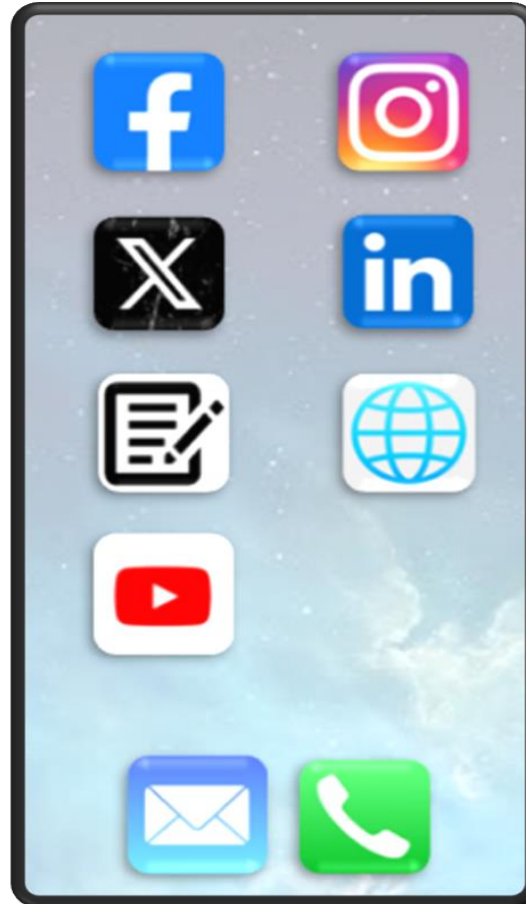
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615.253.0600

SUPPORT STAFF AVAILABLE TO ASSIST YOU M-F 8am - 4:30pm

[All Dept. of Revenue Contact Numbers and Office Locations](#)



UPCOMING!

- **Next Webinar: 1/30 – Business Tax Basics**
- **New Business Workshop: 1/10/24**



Taxpayer Education & Outreach



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TO COMPLETE A BRIEF
SURVEY UPON EXITING!**

IMPORTANT: In order to receive CPE credit for attending, you must answer yes to question 4 of the post-event survey.