MULTISTATE TAX COMMISSION

NOTES of MEETING - DRAFT
MTC Work Group – Sales Taxation of Digital Products
January 5, 2023

I. Welcome and Introductions –

Gil Brewer, Washington, Chair of the Work Group, convened the meeting.

II. Initial Public Comment –

Brewer asked if there were any initial comments on the project or the agenda for the call.

Karl Frieden (public participant) commented on the proposed definition of digital product saying it is very broad. He stated that it is a sweeping definition without clear meaning behind its development. Such a broad definition could be misconstrued by states later using the white paper. He noted that the other broad definitions cited in the outline are not for tax purposes. He stated that there is precedent in other countries for a broad definition, under a value added tax (VAT). A VAT starts with a broad definition and then adds carveouts. He then distinguished a VAT from a sales tax by describing the VAT's structural mechanism for avoiding taxation of business inputs. He also mentioned that many nations with a VAT have a history of carving out business inputs at the national level under taxes other than a VAT. He noted the states' approaches to sales tax are different than this.

Frieden continued that the development of a broad definition may still be a worthwhile exercise, but that the MTC should proceed with great caution. He stated his preference for an incremental approach that builds up definitions. He stated he disfavored the broad approach because there is no clear mechanism for anti-pyramiding. He stated that he and COST will continue to advocate for a robust mechanism for exempting business inputs and avoiding pyramiding.

III. Review of Notes from December 8, 2022 meeting –

Brewer noted that the notes are meant to capture the discussion and serve a distinct purpose from the whitepaper and current outline, which are the actual work products of the group. Brewer asked if there were any changes or additions to the notes from the previous meeting. There were none.

Nancy Prosser (MTC) mentioned that the chat for the December 8 meeting was not captured but the chat would be captured this time.

Brewer then summarized the notes from the December 8 meeting. Brewer noted that there was much discussion and comment on Ray Langenberg's proposed definition, but that there was no finality on that discussion. Brewer also noted the receipt of written comments from Charlie Kearns and Jeff Friedman.

IV. **Review of changes to the detailed white paper outline –**

Prosser summarized the changes that had been made to the detailed white paper outline as highlighted and sent with the agenda for the meeting. She also referred to the written comments received. Prosser also noted that MTC staff will be talking to additional experts and stakeholders about ways in which the various digital products may be characterized and coded in different systems for different purposes, especially tax purposes.

Steve Kranz (public participant) asked whether there had been discussion of a narrower approach. He referred to the breadth of the definition as shocking.

Brewer responded that the definition is not intended to define taxable products, but to educate the group about what is in the digital market and whether that can be defined in a way that is not subject to changing characteristics. The taxable definition will come later in the context of what is out there.

Kranz responded that the whitepaper could refer to this concept as the scope of the project rather than a definition of digital products. He stated that if you call it a definition, they will tax it.

Brewer stated he has no problem with calling it a description of the scope of digital products rather than a definition of digital products. Brewer then moved to a discussion of the definition/description of the scope.

V. **Discussion of definition for digital products and next steps –**

Ray Langenberg (TX) stated he explained his definition at the last meeting. He said the group should not limit itself to defining solely what should be taxable nor to current regimes and their past efforts. He stated the group should not wring its hands about this definition and that the philosophical issue of narrow versus broad remains open for discussion. He stated he was open to the terms scope or concept.

Mark Nebergall (public participant) stated that characterizing the proposal as a definition creates great anxiety in the business community. He believes the work group should consider changing the way the concept is described.

Olufemi Obikoya (DC) stated the two things are related—we must know the scope to define. He stated his preference is development of a broad definition from this work group which would give the states room to determine what to do.

Brad Heller (CDTFA) stated that the group must create a definition for discussion purposes so we are all referring to the same thing when we say digital product. He also stated that the group should have a broad definition but make clear it is not for the purpose of defining the tax base.

Kranz, following up on Mark Nebergall's comment, stated that he thinks the project is beginning to look like MTC's UDITPA rewrite project. He stated that project drew the attention of policy makers nationwide, the NCSL task force in particular, and raised serious concern that the MTC was telling states what their tax base should be. He stated that developing a definition is the first step on the path to legislatures using it to expand the tax base. He called this possibility a massive tax grab and noted this might cause consternation at legislatures.

Bruce Johnson (public participant) noted that he understands the concerns and would be fine with calling it the "scope." He stated he understands the political concerns. He noted, however, that unless the scope is broad, the group cannot possibly consider the tax base issue. He gave the example of the digital provision of tickets to a sports event. He stated that if the group begins by excluding that from the scope, then the conclusion will be that the white paper does not address it and this project is irrelevant to whether that item is taxed. The proper approach is to address everything whether it is referred to as scope or as a definition.

Nebergall encouraged an alternative to spending more time determining how to say something is a digital product. He proposed instead to say that "you know it when you see it." He believes that then the group can focus on what is not a digital product. He wondered whether the time spent so far has been productive.

Brewer says he thinks it has been productive. Brewer described the definition as a guidepost. He stated the group should not have to sweat over every word of this definition. He prompted others to provide alternatives for what to call it.

Kranz commented that the project's scope is to help states identify what their tax base should be. He stated that the group should not include everything and then force states to make the effort to narrow that down. He proposed starting at the bottom and building up. He recommended creating a library of specific definitions that states can tax if they choose. He stated that such an approach would improve uniformity.

Brewer noted that the group is surveying the universe of specific digital products. He noted that the group may be considering which approach is better soon and this survey information may help that. Brewer stated his concern that huge amounts of the economy are going to digital and that states might watch the tax base shrink like it did as services grew. He noted that the United States is different than Europe and states have to build on what they have. Brewer then asked if there is any other recommendation for better terminology for the broad idea of digital products.

Josh Pens (CO) asked whether there should be an interim step. He stated he liked the broad start, but that the proposed definition is going to be too big an elephant to eat all at once. He stated that at some point the group must break things down into categories or classes of products.

Brewer noted that the upcoming discussions with industry representatives might help reveal the outlines of those categories.

Kranz stated the MTC can help its member states by starting small and building up. He noted that proposing the broad approach might do political damage to the organization. He warned against even implying that the broad approach is the correct approach.

Heller stated the MTC has not endorsed any approach, but only discussed issues. He stated that Steve's comments are important, but that no recommendations have been made.

Nebergall responded that you can eat an elephant but you must do it a bite at a time, and that this favors the narrow approach.

Brewer began to conclude the meeting. He stated that a term for the "definition" should be developed. He stated the group is ready to start talking about the format of what

recommendations it should be considering—broad then carve out, or narrow then build up. He stated the whitepaper can discuss the pros and cons of each approach and what is in between. He encouraged the state members to think about what they need from the discussions and from the white paper.

Frieden (COST) noted the discussion has been helpful. He stated it is not just a matter of nomenclature but of approach. He questioned whether the MTC will analyze different approaches or lean in one direction. He suggested the MTC avoid recommending anything that will be perceived as a broad approach and stake out ground on business inputs.

Brewer concluded the meeting by stating that he and MTC staff would discuss everything and determine how to structure the next meeting. He encouraged people to share additional ideas and comments.

VI.   Adjourn