

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 08-48**

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 informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Whether the sale of help desk services is subject to the Tennessee sales and use tax.

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 his detriment.

FACTS

[THE TAXPAYER] is a manufacturer of [EQUIPMENT] and provides [VARIOUS SYSTEMS AND SERVICES] to the [REDACTED] industry. The Taxpayer licenses its systems and services to its customers pursuant to a written agreement (the "Agreement"), a sample copy of which has been provided by the Taxpayer.

The sample Agreement states that the Taxpayer licenses and/or provides to its customers a “System” consisting of specified equipment; prewritten computer software (either developed by the Taxpayer or a third party); customized software; and “architectural” software, which consists of online software tools that are used to create the customized software. The prewritten computer software sold by the Taxpayer processes the customer’s data and/or the data of its respective clients, for whom the customer schedules appointments, processes bills and/or collects charges.

Pursuant to [HELP DESK SUPPLEMENT] of the sample Agreement, the Taxpayer must provide the customer with help desk services in exchange for a fixed monthly help desk services fee. Attachment 1 to [HELP DESK SUPPLEMENT] is a “Service Level Agreement,” which sets forth, among other things, the specific help desk services provided, a responsibilities matrix, and performance standards. The Service Level Agreement is not separately executed by the Taxpayer and the customer. The customer must pay a monthly fee based upon the number of “help desk events” handled by the Taxpayer; the base number of events is [NUMBER] per month.

The Taxpayer has stated that the help desk services are not optional; the Taxpayer will not license or provide the System if the customer refuses to purchase the help desk services. The help desk services are billed separately from the charges for the license and/or provision of the System. The customer may terminate the help desk services in whole or in part at any time after the forty-eighth month of the term of the Agreement.

QUESTION

Is the sale of help desk services by the Taxpayer subject to the Tennessee sales and use tax?

RULING

Yes.

ANALYSIS

The sale of help desk services by the Taxpayer is subject to the Tennessee sales and use tax.

Retail sales of tangible personal property and certain enumerated services in Tennessee are subject to the sales and use tax under Tenn. Code Ann. § 67-6-101 *et seq.* Tenn. Code Ann. § 67-6-102(68) (Supp. 2007) defines a “retail sale” to include any “sale, lease or rental for any purpose other than for resale, sublease, or subrent.” A “sale” is defined in pertinent part as “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,” and includes “the furnishing of any of the things or services taxable” under the Tennessee sales and use tax laws. Tenn. Code Ann. § 67-6-102(70)(A)&(D) (Supp. 2007). The licensing of tangible personal property used in Tennessee is considered a rental of such property, and is subject to the sales and use tax. Tenn. Code Ann. § 67-6-102(80)(A) (Supp. 2007) provides that the term “tangible personal property” means “personal property that can be seen, weighed,

measured, felt, or touched, or that is in any other manner perceptible to the senses.” The term “tangible personal property” includes “prewritten computer software.”¹ *Id.*

The Taxpayer’s licensing or provision of the System to its customer constitutes a sale of tangible personal property for purposes of the Tennessee sales and use tax, because the Taxpayer furnishes tangible personal property to the customer in exchange for a consideration. First, the System provided to the customer by the Taxpayer includes equipment, which obviously comes within the definition of “tangible personal property” under Tenn. Code Ann. § 67-6-102(80)(A). Second, the System includes prewritten computer software, which is also included in the definition of “tangible personal property.” *See id.* In exchange for the license to use the System, the customer pays the Taxpayer a consideration, in the form of an agreed-upon fee. Thus, the licensing or provision of the System by the Taxpayer to its customer constitutes a “sale” for Tennessee sales and use tax purposes.

The Tennessee sales and use tax applies only to sales of services that are specifically enumerated under Tenn. Code Ann. § 67-6-205(c) (Supp. 2007). *See Ryder Truck Rental, Inc. v. Huddleston*, 1994 WL 420911 at *2 (Tenn.Ct.App. August 12, 1994). However, the “sales price” of any tangible personal property sold in conjunction with a service that is not enumerated under this subsection will include any charges for the service, if the service is “necessary to complete the sale” of the tangible personal property. More specifically, Tenn. Code Ann. § 67-6-202(a) (Supp. 2007) imposes the sales tax on the “sales price” of tangible personal property sold at retail in Tennessee. Tenn. Code Ann. § 67-6-102(71)(A)(iii) (Supp. 2007) defines the term “sales price” in pertinent part as “the total amount of consideration, including cash, credit, property, and services, for which personal property or services are sold, leased, or rented,” without any deduction for “[c]harges by the seller for any services necessary to complete the sale.” Thus, charges for any services that are necessary to complete the sale of the Taxpayer’s System will be included in the sales price of the System, even if such services are not specifically enumerated under Tenn. Code Ann. § 67-6-205(c), and even if such charges are billed separately.

Computer help desk services are not specifically listed as services subject to the Tennessee sales and use tax under Tenn. Code Ann. § 67-6-205(c), and the sale of such services is thus generally not subject to taxation. However, in the Taxpayer’s case, charges for the help desk services are included in the sales price of the System, because the services are necessary to complete the sale of the System. Significantly, the Agreement requires the customer to purchase the help desk services when it enters into the Agreement to license the System from the Taxpayer. The Taxpayer has stated that it will not license the System to the customer without the help desk services. Because the sale of the System cannot occur without the sale of the help desk services, the sale of the services is necessary to complete the sale of the System.

One might argue that the Agreement for the licensing of the System and the agreement to provide help desk services, found in [HELP DESK SUPPLEMENT], are separate and divisible contracts, and that the help desk services agreement is therefore not subject to the Tennessee sales and use tax. The Tennessee Supreme Court has held that when two “separate and divisible”

¹ “Prewritten computer software” is defined under Tenn. Code Ann. § 67-6-102(60) (Supp. 2007) in pertinent part as “computer software, including prewritten upgrades, that is not designed and developed by the author or other creator to the specifications of a specific purchaser.”

agreements are embodied in a single divisible contract, each agreement is treated as distinct from the other for purposes of the sales and use tax. *Penske Truck Leasing Co., L.P. v. Huddleston*, 795 S.W.2d 669, 671 (Tenn. 1990). In *Penske Truck Leasing*, the taxpayer leased vehicles to customers under a “lease and service” agreement, which also provided the lessee with the option of purchasing fuel for the leased vehicles from the taxpayer, or of purchasing fuel from other vendors. *Id.* at 670. The court determined that the fuel purchase portion of the contract was separate and divisible from the lease portion. *Id.* at 671.

Importantly, the Tennessee Supreme Court in *Penske Truck Leasing* based its holding on the fact that the parties to the lease and service agreement intended and understood that the lease of equipment was separate and apart from fuel sales, though the terms of both transactions were included in the same document. *Id.* The court gave considerable weight to the fact that the lease portion of the contract was “readily distinguishable” from the portion covering fuel sales, and that neither portion of the contract was dependent upon the other. *Id.* Additionally, the court emphasized that the fuel agreement could be terminated independently, without causing termination of the lease agreement. *Id.* Because the fuel agreement was separate and divisible from the lease agreement, receipts from sales of fuel (which were not subject to the sales and use tax) were not properly included in the gross proceeds from the leasing of vehicles (which was subject to the sales and use tax). *Id.*

The Taxpayer’s case is readily distinguishable from the facts found in *Penske Truck Leasing*. Unlike the contract provisions in *Penske Truck Leasing*, the agreement for the licensing of the System and the agreement to provide help desk services are intrinsically related. Here, the Taxpayer requires that the customer purchase the help desk services in conjunction with the licensing of a System; the taxpayer in *Penske Truck Leasing* did not require the customer to purchase fuel in conjunction with the lease of its vehicles. The requirement that the customer purchase the help desk services is not arbitrary; in fact, the System is very likely of little or no use to the customer in the absence of the help desk services. Notably, the customer must pay a monthly fee for help desk services based upon the number of “help desk events” handled by the Taxpayer; the initial base number of help desk events is [NUMBER] per month. In other words, the parties anticipate that the customer will require the Taxpayer’s assistance in utilizing the System over [NUMBER] times per year. Given this fact, it is very unlikely that a customer would ever enter into an agreement to license a System without also entering into an agreement for technical support, even if the technical support services were optional. Accordingly, the agreement for the licensing of the System and the agreement to provide help desk services are not separate and divisible contracts for Tennessee sales and use tax purposes.

Therefore, the charges for the help desk services are necessary to complete the sale of tangible personal property and will be included in the sales price of the System, pursuant to Tenn. Code Ann. § 67-6-102(71)(A)(iii) (Supp. 2007).

Kristin Husat
Senior Tax Counsel

APPROVED: Reagan Farr
Commissioner of Revenue

DATE: 8/18/08