

**Revenue Ruling
No. 02- 008
August 28, 2002
Sales and Use Tax**

**Custom Computer Software To Be Excluded From The Definition Of
Tangible Personal Property**

This Revenue Ruling describes the procedures for reporting sales and use tax on purchases of “canned” software by vendors of custom computer programs during the four-year phase in period of the sales tax exclusion provided by R. S. 47:301(16)(h), which was enacted by Act 7 of the 2002 First Extraordinary Session of the Legislature.

Act 7 excludes custom computer software from the definition of tangible personal property for state sales and use taxes and local sales and use taxes imposed by jurisdictions that elect to exempt custom software by ordinance. The Act defines custom computer software as “...software prepared, created, adapted, or modified to the special order of a particular purchaser, licensee, or user; or to meet the specific needs or requirements of a particular purchaser, licensee, or user, regardless of the means by or through which such computer software is furnished, delivered, or transmitted, and regardless of whether such software incorporates or consists of preexisting routines, utilities, or other computer software components.” All other computer software that is not included as part of a custom program is subject to state and local sales and use taxes.

The sales tax exclusion provided by Act 7 will be phased in over the four-year period from July 1, 2002, through June 30, 2005. The amount of the sale price of custom computer software to be excluded from the definition of tangible personal property and not subject to sales or use tax is 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

Tax on Canned Software used in Custom Programs

Prior to Act 7, the sale of canned software incorporated into custom programs was treated as a sale for resale because sales tax was collected on the sale of the custom program. Any sales tax paid on these purchases by custom software vendors qualified for an advance tax credit (ATC). Under Act 7, purchases of canned software for use in custom programs will not qualify as sales for resale after June 30, 2005, because once custom programs are excluded from the sales tax, the purchase of canned software for use in custom programs will be subject to use tax to be paid by the custom programmer. However, because the exclusion for custom computer software will be phased in from July 1, 2002, through June 30, 2005, the purchase of canned software for use in custom applications will be treated as a purchase for resale according to the percentage of the custom software’s sales price that is subject to sales or use tax based on the sales date of the custom software.

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Example: Canned software purchased to be incorporated into custom software that is sold between July 1, 2002, and June 30, 2003, would be taxed at 25 percent because sales tax would be collected on 75 percent of the custom software sales price. If the vendor paid sales tax on the canned software purchase, 75 percent of the sales tax paid would be eligible for advance tax credit. If no sales tax was paid on the canned software purchase, the custom software vendor would owe use tax on 25 percent of the canned software purchase price. As the sales tax exclusion is phased in, custom software vendors should pay sales tax on canned software purchases as follows:

Date of Sale of Custom Software	Canned Software Percentage Taxed
July 1, 2002 through June 30, 2003	25 percent taxed—75 percent ATC
July 1, 2003 through June 30, 2004	50 percent taxed—50 percent ATC
July 1, 2004 through June 30, 2005	75 percent taxed—25 percent ATC
July 1, 2005 and thereafter	100 percent taxed—No ATC

If a custom software vendor buys canned software costing \$1,000 for inclusion in a custom software package, the use tax liability or advance tax credit based on the state sales tax rate of four percent will be as follows:

Period*	Advance Tax Credit Allowed if \$40 Sales Tax Paid	Use Tax Due if no Sales Tax Paid
July 1, 2002 - June 30, 2003	\$30 Advance Tax Credit	\$10 Use Tax Due
July 1, 2003 - June 30, 2004	\$20 Advance Tax Credit	\$20 Use Tax Due
July 1, 2004 - June 30, 2005	\$10 Advance Tax Credit	\$30 Use Tax Due
July 1, 2005 - and thereafter	No Advance Tax Credit	\$40 Use Tax Due

*Note: The period refers to the custom software sales date and not the canned software purchase date.

All canned software incorporated into custom software that is sold after June 30, 2005, is subject to sales and use tax and any sales tax paid on the purchase will not qualify for the advance tax credit.

Questions or comments regarding this issue should be directed to the Taxpayer Services Division of the Department of Revenue. They may be contacted by telephone at 225.219.7356 or by mail at Post Office Box 66258, Baton Rouge, Louisiana 70802.

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