

# NEW JERSEY DIVISION OF TAXATION

## TECHNICAL BULLETIN

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**TB-51R**

**ISSUED: 03/13/07**

**TAX: SALES AND USE TAX**

**TOPIC: SOFTWARE**

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### **Pre-written Computer Software Is “Tangible Personal Property”**

Computer software means a set of coded instruction designed to cause a computer or automatic data processing equipment to perform a task. N.J.S.A. 54:32B-8.56.

The New Jersey Sales and Use Tax Act taxes retail sales of tangible personal property, unless a specific statutory exemption or exclusion from sales tax applies. “Tangible personal property” includes pre-written computer software, including pre-written computer software delivered electronically.

### **Change in the Law**

Prior to October 1, 2006, software that was transmitted electronically was not treated as taxable tangible personal property, and therefore its sale was not subject to sales or use tax. P.L. 2006, c. 44, made the following changes regarding the taxability of software, effective October 1, 2006:

1. expanded the statutory definition of “tangible personal property,” *explicitly including “prewritten computer software delivered electronically,”* N.J.S.A. 54:32B-2(g), and
2. limited the exemption for electronically delivered pre-written software, allowing an exemption for sales of electronically delivered pre-written software *only* when it is to be used directly and exclusively in the conduct of the purchaser’s business, trade, or occupation, N.J.S.A. 54:32B-8.56.

### **Taxability of Pre-written Software**

#### ***Pre-written Computer Software***

Pre-written computer software is any computer software, including pre-written upgrades and including combinations or portions of two or more pre-written software programs, that is *not* designed and developed to meet the unique requirements of a specific purchaser and sold for that specific purchaser’s exclusive use. N.J.S.A. 54:32B-8.56. Pre-written software includes pre-written software delivered electronically. Pre-written software can be installed on the purchaser’s computer, either electronically or

through the use of a tangible medium, without significant modification to the software. Pre-written software can also include pre-written software that has been modified for the customer as well as software initially designed as “custom” software for a specific purchaser, which is subsequently sold as is to anyone other than the original purchaser. N.J.S.A. 54:32B-8.56.

The retail sale of pre-written software is taxable. The sale of a license to use pre-written software is treated the same as the sale of outright title to the pre-written software. The use in New Jersey of pre-written computer software purchased at retail without payment of sales or use tax is subject to use tax. N.J.S.A. 54:32B-6.

### *Custom Software*

In the current market, it is rare for a software designer to create software solely for one specific purchaser. Most software is instead already pre-written, and can be sold as is, or with some modifications to adapt it to the customer’s special technical or business needs. In those exceptional circumstances when software is created, written, and designed for the exclusive use of a specific customer, it is not considered pre-written computer software when sold to the specific customer for whom it was designed. N.J.S.A. 54:32B-8.56. That customer’s purchase of this entirely custom-made software is treated as a nontaxable professional service transaction and is not subject to sales tax.

### *Modified Software*

It has become commonplace for business customers to purchase pre-written computer software that has been modified somewhat to fit their technical or business requirements. The sale of pre-written computer software is taxable regardless of whether the pre-written software is sold in its original form, or combined with other pre-written software programs, or with modifications to meet the purchaser’s special needs. However, the seller of modified software has an option to charge a separate fee for the customization service. A separately stated, commercially reasonable charge for the professional service of modifying the software for the customer is not treated as a charge for the sale of pre-written computer software and that separate charge is therefore exempt from sales tax. N.J.S.A. 54:32B-8.56. If the vendor of modified software instead chooses to charge a lump sum, without separately stating the fee for customization services, then the entire charge is subject to sales tax as part of the sale of tangible pre-written software.

### **Exemption for Sales of Electronically Delivered Software Used Exclusively and Directly in Conduct of Purchaser’s Business, Trade, or Occupation**

There is one exception to the taxability of pre-written software delivered electronically. Sales of pre-written software delivered electronically are exempt if the software is to be used directly and exclusively in the conduct of the purchaser’s business, trade, or occupation. N.J.S.A. 54:32B-8.56.

This exception does not apply, however, if the software is being delivered by a “load-and-leave” method. Sellers sometimes send a service representative to a customer’s New Jersey location to install pre-written or modified software. In some circumstances, once the installation is complete, the tangible storage medium (CD, disc) is not left with the customer. This type of installation is referred to as “load and leave.” The transaction is not deemed to be the sale of tangible personal property delivered electronically, and therefore is not exempt, even if the software is to be used directly and exclusively in the conduct of the purchaser’s business, trade, or occupation.

If the purchaser of software initially delivered electronically also receives tangible storage media containing the software, then the transaction is not deemed to be a sale of software delivered electronically and is not exempt, even when the software is to be used directly and exclusively in the purchaser’s business.

### **Installation and Maintenance Services and Service Contracts**

Fees for the service of installing software for the customer are subject to sales tax. They are treated as charges for the installation of tangible personal property.

Charges for the sale of a maintenance contract for pre-written software are generally subject to tax. Software maintenance contracts usually include the provision of updated, supplemental, and corrected software. Contracts covering delivery of such updated, supplemental, and corrected software via tangible storage media are taxable. Contracts for the delivery of such updated, supplemental, and corrected software entirely electronically, with no tangible storage media, are also taxable *unless* these electronically delivered updates are to be used directly and exclusively in the conduct of the purchaser’s business, trade, or occupation. A maintenance contract covering only entirely custom-made updates of custom software, for the exclusive use of the original purchaser, is also nontaxable, regardless of whether delivered electronically or through tangible storage media. If a software maintenance contract covers *only* the provision of training, consultation, or of advice, help and customer support via telephone or online, but no software, then the charges are not taxable.

*Issued by:*  
*Regulatory Services Branch*  
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