

# Computer Programs and Related Services

## About this Guide

The information in this *Guide* explains how Retail Sales Tax (RST) applies to computer programs and related services. Please note that this *Guide* replaces the previous version dated February 2001.

## Contents

<b>Computer Programs</b>	<b>2</b>
Taxable Computer Programs .....	2
Location and Use of a Computer Program .....	2
Sales of Multiple Licences - Use Inside and Outside Ontario .....	3
Sales to Out-of-Province Purchasers.....	3
<b>Custom Computer Programs</b>	<b>3</b>
Modifications to a Pre-Written Computer Program .....	4
In-House Development .....	4
Resale of a Custom Computer Program.....	4
<b>Taxable Services</b>	<b>4</b>
<b>Modifications</b>	<b>5</b>
Configurations vs. Modifications .....	6
When are Modifications Exempt? .....	6
Modifications Performed Separate from the Sale of a Computer Program.....	6
Modifications Performed with the Sale of a Computer Program .....	7
Modifications to Modules and Interface Programs.....	7
Documentation Required .....	8
In-House Modifications .....	8
<b>Non Taxable Services</b>	<b>9</b>
<b>De Minimis Rules</b>	<b>11</b>
Testing Services and De Minimus Rules.....	12
Taxable Bundled Sales .....	12
Excluded Sales .....	12
Documentation.....	12
<b>Determining Fair Value</b>	<b>13</b>
<b>Placement Agencies &amp; IT Consultants</b>	<b>14</b>
<b>Manufacturers of Computer Programs</b>	<b>14</b>
<b>Other Related Information</b>	<b>15</b>
<b>Legislative References</b>	<b>16</b>

## Computer Programs

For Retail Sales Tax (RST) purposes, applications created using programming languages, where the source code is compiled into an executable format or into an intermediate language, are computer programs.

Applications developed using languages other than programming languages, that are not compiled into executable format or an intermediate language, do not qualify as computer programs and are not subject to RST. Developing these types of applications is the provision of a non-taxable service.

### Taxable Computer Programs

All computer programs are taxable, unless the program qualifies as a custom computer program (refer to page 3 for 'Custom Computer Programs'). The method of delivering a program (e.g., via CD, memory devices, electronic transmission, etc.) does not determine the RST status of the program, since computer programs are defined as tangible personal property (TPP) in the *Retail Sales Tax Act*.

RST applies to the sale of a taxable computer program, which includes leases, licensing agreements, or 'right to use' arrangements, even if there is no formal agreement. Any charges for additional licences are also taxable.

Examples of taxable computer programs:

- packaged, pre-written, 'canned' or 'off-the-shelf' programs
- system programs or operating systems
- application programs, such as word processors, spreadsheets, databases, Internet browsers and games
- computer program modules and interface programs
- upgrades that are provided in a ready-to-install format

### Location and Use of a Computer Program

The location of a computer program determines whether RST applies to the use of the program or to any related taxable service(s).

RST applies to charges for the right to use (i.e., licence agreement) a taxable computer program installed on a computer or server located in Ontario, regardless of the location of the person(s) using the program.

#### Examples:

If a taxable computer program is installed on a computer or server located in Ontario, and users can access the computer program from remote locations inside and outside Ontario, RST applies to any charges for the use of the program.

If a taxable computer program is installed on a computer or server located outside Ontario, and users can access the computer program from remote locations inside or outside Ontario, but cannot download the program, RST does not apply to any charges for the use of program.

### Sales of Multiple Licences - Use Inside and Outside Ontario

If a sale includes multiple licences for the use of a taxable computer program, and the contract permits the installation of the program on a computer where each user is located, and the users are located both inside and outside Ontario, Retail Sales Tax (RST) can be prorated based on the number of programs installed in Ontario.

For example, ten licences are sold for \$100,000. Six of the computer programs will be installed in Ontario and four of the programs will be installed in British Columbia. All the licences are of equal value (i.e., \$10,000 each). RST applies as follows:

- if the contract specifies the intended location of each computer program, RST applies to the licences that will be installed in Ontario.
- if the contract does not specify the intended location of computer programs, the vendor must charge RST on the total sale and the customer may claim a refund based on proration. (Customers must complete a General Application for Refund of Retail Sales Tax form. Refund claims must be received within four years of the date RST was paid.)

Proration does not apply if the licence agreement permits the use of the computer program on a server located in Ontario. RST applies to the total sale regardless of the location of the users.

### Sales to Out-of-Province Purchasers

RST does not apply to the sale of a computer program if:

- a hardcopy version is sold and the vendor is responsible for delivering it outside Ontario, or to a third party in Ontario for trans-shipment with other goods outside Ontario (shipping documents and/or bills of lading must be retained by the vendor.)
- it is sold in an electronic version and downloaded by the purchaser, or delivered electronically, to a location outside Ontario (the purchaser's name and out-of-province address must be retained by the vendor).

RST applies to the sale of a computer program if:

- a hardcopy version is sold and the out-of-province purchaser is responsible for delivery, or the purchaser will be picking up the hardcopy from a location in Ontario
- it is sold in an electronic version and the vendor does not receive the purchaser's name and out-of-province address

## Custom Computer Programs

A 'custom computer program' is one that is designed and developed solely to meet the specific requirements of, and that is intended for the exclusive use of, one person (i.e., one legal entity).

Custom computer programs are exempt from RST.

A custom computer program can be developed:

- from scratch, or
- by using pre-developed code from a library maintained and owned by the programmer, or
- by extensively modifying a pre-written computer program (refer to 'Modifications' on page 6 for more details).

**Note:** A pre-written computer program is a pre-packaged program that may be purchased in a form that is ready for use without further modifications and includes a computer program that is designed and developed for the use of more than one person.

A computer program does not qualify as custom if:

- it is designed and developed for the use of more than one person (i.e., more than one legal entity), or
- the intent at the time of development is to resell the computer program to others (e.g., the developer retains the rights to the source code or the program), or
- the same core program is used to develop a program for each person, and only minor modifications are made to that program.

A purchase exemption certificate (PEC) is not required for the sale of a custom computer program.

### Modifications to a Pre-Written Computer Program

As outlined earlier, not all custom computer programs are developed from scratch. Modifications to a pre-written program may result in the creation of a custom program. The following conditions must be met in order for the program to qualify as a custom program:

- the price of the modifications exceed the price of the original pre-written program, and
- the modifications are performed solely to meet the specific requirements of one person (i.e., one legal entity), and
- the resulting computer program is for the exclusive use of that person.

Purchasers are required to provide a PEC when claiming an exemption for modifications performed separate from the sale of a program.

### In-house Development

Custom computer programs may include programs developed in-house by a company for its exclusive use, or pre-written computer programs that are modified extensively by staff in-house (refer to page 6 for 'Modifications'). Companies must maintain documentation to support that the programs qualify as custom computer programs.

### Resale of a Custom Computer Program

Custom computer programs may only be sold exempt from Retail Sales Tax (RST) to the first purchaser. RST applies to subsequent sales of the program. However, if the purchaser is acquiring the seller's ongoing business, with substantially all of the seller's business assets, the program remains a custom computer program.

### Services

Services provided in respect of a custom computer program are exempt from RST. To claim the exemption, the purchaser must provide a valid PEC to the service provider.

## Taxable Services

**'Taxable services'** as related to computer programs are labour provided to install, configure, modify or upgrade a taxable computer program and any contract for the service, maintenance or warranty of a computer program.

Retail Sales Tax (RST) applies to these taxable services, when they are performed in respect of a taxable computer program located in Ontario.

### Install

**'Install'** means to perform work required to load a computer program onto hardware in order to permit the users to set up or operate the computer program.

Installing a computer program may include a number of steps such as verifying the existence of prerequisite programs, unloading the program from the delivery medium to disk storage, etc. RST applies to the total process of installing, reinstalling or uninstalling a taxable computer program.

**Configure** **'Configure'** means to perform work required to input customer-specific values and parameters into a computer program or hardware.

Configuring a program may involve choosing options and/or parameters, or inputting values into data fields or tables which will be created as part of the configuration process. Configuring a program does not change the source code of the program.

**Modify** **'Modify'** means to change the source code of a computer program.

Depending on the amount charged for the source code changes, modifications may convert a taxable program into a custom computer program. (refer to page 6 for 'Modifications').

**Upgrade** **'Upgrade'** means to remedy problems within a computer program or between computer programs, or to provide an improvement to the computer program that is offered or available to all licensees of that computer program.

Upgrades include corrective services performed to resolve problems within a computer program or between computer programs. Upgrades can also be standardized enhancements to a computer program, such as new releases, patches, service packs, add-ons or fixes to the program.

Some upgrades need to be manually coded into the existing source code of a program by a technician or programmer. Other upgrades may be provided in a ready-to-install format (i.e., executable format). While both types of upgrades are taxable, the ready-to-install format is a computer program and not a service.

**Service or Maintenance** **'Service or maintenance of a computer program'** means the installation, configuration, modification or upgrade of a computer program.

Service and maintenance agreements that include any taxable services (i.e., installation, configuration, modification or upgrades to a computer program) are subject to RST.

**Warranty** **'Warranty of a computer program'** means an undertaking that the computer program will function as required by the purchaser or as guaranteed by the producer or vendor.

**Service Providers** Service providers must pay RST on all taxable goods and services purchased in order to provide their services.

## Modifications

**Definitions** Modifications are changes made to the source code of a computer program.

Modifications can convert a taxable computer program into a custom computer program, provided certain conditions are met. Once a computer program qualifies as a custom computer program, any additional services provided to the program qualify for exemption. Taxable services that were provided to the program **before** it qualified as a custom computer program do not qualify for exemption.

**Definitions**  
*(continued)*

To determine if modifications are exempt, the price of the original pre-written computer program, the price of modifications, and the date of the modifications must be established.

**Price of the Original Pre-Written Computer Program:**

- is the price of the initial licence of the computer program **only**, regardless of the number of additional licences that were purchased at the time of sale.

**Price of Modifications:**

- includes any charges for time/labour spent to modify the source code **and** any charges for local travel (i.e., expenses incurred during the course of a normal working day, such as mileage, meals, parking, telephone, and miscellaneous).

**Note:** When calculating the 'price of modifications', charges for upgrades and/or configurations, and expenses such as accommodation and airfare should **not** be included.

**Date of Modifications:**

- the date of modification is important since the cost of modifications could not be accumulated before July 19, 2002. Charges for modifications performed on or after July 19, 2002 can be accumulated.

**Configurations vs. Modifications**

Configuring a computer program **does not** involve changes to the source code. Even where the information is specific to a particular user, the service is not considered a modification since the source code is not altered.

**Note:** Although modification and configuration services are both taxable services, the charge for modifications performed on a computer program can alter the tax status of a program.

**When are Modifications Exempt?**

Modifications can be performed before a computer program is sold or after. They can be performed all at once, or over a period of time; in-house, or by one or more third party service providers. The exemption is dependent on how and when the modifications are provided. The following sections outline the different conditions and requirements for exemption.

**Modifications Performed Separate from the Sale of a Computer Program****On or after July 19, 2002:**

Charges for modifications performed on or after July 19, 2002 may be accumulated and qualify for exemption provided the following conditions are met:

- the price of the modifications exceed the price of the original pre-written program, and
- the modifications are performed solely to meet the specific requirements of one person (i.e., one legal entity), and
- the resulting computer program is for the exclusive use of that person.

The full charge for the modification that results in the value of the accumulated modifications exceeding the price of the original pre-written program is exempt from RST. All taxable services provided after this point are exempt since the program qualifies as a custom computer program.

Purchasers are required to provide a PEC when claiming an exemption from RST for services provided to a custom computer program.

**Modifications Before July 19, 2002:****Performed Separate from the Sale of a Computer Program**  
*(continued)*

Prior to July 19, 2002, separate sales of modifications could **not** be accumulated. Therefore, unless the individual sales of modifications exceeded the price of the original pre-written computer program, the modifications did not qualify for exemption.

The application of RST to modifications performed before July 19, 2002 depended on the contractual agreement and the method of invoicing.

- If there was no contract, or if a contract existed but it did not specify the price and extent of the modifications, RST applied to each separate invoice or contract that did not exceed the price of the original pre-written program, since modifications performed before July 19, 2002 were not cumulative.
- If a contract did exist that detailed the price and extent of the modifications, and the price of the modification was greater than the price of the original pre-written computer program, the modification was exempt since the program qualified as a custom computer program at the time the contract or agreement was signed. If the modifications did not exceed the price of the original pre-written program, these charges could not be added to any future modifications since they occurred before July 19, 2002.

**Modifications Performed with the Sale of a Computer Program** Where modifications are performed **with** the sale of a pre-written program, the program qualifies as a custom computer program provided the following conditions are met:

- the price of the modifications exceeds the price of the original pre-written program, **and**
- the modifications are performed solely to meet the specific requirements of one person (i.e., one legal entity), **and**
- the resulting computer program is for the exclusive use of that person.

In this case, the sale of the program, and all the services provided, are exempt from RST. Since this is the sale of a custom computer program, no PEC is required from the purchaser provided all the conditions are met for the exemption.

If the modifications do not exceed the price of the original pre-written program, RST applies to the sale of the program (including the modifications) since it does not qualify as a custom computer program.

**Modifications to Modules and Interface Programs** Modifications provided after July 19, 2002 should be separated on the invoice/contract to allow the purchaser to use this amount in future cumulative calculations. If the modifications are not separated from the price of the program, then the amount billed is considered the price of the original pre-written program.

To determine whether modifications qualify for exemption, when calculating the price of a pre-written program, you must first determine whether the pre-written modules and interface program(s) are one program, or individual programs connected together.

If the pre-written modules and interface program(s) are one single program, the price of the original pre-written program is the price of the entire package, regardless of any breakdown.

If the pre-written modules and interface program(s) are separate programs connected together, and the price of each separate program is identified on the invoice/contract, the price of each individual program must be used when calculating the price of the pre-written program.

## Example (see invoices below):

- Mar 2/05** Sale of pre-written modules and interface program.
- Apr 13/05** The customer purchases another module and requests modifications to Module A.
- Sept 8/05** The customer requires modifications to Module A and Module C. The modifications provided to Module A are exempt because:
- the price of the cumulative modifications performed on Module A (\$1,000 + \$4,500 = **\$5,500**) exceeds the price paid for the pre-written program (**\$5,000**), and
  - they were performed solely to meet the customer's specific requirements and the resulting program is for the customer's exclusive use, and
  - the customer has provided a PEC to the service provider.

GREEN computers	
Date: March 2, 2005	
Customer Name: ABC Company	
Sales Description	Price
Module A	\$ 5,000 (RST)
Module B	5,000 (RST)
Interface Program	2,000 (RST)
Subtotal	\$ 12,000
RST	960

GREEN computers	
Date: April 13, 2005	
Customer Name: ABC Company	
Sales Description	Price
Module C	\$ 5,000 (RST)
Modification to Module A	1,000 (RST)
Subtotal	\$ 6,000
RST	480

GREEN computers	
Date: September 8, 2005	
Customer Name: ABC Company	
Sales Description	Price
Modification to Module A	\$ 4,500 (no RST)
Modification to Module C	300 (RST)
Subtotal	\$ 4,800
RST	24

### Documentation Required

To claim an exemption from RST, on the purchase of modifications or other taxable services, purchasers must provide a valid PEC to the service provider at the time of sale.

Purchasers must maintain documentation to support the price of the original pre-written program and the price of the modifications. The RST paid for the computer program and the modifications made prior to attaining the custom status is **not** refundable.

### In-House Modifications

The cumulative modification rule also applies to modifications carried out in-house. The cost of staff salaries (not including benefits) relating directly to modifying the program's source code, and any third party modifications, may be used to calculate the cumulative cost of modifications. Purchasers must maintain documentation to support the:

- price of the original pre-written program
- price of any third party modifications
- cost of staff salaries to modify the source code
- sequence of modifications performed.

### Service Providers

Service providers must pay RST on all taxable goods and services purchased in order to provide their services.

## Non-Taxable Services

Services that do not meet the definition of 'taxable services' are not subject to RST, regardless of the tax status of the computer program on which they are being performed.

The amount charged for non-taxable services must be reasonable in relation to the total value of the goods and/or services being provided.

### Examples of Non-Taxable Services

Examples of non-taxable services:

- training with respect to the use of a computer program
- advising users of a computer program (e.g., verbal assistance or support)
- disaster recovery planning (refer to the following section entitled 'Disaster Planning and Recovery Services' for more details)
- system monitoring (refer to the following section entitled 'System Monitoring for more details)
- data entry
- data management, such as making, reorganizing and removing directories, creating and maintaining computer files, data migration and conversion, data back-up and storage
- project planning, including analysing specifications, determining and verifying hardware and software prerequisites, scheduling, preparing reports, reviewing documentation (refer to the following section entitled 'Project Planning' for more details)
- testing a computer program when performed with taxable services, provided the value of the taxable services does not exceed 10 per cent of the value of the testing. If the value of the taxable services exceeds 10 per cent of the value of the testing, then the charge for both services is taxable (refer to the following section entitled 'Testing Services' for more details).

### Conditions

Each of the above-listed services are non-taxable when it is:

- the only service provided, or
- provided with only non-taxable services, or
- not required in order to supply a taxable service.

If a non-taxable service must be performed in order to supply a taxable service, it forms an integral part of the supply of the taxable service and is subject to RST whether it is separated on the invoice/contract or not. In this case, it is no longer the supply of a non-taxable service, but the component of a taxable service (refer to page 14 for 'Determining Fair Value').

Training is non-taxable whether or not it is provided with the sale of taxable goods and/or services as long as the charge is separated from any taxable charges, **or** it is bundled for one price and the de minimis rules apply making the total sale non-taxable (refer to page 12 for 'De Minimis Rules').

### Support Agreements

RST does not apply to support agreements for non-taxable services such as telephone/e-mail or online support. In cases where the support agreement includes a combination of taxable (e.g., upgrades, etc.) and non-taxable services, RST applies as follows:

- If the taxable charges are identified separately from the non-taxable charges, RST applies to the taxable charges.
- If there is one single charge for all the services without a breakdown, RST applies to the total amount unless the sale is non-taxable based on the de minimis rules (refer to page 12 for 'De Minimis Rules').

### Support Agreements (continued)

If a support agreement which consists solely of non-taxable services is sold with a maintenance agreement for one single price, RST applies to the single price unless it is non-taxable as a result of the de minimis rules (refer to page 12 for 'De Minimis Rules'). If the charge for the maintenance agreement is separated from the charge for the support agreement, RST applies only to the maintenance portion.

### Disaster Planning and Recovery Services

Planning services that do not include the provision of a taxable service and/or taxable sale (e.g., licence for a computer program, etc) are non-taxable. When the planning service results in the provision of a written report no RST applies, provided only one copy of the report is issued. If more than one copy of the report is issued, RST applies to the total sale.

RST applies to taxable services and/or taxable sales (i.e., the right to use a computer program, rental of hardware, etc.) that are provided as part of a planning service and/or during the disaster recovery process. De minimis rules apply only to computer programs and related services that are bundled for one price; therefore, unrelated charges (e.g., rental of hardware, hardware related services, etc.) must be separated before the de minimis rules are applied (refer to page 12 for 'De Minimis Rules' ).

Whether RST applies to a particular service or sale will depend on the contractual agreement and the method in which the vendor will provide the service.

#### Example:

A disaster recovery plan has been put into place for a client. The sale includes an initial one time fee to set up the plan, plus a monthly fee to guarantee the availability of all required programs and hardware if/when the need arises. The plan also outlines the conditions (i.e., the programs and hardware will be shipped within 24 hours) and the charges that will apply (i.e., delivery and daily rental for the use of the programs and hardware) if a disaster occurs. The initial set up fee and the monthly fee guarantee are non-taxable, provided they are separated from any taxable services on the invoice/contract or the de minimis rules apply. Any charges for delivery and the use of programs and hardware are taxable.

### System Monitoring

RST applies to the sale (i.e., licence agreement, right to use arrangement, etc.) of a taxable computer program that monitors systems, applications, servers, etc.

RST does not apply to a contract for the provision of a monitoring service where a vendor actively monitors a system, server, application, etc., provided there is no charge for the use of a computer program and/or the provision of any taxable service. Any charges for the use of a computer program and/or taxable service are subject to RST, unless these charges are bundled for one price with non-taxable services and the de minimis rules apply (refer to page 12 for 'De Minimis Rules'). If the sale is bundled for one price, RST would apply to the bundled charge unless the de minimis rules apply making the total sale non-taxable (refer to page 12 for 'De Minimis Rules').

### Project Planning

Project planning services that are provided at the initial stage of a project, where significant information is gathered and the scope of a project, work parameters and deliverables are determined, are non-taxable as long as the services are either separated on the invoice/contract from any taxable charges, or are bundled for one price with taxable charges and the total charge is non-taxable as a result of the de minimis rules.

Any services performed during the development of a taxable computer program form part of the fair value of the program and are taxable, whether or not the services are separated on the invoice/contract.

## Testing Services

Testing is a non-taxable service if:

- it is the only service being provided, or
- it is provided with only non-taxable services, or
- the value of the taxable services being provided does not exceed 10 per cent of the value of the testing service (de minimis rules for testing).

Testing is taxable if it is provided with taxable services and the value of the taxable services exceeds 10 per cent of the value of the testing.

The de minimis rule for testing should only be applied where the testing is performed with related taxable service(s) and it does not form part of the fair value of a taxable service (refer to page 14 for 'Determining Fair Value').

For testing, value is determined by:

- vendor's cost, or
- fair value (i.e., selling price), or
- time spent by the vendor to provide the taxable services and testing, or
- value as determined by any other reasonable method.

### Example A:

Testing that is performed after an installation of a taxable program to confirm that the program is working properly forms part of the fair value of the installation service and is taxable whether or not it is separated on the invoice.

### Example B:

A third party is contracted to test a newly developed operating system (O/S). The O/S is put through a series of tests. Some modifications are required and performed by the third party. The charges for testing and modifications are separated on the third party's invoice to the developer. The charge for testing would be non-taxable, provided the value for modifications does not exceed 10 per cent of the value for testing.

## De Minimis Rules

Effective July 19, 2002, RST does not apply to taxable and non-taxable computer related services sold together for a **single price** (i.e., a bundled charge without a breakdown on the invoice) **if** the taxable charges are **equal to or less than 10 per cent** of the non-taxable charges. This same rule applies to computer programs sold together for a single price with taxable or non-taxable computer related services.

RST is not payable on the bundled price provided one of the following criteria is met:

- the cost to the vendor of the taxable portion of the package is a maximum of 10 per cent of the vendor's **cost\*** to provide the non-taxable portion, or
- the **fair value\*\*** of the taxable portion sold to the purchaser is a maximum of 10 per cent of the fair value of the non-taxable portion, if each were sold separately, or
- in the case of a vendor charging for time spent (e.g., hourly or daily rate) for services rendered, the time spent to provide the taxable portion to the purchaser is a maximum of 10 per cent of the time spent to provide the non-taxable portion, or
- any other reasonable determination that proves the taxable portion is a maximum of 10 per cent of the non-taxable portion.

- \* **Cost** is determined using generally accepted accounting principles (GAAP).
- \*\* **Fair value** is defined as the price paid by the purchaser.

The non-taxable portion must be reasonable in relation to the total value of the goods and/or services being provided.

**Note:** Vendors who use the de minimis rules should treat each sale separately when determining whether RST applies.

Vendors who choose not to use the de minimis rules, and charge separately for their services and/or programs, must apply RST to the taxable portion of the invoice, even though it may not exceed 10 per cent of the non-taxable portion.

### Testing Services and De Minimis Rules

If testing services are provided as part of a bundled sale, vendors must:

- 1) determine whether the testing charge is taxable or non-taxable (refer to 'Testing Services' on page 11), **then**
- 2) determine whether the de minimis rules apply to the bundled sale (using the taxable or non-taxable charge for testing determined in 1 above).

### Taxable Bundled Sales

If the taxable charges are more than 10 per cent of the non-taxable charges, then the amounts must be separated on the invoice/contract and RST applied to the taxable portion. If the taxable and non-taxable portions are not separated, RST applies to the total sale.

### Excluded Sales

Charges that do not relate to computer programs (e.g., hardware, hardware related services, telecommunication services, etc.) must be separated before applying the de minimis rules.

### Documentation

Vendors must maintain documentation to support the non-collection of RST and to prove that the criteria has been met for using the de minimis rules. Examples include payroll records, time sheets and/or contracts.

The following examples show how RST applies in various situations using the de minimis rules:

#### Example 1 - Vendor's Cost

Sales Invoice:	Vendor's Cost:		Calculation:
\$15,000 (single price for multiple services)	Taxable Services	\$ 900	900/10,000 = <b>9 per cent</b>
	Non-Taxable Services	\$10,000	

RST does not apply to the price charged to the customer, since the vendor's cost of the taxable services is less than 10 per cent of the vendor's cost of the non-taxable services. In this case, the vendor does not need to provide a breakdown of the charges on the invoice/contract.

#### Example 2 - Fair Value

Sales Invoice:	Fair Value:		Calculation:
\$12,000 (single price for multiple services)	Taxable Services	\$ 2,000	2,000/10,000 = <b>20 per cent</b>
	Non-Taxable Services	\$10,000	

If the vendor does not provide a breakdown between the taxable and non-taxable charges on the invoice/contract, RST applies to the total price charged (\$12,000) since the fair value of the taxable services exceeds 10 per cent of the fair value of the non-taxable services.

**Example 3 -  
Time Spent**

Sales Invoice:	Time Spent:	Calculation:
\$400 (single price for multiple services)	Taxable Services 1 hour	1/11 =
	Non-Taxable Services 11 hours	<b>9 per cent</b>

RST does not apply to the price charged, since the time spent to provide the taxable services is less than 10 per cent of the time spent to provide the non-taxable services. In this case, the vendor does not need to provide a breakdown of the charges on the invoice/contract.

**Example 4  
- Services  
Sold with  
a Taxable  
Computer  
Program**

Sales Invoice:	Fair Value:	Calculation:
\$8,550 (single price for multiple services and program)	Computer Program \$ 300	550/8,000 =
	Taxable Services \$ 250	<b>7 per cent</b>
	Non-Taxable Services \$8,000	

RST does not apply to the price charged, since the fair value (price) for the taxable services and program is less than 10 per cent of the fair value of the non-taxable services. In this case, the vendor does not need to provide a breakdown of the charges on the invoice/contract.

## Determining Fair Value

Retail Sales Tax (RST) applies to the fair value of the sale of a taxable good and/or taxable service.

An invoice/contract can include the single supply of a good or service, or the multiple supply of goods and/or services. To determine whether the sale is a single supply or a multiple supply, the vendor must identify whether they are performing several activities to supply one good or service (single supply), or whether they are supplying multiple services and/or goods that are independent of one another (multiple supply).

For RST purposes, the fair value of a single supply of a good or service is the total amount charged for all the activities that form an integral part of that good or service. This principle applies whether or not the various activities are listed separately on the invoice, and regardless of whether or not RST applies to the various activities. Therefore, if a non-taxable service is performed in order to supply a taxable good or service, then it is an integral activity and forms part of the fair value of the taxable service. RST applies whether or not this activity is identified separately on the invoice/contract.

**Example A:**

A computer is not functioning properly and a vendor is hired to fix the problem. The vendor suspects a virus. He sells and installs an anti-virus program (taxable sale and taxable service). A virus scan locates a virus, which is removed (taxable service). The vendor reinstalls a program (taxable service) that was affected by the virus. Two taxable services (i.e., the removal of a virus, and reinstallation of a program) were required in order to fix the problem. Since the virus scan was required in order to fix the problem, and the fix is a taxable service, the virus scan forms part of the fair value of the taxable service. Therefore, RST applies to the total invoice, regardless of whether the vendor provides a breakdown of each component.

**Example B:**

During the development of a computer program, many services (writing source code, debugging, testing, etc.) are performed. The fair value (selling price) of the program includes all the charges for services performed, regardless of whether they are broken out on the invoice/contract. This is considered one sale of a computer program, not multiple sales of various services.

**Example C:**

A company has purchased and installed a new database program. The company contracts with a service provider to perform data conversion. The service provider temporarily installs a data conversion program, which he/she will use to perform the service. This data conversion service is non-taxable. The fair value of this non-taxable service includes the time spent installing the data conversion program and performing the data conversion. (This is also a good example of where a service provider would be required to pay RST on the licence of the data conversion program they are using to provide their non-taxable service.)

## Placement Agencies & IT Consultants

### Agencies Placing Temporary IT Consultants

The principal business of a placement agency is the supply of human resources to clients in need of temporary or permanent manpower assistance. Placement services refer to locating, obtaining, or arranging temporary or permanent assistance on behalf of clients. This includes the recruitment and placement of IT professionals as either employees or temporary contractors.

### Non-Taxable IT Placement Services

Where a placement agency provides an IT consultant, the service provided by the placement agency is non-taxable if the contract or arrangement between the placement agency and its client is for the supply of human resources and not for the provision of a taxable service. In this situation, the IT consultant is usually not under the direction and control of the placement agency.

Where the IT consultant is fulfilling the placement agency's contractual obligation to its client to find temporary manpower assistance, the IT consultant is not required to charge RST to either the placement agency or the client.

### Taxable IT Placement Services

RST applies to a contract or arrangement between the placement agency and its client if the contract or arrangement provides for taxable IT services. In this type of contract or arrangement, the agency is assuming responsibility for the project deliverables or the services being provided, and may control or direct the work of the IT consultant. A placement agency that provides taxable services is a vendor for RST purposes and is required to charge, collect and remit RST.

## Manufacturers of Computer Programs

Computer program developers can qualify as manufacturers provided certain conditions are met. Qualifying manufacturers may purchase processing materials and manufacturing equipment (e.g., computers, computer programs, electronic storage, etc) used primarily (i.e., more than 50 per cent) and directly in the development of **taxable** computer programs exempt from RST.

To qualify as a manufacturer, developers must produce computer programs:

- for sale to others, and sales of such programs must exceed \$5,000 in a fiscal year, **or**
- for their own use, and their cost to produce such programs must exceed \$50,000 in a fiscal year.

For more information about manufacturing, please refer to **RST Guide 400 - Manufacturers**.

**Custom Computer Program Developers**

Any equipment (e.g., computers and computer programs, etc.) and processing materials used to develop custom computer programs do not qualify for the exemption, **unless** the same equipment is used primarily (more than 50 per cent) and directly in the development of **taxable** computer programs.

**Goods for Resale**

Computer programs purchased for the purpose of resale (e.g., computer programs that will become 'part of' another program, etc.) can be purchased exempt from RST. This exemption is not limited to manufacturers.

**Research and Development (R&D)**

A **manufacturer** may purchase equipment and processing materials exempt from RST provided they will be used:

- **exclusively** (90 per cent or more) in the research and development of taxable computer programs,
- exclusively for research into, or the development of, manufacturing or production processes for use by any person,
- directly in and exclusively for a combination of manufacturing and R&D activities. 'Research' means the original or further investigation by a manufacturer to gain new knowledge or new ideas for the development of new or improved products or processes for own use or for the use of others. 'Development' is the creation of new or improved products or processes by a manufacturer.

Independent R&D companies cannot claim the exemption from Retail Sales Tax (RST) on the purchase of equipment unless they qualify as a manufacturer for RST purposes.

A valid PEC must be provided to the supplier at the time of sale to claim an exemption from RST on the purchase of manufacturing equipment and processing materials.

## Other Related Information

**Taxable Goods and Services Purchased for Resale**

Vendors may purchase taxable computer programs and taxable services exempt from RST if they are purchased for resale purposes. A valid PEC must be issued to the supplier at the time of sale to claim an exemption from RST.

**Example A:**

A program developer has contracted with a customer for the development of a program including installation. The program developer contracts with a third party to perform installation services. The installation charges invoiced by the third party to the developer, are being resold to the customer as part of the developer's contract. Since the developer is reselling the service, the developer may purchase the installation services exempt from the third party.

**Example B:**

A vendor contracts with a third party to develop a small program that will be incorporated into a larger program that is being developed for a customer. Since the program is being purchased for resale purposes and will form part of the program that is for resale, the vendor may purchase it from the third party exempt from RST.

## Legislative References

*Retail Sales Tax Act* (Act), subsection 1(1), 1(3) and subsection 7(1)62  
Regulation 1012 under the Act, section 1.1, 1.2 and 1.3, and section 14.2

## For More Information

The information contained in this publication is only a guideline. Due to the complex nature of this topic, it is not possible to address every situation in this *Guide*. To obtain an official interpretation on a specific situation, write to: Ontario Ministry of Revenue, Tax Advisory Services Branch, Retail Sales Tax, 33 King Street West, Oshawa, Ontario, L1H 8H5.

For more information, please contact the Ontario Ministry of Revenue at 1 866 ONT-TAXS (1 866 668-8297) or visit our website at [ontario.ca/revenue](http://ontario.ca/revenue)

.

*Ce guide est disponible en français sous le nom « Programmes informatiques et services connexes n° 650F ».  
Vous pouvez obtenir un exemplaire en appelant le 1 866 ONT-TAXS (1 866 668-8297).*