What are digital goods?

- People generally mean variations on:
  - e-books
  - digital audio
  - digital video

Sourcing Entertainment in a Digital World
Types of Digital Goods

- E-books
  - Purchased/downloaded
  - Has no physical counterpart
  - Temporarily accessible by customer

- Purchased/downloaded audio
  - Can be streamed by customer

- Purchased/downloaded video
  - Can be streamed by customer

- Mobile Apps and Games
  - Permanently possessed by customer

- Audio streamed by subscription
- Video on demand/pay-per-view
- Limited-time rentals

- Online services (chat, dating)
- Gaming

Sales and Use Taxation

- How are they sourced?
- Depends on how you define them
- State approaches to definition
  - Undefined
  - Defined explicitly or implicitly via reference to an equivalent (tangible personal property, services)
  - SSUTA: Specific digital products taxed as a new category of taxable good

Normand v. Cox Commc’ns Louisiana, LLC

- La. Rev. Stat. Ann. 47:301(16)(a) “Tangible personal property” means and includes personal property which may be seen, weighed, measured, felt or touched, or is in any other manner perceptible to the senses.
- 61 La. Admin. Code Pt 1, 4301: Examples of tangible personal property include but are not limited to:
  - iv. digital or electronic products such as “canned” computer software, electronic files, and “on demand” audio and video downloads.
Normand v. Cox Commc'ns Louisiana, LLC

- LA Revenue Information Bulletin No.10-015: pay-per-view and video-on-demand movies were tangible personal property subject to Louisiana sales and use tax
  - perceptible to the senses
  - customers do not take title to the programs, but have control over paying fees to watch the programs.
- Followed by issuance of RIB No. 11-009, which repealed No. 10-015

Normand v. Cox Commc'ns Louisiana, LLC

- Video-on-demand and pay-per-view programming not subject to Jefferson Parish sales tax
  - Was not taxable lease/rental of tangible personal property
  - Was service

Chicago’s Amusement Tax

- Effective July 1, 9% tax on all cloud-based streaming services
  - Does not affect the sales of movies, songs and games delivered electronically
  - Companies have till Sept. 1 to comply
- Netflix will be raising subscription rate for any accounts with a billing address in Chicago
Varying state definitions of digital goods: undefined

- Arizona: digital goods undefined, but state broadly defines tangible personal property
- Alabama: digital goods undefined (but does specifically identify digital photographs as tangible property and thus taxable)(Ala. Admin. Code 810-6-1-119)
- Florida: no definition of digital goods

Varying state definitions of digital goods: undefined

- Undefined ≠ untaxable, but may be harder to source
- Arizona: Digital goods considered included in definition of tangible personal property and taxable as TPP.
- Florida: Technical Assistance Advisement 11A-002, 1/31/2011 (finding digital transfer of video production and editing) that digital goods are not subject to tax. Same item transferred in tangible form would have been taxable.

Varying state definitions of digital goods: defined via reference to TPP

- Texas Tax Code §151.010 "taxable item" includes tangible personal property and taxable services.
  - Sale or use of a taxable item in electronic form instead of on physical media does not alter the item's tax status
  - Do digital photographs constitute tangible personal property?
    - the internet and e-mail involve the transmission of electrical impulses, i.e., electricity, which, as indicated, constitutes tangible personal property. Consequently, the electronic transfer of digital photographic images from a seller to a purchaser for a price constitutes the sale of tangible personal property
  - Was taxpayer providing a nontaxable service, with the transfer of the tangible photographs only incidental?
    - No; "the retail sale of photographs is taxable, whether delivered in final printed form or in digital form over the internet or by e-mail"
Taxed as tangible personal property

- Syndicated programming purchased by broadcaster was delivered by satellite transmission from the distributor’s transmitter to May’s receiver, then stored on videotape
  - programming was taxable as “tangible personal property:” “A transmission by satellite is the transmission of a tangible thing—an electronic signal.”

Varying state definitions of digital goods: defined via reference to an intangible

- Texas Comptroller of Public Accounts, Letter No. 201207532L (7/31/12):
  - subscription fees for video streaming subject to sales tax as a sale of cable television services
  - subscription fee for "borrowing" electronic books subject to sales tax as a sale of information services.
  - Sourced accordingly

Varying state definitions of digital goods: defined under SSUTA

- “Specified digital products” means electronically transferred:
  - Digital Audio-Visual Works
  - Digital Audio Works
  - Digital Books
- All other digital goods are categorized as “products transferred electronically”
- Member states must adopt these definitions
Varying state definitions of digital goods: defined under SSUTA

- In addition, SSUTA provisions discuss the sale of a "digital code."
- If member states want to tax digital products that fall outside these terms, they must specifically tax them by statute.
  - May extend sales and use tax to digital products sold regardless of whether the purchaser has a right to permanent use.

Varying state definitions of digital goods: defined under SSUTA

- Under SSUTA, unless state statute specifically states otherwise, a tax on digital products is construed as being imposed on a sale
  - (i) to a purchaser that is an "end user;"
  - (ii) when the seller grants the right of "permanent use;" and
  - (iii) that is not conditioned upon continued payment to the seller by the purchaser

Sourcing under SSUTA

- Seller’s place of business if received there
- Location where purchaser receives the item
- Purchaser’s address from seller’s business records
- Purchaser’s address from time of sale (from pay instrument)
- Origin sourcing address where item first made available for transmission by seller
SSUTA State Variations

- A number of states impose broader definition/taxation of digital products
- Examples:
  - Wisconsin: SSUTA-defined digital products, plus electronic greeting cards, artwork, periodicals, video games (unless tax exempt in tangible form)
  - Kentucky: same as above, but exempts audio-visual products
  - Vermont: SSUTA-defined digital products, plus ringtones

Source: CCH Intelliconnect

SSUTA State Variations

- Taxable if right to use a digital good is not permanent:

<table>
<thead>
<tr>
<th></th>
<th>YES</th>
<th>NO</th>
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<tbody>
<tr>
<td>KY, MN, NJ, NC, OH, SD, UT, VT, WA, WI</td>
<td>AR, GA, IN, IA, KS, MI, NV, ND, OK, IL, WV, WY</td>
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</tbody>
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- Taxable if right to use digital good is conditioned on continual payment:

<table>
<thead>
<tr>
<th></th>
<th>YES</th>
<th>NO</th>
</tr>
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<tbody>
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</tr>
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</table>

Source: CCH Intelliconnect

SSUTA State Variations

- Taxable if sold to user other than end user:

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</tbody>
</table>

- Exemptions:
  - MN: digital textbooks when used in a course of study
  - WA: entity-based exemption for audio and television broadcasters

Source: CCH Intelliconnect
Inconsistency has attracted federal attention

- Digital Goods & Services Tax Fairness Act
  - S. 851 (114th Congress)
    - Intent is to prevent state and local governments from imposing "multiple and discriminatory" taxes on digital goods and services.
    - Excludes certain services from the definition of "digital service"

Sourcing under Digital Goods & Services Tax Fairness Act

- Location good was first available for transmission by seller, such business location
- Primary use location of digital good or service
  - Primary use location = street address representative of where the actual end user's use will primarily occur
- Location good is received by customer or customer's donee, if known to seller and maintained in the ordinary course of business
- Customer's address as maintained in the ordinary course of business
- Customer's address obtained during sale (payment instrument)
- Location good was first available for transmission by seller

Sales Factor Sourcing

- Section 17 — modeled on MA sourcing rules
- Shift to market sourcing — hierarchy of rules for services and intangibles