

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 11-58**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is information only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

The application of the Tennessee sales and use tax to a customer relationship management software application and related services.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[NAME] (the “Taxpayer”) is a [TYPE OF ENTITY] located in [CITY], Tennessee.¹ The Taxpayer has engaged a [STATE – NOT TENNESSEE] company (the “Vendor”) to provide it with access to a comprehensive customer relationship management software application (the “CRM software application”). The CRM software application is used by the Taxpayer to manage its customer data.

The CRM software application is preexisting software owned and operated by the Vendor, which licenses it to users in the course of its business. The Vendor generally configures the application’s functionality to fit a customer’s specific business needs. The CRM software application resides at all times on the Vendor’s servers in [STATE – NOT TENNESSEE].

The Taxpayer will be granted a license to use the CRM software application on a subscription basis. The Taxpayer will pay a monthly subscription fee to obtain unique user accounts for use by the Taxpayer’s employees. The Taxpayer’s Tennessee users will access the system through the Internet using a standard web browser and a password. The Taxpayer is not permitted to install or transfer the CRM software application onto its own computers.

Initially, the Vendor will have its employees travel to Tennessee to analyze the Taxpayer’s specific business requirements. The Vendor will then customize the CRM software application to fit the Taxpayer’s needs. The Vendor charges for the initial system requirements analysis; these charges are billed separately. Additionally, the Vendor bills separately for the customization, as part of the Vendor’s implementation services.

RULINGS

1. Is the Vendor’s analysis of the Taxpayer’s system requirements a service that is subject to the Tennessee sales and use tax?

Ruling: No. The Vendor’s analysis of the Taxpayer’s system requirements is not a service that is subject to the Tennessee sales and use tax.

2. Is the customized configuration of the CRM software application by the Vendor subject to the Tennessee sales and use tax?

Ruling: No. The customized configuration of the CRM software application by the Vendor is not subject to the Tennessee sales and use tax.

3. Is the monthly subscription fee to use the CRM software application subject to the Tennessee sales and use tax?

Ruling: No. The monthly subscription fee to use the CRM software application is not subject to the Tennessee sales and use tax.

¹ [REDACTED].

ANALYSIS

Under the Retailers' Sales Tax Act, TENN. CODE ANN. § 67-6-101 *et seq.*, the retail sale in Tennessee of tangible personal property and specifically enumerated services is subject to the sales and use tax.

The retail sale of computer software in Tennessee is subject to the sales and use tax as the sale of tangible personal property. TENN. CODE ANN. § 67-6-102(80)(A) (2011) defines the term "sale" in pertinent part to mean "any transfer of title or possession, or both, exchange, barter, lease or rental, conditional or otherwise, in any manner or by any means whatsoever of tangible personal property for a consideration." TENN. CODE ANN. § 67-6-102(91)(A) defines "tangible personal property" to include prewritten computer software.² TENN. CODE ANN. § 67-6-102(80)(K) further provides that the term "sale" includes "any transfer of title or possession, or both, lease or licensing, in any manner or by any means whatsoever of computer software for consideration, and includes the creation of computer software on the premises of the consumer and any programming, transferring or loading of computer software into a computer." Additionally, TENN. CODE ANN. § 67-6-231(a) (2010) specifically provides that the "retail sale, lease, licensing or use of computer software" in Tennessee is subject to the sales and use tax, "regardless of whether the software is delivered electronically, delivered by use of tangible storage media, loaded or programmed into a computer, created on the premises of the consumer or otherwise provided."

TENN. CODE ANN. § 67-6-102(80)(C) also defines the term "sale" to include "the furnishing of any of the things or services taxable" under the Retailers' Sales Tax Act. One of the services subject to the sales and use tax is the furnishing of "intrastate, interstate or international telecommunication services," pursuant to TENN. CODE ANN. § 67-6-205(c)(3) (2011).³ The term "telecommunications service" is defined under TENN. CODE ANN. § 67-6-102(92)(A) as the "electronic transmission, conveyance, or routing of voice, data, audio, video, or any other information or signals to a point, or between or among points." However, TENN. CODE ANN. § 67-6-102(92)(B)(i) excludes from the definition of "telecommunications service" data processing and information services "that allow data to be generated, acquired, stored, processed, or retrieved and delivered by electronic transmission to a purchaser, where such purchaser's primary purpose for the underlying transaction is the processed data or information."

As noted above, the sales tax does not apply to all services; rather, it only applies to retail sales of those services specifically enumerated by the statute. *Ryder Truck Rental, Inc. v. Huddleston*, 1994 WL 420911 (Tenn. Ct. App. Aug. 12, 1994). Even if a service is not specifically enumerated by the statute, however, the service may be subject to the sales tax where charges for the service are included in the sales price of a taxable good or service. Specifically, TENN. CODE

² TENN. CODE ANN. § 67-6-102(20) defines "computer software" as "a set of coded instructions designed to cause a computer or automatic data processing equipment to perform a task." TENN. CODE ANN. § 67-6-102(70) defines "prewritten computer software" in pertinent part to mean "computer software, including prewritten upgrades, that is not designed and developed by the author or other creator to the specifications of a specific purchaser."

³ The Vendor's services cannot be characterized as any other type of service that is taxable under the Retailers' Sales Tax Act; this letter ruling therefore does not discuss any specifically enumerated services other than telecommunications services.

ANN. § 67-6-102(81)(A) provides that the sales price of a good or service equals the “total amount of consideration . . . for which personal property or services are sold.” Thus, when the sale of a non-enumerated service is part of the sale of a taxable good or service, the charges for the non-enumerated service are included in the sales price of the taxable good or service and as such are subject to taxation.

Accordingly, the transactions described herein will be subject to the Tennessee sales and use tax if the charges relate to the 1) the retail sale or use of computer software in Tennessee; 2) the furnishing at retail of a telecommunications service; and/or 3) the furnishing at retail of an otherwise nontaxable service that is sold as part of the sale of a taxable good or service.

First, no retail sale or use of tangible personal property occurs in Tennessee when the Vendor provides access to the CRM software application via the Internet. As discussed above, the retail sale, lease, licensing or use *in Tennessee* of computer software is subject to the sales and use tax.

Here, the Vendor provides access via the Internet to computer software that is housed on a server in [STATE – NOT TENNESSEE]. No sale or use of tangible personal property occurs in Tennessee when the Taxpayer accesses the CRM software application via the Internet, because the Vendor does not transfer title, possession, or control of the CRM software application to the Taxpayer at any time. Additionally, while the granting of a license to use computer software constitutes a taxable sale, any such sale in the Taxpayer’s case occurs where the server is located, outside Tennessee. Significantly, the CRM software application remains on the Vendor’s servers at all times; the CRM software application is never delivered to, transferred to, or installed on, the Taxpayer’s computers. In fact, the Taxpayer is prohibited from downloading or otherwise installing the software on its own computers; rather, access to and use of the CRM software application takes place entirely over the Internet. The Vendor always retains full control over the CRM software application. Thus, no retail sale or use of computer software occurs in Tennessee for sales and use tax purposes.

While the modification of software may in some cases constitute the sale of tangible personal property,⁴ no such sale occurs when the Vendor configures the CRM software application to fit the Taxpayer’s specific business needs. As noted above, the Vendor does not transfer title, possession, or control of the CRM software application to the Taxpayer at any time. Any adjustments to the CRM software are made by the Vendor at its location outside Tennessee. Because title, possession, and control of the CRM software application always reside with the Vendor, no sale of computer software occurs when the Vendor configures the software.

For obvious reasons, the Vendor’s analysis of the Taxpayer’s system requirements cannot be considered a sale of tangible personal property.

Second, the provision of access to the CRM software application does not constitute a taxable service for Tennessee sales and use tax purposes. As noted above, only specifically enumerated services are subject to the Tennessee sales and use tax. In particular, TENN. CODE ANN. § 67-6-

⁴ The Tennessee Supreme Court has stated that the fabrication of, or customized modification or enhancement to, computer software may be considered a taxable sale of computer software. *See Creasy Sys. Consultants, Inc. v. Olsen*, 716 S.W.2d 35, 36 (Tenn. 1986).

205(c)(3) makes the furnishing of “intrastate, interstate or international telecommunications services” subject to Tennessee sales and use tax. The term “telecommunication service” is defined under TENN. CODE ANN. § 67-6-102(92)(A) as the “electronic transmission, conveyance, or routing of voice, data, audio, video, or any other information or signals to a point, or between or among points.” However, TENN. CODE ANN. § 67-6-102(92)(B)(i) excludes from the definition of “telecommunications service” data processing and information services “that allow data to be generated, acquired, stored, processed, or retrieved and delivered by electronic transmission to a purchaser, where such purchaser’s primary purpose for the underlying transaction is the processed data or information.”

Use of the CRM software application involves the electronic transmission, conveyance, or routing of data between points, and the CRM software application as such could potentially be characterized as a telecommunications service under TENN. CODE ANN. § 67-6-102(92)(A). However, the CRM software application is excluded from the definition of “telecommunication services” by operation of TENN. CODE ANN. § 67-6-102(92)(B)(i). The Vendor offers a service that allows data to be generated, acquired, stored, processed, retrieved, or delivered electronically to the Taxpayer. Additionally, the Taxpayer’s primary purpose for the underlying transaction is the management and processing of its customer data and information. Accordingly, the CRM software application falls under the category of data processing and information services, which are specifically excluded from the definition of “telecommunication service” under TENN. CODE ANN. § 67-6-102(92)(B)(i). The provision of access to the CRM software application therefore does not constitute a taxable telecommunications service.

Third, because the Vendor does not make sales of tangible personal property and does not provide a taxable service, no part of the transaction can be described as the furnishing of an otherwise nontaxable service that is sold as part of the sale of a taxable good or service.

Accordingly, the Vendor’s analysis of the Taxpayer’s system requirements is not a service that is subject to the Tennessee sales and use tax. The configuration of the CRM software application by the Vendor is also not subject to the Tennessee sales and use tax. Finally, the monthly subscription fee for access to the CRM software application is not subject to the Tennessee sales and use tax.

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APPROVED: Richard H. Roberts
Commissioner of Revenue

DATE: 10-10-11