Sales and Use Tax Topics: Computer Software

COLORADO
Department of Revenue
Taxation Division

As a result of *House Bill 26-1223*, the statutory provisions governing the taxation of computer software are changing effective January 1, 2027. This publication provides guidance regarding the tax treatment of computer software both before and after this change.

This publication is designed to supplement the guidance provided in the *Colorado Sales Tax Guide*. Nothing in this publication modifies or is intended to modify Colorado's statutes and regulations authorizing these exemptions. Taxpayers are encouraged to consult their tax advisors for guidance regarding specific situations.

The information in this publication applies to state and local sales taxes administered by the Department. The information in this publication does not apply to the sales taxes of any home rule cities that the Department does not administer. Please contact any applicable home-rule city directly for information about their sales and use taxes. Contact information for home-rule cities can be found in Department publication *Colorado Sale/Use Tax Rates (DR 1002)*.

Taxation of software after 2026

Effective January 1, 2027, computer software is generally subject to Colorado and state administered sales and use taxes. Computer software is exempt from sales and use taxes only if it is either governed by a negotiable license agreement or developed for use by a particular user. The taxability of computer software is determined the same regardless of the means of delivery, whether it is delivered by compact disc, download, remote access through the internet, or by any other means.

"Computer software" defined

Computer software is a set of coded instructions that are both designed to cause a computer or other electronic device to perform a task. Taxable computer software may be delivered by any means, including compact disc, download, or remote access through the internet. Applications installed on cellular phones, tablets, or other mobile devices are computer software for Colorado sales and use tax purposes.

Negotiated license agreements

For the purpose of determining the taxability of computer software on and after January 1, 2027, a negotiated license agreement is a written agreement or contract that is individually bargained between the licensor and licensee and that is signed in writing by authorized representatives of both the licensor and licensee prior to or contemporaneous with the licensee's access to or use of the software.

An agreement is not considered to be "signed in writing by authorized representatives of both the licensor and licensee" in the case of any acceptance by the licensee on a click-through, browse-wrap, shrink-wrap, embedded signature, implied, account creation, or any other automated basis.

However, an agreement may be considered to be "signed in writing by authorized representatives of both the licensor and licensee" in the case of a signature performed through an electronic signature method authorized pursuant to section 39-21-120, C.R.S., and Department rules and, in particular, in the case of any electronic signature methods such as Docusign or a similar authenticated electronic signature.

Individually bargained

For the purpose of determining the taxability of computer software on and after January 1, 2027, an agreement is not considered to be "individually bargained between the licensor and licensee" if it is a standard, form, or boilerplate agreement that is offered by the licensor on a nonnegotiable or substantially nonnegotiable basis to multiple licensees. Such agreements are commonly:

- printed on, within, or affixed to the software packaging;
- embedded within the computer software itself; or
- presented as part of the terms and conditions of any website or application through which the software is acquired, accessed, or used.

Furthermore, any standard, form, or boilerplate agreement that is offered by the licensor on a nonnegotiable or substantially nonnegotiable basis to multiple licensees is not considered to be "individually bargained between the licensor and licensee" even if the agreement bears a handwritten or electronic signature.

Rulemaking

The Department has begun the process to develop new rules with respect to legislative changes made to computer software enacted in *House Bill 26-1223*. Announcements regarding this rulemaking process can be found on *the Department's website*. Workgroup recordings, documents, and other relevant materials and information can be found in the *public drive maintained for the rulemaking process*.

Interested parties can sign up to receive rulemaking announcements.

Taxation of software prior to 2027

Prior to January 1, 2027, Colorado sales tax applies to a sale of computer software only if all three of the following conditions are met: (1) it is prepackaged for repeated sale or license; (2) its use is governed by a tear-open nonnegotiable license agreement; and (3) it is delivered in a physical medium such as a tape, disk, compact disc, or card.

Computer software is not subject to sales tax if it is delivered to the purchaser through any of the following methods: it is provided to the customer through an application service provider; it is delivered to the customer by electronic computer software delivery; or it is transferred to the customer by load and leave computer software delivery.

The criteria for the taxation and exemption of computer software sales prior to January 1, 2027, are discussed in the tables presented later in this publication.

"Computer software" defined

For Colorado sales tax purposes prior to January 1, 2027, the term "computer software" refers to a set of coded instructions designed to cause a computer or automatic data processing equipment to perform a task. Computer software does not include the internalized instruction code that:

- controls the basic operations of the computer, such as arithmetic and logic;
- causes the computer to execute instructions contained in system programs;
- is an integral part of the computer; and
- is not normally accessible or modifiable by the user.

Such internalized instruction code is considered part of the hardware and considered tangible personal property that is taxable as such.

Necessary Conditions for Sales Tax on Software Prior to 2027

Condition	*Description*
The computer software is ***prepackaged for repeated sale or license***.	The computer software is prepackaged for repeated sale or license in the same form to multiple users without modification, and is typically sold in a shrink-wrapped box.
The use of the computer software is governed by a ***tear-open nonnegotiable license agreement***.	"Tear-open nonnegotiable license agreement" means a license agreement contained on or in the package, which by its terms becomes effective upon opening of the package and accepting the licensing agreement. "Tear-open nonnegotiable license agreement" does not include a written license agreement or contract signed by the licensor and the licensee.
The computer software is delivered to the customer in a ***tangible medium***.	"Tangible medium" means a tape, disk, compact disc, card, or comparable physical medium. Computer software is not delivered to the customer in a tangible medium if it is provided through an application service provider, delivered by electronic computer software delivery, or transferred by load and leave computer software delivery.

Purchase of multiple licenses

For sales made prior to January 1, 2027, if a buyer located in Colorado purchases multiple taxable computer software licenses with the intention of distributing and using some portion of those licenses at the buyer's locations outside of Colorado, Colorado sales tax is due on that part of the license fees associated only with the licenses that are actually used in Colorado. The Colorado purchaser must provide a written statement to the retailer, attesting to the amount of the license fees associated with Colorado and with locations outside of Colorado. The written statement relieves the retailer of any liability for the licenses not used in Colorado.

Maintenance agreements

In general, any charge for a mandatory maintenance agreement included in the sale of taxable computer software is also taxable. See Part 3 of the *Colorado Sales Tax Guide*, for additional information regarding the taxability of maintenance agreements.

Nontaxable computer software sales

Prior to January 1, 2027, computer software is not subject to Colorado sales tax if it is provided, delivered, or transferred to the customer by way of any of the nontaxable software delivery methods described in the table below.

Nontaxable Software Delivery Methods Prior to 2027

Method	*Description*
Provided through an application service provider	"Application service provider" or "ASP" means an entity that retains custody over or hosts computer software for use by third parties. Users of the computer software hosted by an ASP typically will access the computer software via the internet. The ASP may or may not own or license the computer software, but generally will own and maintain hardware and networking equipment required for the user to access the computer software. Where the ASP owns the computer software, the ASP may charge the user a license fee for the computer software or a fee for maintaining the computer software or hardware used by its customer.
Delivered by electronic computer software delivery	"Electronic computer software delivery" means computer software transferred by remote telecommunications to the purchaser's computer, where the purchaser does not obtain possession of any tangible medium in the transaction.
Transferred by load and leave computer software delivery	"Load and leave computer software delivery" means delivery of computer software to the purchaser by use of tape, disk, compact disc, card, or comparable physical medium where the title to or possession of the tape, disk, compact disc, card, or comparable physical medium is not transferred to the purchaser, and where the computer software is manually loaded by the vendor, or the vendor's representative, at the purchaser's location.

Additional resources

The following is a list of statutes, regulations, forms, and guidance pertaining to sales tax on computer software. This list is not, and is not intended to be, an exhaustive list of authorities that govern the tax treatment of every situation. Individuals and businesses with specific questions should consult their tax advisors.

Statutes and regulations

- § 39-26-102, C.R.S. Definitions.
- § 39-26-105, C.R.S. Vendor liable for tax.
- § 39-26-713, C.R.S. Tangible personal property.
- *House Bill 26-1223*

Forms and guidance

- *Tax.Colorado.gov*
- *Colorado Sales Tax Guide*