

penalties to retail dealers of motor fuels for failure to display signage stating price per gallon of motor fuels sold by the dealer, for selling motor fuel at a price other than the price stated in the signage, and other requirements of N.J.S.A. 56:6-2 dealing with rebates and storing of equipment. The law substituted “not more than \$1,500 for the first offense and not more than \$3,000 for the second and any subsequent offense” for “not less than \$50.00 nor more than \$200.00 for each offense.” In order to bring N.J.A.C. 18:19-3.1 into conformity with N.J.S.A. 56:6-3, as amended by P.L. 2007, c. 221, the proposed amendment deletes the language regarding the amount of the prior penalty and adds language regarding the amount of penalty set forth in P.L. 2007, c. 221. The proposed amendment will state that a violation of N.J.S.A. 56:6-2 will bring a penalty of not more than \$1,500 for the first offense and not more than \$3,000 for the second and any subsequent offense.

Because the Division has provided a 60-day comment period on this notice of proposal, this notice is excepted from the rulemaking calendar requirements pursuant to N.J.A.C. 1:30-3.3(a)5.

Social Impact

The Motor Fuels-Retail Sales rules were originally adopted to provide motorists, oil companies, and retail dealers of motor fuels with guidance and assistance in the administration of the Act. Because the Legislature has determined that regulation of the sale of motor fuels is in the public interest, the rules implement and carry out the legislative purposes in a manner consistent with such public purpose. The statute and the rules pursuant to it reflect a balancing of various interests including the motorists’ right to know the price of fuels available, and the prevention of potentially destructive competition among motor fuels dealers.

In 2007, the Legislature enacted P.L. 2007, c. 221, which amended the penalty provision of N.J.S.A. 56:6-3 to read as follows: “Every retail dealer who shall fail to post and publicly display, in the manner herein required, a sign stating the price per gallon, or per gallon and per liter, of all motor fuel sold by said retail dealer, or who shall sell motor fuel at a price other than the per gallon or per liter price, as provided in article II hereof, or who shall violate any other provisions of article II of this act, shall, upon conviction, be subject to a penalty of not more than \$1,500 for the first offense and not more than \$3,000 for the second and any subsequent offense, and his license shall be suspended for a period of not less than five (5) days nor more than thirty (30) days, and in default of the payment of such penalty shall be imprisoned for a period not to exceed 30 days. If there shall be a conviction upon a second or subsequent offense, the license of the convicted retail dealer, issued under the provisions and procedure in chapter thirty-nine of Title 54 of the Revised Statutes, shall be revoked by the Director of the Division of Taxation.” The proposed amendment will have a positive social impact by bringing the rule into conformity with the statute as amended, thereby avoiding confusion and potential litigation about the applicable penalty.

Economic Impact

The rules promulgated pursuant to the Act were adopted to provide for the orderly marketing of motor fuels in New Jersey and thus directly affect the economy of the State and region. However, the proposed amendment to N.J.A.C. 18:19-3.1 is not expected to have any economic impact because the proposed amendment is merely a technical correction to an existing rule on penalties, in order to bring the rule into conformity with the law, which has been in effect since January 3, 2008.

Federal Standards Statement

A Federal standards analysis is not required because State regulation of the retail sales of motor fuels is not subject to Federal regulatory standards. The administration of rules addressing these issues at the State level is an independent and separate jurisdiction.

Jobs Impact

The proposed amendment will not result in the creation or loss of jobs and is not expected to have any independent effect on jobs in this State.

Agriculture Industry Impact

The proposed amendment will have no impact on the agriculture industry.

Regulatory Flexibility Statement

The proposed amendment applies to all taxpayers subject to the statutory provisions regulating the trade practices of retail sales of motor fuels, whether or not they are small businesses as the term is defined in the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq. The proposed amendment amends a rule that was promulgated pursuant to N.J.S.A. 56:6-1 et seq., which places certain trade practice requirements on retail sellers of motor fuels, such as requirements for the display of prices.

The proposed amendment does not impose new reporting, recordkeeping, or other compliance requirements. No accounting or other professional services are needed for a business to comply with the proposed amendment. The proposed amendment relates to a penalty provision of the Act. Each taxpayer is free to choose to make expenditures or to retain the services of a professional, to determine if the proposed amendment would apply to their own situation. The proposed amendment is intended to benefit sellers of motor fuels by providing accurate information on the penalty for failure to comply with statutory fair trade practices in the sale of motor fuels.

Housing Affordability Impact Analysis

The proposed amendment would not result in a change in the average costs associated with housing. The proposed amendment would have no impact on any aspect of housing because the proposed amendment deals with the retail sales of motor fuels.

Smart Growth Development Impact Analysis

The proposed amendment would not result in a change in the housing production within Planning Areas 1 or 2, or within designated centers, under the State Development and Redevelopment Plan. The basis for this finding is that the proposed amendment has nothing to do with housing production, either within Planning Areas 1 or 2, within designated centers, or anywhere in the State of New Jersey. The proposed amendment deals with the retail sales of motor fuels.

Full text of the proposal follows: (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

SUBCHAPTER 3. PREPARATION OF FINES

18:19-3.1 Violations and penalties

(a) Rules concerning violations and penalties follow:

1.-2. (No change.)

3. Who violates any other provisions of N.J.S.A. 56:6-2, shall, upon conviction:

i. Be subject to a penalty of not [less] **more** than [\$50.00 nor] **\$1,500 for the first offense and not** more than [\$200.00] **\$3,000** for [each] **the second and any subsequent** offense; and

ii-iii. (No change.)

4. (No change.)

(a)

DIVISION OF TAXATION

Sales and Use Tax

Sales of Software and Related Services

Proposed Amendments: N.J.A.C. 18:24-25.1

Proposed Repeal and New Rule: N.J.A.C. 18:24-25.6

Proposed New Rule: N.J.A.C. 18:24-25.1 and 25.7

Authorized By: Michael J. Bryan, Director, Division of Taxation.

Authority: N.J.S.A. 54:32B-24 and 54:50-1.

Calendar Reference: See Summary below for explanation of exception to calendar requirement.

Proposal Number: PRN 2014-049.

Submit written comments by June 20, 2014, to:

Mitchell C. Smith
Administrative Practice Officer
Division of Taxation
50 Barrack Street
P.O. Box 269
Trenton, NJ 08695-0269
Email: Tax_RuleMakingComments@treas.state.nj.us

The agency proposal follows:

Summary

The proposed amendments, repeal, and new rules to N.J.A.C. 18:24-25 provides definitions and guidance regarding the sales tax treatment of software and related services.

Background

N.J.S.A. 54:32B-3(a) imposes sales tax on receipts from every retail sale of tangible personal property. N.J.S.A. 54:32B-3(b)(2) imposes sales tax on receipts from maintaining, servicing, or repairing tangible personal property.

Historically, the law did not impose sales tax on services performed on software in the electronic state because such software was deemed to be intangible in nature. In 2005, however, the Sales and Use Tax Act (N.J.S.A. 54:32B-1 et seq.) was amended to include “prewritten computer software” within the definition of “tangible personal property.” Effective October 1, 2006, the law was further amended to include “prewritten computer software delivered electronically” as tangible personal property. Consequently, as of that date, services performed on prewritten or “canned” software in electronic form are subject to sales tax. In addition, also effective October 1, 2006, the purchase of electronically delivered prewritten software purchased for business use became exempt. See N.J.S.A. 54:32B-8.56.

The Division published written guidance on the 2005 and 2006 legislative amendments but has concluded that formal guidance in the form of rules is necessary to communicate these changes and the Division’s interpretation to the industry and the general public more effectively. This notice will also provide an opportunity for the public to provide comments.

The Division has also found that the billing terms used by the industry are inconsistent and tend to further confuse both sellers and purchasers as the applicability of the Sales and Use Tax Act.

Current Proposed Changes

New N.J.A.C. 18:24-25.1 is proposed to state the scope of Subchapter 25.

N.J.A.C. 18:24-25.1 proposed for recodification as N.J.A.C. 18:24-25.1A and is amended to add several definitions, which are intended to clarify the Division’s understanding of certain products and services. “Custom software” is amended to clarify that the use of development languages or prewritten functions or routines in the creation of custom software does not cause the resulting software to be deemed prewritten. The Division has observed that “software maintenance contract” is used throughout the industry to reflect a variety of packaged services. Since the Division wants to provide the most accurate information regarding the application of the law to these services, a standardized meaning of this phrase is needed to clearly convey the Division’s understanding of the product. Accordingly, “software maintenance contract” is proposed to mean a “contract to provide future updates or upgrades to computer software and/or customer support services.” This definition has been added and is based on the definition contained in the Streamlined Sales and Use Tax Agreement. Definitions of “installing,” “modifying,” “servicing,” and “customer support services” have also been proposed to clarify what those terms represent to the Division.

Existing N.J.A.C. 18:24-25.6 is proposed for repeal and replaced with new N.J.A.C. 18:24-25.7, as discussed below.

New N.J.A.C. 18:24-25.6 explains the sales tax status of software-related services using the proposed definitions in context and provides examples to illustrate proper application of the defined terms.

New N.J.A.C. 18:24-25.7 replaces existing N.J.A.C. 18:24-25.6, but there is no shift in policy reflected by the changed language. Rather, the new organization of this material and use of the updated definitions will

allow for a more user-friendly review of the rules. A statement clarifying the Division’s position was added to address the sales tax treatment where taxable and non-taxable goods or services are bundled by the seller as new paragraph (c)3.

As the Division has provided a 60-day comment period on this notice of proposal, this notice is excepted from the rulemaking calendar requirement pursuant to N.J.A.C. 1:30-3.3(a)5.

Social Impact

Over the last several years, advances in technology have allowed software developers and software service providers to offer a host of delivery options and product packaging and services. Further, the software formats and modes of delivery used by the computer software industry have evolved greatly in recent years. Where disks and CDs were once the only media available to purchasers, software sellers can now send electronic versions of software directly to purchasers via email or have purchasers download software from sellers’ websites. Service providers may also install software remotely or in a “load and leave” manner. Updates, upgrades, and software patches are often automatically sent as maintenance to the software. Telephone support or consultation services are often packaged with the sale of software. With so many methods of delivery and service package options available, the Division determined that it is necessary to provide more comprehensive guidance in this area.

The clarification provided by the amendments and new rules will ease the existing confusion within the industry as to how to properly impose sales tax. Purchasers of software and software services will also benefit from clear and understandable guidance. The proposed amendments and new rules will not necessarily require a taxpayer to pay more tax. The Division also anticipates that the promulgation of the proposed amendments and new rules will result in heightened voluntary compliance.

Economic Impact

The proposed amendments and new rules expand guidance regarding sales of software and software-related services. The amendments and new rules are also intended to clarify the Division’s current position concerning a number of computer-related services. Since invoice terms and billing practices vary throughout the industry, the Division has found that many software sellers, service providers, and purchasers of software and software-related services may currently be uncertain as to their sales tax obligations. The amendments and new rules do not change the sales tax treatment of computer software or software-related services. However, as a result of the implementation of these changes, some software sellers and service providers may begin to collect sales tax on services that they previously had not taxed. Businesses that are not currently in compliance with New Jersey law may experience some economic impact in facilitating sales tax collection and return filing.

The proposed amendments and new rules will not require any taxpayers that were not previously liable to pay tax to now pay tax.

Federal Standards Statement

A Federal standards analysis is not required. This rulemaking is based on N.J.S.A. 54:32B-24 of the New Jersey Sales and Use Tax Act. There are no Federal regulatory requirements or standards that affect this rulemaking. Therefore, a Federal standards analysis is not required.

Jobs Impact

The Division does not anticipate that any jobs will be generated or lost as the result of the proposed amendments and new rules.

Agriculture Industry Impact

The proposed amendments and new rules will have no impact on the agriculture industry.

Regulatory Flexibility Statement

The proposed amendments apply to small businesses, as defined under the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq., as well as to businesses employing more than 100 people full-time. The software industry is ever evolving. New delivery methods and service options are constantly introduced into the marketplace. As most businesses, large and small, utilize these services, the Division anticipates wide-spread impact felt as a result of these changes. The proposed amendments are intended

to provide businesses with a greater level of confidence in their ability to understand the sales tax treatment of common purchases of computer-related goods and services.

The proposed amendments and new rules will not impose any new reporting, recordkeeping, or compliance requirements, as the changes only clarify existing requirements.

Housing Affordability Impact Analysis

The proposed amendments and new rules would not result in a change in the average costs associated with housing. The proposed amendments and new rules would have no impact on any aspect of housing because the proposed amendments and new rules relate to the taxation of the sales of software and related services in New Jersey.

Smart Growth Development Impact Analysis

The proposed amendments and new rules would not result in a change in the housing production within Planning Areas 1 or 2, or within designated centers, under the State Development and Redevelopment Plan. The basis for this finding is that the proposed amendments and new rules are not related to housing production, either within Planning Areas 1 or 2, within designated centers, or anywhere in the State of New Jersey. The proposed amendments relate to the taxation of the sales of software and related services in New Jersey.

Full text of the proposal follows: (additions indicated in boldface thus; deletions in brackets [thus]):

SUBCHAPTER 25. SALES OF SOFTWARE AND RELATED SERVICES

18:24-25.1 Scope

This subchapter is intended to clarify the application of the Sales and Use Tax Act (N.J.S.A. 54:32B-1 et seq.) to sales of software and software related-services. This subchapter does not address the sale of clerical, data entry, or accounting services, etc., which may be performed with the use of software.

18:24-[25.1]25.1A Definitions

The following words and terms, as used in this subchapter, shall have the following meanings, unless the context clearly indicates otherwise:

...
 “Custom software” means software created, written, and designed for the exclusive use of a specific [customer] **purchaser** and sold to the [customer] **purchaser** for whom it was designed. **The use of development languages or prewritten functions or routines does not necessarily cause software, designed for a specific purchaser, to become taxable prewritten computer software.**

“Customer support services” means verbal and written computer software advice or guidance (for example, provided via the Internet or telephone).

...
 “Installing” software means the act of loading an executable file, whether tangible or electronic, containing a prewritten computer software application or program onto a device or equipment. **The mere act of electronic delivery does not constitute installation.**

“Load-and-leave” is a method of software delivery whereby a seller or its representative installs software on a [customer’s] **purchaser’s** computer by using a tangible storage medium, which is then removed and not left in the [customer’s] **purchaser’s** possession.

“Modifying” software means any action, other than installing or servicing software, performed to enhance, improve, or customize software, regardless of whether the computer code is changed.

“Prewritten computer software” means any computer software, including prewritten upgrades and updates and combinations of two or more prewritten software programs, or prewritten portions thereof, that is not designed and developed to meet the unique requirements of a specific purchaser and sold to that specific purchaser for the purchaser’s exclusive use.

“Servicing” software means any action to maintain the compatibility of computer software with other hardware and software products and performing other corrective services that do not involve changing computer code.

“Software maintenance contract” means a contract to provide future upgrades and/or updates to computer software and/or customer support services.

...

[18:24-25.6 Treatment of maintenance contracts and software-related services

(a) Charges for installation of pre-written software on a computer are subject to sales tax.

(b) Fees for maintenance contracts that include only the provision of online or telephone advice, guidance, and customer support are not taxable.

(c) Fees for maintenance contracts that include the delivery of updated, corrected, or supplemental software via tangible storage media or via electronic delivery are taxable unless the updates will be:

1. Delivered only electronically and will be used directly and exclusively in the purchaser’s business, trade, or occupation; or

2. Entirely custom-made of custom software, for the exclusive use of the original purchaser.

(d) Since electronically delivered prewritten software is tangible personal property, the services of installing, maintaining, servicing, and repairing such software are taxable to the same extent as those services rendered for prewritten software delivered via tangible storage media.]

18:24-25.6 Treatment of software-related services

(a) **Since prewritten computer software is defined as tangible personal property under the Sales and Use Tax Act, servicing, installing, or maintaining software is subject to tax pursuant to N.J.S.A. 54:32B-3(b)(2), whether the software is serviced, installed, or maintained at the purchaser’s location or from or at a seller or service provider’s remote location.**

Example: Upon purchase of prewritten computer software, and for a separate additional cost, a technician goes to a customer’s business location to download (install) software to the business’s server. The charge for this installation service is subject to sales tax.

(b) **Modifying prewritten computer software for a purchaser is treated as a sale of non-enumerated services and is not subject to sales tax.**

Example: A computer technician creates a string of code to “bridge” two software platforms already in place at the location of the business customer. This requires the entry of computer code programming. The charge for modifying the existing software is not subject to sales tax.

(c) **Customer support services are treated as a sale of a non-enumerated service and are not subject to sales tax.**

Example: A software developer provides customers the opportunity to call a manned hot-line whereby customers who are experiencing issues/problems may receive verbal advice or advice by email about how to resolve their issues/problems. The charge for this service is not subject to sales tax.

(d) Clerical, data entry, or accounting services, etc., which may be performed with the use of software are not considered to be servicing software. The charge for these services is not subject to sales tax.

Example: An accountant assists one of his business customers by creating an Excel template spreadsheet that may be used as a basis for day-to-day inventory tracking. The charge for this service is clerical or professional in nature. It is not considered the servicing of software and is not subject to sales tax.

18:24-25.7 Software maintenance contracts

(a) Software maintenance contracts are taxed as follows:

1. A software maintenance contract that only provides upgrades and updates is treated as a sale of prewritten computer software and is subject to tax regardless of whether the software is delivered on tangible storage media (for example, disk, CD-ROM) or electronically; however, if the upgrades and updates are delivered only electronically and for use directly and exclusively in the conduct of the purchaser’s business, trade, or occupation, the software maintenance contract is not taxable.

2. A software maintenance contract that only provides customer support services is treated as a sale of non-enumerated services and is not subject to sales tax.

3. A software maintenance contract that includes both taxable and nontaxable or exempt products that are not separately itemized on the invoice or similar billing document is a bundled transaction and shall be treated as taxable unless the seller can demonstrate, using a

reasonable and verifiable method based on its books and records as of the time of sale, the portion of the contract that is for nontaxable or exempt products. The method selected by the seller shall be binding on the purchaser.

18:24-[25.7]25.8 (No change in text.)
