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**Computer Software Services  
Subject to Sales and Use Tax**

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**Sales &  
Use tax  
notice**

This notice is to clarify the taxability of computer software services. Under Tenn. Code Ann. Section 67-6-102(24)(B), packaged or customized software is considered tangible personal property which is subject to the sales and use tax. Tennessee law defines “sales price” to include the total amount for which a taxable service or tangible personal property is sold, including any services that are a part of the sale of tangible personal property. See, Tenn. Code Ann. Section 67-6-102(25). Thus, consulting services and charges for services to create, design, develop, fabricate, program, alter or modify computer software are subject to the sales or use tax when the charges are made as part of the sale of software. Similarly, separately itemized travel expenses incurred in conjunction with the sale of software are also taxable as part of the sales price of the software.

Software that a person fabricates for his or her own use is not considered taxable under Tenn. Code Ann. Section 67-6-102(24)(B). In a business setting, this exclusion only applies if employees of the company create or alter the software program for the company’s own use. If a consultant that is not an employee of the company creates or alters software, the entire charge made by the consultant is subject to the sales and use tax.

Some services related to computer software are considered taxable services under Tenn. Code Ann. Section 67-6-

102(23)(F). These services include repair, maintenance and installation, as well as charges for warranty or service contracts which warrant the repair or maintenance of software. Training services and telephone support services that are contracted for separately from the sale or license of software and that are separately invoiced are not taxable.

Software is commonly licensed under agreements that include taxable and nontaxable services. License agreements constitute a lease of tangible personal property under Tennessee law and the payments made pursuant to the license agreements are subject to sales and use tax. The tax is imposed on the gross proceeds of the license agreement under Tenn. Code Ann. Section 67-6-204. Thus, the total payments made pursuant to a license agreement, including any services, are subject to sales and use tax, even if the licensor separately itemizes the charges. The only exception to this is if a license agreement contains optional provisions that may be considered separately from the basic license agreement. For example, if a license agreement provides for ten hours of training at \$100 per hour and the licensee has the option of refusing this training, and therefore avoiding this charge, then the licensor would not have to charge sales tax on the separately itemized training charge. If the charge for training is included in the license fee for the software, or if the licensee has no option other than to pay

for training, then the charges for training are subject to sales and use tax.

Tenn. Code Ann. Section 67-6-102(24)(B) provides:

"Sale" also means such transfer of customized or packaged computer software, which is defined to mean, information and directions loaded into a computer which dictate different functions to be performed by the computer, whether contained on tapes, discs, cards, or other device or material. For such purpose, computer software shall be considered tangible personal property; however, the fabrication of software by a person for such person's own use or consumption shall not be considered a taxable "use" under subdivision (30) or any other section of this chapter;

"Sales price" is defined in Tenn. Code Ann. Section 67-6-102(25) as:

the total amount for which a taxable service or tangible personal property is sold, including any services that are a part of the sale of tangible personal property, valued in money, whether paid in money or otherwise, and includes any amount for which credit is given to the purchaser by the seller, without any deduction therefrom on account of the cost of the property sold, the cost of materials used, labor or service costs, losses, or any other expense whatsoever; ...

Tenn. Code Ann. Section 67-6-102(23)(F) provides that "Retail sale," "sale at retail" and "retail sales price" include the following services:

(iv) The performing for a consideration of any repair services with respect to any kind of tangible personal property; ...

(vi) The installing of tangible personal property which remains tangible personal property after installation where a charge is made for such installation whether or not such installation is made as an incident to the sale thereof and whether or not any tangible personal property is transferred in conjunction with such installation service;...

(ix) Charges for warranty or service contracts warranting the repair or maintenance of tangible personal property; provided, that any repairs to the extent covered by the contract shall not also be subject to tax;

Tenn. Code Ann. Section 67-6-204(a) provides:

(a) It is declared to be the intention of this chapter to impose a tax on the gross proceeds of all leases and rentals of tangible personal property in this state where the lease or rental is a part of the regularly established business, or the same is incidental or germane thereto. The tax is levied as follows:

(1) At the rate of 6% of the gross proceeds derived

from the lease or rental of tangible personal property, as defined herein, where the lease or rental of such property is an established business, or part of an established business, or the same is incidental or germane to the business.

(2) At the rate of 6% of the monthly lease or rental price by lessee or renter, or contracted or agreed to be paid by lessee or renter, to the owner of the tangible personal property.

Have questions or comments? Please let us know. [Contact us.](#)

Publication Date: June 1998