North Carolina Department of Revenue

Pat McCrory
Governor

Lyons Gray
Secretary

June 24, 2013

[redacted]

Re: Private Letter Ruling

Dear Ms. [redacted]

We have completed our review of your letter dated January 3, 2012 in which you request a private letter ruling on the application of North Carolina sales and use taxes to business transactions. Please accept our apology for the delay in providing a response.

Facts:
In your letter, you state "[your] customer purchased software licenses that will be implemented and installed on multiple computers within their network. Previous purchases [by] the same customer for the same type of software were taxed and paid without question. In December 2011, [your] customer place[d] an order for software licenses and the invoice generated include[d] sales tax pursuant to G.S. 105-164.3(29a). Upon receipt, the customer assert[ed] that tax is not owed on the sale pursuant to the exception indentified in G.S. 105-164.13(43a) which states that 'a sale of computer software that is designed to run on an enterprise server operating system is exempt from sales and use tax.'"

Question:
"Please explain the difference between the two interpretations and provide an example or a definition of 'an enterprise server operating system'. We are trying to determine if our software should be classified differently and therefore would be exempt from North Carolina sales tax to all of our North Carolina customers.'"

Answer:
N.C. Gen. Stat. § 105-164.4(a)(1) imposes a state sales tax on a retailer on the "sales price of each item or article of tangible personal property that is sold at retail and is not subject to tax under another subdivision in the section." Corresponding county tax levies are contained in Subchapter VIII of Chapter 105 of the North Carolina General Statutes.

N.C. Gen. Stat. § 105-164.3(46) defines the term "tangible personal property" as "[p]ersonal property that may be seen, weighed, measured, felt, or touched or is any other manner perceptible to the senses. The term includes electricity, water, gas, steam, and prewritten computer software."

N.C. Gen. Stat. § 105-164.3(29a) defines "prewritten computer software" as "[c]omputer software, including prewritten upgrades, that is not designed and developed by the author or another creator to the specifications of a specific purchaser. The term includes software designed and developed by the

author or another creator to the specifications of a specific purchaser when it is sold to a person other than the specific purchaser."

Effective January 1, 2010, N.C. Gen. Stat. § 105-164.13(43a) provides an exemption for the sale at retail and the use, storage, or consumption in this State of "[c]omputer software that meets any of the following descriptions:

a. It is designed to run on an enterprise server operating system.
b. It is sold to a person who operates a datacenter and is used within the datacenter.
c. It is sold to a person who provides cable service, telecommunications service, or video programming and is used to provide ancillary service, cable service, Internet access service, telecommunications service, or video programming."

The term "enterprise server operating system" is not defined in Chapter 105 of the North Carolina General Statutes. After consulting with industry representatives and North Carolina General Assembly staff, the Department issued *Important Notice: Computer Software*, in February 2010. The notice states, in part, "[a] sale of computer software that is designed to run on an enterprise server operating system is exempt from sales and use tax. The exemption includes a purchase or license of computer software for high-volume, simultaneous use on multiple computers, that is housed or maintained on an enterprise server or end users' computers. The exemption includes software designed to run a computer system, an operating program, or application software. The delivery method of the computer software is irrelevant."

If [redacted] software as *designed* [emphasis added] meets the criteria contained in the above paragraph, sales of such product on or after January 1, 2010 are exempt from North Carolina sales and use taxes pursuant to N.C. Gen. Stat. § 105-164.13(43a). A software engineer on your staff could likely determine if the product as *designed* [emphasis added] falls within the purview of the information contained in the Department's notice of February 2010. Prior to January 1, 2010, N.C. Gen. Stat. § 105.164.13(43a) provided an exemption for the sale at retail and the use, storage, or consumption in this State of "[c]omputer software delivered electronically or delivered by load and leave."

This ruling is based solely on the facts submitted to the Department of Revenue for consideration of the transactions described. If the facts and circumstances given are not accurate, or if they change, then the taxpayer requesting this ruling may not rely on it. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the factual situation of the taxpayer is different in any material aspect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that this document is not to be cited as precedent and that a change in statute, a regulation, or case law could void this ruling.

If we may be of additional assistance, you may contact the Sales and Use Tax Division at the telephone number listed on the bottom of the first page.

Sincerely,

[redacted]
Administration Officer
Sales and Use Tax Division

[redacted]

cc: [redacted], Director of Sales and Use Tax Division