

## Digital Goods and Services: How States Define, Tax, and Exempt These Items

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In this article, the authors describe a variety of approaches across the United States for taxation of digital goods and services (for purposes of sales and use taxes or transaction privilege tax only).

The information and findings in this paper do not constitute legal advice or any official guidance. The laws are rapidly changing or undergoing revisions and clarifications by courts and regulatory agencies. All legal conclusions must be verified with references to all appropriate and updated sources of law and guidance applicable at the time of any specific transaction. Consultation with a legal or accounting professional is strongly recommended before any real-life implementation of a decision to collect or not any applicable tax in all applicable jurisdictions (to include both state and local taxes). This paper is intended to start a discussion, not deliver ready solutions.

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How do the states define, tax, and exempt from taxation digital goods and services? Each and every way. The end.

If we designed our society from scratch, would we want the variety? Do we need it? To what extent? Perhaps variety is the way to figure out one best way, but at what cost? Dr. King's quote comes to mind: "Whatever affects one directly affects all indirectly." What's the cost of complexity that the states have created for the industry? Or, in our computer age, is complexity not even an issue?

For starters, could we even agree that automated services such as software-delivered digital products — whether information, data, or intellectual property such as a movie, music, or a book — are akin to goods, when the involvement of labor is indirect? Could we agree that automated services are not the same as services in a traditional sense, those provided directly by humans to humans? What about the ones and zeros of binary code, which we use to assemble and record data in bits that are often stored in a cloud and come together to form our digital world of software, data, music, and movies? And should we pay attention to the following observation by Bill Gates:

Right now, the human worker who does, say, \$50,000 worth of work in a factory, that income is taxed, and you get income tax, social security tax, all those things. If a robot comes in to do the same thing, you'd think that we'd tax the robot at a similar level.<sup>1</sup>

<sup>1</sup> See Richard Waters, "Bill Gates Calls for Income Tax on Robots," *Financial Times*, Feb. 19, 2017.

So far, more than a handful of states seem comfortable allowing software acting as a service to not only replace jobs and eliminate a source for income taxes, but also be treated as a nontaxable service for purposes of their sales and use (or transaction privilege tax) revenue streams.

The stakes could not be more consequential for businesses, consumers and states. The tax treatment of the ever-growing suite of products in the digital marketplace becomes more consequential from a fiscal standpoint with each passing year as technology firms replace cable with streaming content, boxed software with remotely accessed offerings and self-managed data storage with rented cloud storage solutions. As an example, for the quarter ending December 31, 2019, Microsoft reported revenues for its commercial cloud unit of \$12.5 billion, accounting for nearly one-third of its revenue for the period. Microsoft's stock reached an all-time high after release of the information, a vindication of the company's multiyear effort to orient its business model toward cloud solution and software subscription business models.<sup>2</sup> During the same period, Amazon Web Services grew faster than Amazon's International and North America and business units.<sup>3</sup> Whether these new delivery methods or digital solutions are treated as taxable goods or nontaxable services will augment, sustain, or erode state tax bases.

Additionally, to tax or exclude digital products presents issues of marketplace and social fairness. Imposing sales tax on boxed software purchased from a brick-and-mortar retailer while legislatively or judicially exempting the same software sale that is remotely accessed over the internet can create a legislative or "judicially created tax shelter" the Supreme Court instituted in *Quill Corp. v. North Dakota* until it was overturned in *South Dakota v. Wayfair*. This same disparate tax treatment between the physical and digital versions of (virtually) the same product can exacerbate the regressive nature of sales taxes, as the average

household income lacking internet access is less than that of households with.<sup>4</sup>

### U.S. States' Taxation of Digital Products and Services

Analysts complain about the impossibility of laws keeping up with technology and the blurred definitions between digital products and digital services. There is a patchwork of regulatory approaches, and digital products and services are not defined with consistency or specificity across states. Taxpayers, litigants, and tax authorities need clarity on the taxability of digital products.

After spending hours reviewing state laws and articles and creating a comprehensive Excel spreadsheet with links and references to state laws and websites, the hope was to deliver an easy-to-grasp classification of state approaches to taxing digital goods and services. The wide divergence of approaches does not lend itself to an easy-to-visualize or easy-to-grasp product. The inability to provide an easy-to-follow visual representation of the situation is compounded by:

- some jurisdictions' failure to provide guidance that is easy to find and understand;
- many jurisdictions' apparent lack of guidance on whether the method of delivery of digital goods changes their taxability;
- a disconnect between some jurisdictions' taxation of digital goods and what is referred to as "video or television programming" and "streaming services"; and
- some jurisdictions enact ways of taxing digital goods and services that are so elaborate and overwhelmingly detailed that their statutes and rules simply cannot be diagrammed on a single page or understood without devoting a separate paper to cover each nuance.

Failing to have clear information about the types of goods and services may inhibit good policymaking. On the other hand, having regulations, information, and systems in place to

<sup>2</sup> See Stephen Nellis, "Microsoft Cloud Revenue Regains Momentum, Sending Profit Above Street Estimates" Reuters (Jan. 29, 2020).

<sup>3</sup> See Jordan Novet, "AWS Generated Revenue of \$9.95 Billion in Q4, Up 34% From a Year Ago," CNBC (Jan. 30, 2020).

<sup>4</sup> See New York City Independent Budget Office, "To Tax or Not to Tax the New Economy: Digital Goods and Sales Taxes in New York" (Sept. 2015).

control new goods and services as they emerge may burden their very emergence and development. What would be the perfect law for measuring the value of the digital economy and determining how much of it, if any, should be taxed? The paradox is that in the information age, we want to measure so we can manage, but perhaps not too much.

Like in quantum physics, light has the qualities of both a wave and a particle — the line between what once was considered a product or a consumer good and a service is no longer as easy to see and observe. Unlike in the industrial economy, in the digital economy most of the value that was previously captured in goods can be transferred digitally in ways unseen to the eye. In addition to goods, many services are being digitized or automated. Hence the frenzy of headlines about whether Netflix and streaming videos are digital goods or services and whether they should be taxed. This is not a mere semantic matter, since, traditionally, the tendency in the area of sales and use taxes has been to tax goods but not services unless enumerated as taxable. And two states have passed constitutional amendments prohibiting taxation of any new services.<sup>5</sup>

Additionally, the uncertain division between the taxable good and nontaxable service in the digital realm, particularly as the offerings and business models proliferate, complicates one of the most critical elements of any legislative attempts to clarify or address for the first time the treatment of such products: fiscal scoring. In Arizona, for example, efforts in 2017-2019 to address digital goods taxation have bogged down, among other issues, due to varying estimates of the fiscal impact. Fiscal estimates of digital goods legislation during this time ranged from producing a net revenue increase attributable to greater taxpayer compliance arising from clarity in the law to revenue losses approaching \$100 million to something in between.<sup>6</sup> Not only is transaction privilege tax

(sales and use tax) revenue at stake, but corporate income tax as well: Arizona is one of an ever-shrinking list of states wherein a cost of performance method is still used for income apportionment when the income-producing activity stems from stand-alone services and intangibles (not rents or leases) and is determined to take place across state boundaries.

What follows is information about digital goods and types of digital goods as we know them:

- in general terms;
- under the inventory approach offered by the Streamlined Sales and Use Tax Agreement;
- in states' specific legislature; and
- in prominent cases addressing taxability of digital goods.

The ultimate policy questions are whether digital goods are a subset of tangible personal property or whether they should be separately defined and regulated. If so, what are the types of digital goods, and should we tax them differently?

Understanding the regulatory landscape may assist policymakers and lawmakers in easing tax administration to match the needs of the expanding digital economy. It may also assist private industry with setting up the accounting and auditing of companies that offer digital goods and services.

## Types of Digital Goods

### A General View — Wikipedia and Examples of Regulatory Approaches

In the information age (or as some may feel, the disinformation age), one can find any definition of digital goods they like. The consensus on Wikipedia appears to be that:

Digital goods or e-goods are intangible goods that exist in digital form. Examples include this Wikipedia article; digital media, such as e-books, downloadable music, internet radio, internet television and streaming media; fonts, logos, photos and graphics; digital subscriptions; online ads (as purchased by the advertiser); internet coupons; electronic tickets; online casino tokens; electronically traded

<sup>5</sup> A.R.S. Const. Art. 9 section 25 (Prohibition of new or increased taxes on services); Mo. Ann. Stat. Const. Art. 10, section 26 (Prohibition on new transaction-based tax not subject to such tax as of Jan. 1, 2015).

<sup>6</sup> See Ben Giles, "Digital-Goods Taxation Data Unreliable, Leaves Fate of Bill Uncertain," *Arizona Capitol Times* (Mar. 20, 2019).

financial instruments; downloadable software (Digital Distribution) and mobile apps; cloud-based applications and online games; virtual goods used within the virtual economies of online games and communities; workbooks; worksheets; planners; e-learning (online courses); webinars, video tutorials, blog posts; cards; patterns; website themes; templates.<sup>7</sup>

Put simply, “if you pay to watch a web conference on your computer screen, you have bought a digital good.”<sup>8</sup> Digital e-commerce encompasses a variety of goods, including: “video, audio, remote access to software (cloud computing), information services, data processing, any website where payment is required for username access and subscription.”<sup>9</sup> Some would say that this is an oversimplification, and that putting software and movies (or even books) in the same category is questionable at best.

For example, in the world of Wikipedia definitions, if you pay to watch a web conference on your computer screen, you have bought a digital good, but, for tax purposes, some caveats must be considered. The Iowa Department of Revenue notes the difference between a live and prerecorded webinar, and if the live webinar allows the same participation to viewers as to a live audience. The DOR’s website says:

Webinars are generally taxable as specified digital products. Specifically, webinars fall into the “other digital products” category as a “news or information product.” Some webinars may not be subject to sales tax. Purchases of access to a live webinar (i.e. access to viewing a presentation occurring in real-time) are not always subject to sales tax. Attending a presentation in-person, if it is not an admission to an amusement, is generally not taxable under Iowa law. Purchasing access to a live webinar is not

taxable, if the live webinar allows for a level of participation which is substantially similar to an in-person presentation.<sup>10</sup>

Similarly, the Minnesota DOR explained that webinar charges “for live or pre-recorded audio and audiovisual presentations” are exempt if they are accessed electronically and:

- Admission to the in-person presentation is not subject to tax
- Online participants and the presenter can interact with each other while the participants view the presentation
- Any limits on the amount of interaction (and when it occurs) are the same for both online and in-person participants.<sup>11</sup>

The states have come up with many different classifications of digital goods — no two of which are the same. A visual analysis of five sample states — South Dakota, Tennessee, Texas, Washington, and Wisconsin — demonstrates this point.

South Dakota taxes tangible personal property — the term has been statutorily defined (like in other states) to include electricity, water, gas, steam, and pre-written computer software.<sup>12</sup> Separately, South Dakota taxes “product transferred electronically.”<sup>13</sup> It does not differentiate between software, music, and videos and puts all of these goods in one bucket — whether they are provided for temporary or permanent use. The relevant statute says, “Examples of products transferred electronically — this is not an all-inclusive list: Music, Books, Videos, Movies, Newspapers, Custom computer software, Photos, clip art etc.”<sup>14</sup>

Tennessee (Figure 1), in contrast, creates a more elaborate approach for taxing most digital goods, carving out pockets of digital products free from taxation.<sup>15</sup>

<sup>10</sup> Iowa Department of Revenue, Taxation of Specified Digital Products, Software, and Related Services.

<sup>11</sup> Minnesota Department of Revenue, Sales Tax Fact Sheet 177. The DOR clarifies that “tuition is not taxable for classes a student attends online as part of a course of study at a post-secondary school, college, university, or private career school.”

<sup>12</sup> S.D. Codified Laws section 10-45-1.

<sup>13</sup> S.D. Codified Laws section 10-46-1.

<sup>14</sup> S.D. Department of Revenue, Tax Fact Sheet (Mar. 2011).

<sup>15</sup> Tenn. Code Ann. section 67-6-102 (27).

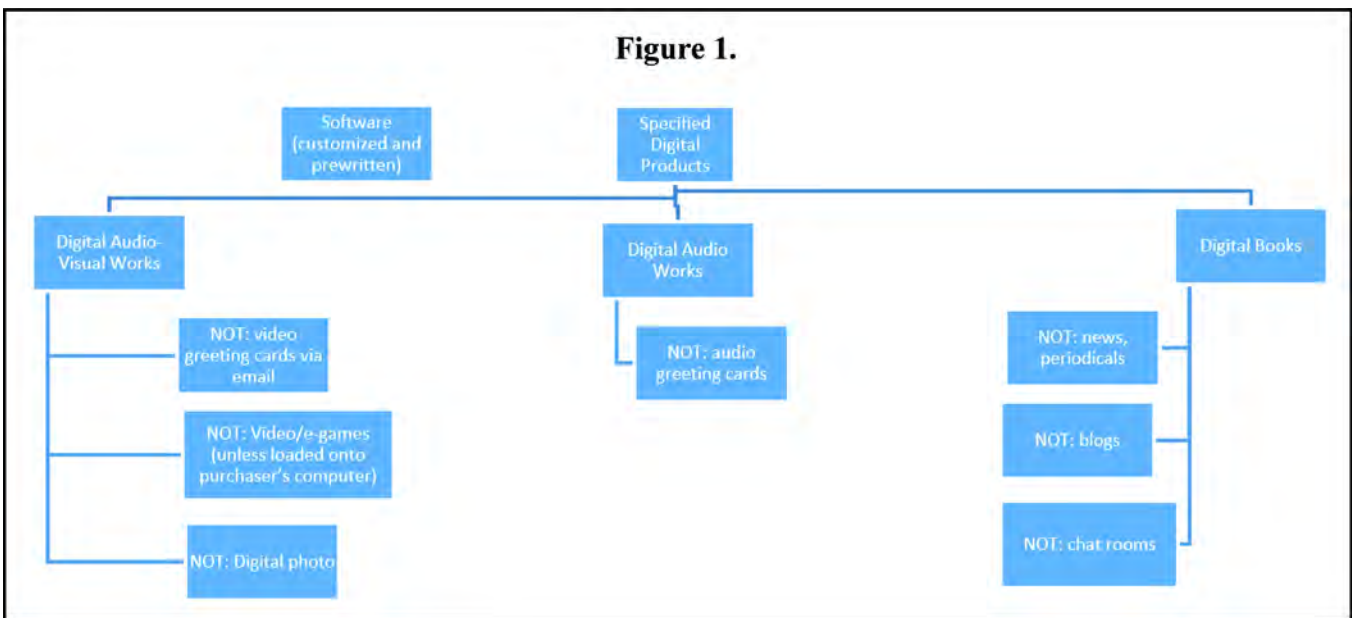
<sup>7</sup> See Wikipedia entry for digital goods (accessed Jan. 2020).

<sup>8</sup> *Id.*

<sup>9</sup> W. Ault, K. Phillips, “Digital Goods and Services: How to Avoid Tax-Related Traps,” 28 *J. Multistate Tax’n* 16 (2018).

**Table 1.**

Digital Audiovisual Works	Digital Audio Works	Digital Books
<p>A series of related images which, when shown in succession, impart an impression of motion, together with any accompanying sounds, that are transferred electronically. Examples include motion pictures, musical videos, entertainment and news programs, and live events.</p> <p>Not included are video greeting cards sent by electronic mail, video or electronic games, and individual digital photographs that do not impart an impression of motion when viewed successively.</p>	<p>Works that result from the fixation of a series of musical, spoken, or other sounds, that are transferred electronically, including prerecorded or live songs, music, readings of books or other written materials, speeches, ringtones, or other sound recordings.</p> <p>Not included are audio greeting cards sent by electronic mail.</p>	<p>Works generally recognized in the ordinary and usual sense as “books” that are transferred electronically, including works of fiction and nonfiction and short stories.</p> <p>Not included are newspapers, magazines, periodicals, web blogs, and chat room discussions.</p>



The relevant section of Tennessee’s sales and use tax guide is longer than a few pages and details various exceptions. (See Table 1.)

The implementation of tax statutes for the digital economy is not as straightforward in Tennessee.<sup>16</sup>

Texas provides an example of yet another approach, which is focused on types of services more than types of digital products (see Figure 2).

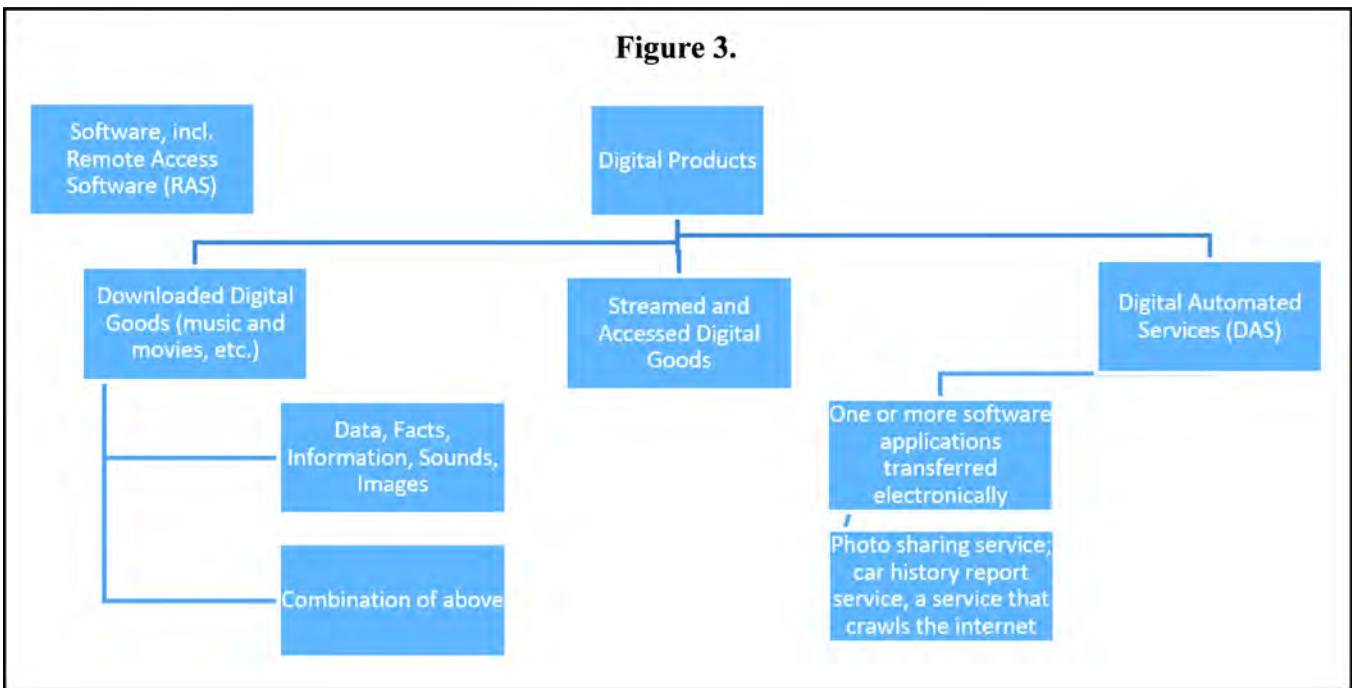
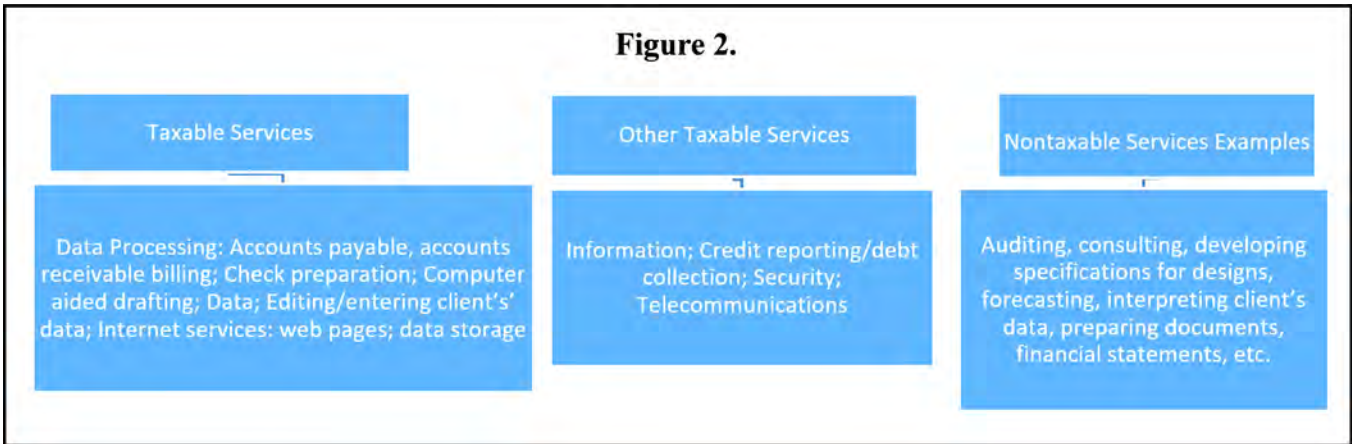
Texas prefaces its tax statutes by stating “the sale or use of a taxable item in electronic form

instead of on physical media does not alter the item’s tax status,”<sup>17</sup> and declares that it taxes the digital distribution of video programming to purchasers by any means now in existence or that may be developed.<sup>18</sup> The focus in Texas is on digital services, defined as either data processing or information services, which are distinguished from professional services. A service may be performed with a computer using data, or by a professional using a computer as a tool. For those who are unsure about the difference between data

<sup>16</sup>Tennessee Department of Revenue, Sales and Use Tax Guide (Sept. 2019).

<sup>17</sup>Tex. Tax Code Ann. section 151.010.

<sup>18</sup>34 Tex. Admin. Code section 3.313.



processing services and professional services, Texas invites them to call a toll-free number.<sup>19</sup>

Blending the complexity of a rule-with-exceptions (Tennessee) with the complexity of additional classification of some digital services (Texas), in attempts to create clarity, some states offer even more sophisticated models. In Washington (Figure 3) the statute separately defines the terms “digital products” as a broader category including “digital goods” and highlights the difference between downloaded

goods, whether music or movies, and streamed goods as well as digital automated services, which are then distinguished from professional and nontaxable services.<sup>20</sup>

Unlike Texas, Washington excludes data processing services from the definition of what it deems taxable automated services.<sup>21</sup> (See Figure 4.)

<sup>19</sup>Texas Comptroller, Data Processing Services Are Taxable.

<sup>20</sup>Wash. Rev. Code Ann. section 82.04.192.

<sup>21</sup>Washington State Department of Revenue, Digital Products Including Digital Goods.

Figure 4.

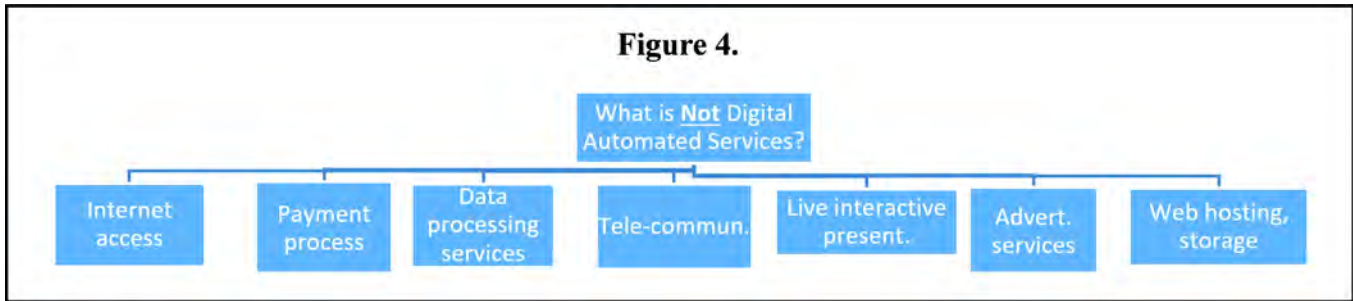
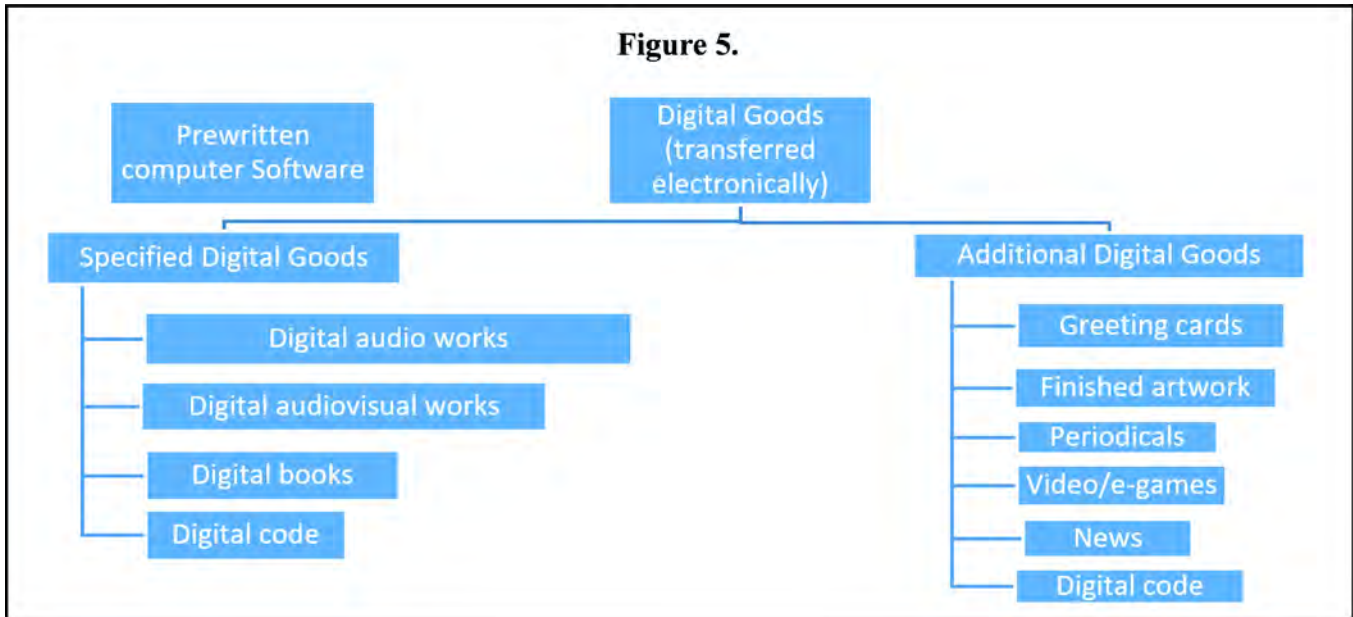


Figure 5.



In Wisconsin digital goods are largely taxed, except for software as a service (SaaS). (See Figure 5.)

Unlike South Dakota, Wisconsin (see Figure 6) does not treat software and music downloads alike. An electronic delivery of software refers to downloading of software only — and not accessing software that would be nontaxable, whereas an electronic transfer of digital goods includes either downloading or accessing.

The Wisconsin DOR has stated that:

“Transferred electronically” is a term that applies to digital goods. “Delivered electronically” is a term that applies to prewritten computer software. Prewritten computer software delivered electronically is tangible personal property and not a

digital good for purposes of Wisconsin’s sales and use tax laws.<sup>22</sup>

Over 30 years ago in 1989, one court observed the arbitrary nature of any logic in favor of or against taxing digital products, writing:

The wide divergence of results demonstrates both the importance of and the necessity for state legislatures updating their taxing laws in terms of modern technology. The divergent results suggest that as a matter of policy, a good case can be made for taxing the use of all software, none of the software, or only part of the software.<sup>23</sup>

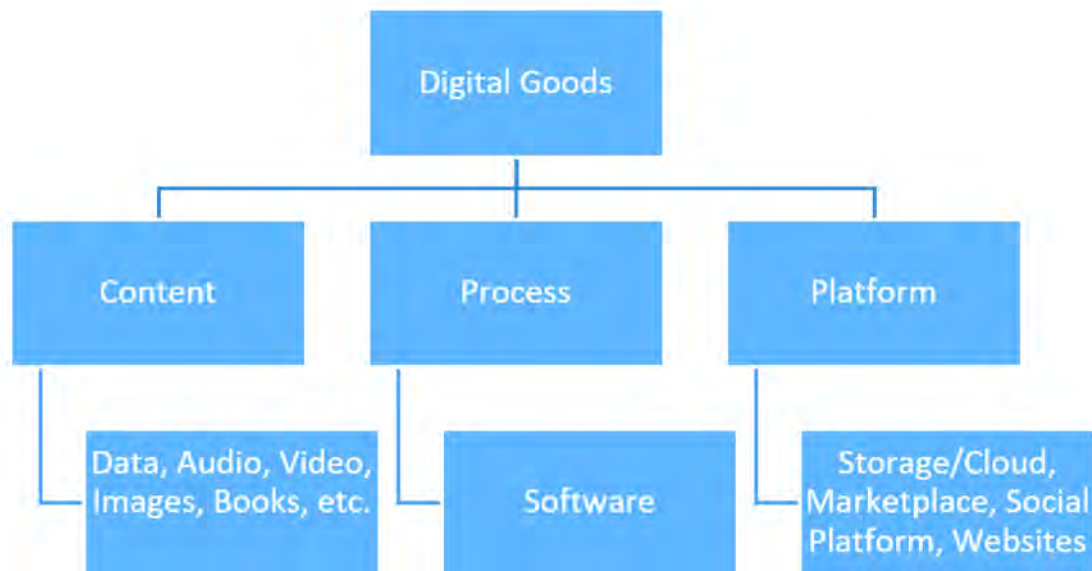
<sup>22</sup>Wisconsin Department of Revenue, “How Do Wisconsin Sales and Use Taxes Apply to Sales and Purchases of Digital Goods?” Publication 240, at 8 (May 2016).

<sup>23</sup>*International Business Machines Corp. v. Director of Revenue*, 765 S.W.2d 611, 612 (Mo. 1989).

Figure 6.



Figure 7.



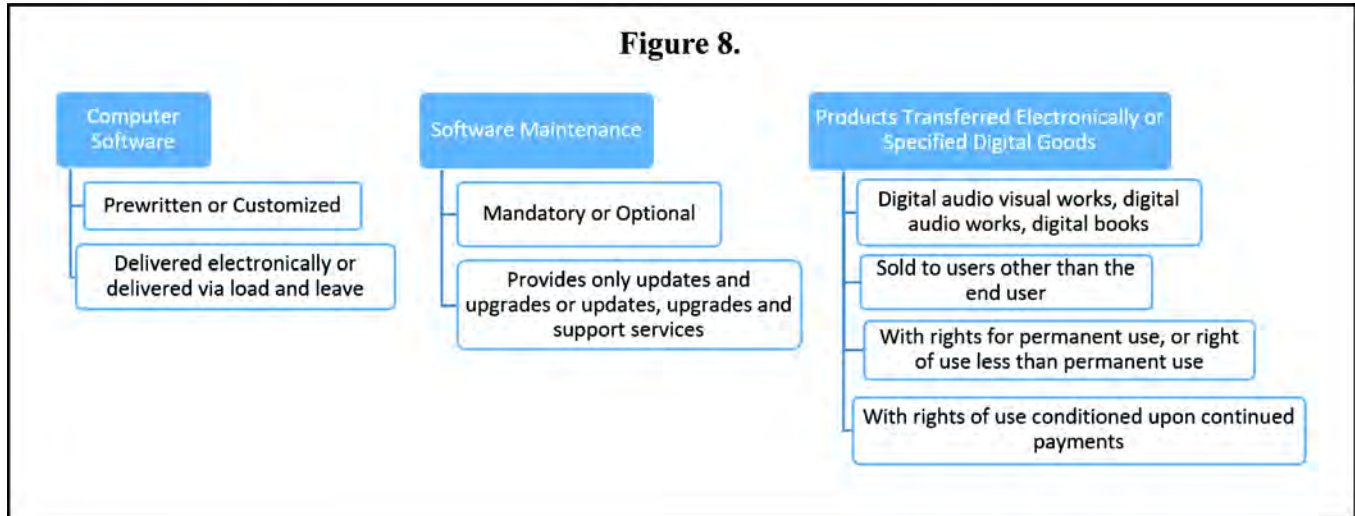
The policy discussions do not seem to have gained clarity in the last few decades. Based on the above examples, there are at least four aspects to watch for when analyzing how the states have defined the universe of digital products and services. These are whether:

- digitally delivered value is a product or a service;
- software (which is akin to a device or equipment) should be treated differently from digitally delivered content (music, movies, books);
- there should be a difference in tax treatment based on whether the software or content is digitally downloaded or merely accessed; and
- it makes sense to differentiate streaming of live content from recorded content and to further differentiate between types of digital content. If so, what basis, including itemization of charges for storing digital content, should change taxability?

Digital products must be distinguished from manual or professional services provided by individuals directly. Like any other product sold or rented, digital products can easily be bundled together as well as mixed with accompanying services. (See Figure 7.) To ensure the analysis is not blurred, it may help to separate the following obvious manifestations of digital goods:

- digital content (data, whether digital audio works, digital audio-video works, or digital books);
- digital processes (software, consisting of computer programs, algorithms, or instructions);
- digital platforms (consisting of digital storage space or memory);
- digital marketplaces;
- digital payment methods or currency; and
- digital highways, internet communications, and exchanges, etc.





The universe and variety of digital goods, and combinations thereof, including any accompanying services, prompt many policy-related questions about whether and why these goods are different and deserve separate treatment from physical objects. These questions include whether:

- software is like movie film and should be treated the same or different for tax purposes;
- software is like digital audio/video works and should be treated the same or different for tax purposes;
- the difference between customized and canned software makes sense;
- the delivery of digital content (digital audio/visual works) on a permanent or less-than-permanent basis should make a difference;
- the method of delivery of software or digital content should make a difference;
- digital content should be treated differently depending on whether it is data, creative content, or an algorithm; and
- the purchase or rental of storage for various digital data (whether software or digital audio/video works) is also a purchase or rental of a product or service and under what circumstances.

### Digital Goods' Classification Under the SSUTA Inventory Approach

Out of 50 states and the District of Columbia, 24 states are members of the SSUTA. The agreement's intent is to provide uniform definitions of goods

and services, indicating if they are either taxable or tax exempt, and uniform sourcing rules. The member states may expand on the definitions. The 24 SSUTA states are Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, Tennessee, South Dakota, Utah, Vermont, Washington, West Virginia, Wisconsin, and Wyoming.

A quick glance at the SSUTA Taxability Matrix<sup>24</sup> reveals a complex structure of digital products and associated reference numbers that may be broken into several large classes of products. (See Figure 8.) These are:

- computer software products (pre-written and customized);
- mandatory and optional-maintenance computer-related contracts;
- digital products consisting of:
  - digital audiovisual works;
  - digital audio works; and
  - digital books; further categorized as:
    - products/goods sold to end-users as opposed to intermediaries;
    - products/goods offered with rights for permanent use or less than permanent use; and
- with rights of use conditioned upon continued payment.

<sup>24</sup> Streamlined Sales Tax Governing Board Inc., Taxability Matrix.

Table 2.

Tax software, digital product	Some Tax software, SaaS, not digital product	Some Tax not SaaS, digital product	Limited Tax e-delivered software, not SaaS, not digital product	No Tax tangible media, not SaaS, not digital product
Iowa Nebraska Ohio Rhode Island South Dakota Tennessee Utah Washington	West Virginia	Arkansas Indiana Kentucky Minnesota New Jersey North Carolina Vermont Wisconsin Wyoming	Kansas Michigan North Dakota	Georgia Nevada Oklahoma
<b>Bold = custom and canned software taxable</b>				

Based on its matrix-like structure and the use of product reference codes, the SSUTA framework is best described as the “inventory approach.” The existence of uniform definitions and product codes was undoubtedly designed to help businesses and their accountants or consultants automate transaction processing to increase compliance nationwide, considering the peculiarities of each jurisdiction. The idea behind the inventory approach is that tax authorities and industry would be best served if they used the same tools for tax reporting and remittance based on clearly defined and agreed upon codes. The idea aligns with what is becoming known as the blockchain revolution (whether through software or digital currency) consisting of the digitization of all transactions, including tax compliance at the time each transaction is processed based on the code of product chosen and agreed on by the parties, and possibly verified by third parties.<sup>25</sup>

Implementation of the SSUTA’s inventory approach appears to have run into some difficulty with providing uniformity or streamlined definitions. The approach framework allows for as many as 42 separate definitions of subvarieties of digital goods and options for taxing them. Yet it does not appear to define what the term “delivered electronically” means, and states vary on how this

key term is defined.<sup>26</sup> Generally, the SSUTA’s “delivered electronically” phrase does not appear to cover products accessed electronically such as SaaS, remotely accessed software, or vendor-hosted software. Although the SSUTA’s framework differentiates between goods “sold with rights of use less than permanent use” or “with rights of use conditioned on continued payment,” this framework applies to “specified digital goods,” not software. The SSUTA’s matrix, with its product reference chart, also does not address digital codes and numerous other digital products and information services. The 24 SSUTA member states may have agreed in general terms on the inventory approach, but they have not agreed on the uniform treatment of digital goods or services. In fact, one gets the impression that no two states tax digital goods in the same way. More than a handful of states tax it all — software and specified digital goods; about a handful of states do not tax most digital products; and many states are in between, taxing some but not all digital products. (See Table 2.)

<sup>25</sup> See, e.g., Microsoft and PwC, “Digital Transformation of Tax Administration” (2017); Chelsey Dulaney, “EU Inches Toward Blockchain in Fight Against VAT Fraud,” *Bloomberg Tax* (Sept. 30, 2019).

<sup>26</sup> In Iowa (a SSUTA state), the tax is on software that is electronically transferred, and the term “electronically transferred” includes obtained or accessed. Iowa Code Ann. section 423.1(b)(4) (“Electronically transferred” means obtained or accessed by the purchaser by means other than tangible storage media, including but not limited to a specified digital product purchased through a computer software application, commonly referred to as an in-app purchase, or through another specified digital product, or through any other means.). In contrast, Nebraska (a SSUTA state), defines the term “delivered electronically” more narrowly as “obtained by the purchaser by means other than tangible storage media.” Neb. Rev. Stat. section 77-2701.49. Similarly, in Tennessee (a SSUTA state), “electronically transferred” means obtained by the purchaser by means other than tangible storage media. Ten. Code Ann. section 67-6-102(89)(A).

Table 3.

Tax no statute	Tax software, digital product	Some Tax software, SaaS, not digital product	Some Tax software, not SaaS, digital product	Limited Tax software, not SaaS, not digital product	No Tax only tangible media, not SaaS, not digital product
<b>Alabama</b> Arizona <b>Hawaii</b> <i>New Mexico</i>	<b>Connecticut</b> <b>District of Columbia</b> <b>Iowa</b> <b>Nebraska</b> <i>Ohio</i> Pennsylvania <i>Rhode Island</i> <b>South Carolina</b> <i>South Dakota</i> <b>Tennessee</b> <b>Texas</b> <i>Utah</i> <i>Washington</i>	Massachusetts New York <b>West Virginia</b>	<i>Arkansas</i> Colorado Florida Idaho <i>Indiana</i> <i>Kentucky</i> Louisiana Maine <i>Minnesota</i> <b>Mississippi</b> <i>New Jersey</i> <i>North Carolina</i> <i>Vermont</i> <i>Wisconsin</i> <i>Wyoming</i>	Illinois Kansas <i>Michigan</i> North Dakota	California Georgia Maryland Missouri <i>Nevada</i> <i>Oklahoma</i> Virginia
<b>Bold = custom and canned software taxable</b> <i>Italics = SSUTA</i>					

One may wonder if the SSUTA states should continue to further parse digital products and contract provisions on how they are serviced or invoiced? It will be interesting to see how the SSUTA governing board addresses this ever-growing complexity by adding more lines to its product reference codes or perhaps reinventing its approach.

### Digital Goods in the States' Statutes and Administrative Regulations

The following summary (Table 3) groups various approaches that states have adopted.<sup>27</sup>

Traditionally, the sales and use taxes are applied to tangible personal property, although many states also tax services. Still, one aspect of approaching taxation of digital goods is to see

whether the states have expanded the definition of tangible personal property to include digital goods or if they have created separate categories for some or all tangible products. The brief answer is that while most states have expanded the definition of tangible personal property to include pre-written computer software, they did not expand it to include other digital goods such as music, digital books, or movies, which are taxed as a separate category. There is no uniform definition of the term "tangible personal property." At least three states — Hawaii, Nebraska, and New Mexico — do not statutorily define tangible personal property. Mississippi refers to it as property perceptible to human senses or by chemical analysis but also includes pre-written computer software.<sup>28</sup> Four states and the District of Columbia have definitions that refer to it as being corporeal property or having

<sup>27</sup> This paper focuses on 46 jurisdictions, excluding states that do not have sales tax: Alaska, Delaware, Montana, New Hampshire, and Oregon.

<sup>28</sup> Miss. Code Ann. section 27-67-3(i).

some physical existence (Colorado, the District of Columbia, Maryland, Nebraska, and New York),<sup>29</sup> with Colorado and New York broadening their definition of corporeal property to include pre-written computer software. Pennsylvania's definition refers to its being corporeal property, but then broadens the term to include videos and so forth, whether delivered or streamed.<sup>30</sup> Louisiana refers to tangible personal property as equivalent to corporeal movable property including canned computer software, electronic files, and on-demand audio and video downloads.<sup>31</sup> Missouri and Virginia define tangible personal property by referring to a list of items referenced in a separate section.<sup>32</sup>

Most states — 33 — have a definition that refers to “tangible personal property” as “property that may be seen, weighed, measured, felt, or touched, or is in any other manner perceptible to the senses.”<sup>33</sup> Of the 33 states, three have a definition that does not refer to software (Arizona, California, and Florida). South Carolina includes in the term “tangible personal property” some services and intangibles such as communications. Three states' definitions include “computer program” or “computer software” (Alabama, Colorado, and Texas). Massachusetts declares that the transfer of standardized computer software (any electronic transfer) shall be considered a transfer of tangible personal property.<sup>34</sup>

<sup>29</sup> Colo. Rev. Stat. Ann. section 39-26-102(15); D.C. Code Ann. section 47-2001(s); Md. Code Ann. Tax-Gen. section 11-101; Neb. Rev. Stat. section 77-105; and N.Y. Tax Law section 1101(6).

<sup>30</sup> Pa. Stat. Ann. 72 P.S. section 7201(m).

<sup>31</sup> La. Civ. Code Ann. art. 471; and La. Admin. Code tit. 61, Pt. I, section 4301.

<sup>32</sup> Mo. Ann. St. 144.605(11); and Va. Code Ann. section 58.1-3523.

<sup>33</sup> Ala. Code section 45-2-244.180; Ariz. Rev. Stat. section 42-5001; Ark. Code Ann. section 26-53-102; Cal. Rev. & Tax Code section 6016; Conn. Gen. Stat. Ann. section 12-407; Fla. Stat. Ann. section 212.02(19); Ga. Code Ann. section 48-8-2(37); Idaho Code section 63-3616; Ill. Comp. Stat. Ann. 110 section 26/5; Ind. Code Ann. section 6-2.5-1-27; Iowa Code Ann. section 423.1; Kan. Stat. Ann. section 79-3602; Ky. Rev. Stat. Ann. section 139.010(41); Me. Rev. State. Ann. tit. 36 section 175; Mich. Comp. Laws Ann. section 205.51a(r); Minn. Stat. Ann. section 297A.61; Nev. Rev. Stat. Ann. section 360B.470; N.J. Stat. Ann. section 54:32B-2(g); N.C. Gen. Stat. section 105-164.3; N.D. Cent. Code section 57-39.2-01(25); Ohio Rev. Code Ann. section 5739.01(Y); Okla. Stat. Ann. tit. 68 section 1352; R.I. Gen. Laws section 44-18-16; S.C. Code Ann. section 12-36-60; S.D. Codified Laws section 10-45-1(14); Tenn. Code Ann. section 67-6-102(89)(C); Tex. Tax Code Ann. section 151.009; Utah Code Ann. section 59-12-10; Vt. Stat. Ann. tit. 32 section 970; Wash. Rev. Code Ann. section 82.08.010; W. Va. Code Ann. section 11-15-2; Wis. Stat. Ann. section 77.5(20); Wyo. Stat. Ann. section 39-15-101 (ix).

<sup>34</sup> Mass. Gen. Laws Ann. 64H section 1.

Twenty-eight states have defined “tangible personal property” to specifically include “prewritten computer software.”<sup>35</sup> Yet these states' approaches to taxation of pre-written computer software differ. For example, Arkansas states in its definition of “computer software” that the term “does not include software that is delivered electronically or by load and leave.” The term “delivered electronically” is further defined as “delivered to the purchaser by means other than tangible storage media.”<sup>36</sup>

Most states part ways with Arkansas's too-narrow requirement that pre-written software is not taxable if delivered electronically. New Jersey specifies that pre-written computer software is included in the definition of tangible personal property, including if it is delivered electronically.<sup>37</sup> Indiana also includes software “electronically transferred” or via “load and leave.”<sup>38</sup> Iowa separately addresses pre-written computer software and SaaS by listing SaaS as an enumerated taxable service,<sup>39</sup> whereas pre-written computer software is a tangible personal property. Minnesota taxes the transfer of pre-written computer software whether delivered electronically, by load and leave, or otherwise.<sup>40</sup> Wisconsin includes pre-written computer software in the definition of “tangible personal property” “regardless of how it is delivered to the purchaser.”<sup>41</sup>

On one end of the spectrum, at least nine states have chosen to tax software — but only if delivered via tangible medium (Arkansas, California, Colorado, Georgia, Maryland,

<sup>35</sup> Arkansas, Connecticut, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Maine, Michigan, Minnesota, New Jersey, New York, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, Rhode Island, South Dakota, Tennessee, Utah, Vermont, Washington, West Virginia, Wisconsin, and Wyoming.

<sup>36</sup> Ark. Code Ann. section 26-53-109.

<sup>37</sup> N.J. Stat. Ann. section 54:32B-2(g).

<sup>38</sup> Ind. Code Ann. section 6-2.5-1-28.5.

<sup>39</sup> Iowa Code Ann. section 423.2.

<sup>40</sup> Minn. Stat. Ann. section 297A.61(f).

<sup>41</sup> Wis. Stat. Ann. 77.51 (20).

Missouri, Nevada, Oklahoma, and Virginia).<sup>42</sup> Of these states, California and Missouri declare they do not tax SaaS; Nevada taxes hosting and data processing services but appears to have no guidance on SaaS.<sup>43</sup> At least 11 states tax software if delivered via tangible medium or electronic delivery but indicate expressly or through some guidance that they do not tax SaaS or remotely accessed software: Idaho, Indiana, Kansas, Michigan, Minnesota, Mississippi, North Carolina, North Dakota, Vermont, Wisconsin, and Wyoming.<sup>44</sup>

On the other end of the spectrum, at least 12 states tax software whether delivered via tangible medium, delivered electronically, or accessed as vendor-hosted software (SaaS).<sup>45</sup> Four states tax SaaS based on nonstatutory guidance provided: Arizona, Hawaii, New Mexico, and West Virginia. At least two states may tax SaaS depending on the details. South Carolina does not tax canned software unless delivered via tangible media but would allow taxation of software accessed via the cloud as a communication service.<sup>46</sup> New Jersey does not tax SaaS unless it qualifies as an information service.<sup>47</sup>

In between these extremes, at least eight states tax software if delivered via tangible medium or

electronic delivery (via a download, load and leave, and so forth) but do not clearly address SaaS: Alabama, Florida, Illinois, Kentucky, Louisiana, Maine, Ohio, South Dakota.<sup>48</sup> Both custom and canned software are taxed in Alabama, Connecticut, the District of Columbia, Hawaii, Iowa, Mississippi, Nebraska, South Carolina, Tennessee, Texas, and West Virginia.

Idaho, Indiana, and Wyoming tax specified digital goods only if delivered permanently.<sup>49</sup> Other states tax digital goods whether based on permanent delivery or less-than-permanent delivery, or a usage terminable upon condition: Arkansas, Iowa, Kentucky, Nebraska, and New Jersey.<sup>50</sup> Further, while New Jersey, Ohio, Rhode Island, Tennessee, Utah, and Vermont allow for the taxability of specified digital goods delivered or transferred electronically,<sup>51</sup> others tax specified digital goods whether electronically transferred or accessed: the District of Columbia, Iowa, Minnesota, North Carolina, Washington, and Wisconsin.<sup>52</sup>

At least 17 states and the District of Columbia tax video programming, broadcasting, cable, or television services — Arkansas, Connecticut, the District of Columbia, Florida, Hawaii, Indiana, Iowa, Kansas, Kentucky, Maine, Massachusetts, Minnesota, Nebraska, Pennsylvania, South Dakota, Tennessee, and Texas — or pay per view: Maryland or Washington.<sup>53</sup> Similarly, through case law or administrative guidance, Arizona and Louisiana<sup>54</sup> have developed a conceptual

<sup>42</sup> Ark. Code Ann. section 26-53-109; Cal. Rev. and T. Code section 6051; 18 Cal. Admin. Code section 1502(D); Colo. Rev. Stat. Ann. section 39-26-102(c)(I); Ga. Code Ann. sections 48-8-2(37), 48-8-3(91), 48-8-30(a); Md. Code Ann. Tax-Gen. sections 11-101, 11-102, 11-219, Md. Publication. "Sales and Use Tax Guide" — List of Taxable Goods and Services (Oct. 1, 2019); Mo. Code Regs. Ann. tit. 12, section 10-109.050; Nev. Admin. Code section 372.880; Okla. Admin. Code section 710-65-19-53(c); and Va. Code Ann. section 58.1-602.

<sup>43</sup> 18 Cal. Admin. Code section 1502(c)(7), Mo. Code Regs. Ann. tit. 12, section 10-109; Nev. Rev. Stat. 363C.430; and Nev. Admin. Code section 372.880.

<sup>44</sup> Idaho Code section 63-3616(b); Ind. Sales Tax Information Bulletin No. 8 (12/2019); Kan. Guidelines, EDU-71R (July 23, 2010); *Auto-Owners Ins. Co. v. Dep't of Treasury*, 880 N.W. 2d 337 (Mich. App. 2015); Minn. Dep't of Revenue, Computer Software and Digital Products; Miss. Rules, Part IV Sales and Use Tax, 300; N.C. Gen. Stat. 105-164.4B; N.D. Cent. Code section 57-39.2-02.1; Vt. Stat. Ann. tit. 32 section 9701(7); Wis. Stat. Ann. sections 77.51, 77.52; Wyo. Stat. Ann. section 39-15-101.

<sup>45</sup> Conn. Gen. Stat. Ann. section 12-407(37); D.C. Code Ann. section 47-2001(d-1); D.C. Mun. Regs. tit. 9, section 471; 474.1 and 474.4; Iowa Code Ann. section 423.2; Mass. Regs. Code tit. 830 section 64H.1.3; Neb. Admin. Reg-1-088; N.Y. Tax Law section 1101(6), Tax Bulletin Sales and Use Tax TB-ST-128 (8/5/2014); Pa. Stat. Ann. section 72 P.S. section 7201 (m)(2); R.I. Gen. Laws section 44-18-7(14), (15); Tenn. Code Ann. section 67-6-231(b); Utah Code Ann. section 59-12-102, Publ'n 64, Priv. Letter Ruling 09-003 (2/13/2009); Tex. Tax Code Ann. section 151.035, Priv. Letter Ruling No. 151250584 (5/20/2017); Vt. Stat. Ann. tit. 32 section 970; Wash. Rev. Code Ann. section 82.04.050(6).

<sup>46</sup> S.C. Revenue Ruling No. 03-5.

<sup>47</sup> N.J. Tech. Bulletin, TB-72, at 2 (7/3/2013); N.J. Stat. Ann. 54:32B-3(b).

<sup>48</sup> Ala. Admin. Code r. 810-6-1-.37; Fla. Stat. Ann. section 212.02; 86 Ill. Adm. Code 130.1935; Ky. Rev. Stat. Ann. section 139.200; La. Rev. Ruling 10-001 (3/23/2010); Me. Rev. Stat. Ann. tit. 36 sections 1752 and 2552; Ohio Rev. Code Ann. section 5739.01(CCC); S.D. Tax Fact Sheet (3/2011).

<sup>49</sup> Idaho Code section 63-3616(b); Ind. Code Ann. section 6-2.5-4-16.4; and Wyo. Stat. section 39-15-101(a)(i)(P).

<sup>50</sup> Ark. Code Ann. section 26-52-301; Iowa Code Ann. section 423.2; Ky. Rev. Stat. Ann. section 139.200; Neb. Rev. Stat. section 77-2701.16; and N.J. Stat. Ann. section 54:32B-3.

<sup>51</sup> N.J. Stat. Ann. section 54:32B-8.62; Ohio Rev. Code Ann. section 5739.0; R.I. Gen. Laws section 44-18-7.1; Tenn. Code Ann. section 67-6-102(86); Utah Code Ann. section 59-12-102; Vt. Stat. Ann. tit. 32 section 9701 (45).

<sup>52</sup> D.C. Code Ann. section 47-2001(d-1); D.C. Mun. Regs. tit. 9, section 474 474.1; Iowa Code Ann. section 423.1; Minn. Stat. Ann. section 297A.61; N.C. Gen. Stat. section 2019-169; Wash. Rev. Code Ann. section 82.04.192(8); and Wis. Stat. Ann. section 77.51-(21q).

<sup>53</sup> Md. Ann. Code section 11-101(m)(8); Wash. Rev. Code Ann. section 82.04.192(11); and Wash. Admin. Code section 458-20-15503.

<sup>54</sup> Ariz. Rev. Stat. sections 42-5001; -5061, and -5071; La. Rev. Stat. Ann. section 47:301; 47:321; La. Admin. Code tit. 61 Pt I, section 4301; *South Central Bell Telephone Co. v. Barthelemy*, 643 So.2d 1240 (La. 1994).

framework that encompasses taxation of digital goods that fall outside the scope of commonly understood service-type transactions. Like Arizona, Colorado taxes digital pictures, movies, and other goods, even though there is no specific statute.<sup>55</sup> Although it is a SSUTA state, Nebraska is in its own category because it follows the conceptual approach and taxes digital goods as “intellectual or entertainment property,” including all types of software and digital products furnished to customers, regardless of delivery methods (although some question remains as to the taxability of SaaS).<sup>56</sup>

What to make of all this variety? The Supreme Court Justice Louis Brandeis opined, “It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country.”

## Software and Digital Goods in State Court Decisions

### Viewing Software as Intellectual Property And a Nontaxable Service

One of the first digital goods cases started with the debate over whether the software is like movie film. The debate goes back at least to the 1970s. The struggle seemed to center around whether software is intangible, like an information service (which should not be taxed), or whether it is more like a roll of film that is a taxable physical object. Some courts chose to view software as information, stating that in the case of software, unlike a phonograph record, no product is created; and that “the whole of computer software could be transmitted orally or electronically without any tangible manifestations of transmission,” and “a magnetic tape is only one method whereby information may be transmitted . . . that same

information may be transmitted . . . by way of telephone lines, or it may be fed into the user’s computer directly by the originator of the program.”<sup>57</sup> These authorities primarily applied the “true object,” “focus of the transaction,” or the “dominant purpose” test.<sup>58</sup>

### Different Types of Software (Customized vs. Canned)

Trying to locate a middle ground, one court, not seeing enough tangible value in the physical manifestation of software on magnetic tapes or discs, found that only operating system software (not application software) should be taxed because it is needed for the computer hardware to function and, even if it is not tangible, enhances the value of hardware, whereas application software should not be so taxed.<sup>59</sup> Yet another court departed from the view that software is intangible by differentiating between those cases in which the customer paid for customization of the program and those in which a program was purchased from a catalog.<sup>60</sup>

<sup>57</sup> *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405, 407 (Tenn. 1976) (citing *Crescent Amusement Co. v. Carson*, 213 S.W.2d 27 (Tenn. 1948)) (superseded by statute as stated in *Lockheed Martin Energy Systems v. Johnson*, 78 S.W.3d 918 (Tenn. 2002)).

<sup>58</sup> See also *Janesville Data Center Inc. v. Wis. Department of Revenue*, 267 N.W.2d 656 (Wis. 1978) (holding coded or processed data is an intangible, and that its embodiment in the cards, tapes or printouts was not the essence of the transaction, which, therefore, was not taxable); *First National Bank of Fort Worth v. Bullock*, 584 S.W.2d 548 (Tex. 1979) (holding “although . . . tapes did change hands, the sale of a license for computer software . . . was the sale of intangible property and, therefore, not taxable”); *Spencer Gifts Inc. v. Director, Division Taxation*, 440 A.2d 104 (N.J. Super. 1981) (holding that leasing of computer mailing lists was not leasing of tangible personal property); *James v. Tres Computer Systems Inc.*, 642 S.W.2d 347 (Mo. 1982).

<sup>59</sup> *CompuServe Inc. v. Lindley*, 535 N.E. 2d 360 (Ohio App. 1987).

<sup>60</sup> *IBM*, 765 S.W. 2d 611, 613; *Maccabees Mut. Life Ins. Co. v. State Department of Treasury*, 332 N.W.2d 561, 563-64 (Mich. App. 1983) (customized computer software programs are different from off-the-shelf or canned software programs because customized programs are akin to a personalized service and are designed to fit a specific client’s needs).

<sup>55</sup> See Colo. Gen. Info. Letter, 2011 WL 10755855, at \*2.

<sup>56</sup> Neb. Rev. Stat. section 77-2701.16; and *A&D Technical Supply Co. Inc. v. Department of Revenue*, 607 N.W.2d 857 (Neb. 2000).

## Software as a Tangible Product Based on The Medium of Delivery

A number of courts refused to see software as something different from recorded music or video.<sup>61</sup> When faced with a response that software is more like an idea or service, some courts noted that every product (a loaf of bread, radio, or car) is the result of the skill and labor or services, and that many physical ingredients that go into the making of a product may not cost as much as the judgment and expertise of the laborers. Nonetheless, if these elements (the cost of ingredients, ideas, etc.) “should be separated from the finished product and the sales tax applied only to the cost of the raw material, the sales tax act would, for all practical purposes be entirely destroyed.”<sup>62</sup>

In *Chittenden Trust Co. v. King*,<sup>63</sup> the court pointed out that the program was designed and sold “off the shelf” and did not involve the type of personal service that was contemplated as nontaxable. The court further found that the tape was tangible and no different from “other taxable personal property such as films, videotapes, books, cassettes and records.”<sup>64</sup> A Maryland court<sup>65</sup> summoned a lot of research questioning the validity of treating software sold on magnetic tapes differently from a book or a movie. The court emphasized that software is not merely an

idea or information and that the recording of information for further transmission is a factor:

Theoretically, a program could exist in the mind of the programmer, but, as a practical matter, programs . . . must be recorded somewhere in some physical representation.<sup>66</sup>

...

The advantage to a computer user of a canned program is that the user need not start from the beginning in developing the particular program. Reinventing the wheel is avoided.<sup>67</sup>

The court then explained that under the dominant purpose test, the object of books, films, video display discs, phono records, and music tapes is also information. These items are nonetheless taxable. Whether it is recorded music or a computer program — these are sets of information in a form that, when passed over a magnetized head, cause minute currents to flow in such a way that desired physical work is accomplished.<sup>68</sup> The physical form of the program, as delivered, was a coded series of magnetic impulses, and it made a difference.<sup>69</sup>

## Software as a Tangible Product Based on Its Nature

A breakthrough in the analysis happened when one court started looking at software beyond the medium through which it is transferred. In *South Central Bell Telephone Co. v. Barthelemy*,<sup>70</sup> the court confronted the issue of whether software was tangible personal property or intellectual property.<sup>71</sup> The court reasoned that Louisiana Civil Code departed from the narrow Roman law concept of tangible objects being corporeal or movable, instead declaring that “perceptibility by any of the senses sufficed for the classification of a material thing as

<sup>61</sup> In *Citizens & Southern Sysms Inc. v. South Carolina Tax Commission*, 311 S.E.2d 717 (S.C. 1984), the court referred to an example of a professor who conveyed knowledge or information in person versus through a published book or a recorded lecture. The court pointed out the delivery of information in a form that could be seen, weighed, measured, felt, or touched qualified it as taxable, stating that taxability should not depend on whether the buyer decides to store the program continuously on the magnetic tape. In *Mark O. Haroldsen Inc. v. State Tax Commission*, 805 P.2d 176 (Utah 1990), despite a compelling case that professional brokers rendered services in preparing mailing lists, the court held that the lease or purchase of mailing lists on paper or magnetic tapes was taxable as a product, and would not escape taxation as a service. The court found that the medium of transferring information was “dispositive,” rejecting suggestions that the existence of tapes should not be given weight because the information on them could have been transferred without using a tangible medium. *Id.* at 180.

<sup>62</sup> *Commerce Union*, 538 S.W.2d 405, 407 (Tenn. 1976) (citing *Crescent Amusement*, 213 S.W.2d 27) (stating that “The material used in the making of a phonograph record probably costs only a few cents. The voice of a Caruso recorded thereon makes it sell for perhaps a dollar. To measure the sales tax only by the value of the physical material in this phonograph record is to apply an impossible formula.” (citation omitted)).

<sup>63</sup> 465 A.2d 1100 (Vt. 1983).

<sup>64</sup> *Id.* at 1102.

<sup>65</sup> *Comptroller of Treasury v. Equitable Trust Co.*, 464 A.2d 248 (Md. App. 1983).

<sup>66</sup> *Id.* at 250.

<sup>67</sup> *Id.*

<sup>68</sup> *Id.* at 261.

<sup>69</sup> *Id.*

<sup>70</sup> 643 So. 2d 1240 (La. 1994).

<sup>71</sup> *Id.* at 1243.

corporeal.”<sup>72</sup> The court observed that more courts had been concluding that software is tangible personal property as their knowledge and understanding of computer software grew, and that computer software has generally been held to constitute “goods” under the Uniform Commercial Code.

The court further explained that the method of storing computer software (or a set of instructions that tells a computer how to do something) is irrelevant, but what is relevant is that the software purchaser does not merely receive knowledge but “a certain arrangement of matter that will make his or her computer perform a desired function,” and that this “arrangement of matter, physically recorded on some tangible medium constitutes a corporeal body.”<sup>73</sup> The court questioned the classification of software as custom or canned, stating that the nature of the software is the same, and that often “the software at issue is mixed.”<sup>74</sup>

Afterward, courts continued to zero in on the idea that software is tangible because it is the “arrangement of matter.” One taxpayer argued that software is not tangible or taxable because it “changes its nature” during the installation when it moves from one medium onto the next.<sup>75</sup> The court rejected the temporary transformation during software installation or transmission, writing:

A software program is a series of magnetic or electronic signals and stored either internally (e.g., in the computer’s hard drive or on the network) or externally (e.g., on floppy discs or magnetic tapes). When read by a computer, this program directs the computer through an arranged series of electronic signals to perform certain functions. . . . The signals themselves [are] not changed or modified but [are] merely transferred from one form of storage media . . . to another . . . Although perhaps difficult to comprehend and perceive at these

microscopic levels, the electronic signals of installed software are tangible.<sup>76</sup>

Adopting *Barthelemy*’s logic, another court stated:

We agree with . . . Louisiana that a purchaser of canned computer software is acquiring more than incorporeal knowledge or an intangible right; rather, the purchaser is acquiring an electronic copy of a computer program that is stored on a computer’s hardware, takes up space on the hard drive and can be physically perceived by checking the computer’s files. It remains in the computer and operates the program each time it is used.<sup>77</sup>

Even electronic transmittal of canned software, without usage of any tangible medium, would not change a court’s conclusion that tangible personal property was transferred.<sup>78</sup>

A taxpayer made an interesting argument in *Ball Aerospace*,<sup>79</sup> suggesting that software downloaded from the internet was not taxable because it was not “contained on cards, tapes, discs, coding sheets, or other machine-readable or human-readable form,” as required by the city ordinance because it did not have any form and was not machine-readable during “the downloading process [which] convert[ed] the software from machine-readable binary code to ‘disaggregated and dispersed electromagnetic signals.’”<sup>80</sup> The appellate court disagreed with the argument that “because the electronic signals comprising the download have no coherent boundary, are fleeting, and are not in binary form during transmission,” the software is not machine-readable.<sup>81</sup> The court stated that “the emphasis on the mode of conveyance is misplaced,” and that what matters is that the software is in the machine-readable form “at the

<sup>76</sup> *Id.* at 223-24.

<sup>77</sup> *Graham Packaging Co. LP v. Commonwealth*, 882 A.2d 1076 (Pa. 2005).

<sup>78</sup> *Dechert LLP v. Commonwealth*, 922 A.2d 87 (Pa. 2007).

<sup>79</sup> *Ball Aerospace & Technology Corp. v. City of Boulder*, 304 P.3d 609 (Colo. App. 2012).

<sup>80</sup> *Id.* at 612.

<sup>81</sup> *Id.* at 613.

<sup>72</sup> *Id.* at 1244.

<sup>73</sup> *Id.* at 1246 (emphasis added).

<sup>74</sup> *Id.* at 1249-50.

<sup>75</sup> *South Central Utah Telephone Association Inc. v. Auditing Division*, 951 P.2d 218 (Utah 1997).



time that the purchaser exercises any right, power, dominion, or control over the software.”<sup>82</sup>

### Level of Usage and Control – Factor in Determining Whether Software is Taxable

In *Auto-Owners Insurance*,<sup>83</sup> the taxpayer and tax authority disagreed as to the meaning of the term “deliver” and whether it includes accessing the functionality of pre-written computer software. The court noted that the plain and ordinary meaning of the term is unclear, and that it is proper to consult a dictionary to determine the plain and ordinary meaning. The court construed the term literally as the delivery of a physical object and sought to determine if the taxpayer received control over the software code. For instance, regarding a legal research database, the court stated that the taxpayer never exercised an ownership-type right or power over any West computer software. Instead, all the code remained on West’s server. West controlled the code, maintained it, and updated it as it saw fit. The taxpayer only accessed a website that allowed it to submit requests to the West system that controlled the code. Accessing West’s code in such a limited manner was determined not to be an exercise of a right or power incident to the ownership of that code, so the taxpayer-plaintiff did not use tangible personal property regarding West and owed no tax.

### Focus on the Value Received, Not the Method Of Delivery

While many jurisdictions have struggled with the issue of whether software is similar to movie film or a record player, one jurisdiction appears to have avoided this discussion by focusing from the outset not on the form of the object — a method of conveyance — but the ultimate value of the invisible sound as sufficient proof that a customer received tangible product. In *State v. Jones*,<sup>84</sup> the customer inserted a coin in the slot, pressed a button indicating the record desired and the machine played it. The court considered whether the playing of the record was a taxable sale of tangible personal property. As in many other

states, the Arizona statute provided that the term “tangible personal property” means personal property that may be seen, weighed, measured, felt, touched, or is in any other manner perceptible to the senses. The court held that the playing of the record was perceptible to the sense of hearing and, hence, constituted what the statute termed tangible personal property. The court explained:

If the machine were one in which a coin were inserted and the customer received in return a package of candy, gum or other article of merchandise, there would be no question but that the transaction would constitute a sale of tangible personal property. But is it a sale of tangible personal property when all the customer secures for his money is the pleasure of hearing the phonograph play a record?<sup>85</sup>

The court concluded that the statute could not have more effectively made the playing of the record, in response to the coin placed in the slot, the sale of tangible personal property if it had made a special provision covering the situation.

Whether through a remarkable insight or a mere coincidence, almost 80 years ago, in 1943, in a transaction involving a physical object and intellectual property (copyrighted song), at least one state’s highest court did not focus on whether the object (either a jukebox or a copyrighted song) was tangible personal property but rather on whether the transaction was taxable because the sound was “perceptible to sense” and therefore constituted tangible personal property. The court held in favor of taxability. Under this approach, the method of delivery of tangible personal property would not change the taxability determination.

### The Difference Between Transferring an Idea And Transferring a Product

Unlike a license to use software or a movie and ideas encapsulated therein as a “finished product,” a person may enter into a broader licensing agreement that authorizes it to use content in the course of its business. Such purchases may be accompanied by a physical

<sup>82</sup> *Id.*

<sup>83</sup> *Auto-Owners Insurance Co. v. Department of Treasury*, 880 N.W.2d 337, 345 (Mich. App. 2015).

<sup>84</sup> 137 P.2d 970 (Ariz. 1943).

<sup>85</sup> *Id.*

object, but under those circumstances, jurisdictions may see no occasion for imposing a tax as if it were the sale of a product. In *City of Boulder v. Leanin' Tree Inc.*,<sup>86</sup> a company borrowed artwork from original artists and received the right to reproduce and publish the images on the greeting cards it manufactured. The court noted that the transaction “never permitted [taxpayer] to keep, sell, display, or otherwise benefit from the artwork as a finished product.” Indeed, in that case, the company was paying for an idea or image that it copied, creating its own product, and it paid the artist royalties as a percentage of the revenues it received for the product. The court held that the taxpayer did not purchase a tangible product but indeed acquired an intangible right.

### Conclusion

The discussion about whether computer software sold on magnetic tape is like a movie sold on film seems rather outdated yet helpful. A notion of the earlier courts that, unlike software, movie film cannot be separated or viewed without a physical tape is no longer accurate. A radio wave or a television signal no longer needs cable wires or air waves (analog signals) for transmission. The infinite analog signals (waves) are now converted into digital signals (bits) that occupy less space and can be transmitted faster over the internet. Digital information (whether visual, audio, audiovisual, or a set of signals) can be stored and transferred without any tangible medium and can be used even if it does not reside on any

device of the user but is accessed through the hardware or cloud where this information is stored.<sup>87</sup>

Thus, music, motion pictures, digital pictures, or software no longer need to be on a tangible medium to be able to be heard, viewed, or otherwise used. There are several characteristics that unite these digital goods into one category:

- These products result from an idea, knowledge, or information recorded in some tangible form (whether it is an image, video, audio, or a set of instructions) whether analog or digital.
- Once digitally recorded, these products can be stored, copied, and offered to the public for usage and consumption.
- These products can be transferred to the user in a variety of ways: via a tangible medium, load and leave, download, streaming, or through access to a host computer on which these products are stored.
- The usage of products requires a certain amount of storage space, and depending on their size and complexity, these products may be offered for use coupled with real-time or periodic upgrades and other products or functionalities.

One difference is that while some digital products merely consist of data or information that is in the nature of content, others (that is, software) consist of data or information that is in the nature of a process or tool — it allows the processing and use of content information. Because software can perform data processing functions, the industry has coined a term for it:

<sup>87</sup> Adorama Learning Center, “Analog vs. Digital Audio: What’s the Difference?” (Dec. 17, 2018):

The easiest way to explain the recording processes of analog and digital audio is to think of them as “steps” rather than two completely different methods. Analog audio was born during the earliest technologies of sound recording. The process involves using a microphone to turn air pressure or sound into electrical analog signals and imprinting them directly on analog tapes (large reels and cassettes) through magnetization or on vinyl records through its spiral “grooves.” Interestingly, digital audio recording also requires the step of turning sound into an electric analog signal, except it extends the process to convert that analog signal into digital, or as a series of numbers that digital software (like those found in your computer or mp3 player) can read and reproduce. This digital form of audio is then easily copied onto compact disks, hard drives, or uploaded online for widespread playback.

<sup>86</sup> 72 P.3d 361 (Colo. 2003).

“software as a service,” or SaaS. This term, however, is not to be confused with the services provided to develop software to fit custom needs or other professional or individualized services that many states do not tax. The term SaaS should be viewed as reflective of software as a type of digital good that offers more than content but also functions that could be used for content creation, development, processing, or automating tasks that previously may have required human effort, judgment, or expertise but can now be reduced to a set of standardized instructions.

Yet given the above struggle on what the main purpose of the transaction may be and how intellectual property is shared or used, many jurisdictions have opted not to give the same tax treatment to software and other digital goods. The decision regarding tax treatment of digital goods appears to be based on the goods’ nature or function, their method of delivery or transfer or storage, and the level of control the recipient can exercise over the digital good.

Not all states seek to develop their regulation of digital goods and services using the inventory approach. A few states have not defined each specified digital product as taxable and yet have been able, based on their laws, to subject digital products to sales, use, or similar excise tax. Such approaches are used in states that include Hawaii, which taxes most goods and services, and New Mexico. Nebraska declares that it taxes intellectual and entertainment property, which covers most digital goods. Florida can tax many digital goods by taxing communication services, and Arizona has had a case law under which transmission of sound is viewed as a taxable retail transaction. Still, both software companies and entertainment companies (Netflix, Hulu, etc.) are convinced that unless their precise product, including its method of delivery, is described in a state’s laws, they are not subject to its sales and use tax obligations.

While this position rewards development of new technology, it necessarily complicates the ability of legislatures and administrative agencies to respond to technological changes and keep the cost of tax administration low. Rather than focusing on the types of computer-related products, digital products, and the mechanisms in which they are delivered and sold, the conceptual

approach would rely on the analysis of not the type of product and its sub-variety based on the method of invoicing or delivery chosen by a business but by the ultimate value received by the end-user. If the value is in the nature of a product, it is taxed, but if it is in the nature of a professional or manual service customized for each customer it is not taxed.

The term “digital goods” encompasses the transfer of value containing the elements of both products and services. Contrary to the suggestion that the line between products and services is so blurred that it is impossible to determine whether a customer receives a product or service, it does not require a grasp of sophisticated technologies to make the distinction. In most transactions, it is possible to determine whether the main value delivered to a customer is in the nature of either (1) a finished product that is ready to be used by a consumer independently, without involvement of a professional or (2) a customized service or experience that requires reliance on the professional judgment of a service provider. After all, the term “service” has servant or serf in its root, which implies human (not machine) labor. With that in mind, digital goods may be grouped into one of the following categories:

- Potential Products
  - Raw Data
  - digital information or content generated by a customer;
  - digital information generated by algorithms/software; and
  - digital information or content generated by others.
- Software: Functional, Command, or Procedural Data:
  - digital programs (applications, software, algorithms, codes).
  - digital content — audio materials (audio books, podcasts, music);
  - digital content — visual materials (e-books, e-articles, blogs, pictures, graphs, maps); and
  - digital content — audiovisual materials (movies/videos).
- Intellectual or Substantive Data
  - digital content — audio materials (audio books, podcasts, music);

- digital content — visual materials (e-books, e-articles, blogs, pictures, graphs, maps); and
- digital content — audiovisual materials (movies/videos).
- Services
  - Product Development: services to create software;
  - Product Management: services to assist in usage of data or data processing;
  - Product Maintenance: updating canned software or applications; and
  - Product Storage: services to store or maintain data.

**Suggested Principles for Taxability**

Based on the mainstream approach in most states, tax authorities may opt to tax products but not services, with the term “service” narrowly defined as a transaction the primary value (and direct cost) of which is the direct or manual labor of a professional or individual.

**Table 4.**

Tax	No Tax
Receipt of or access to data generated by others	Access to one’s own data (web hosting or cloud storage of data generated by the user)
Receipt of or access to digital content or products generated by others	Professional services to create digital content or products for a specific customer, or professional creation of customized software
Receipt of or access to software or functions performed by software or algorithms	Services of analyzing or processing data if performed by a professional for a specific customer
Renting access to hardware or servers at a data center; housing, web hosting, cloud storage for purposes of gaining access to or storing items described above (first three items).	Renting access to hardware or servers at a data center; housing, web hosting, cloud storage for purposes of personal data or one’s own data.

**Taxability of Digital Goods and Services In Each State**

**Alabama**

Alabama<sup>88</sup> is not a SSUTA state and lacks guidance on its website. Based on litigated decisions, Alabama taxes both pre-written and custom computer software products. However, the services associated with developing software would not be taxable if separately invoiced.<sup>89</sup> There is no express guidance on whether Alabama would tax SaaS, but it appears that SaaS is considered a nontaxable service if the purchaser does not download or possess the software code, but only accesses the software hosted on seller’s servers. Notably, Alabama makes no mention of other digital goods, leaving it unclear if they are taxable in Alabama.

Effective in 2020, Alabama amended its rules to state it no longer uses the distinction between canned and custom software. There is also an interesting clarification that licensing of software is retail, not rental. Importantly, the rule states that the “form of transmission” of software does not alter taxability (it is still unclear if accessing software via cloud computing constitutes transmission).

**Arizona**

Arizona<sup>90</sup> is not a SSUTA state. Like Hawaii, Arizona’s approach has been that some periodic and often rapid changes in technology should not change taxability of tangible personal property, which has been construed broadly, based on the Arizona Supreme Court’s long-standing precedent in *State v. Jones*.<sup>91</sup> The Arizona Supreme Court analyzed whether paying to hear a song from a jukebox (phonograph) was the sale of tangible personal property. The court did not focus on whether the jukebox was tangible

<sup>88</sup> Ala. Code sections 45-8-241.60 (Definitions), 45-2-244.180 (Definitions), and 40-23-67 (Seller to collect tax; seller not to assume or absorb tax); and Ala. Admin. Code 810-6-1-.37 (Computer hardware and software).

<sup>89</sup> See *Ex parte Russell County Community Hospital LLC, \_\_So.3d\_\_,* 2019 WL 2150922, at \*3 (Ala. 2019) (“If the costs of such services are separately stated and invoiced, they are nontaxable.”).

<sup>90</sup> Ariz. Rev. Stat. sections 42-5001 (Definitions); 42-5061 (Retail classification); 42-5071 (Personal property rental classification).

<sup>91</sup> 137 P.2d 970 (Ariz. 1943).

personal property, but rather on whether the transaction was taxable because the sound was “perceptible to sense” and therefore constituted the tangible personal property. The court held in favor of taxability. Under this approach, the method of delivery of tangible personal property would not change the taxability determination. Arizona’s approach, which has been built over the intervening decades and supplemented by municipal privilege tax codes, has been met in the last few years with legislative attempts to explicitly address definitions, sourcing and taxability and litigation. While legislative efforts have been frustrated by a lack of stakeholder consensus and the indeterminacy of fiscal impacts, the stakes have grown following the constitutional amendment passed in 2018 that bars the state and municipalities from increasing tax rates or imposing new taxes on services.

### Arkansas

Arkansas<sup>92</sup> is a SSUTA state. Its website does not provide any specific guidance about the taxability of its digital goods. Arkansas levies an excise tax on gross receipts derived from sales of items including tangible personal property, specified digital products sold, digital codes, and enumerated services including cable television, community antenna television, and other distribution of television, video, or radio services with or without the use of wires provided to subscribers or paying customers or users.<sup>93</sup> Arkansas’s definition of tangible personal property does not include specified digital goods, which are separately taxed. The term tangible personal property includes pre-written computer software. Arkansas taxes pre-written computer software but not if it is delivered electronically. The statute provides that “‘computer software’ does not include software that is delivered electronically or by load and leave.”<sup>94</sup> Thus, electronically delivered or remotely accessed software is not taxed in Arkansas.

<sup>92</sup> Ark. Code Ann. sections 26-53-102 (Definitions), 26-52-301 (Excise tax levied), 26-52-304 (Tax levied on sales of computer software and maintenance), 26-52-315 (Telecommunications).

<sup>93</sup> Ark. Code Ann. section 26-52-301.

<sup>94</sup> Ark. Code Ann. section 26-52-304.

The law to tax specified digital goods was passed in 2017. These products are taxed whether the seller gives the consumer permanent use or less-than-permanent use.<sup>95</sup> Streaming is specifically taxed as the service of cable television.<sup>96</sup>

### California

California<sup>97</sup> is not a SSUTA state. Except for in some municipalities, California does not tax digital goods unless they are on a tangible medium such as a CD. California’s statutory definitions of computers and programs are rather elaborate — yet mostly these items are nontaxable.<sup>98</sup> California is primarily interested in tax on storage media defined as “hard disks, floppy disks, diskettes, magnetic tape, cards, paper tape, drums and other devices upon which information is recorded.”<sup>99</sup> Charges for the transfer of computer-generated output are subject to tax when the true object of the contract is the output (artwork, graphics, and designs) and not the services rendered in producing the output.<sup>100</sup> SaaS is expressly not taxable.<sup>101</sup>

However, “tax applies to the sale or lease of the storage media or coding sheets on which or into which such prewritten (canned) programs have been recorded, coded, or punched.”<sup>102</sup> California addresses manipulation of customer-furnished information as a sale or service, taxing conversion of customer-furnished data from one physical form to another form of recording.<sup>103</sup> It even taxes situations in which “a data processing firm’s agreement provides only for data entry, data verification, and proof listing of data, or any combination of these operations,” irrespective of

<sup>95</sup> Ark. Code Ann. section 26-52-301.

<sup>96</sup> Ark. Code Ann. section 26-52-301(C)(i).

<sup>97</sup> Cal. Rev. & Tax Code sections 6016 (Tangible personal property), 6051 (Levy on retailers’ gross receipts; rate), 6378 (Tangible personal property purchased for use in teleproduction), Cal Code Regs. tit. 18, section 1502 (Computers, Programs and Data Processing).

<sup>98</sup> Cal. Rev. & Tax Code section 6051.

<sup>99</sup> Cal Code Regs. tit. 18 section 1502.

<sup>100</sup> Cal Code Regs. tit. 18 section 1502(c)(4).

<sup>101</sup> Cal Code Regs. tit. 18 section 1502(c)(7)(“Charges made for the use of a computer, on a time-sharing basis, where access to the computer is by means of remote telecommunication, are not subject to tax.”)

<sup>102</sup> Cal Code Regs. tit. 18 section 1502(f)(1).

<sup>103</sup> Cal Code Regs. tit. 18 section 1502(d)(1).

whether “the storage media are furnished by the customer or by the data processing firm.”<sup>104</sup>

California’s rules are too detailed (dissecting taxation or nontaxation of copying, address label printing, and so forth) and complex to be summarized here more fully.

### Colorado

Colorado<sup>105</sup> is not a SSUTA state and does not tax software unless it is pre-written and sold in a tangible medium. Colorado specifically states that:

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.<sup>106</sup>

Interestingly, Colorado taxes digital goods, even though it does not have a specific statute.<sup>107</sup>

### Connecticut

Connecticut<sup>108</sup> is not a SSUTA state and has recently enacted changes, effective January 1, 2020. The state provides clear guidance and taxes all known digital goods — software and digital content, including streaming content (Connecticut uniquely offers a significantly lower, 1 percent, tax rate for digital goods accessed electronically, which is referred to as data processing).<sup>109</sup> The definition of tangible personal

property is broad and all encompassing.<sup>110</sup> Connecticut states that a transfer of a digital product will be treated in the same way as accessing it. While telecommunications services are treated as their own category of taxable services, Connecticut taxes community antenna television service and certified competitive video service — all manner of streaming and broadcasting digital content.<sup>111</sup> Connecticut also taxes “computer and data processing services, including, but not limited to, time, programming, code writing, modification of existing programs, feasibility studies and installation and implementation of software programs and systems even when such services are rendered in connection with the development, creation or production of canned or custom software or the license of custom software, but excluding digital goods.”<sup>112</sup>

### District of Columbia

The District of Columbia<sup>113</sup> is not a SSUTA member and is among a handful of jurisdictions that tax all types of software, both pre-written and customized. Favoring taxability, the District makes digital goods taxable whether they are electronically or digitally delivered or accessed. The term “digital goods” excludes “cable television service, satellite relay television service, or any other distribution of television, video, or radio service.” However, the District imposes tax on companies that sell or charge for cable television service, satellite relay television service, and any and all other distribution of television, video, or radio service under section 47-2501.01. Put simply, the District taxes all software and the streaming of digital products and live broadcasting, although the last is taxable as telecommunication or a type of utility, not as a digital product. Software is not found under the definition of “digital goods” but rather under data processing services. The District of Columbia

<sup>104</sup> Cal Code Regs. tit. 18 section 1502(d)(2).

<sup>105</sup> Colo. Rev. Stat. Ann. sections 39-26-104 (Prop. and serv. taxed-definitions-repeal), 39-26-102 (Definitions), Gen. Info. Letter, 2011 WL 10755855.

<sup>106</sup> Colo. Rev. Stat. Ann. section 39-26-102(c)(I).

<sup>107</sup> See Gen. Info. Letter, 2011 WL 10755855, at \*2 (“Colorado levies sales and use tax on the sale, use, storage, or consumption of tangible personal property. Intangible personal property is conceptual in nature, such as a contract, stock, and goodwill. When we speak of digital goods, we are referring not to a concept but, rather, to something that exists in the physical world. Just as a digital song or digital photograph stored and played or displayed on an electronic device is physical property that is perceptible by the senses, a newspaper electronically delivered is also part of the physical world.”); see also Gen. Info. Letter, 2015 WL 9702390, at \*1 (“We do not believe that transferring the photographs electronically renders the photographs intangible.”).

<sup>108</sup> Conn. Gen. Stat. sections 12-407 (Definitions), 12-408 (Sales tax).

<sup>109</sup> Connecticut Department of Revenue, SN 2019(8), “Sales and Use Taxes on Digital Goods and Canned or Prewritten Software” (Sept. 4, 2019).

<sup>110</sup> Conn. Gen. Stat. Ann. section 12-407(13).

<sup>111</sup> Conn. Gen. Stat. Ann. section 12-407(27), (39).

<sup>112</sup> Conn. Gen. Stat. Ann. section 12-407(37)(A).

<sup>113</sup> D.C. Code Ann. sections 47-2001 (Definitions), 47-2002 (Imposition of tax), 47-2501.01 (Television, video, or radio service to subscribers or paying customers); D.C. Mun. Regs. tit. 9, sections 474 (Data Processing Services), 475 (Information Services).

Office of Tax and Revenue website offers helpful and easy-to-follow guidance.<sup>114</sup>

## Florida

Florida<sup>115</sup> is not a SSUTA state and does not tax software of any kind but it taxes streaming video content not under its sales tax but under its communications services tax (CST).<sup>116</sup> The CST base rate is 7.44 percent (two percentage points higher than the base sales tax rate). The Florida DOR provides some guidance on its website.<sup>117</sup>

SaaS is nontaxable in Florida when it is only a service transaction and is not accompanied by the transfer of tangible personal property. However, the DOR has ruled that when a video service (or other communications service) bundled with other services for billing purposes is not separately allocable in the taxpayer's books and records, the entire fee is subject to the CST.<sup>118</sup>

## Georgia

Georgia<sup>119</sup> is a SSUTA state. Georgia is similar to California and Colorado in that it does not tax software unless it is sold in a tangible physical form.<sup>120</sup> Cloud subscription services allowing customers to access and use vendor software via the internet are also not among the enumerated

taxable services and are therefore not subject to sales and use tax.<sup>121</sup>

## Hawaii

Hawaii<sup>122</sup> is not a SSUTA state. Even in the absence of a specific definition or description of digital goods, Hawaii's regulations state that Hawaii law subjects nearly every economic activity to the general excise tax. Hawaii's general excise tax applies to all nonexempt goods and services, and SaaS is considered a nonexempt service, with Hawaii awaiting any contrary further clarification from Congress.<sup>123</sup>

## Idaho

Idaho<sup>124</sup> is not a SSUTA state. It has detailed guidance in its statutes and administrative code, and the Idaho Tax Commission provides links to both legal resources.<sup>125</sup> Idaho imposes an excise tax on retail sales, taxing tangible personal property, which includes computer software.<sup>126</sup> The term "computer software" excludes custom software and software remotely accessed or delivered via load and leave method,<sup>127</sup> but it does include digital music, books, videos, and games if transferred permanently.<sup>128</sup> Regarding digital products, Idaho regulations provide that: "Digital music, digital books, digital videos, and digital games are tangible personal property regardless of the delivery or access method but only if the purchaser has a permanent right to use the digital music, digital books, digital videos, or digital games," and that "leases or rentals of these digital products are not taxable."<sup>129</sup> Streaming is not

<sup>114</sup> D.C. Office of Tax and Revenue, "Taxation of Digital Goods in the District of Columbia" (Jan. 3, 2019); and "Taxable and Non-Taxable Services."

<sup>115</sup> Fla. Stat. Ann. section 212.02 (Definitions).

<sup>116</sup> Fla. Stat. Ann. section 202.12. "Sales of communications services in Florida are taxable, unless specifically exempt. Communications services are defined as voice, data, audio, video, or any other information or signals, transmitted by any medium." Specifically enumerated taxable communications services include local, long distance, and toll telephone; Voice over Internet Protocol (VoIP) telephone; video service whether provided by a cable, telephone, or other communications services provider; direct-to-home satellite; mobile communications; private line services; pager and beeper; telephone charges made at a hotel or motel; fax, when not provided in the course of professional or advertising service; telex, telegram, and teletype. The definition of "video service" includes "basic, extended, premium, pay-per-view, digital video, two-way cable, and music services."

<sup>117</sup> Florida Department of Revenue, Florida Communications Services Tax.

<sup>118</sup> Florida Department of Revenue Technical Assistance Advisement No. 14A-010 (Apr. 7, 2014).

<sup>119</sup> Ga. Code Ann. sections 48-8-2 (Definitions), 48-8-30 (Imposition of tax; rate); Ga. Comp. R. and Regs. r. 560-12-2-.111(3); Ga. Comp. R. and Regs. r. 560-12-2-.24 (Communication Services).

<sup>120</sup> Georgia Department of Revenue, Letter Ruling SUT No. 2014-02-20-01; see also LR SUT-2018-10 (software); LR SUT-2017-04 (services, software and online courses); and LR SUT-2016-09 (software).

<sup>121</sup> *Id.*

<sup>122</sup> Haw. Rev. Stat. Ann. section 237-13.

<sup>123</sup> See Hawaii Letter Ruling 2012-06 (Mar. 23, 2012) (citing *Matter of Grayco Land Escrow Ltd.*, 559 P.2d 264, 270 (Haw. 1977)) ("The statute evidences the intention of the legislature to tax every form of business, subject to the taxing jurisdiction, not specifically exempted from its provisions.")

<sup>124</sup> Idaho Code sections 63-3616 (Tangible personal property); 63-3619 (Imposition and rate of the sales tax); Idaho Admin. Code sections 35.01.02.02, 35.01.02.027.

<sup>125</sup> Idaho Sales and Use Tax Administrative Rules.

<sup>126</sup> Idaho Code section 63-3619.

<sup>127</sup> Idaho Admin. Code section 35.01.02.027 ("04. Remotely accessed computer software is not tangible personal property and charges to use or access such software are not subject to tax. (4-11-15)").

<sup>128</sup> Idaho Admin. Code section 63-3616.

<sup>129</sup> Idaho Admin. Code section 35.01.02.02.

taxed.<sup>130</sup> Also, Idaho published a statement by Netflix on its website explaining why it provides a service and is not taxable.<sup>131</sup>

### Illinois

Illinois<sup>132</sup> is not a SSUTA state. The Illinois DOR provides guidance through detailed regulations and private letter rulings. Illinois statute provides that “a tax is imposed upon persons engaged in the business of selling at retail tangible personal property [TPP], including computer software.”<sup>133</sup> The term “computer software” is defined as “all types of software,” and, further, that only “canned software is considered to be tangible personal property regardless of the form in which it is transferred or transmitted, including tape, disc, card, electronic means or other media.”<sup>134</sup> Yet SaaS is considered a nontaxable service.<sup>135</sup> Chicago has a separate provision taxing streaming.<sup>136</sup>

### Indiana

Indiana<sup>137</sup> is a SSUTA state with clear and detailed guidance on taxability of digital goods and services provided in its 24-page Information Bulletin #8.<sup>138</sup> Indiana imposes tax on the retail merchant’s gross revenue from any combination

of: the sale of tangible personal property that is delivered into Indiana; a product transferred electronically into Indiana; or a service delivered in Indiana.<sup>139</sup> Tangible personal property includes pre-written computer software (including software electronically transferred or software obtained via load and leave). In its Information Bulletin, the DOR explained that:

(1) As of July 1, 2018, prewritten computer software sold, rented, leased, or licensed for consideration that is remotely accessed over the internet . . . is not considered an electronic transfer of computer software and is not considered a retail transaction. . . . (2) Any payments made prior to July 1 for remotely accessed software are not eligible to be refunded, including payments encompassing periods occurring after July 1, unless another reason is provided for the refund request. The term “transferred electronically” means obtained by a purchaser by means other than tangible storage media.<sup>140</sup>

The term “specified digital products” is separately defined as electronically transferred: digital audio works; digital audiovisual works; or digital books, but only if transferred to allow for permanent use.<sup>141</sup> Electronic transfer of specified digital products is defined to occur when the vendor “grants to the end user the right of permanent use of the specified digital products that is not conditioned upon continued payment by the purchaser.”<sup>142</sup> Radio, video, or cable television services are taxable retail service transactions.<sup>143</sup>

<sup>130</sup> Idaho Admin. Code section 35.01.02.027 (“07. Digital subscriptions are not taxable. (3-25-16”).

<sup>131</sup> Idaho State Tax Commission, “Statement by Netflix, Inc. — Sales Tax Rule 027.”

<sup>132</sup> Ill. Comp. Stat. Ann. 110 section 26/5 (Definitions), 35 section 105/3 (Tax imposed), 35 section 120/2; Ill. Admin. Code tit. 86, section 130.1935 (Computer Software).

<sup>133</sup> Ill. Comp. Stat. Ann. 35 section 105/3.

<sup>134</sup> Ill. Admin. Code tit. 86, section 130.1935.

<sup>135</sup> ST 11-0052-GIL (06/30/2011) (“Information or data that is electronically transferred or downloaded is not considered the transfer of [TPP],” and “if a company provides access to a database of information and does not transfer any software or other tangible personal property to its customers,” the company would not incur any tax).

<sup>136</sup> Chicago Mun. Code section 4-156-020(G1) (added Nov. 21, 2017); *Labell v. City of Chicago*, 2019 WL 6258401 (Ill. App. 2019) (upholding constitutionality of the municipal streaming services tax).

<sup>137</sup> Ind. Code Ann. sections 6-2.5-1-26.5 (Specified digital products), 6-2.5-1-27 (Tangible personal property), 6-2.5-1-27.5 (Telecommunication), 6-2.5-1-28.5 (Transferred electronically), 6-2.5-2-1 (State gross retail tax), 6-2.5-4-10 (Rental or leasing of personal property), 6-2.5-4-16.4 (Electronic transfer of specified digital products), 6-2.5-4-11 (Radio, cable or satellite television service), 6-2.5-4-16.7 (Transactions involving right to use pre-written computer software delivered electronically), 6-2.5-4-17 (Maintenance contract).

<sup>138</sup> Indiana Department of Revenue, “Information Bulletin #8” (Dec. 2019).

<sup>139</sup> Ind. Code Ann. section 6-2.5-2-1.

<sup>140</sup> Ind. Code Ann. section 6-2.5-1-28.5.

<sup>141</sup> Ind. Code Ann. section 6-2.5-1-26.5.

<sup>142</sup> Ind. Code Ann. section 6-2.5-4-16.4.

<sup>143</sup> Ind. Code Ann. section 6-2.5-4-11(a) (A person is a retail merchant making a retail transaction when the person furnishes cable television or radio service or satellite television or radio service that terminates in Indiana.).



## Iowa

Iowa<sup>144</sup> is not a SSUTA state. It implemented new laws in January 2019. The DOR website states:

Before January 1, 2019, prewritten computer software was subject to sales tax if it was delivered via a disc or other tangible medium but exempt if delivered in an electronic form. Also exempt was the service of creating custom software. Beginning January 1, 2019, prewritten computer software is subject to sales tax whether delivered or accessed in physical form (as tangible personal property) or electronically (as a specified digital product). In addition, custom software sold in either physical or electronic form is taxed in the same manner as prewritten computer software.<sup>145</sup>

The Iowa DOR provides excellent guidance on taxation of digital products. The scope of taxability is very broad. The logic of why Iowa taxes digital goods is revealed through a hypothetical, provided in DOR guidance, in which two types of webinar course are sold: one in which participants have fewer rights than in-person participants, and the other in which participants have the same rights, such as the ability to participate live. According to Iowa, the first “passive” webinar is treated as a digital product and is taxable, whereas the second “active” webinar is treated as experience and is not taxable.

Additionally, Iowa taxes electronically transferred products (transferred by any means), information services, services related to operating specified digital products, and storage. Rather than adding the term “access” to the definition of software to capture taxability of SaaS, Iowa uses the definition of electronically transferred as “obtained or accessed by the purchaser by means other than tangible storage media, including but not limited to a specified

<sup>144</sup> Iowa Code Ann. sections 423.1 (Definitions), section 423.2 (Tax imposed), 423.3 (Exemptions); Iowa Admin. Code 701-224.3(423) (Imposition of tax), 701-18.34(422), (423) (Automatic data processing).

<sup>145</sup> Iowa Department of Revenue, “Taxation of Specified Digital Products, Software, and Related Services.”

digital product purchased through a computer software application, commonly referred to as an in-app purchase, or through another specified digital product, or through any other means.”<sup>146</sup> However, Iowa exempts from taxation SaaS if sold to a commercial enterprise for use exclusively by the commercial enterprise.<sup>147</sup> Iowa taxes pay television, streaming video, video on demand, and storage of electronic records.

## Kansas

Kansas<sup>148</sup> is a SSUTA state. In Kansas, tangible personal property includes pre-written computer software “regardless of the method by which the title, possession or right to use the tangible personal property is transferred.” However, SaaS is nontaxable, and SaaS providers are referred to as application service providers.<sup>149</sup> Kansas does not define digital goods. Streaming and digital goods delivered electronically are not taxable. However, Kansas taxes cable and similar services.<sup>150</sup>

## Kentucky

Kentucky<sup>151</sup> is a SSUTA state and is not as clear in its guidance on digital goods, referring to them as digital property. Still, all the elements appear to be in place to require taxpayers in Kentucky to collect tax for pre-written software and for both SaaS and streaming service. While Kentucky clearly covers pre-written software, it does so under the definition of retail sales. Kentucky clarifies statutorily that the levy on the

<sup>146</sup> Iowa Code Ann. section 423.1(55B)(4).

<sup>147</sup> Iowa Code Ann. section 423.3(104).

<sup>148</sup> Kan. Stat. Ann. sections 79-3602 (Definitions), 79-3603 (Retailers’ sales tax imposed; rate).

<sup>149</sup> Kansas Department of Revenue, “Revised Sales Tax Guidelines: Taxing Charges for Computer Products and Services and Internet Related Sales and Services” (July 23, 2010).

<sup>150</sup> Kan. Stat. Ann. section 79-3603(k).

<sup>151</sup> Ky. Rev. Stat. Ann. sections 136.602 (Definition), 136.604 (Excise tax; multichannel video programming services; rate-sourcing rule), 139.010 (Definitions), 139.195 (Definition), 139.200 (Imposition of sales tax), 139.215 (Taxation of bundled transactions).

retail sale applies regardless of whether the purchaser has the right to permanently use the property or to access or retain the property, even if not permanently.<sup>152</sup>

### Louisiana

Louisiana<sup>153</sup> is not a SSUTA state. It offers an elaborate definition of tangible personal property. For example, it is not coins, repair of vehicles, information, or work product written on paper or magnetic or optical media, and, starting 2005, the definition does not include custom computer software. Yet Louisiana's guidance appears to be under review and is not entirely clear. In its Revenue Ruling No. 10-001, Louisiana stated that tangible personal property:

includes . . . all electronically delivered products, including computer software and applications . . . [and] are not limited to, remotely accessed software, information materials, and entertainment media or products, whether as a one-time use or through ongoing subscription, and whether capable of only being viewed, or being downloaded when that transfer requires payment of consideration in any form."<sup>154</sup>

However, this ruling was later suspended. Based on Revenue Information Bulletin No. 11-005 (Feb. 14, 2011), only the sale and use of:

a downloaded digital product such as music, a movie, book or game is a taxable transaction. These transactions fall within the definition of tangible personal property found in LAC 61:I.4301 Tangible Personal Property.

<sup>152</sup> Ky. Rev. Stat. Ann. section 139.200. Different from other states, the term "digital property" does not include movies or audiovisual works (only digital audio works, digital books, finished artwork, digital photographs, periodicals, newspapers, magazines . . . video games . . . any digital code), section 139.010(10) (a), (b) still the streaming of movies appears taxable under multichannel video programming services (which include cable, satellite, internet protocol, and video streaming).

<sup>153</sup> La. Rev. Stat. Ann. section 47:301 (Definitions), 47:321 (Imposition of tax); La. Admin. Code tit. 61, Pt I, section 4301 (Uniform Sales and Local Sales Tax Definitions); *South Central Bell*, 643 So.2d 1240; and *Normand v. Cox Communications*, 167 So.3d 156 (La. App. 2014) (pay per view is an exempt cable service, not rental of tangible personal property).

<sup>154</sup> Louisiana Revenue Ruling No. 10-001 (Mar. 23, 2010).

Thus, it appears that only downloaded digital goods currently qualify as taxable.

### Maine

Maine<sup>155</sup> is not a SSUTA state. Maine Revenue Services has helpful guidelines on its website.<sup>156</sup> In Maine, tangible personal property includes any computer software that is not a custom computer software program, and any "product transferred electronically." The electronic transfer term is not broadly construed. For example, "the sale of a digital copy of a publication is taxable provided the publication is downloadable to the subscriber's electronic device. If the subscriber is allowed only to access and view an online version of the publication and the digital copy may not be downloaded, the subscription is not taxable." Cable, satellite, and radio are taxable services.

### Maryland

Maryland<sup>157</sup> is not a SSUTA state. The Comptroller of Maryland lists tangible personal property and services subject to sales tax on its website.<sup>158</sup> Maryland has a narrow definition of tangible personal property, referring to it as corporeal personal property. The sale of canned software products is subject to sales and use tax if it is accessed by physical medium such as a CD-ROM or load-and-leave software. The sales and use taxes do not apply to the sale of a digital product unless the buyer has the right to receive tangible personal property. Maryland lists digital products, the sale of which are not subject to sales and use tax:

- canned computer software accessed electronically through digital download;
- mobile applications (apps);
- in-app purchases;
- satellite radio services and subscriptions;
- SaaS;

<sup>155</sup> Me. Rev. State. Ann. tit. 36 section 1752 (Definitions), section 2552 (Tax imposed).

<sup>156</sup> Maine Revenue Services, Sales, Fuel, and Special Tax Division General Information Bulletin No. 104 (June 1, 2014) (discussing taxation of "products transferred electronically"); and A Reference Guide to the Sales and Use Tax Law (Oct. 2018).

<sup>157</sup> Md. Ann. Code sections 11-101 (Definitions), 11-102 (Tax imposed on retail sales, use of tangible personal property, or taxable services).

<sup>158</sup> Comptroller of Maryland, "List of Tangible Personal Property and Services Subject to Sales and Use Tax" (Apr. 1, 2020).

- video and audio including downloads, subscriptions, and streaming services; and
- video games accessed electronically through downloads, subscriptions, and streaming services.

Pay-per-view television service is identified as a separately taxable service.<sup>159</sup> In sum, Maryland only taxes software delivered on a tangible medium, does not specifically address digital goods, and taxes only canned software delivered on tangible media.

## Massachusetts

Massachusetts<sup>160</sup> is not a SSUTA state and provides detailed guidance on taxation of software.<sup>161</sup> Massachusetts is unique in that it gives very detailed guidance on software, but not so much on digital products (video and audio content). Whereas the method of delivery apparently does not matter for software, it does for other digital goods. Massachusetts does not define tangible personal property to include software, but rather states that “the transfer” of standardized computer software “shall be considered” a transfer of tangible personal property.<sup>162</sup> Importantly, the transfer may occur electronically, telephonically, or similarly.<sup>163</sup> Also, the term lease is defined broadly, as any “temporary transfer of possession or control for consideration, regardless of how the transfer is characterized by the parties.” The state differentiates between a license and a lease, stating that “unlike a lease, a licensing arrangement may or may not be time limited.” Also, Massachusetts shifts the obligation from a vendor to collect and remit the sales tax to the purchaser if the usage of the software is in multiple states.

<sup>159</sup> Md. Ann. Code section 11-101(m)(8).

<sup>160</sup> Mass. Gen. Laws Ann. 64M section 1 (Definitions); 64H section 2 (Sales tax; services tax; imposition; rate; payment); Mass Regs. Code tit. 830 section 64H.1.3: Computer Industry Serv. and Prod.

<sup>161</sup> Mass Regs. Code tit. 830 section 64H.1.3; Technical Information Release (TIR) 05-8: Taxation of Internet Access, Electronic Commerce and Telecommunications Services: Recent Federal Legislation (July 14, 2005); TIR 09-14: Taxation of Direct Broadcast Satellite Service (July 28, 2009).

<sup>162</sup> Mass. Gen. Laws Ann. 64H section 1.

<sup>163</sup> *Id.*

Notably, regarding digital goods that are not really defined or mentioned, Massachusetts taxes satellite services but not cable services and data processing.<sup>164</sup> Consistently, the term “telecommunications” is broadly defined to include transfer of messages or information by wire, cable, fiber optics, laser, microwave, radio, satellite, and so forth, but excluding cable television. In sum, Massachusetts taxes satellite television providers, but that does not seem to include audio or video streaming.

## Michigan

Michigan<sup>165</sup> is a SSUTA state, which defines tangible personal property to include pre-written software, which is taxable if delivered electronically.<sup>166</sup> The term “delivered electronically” is construed to mean the transfer of the software code, according to *Auto-Owners Insurance*.<sup>167</sup> Software accessible via cloud is not taxable.<sup>168</sup> The term “prewritten computer software” is defined to include pre-written upgrades.<sup>169</sup> SaaS is nontaxable in Michigan.<sup>170</sup> The state did not adopt a definition of specified digital goods and, therefore, does not tax delivery of digital content like audio or video content.

<sup>164</sup> See *DirecTV LLC v. Department of Revenue*, 25 N.E.3d 258, 263 (Mass. 2015) (direct broadcast satellite transmissions are subject to excise tax and involve distribution of video programs: national, local, or pay per view).

<sup>165</sup> Mich. Comp. Laws Ann. sections 205.92b (Definitions), 205.93a (Telecommunications services), 205.52 (Tax on sales at retail; rate).

<sup>166</sup> Mich. Comp. Laws Ann. section 205.51a(r).

<sup>167</sup> 880 N.W.2d 337.

<sup>168</sup> Other Deductions Manual (“License to use prewritten computer software is subject to sales tax if a copy of the software code or program is provided to the buyer along with the license . . . The right to access/use prewritten computer software (cloud computing) will generally not be subject to sales tax if the consumer does not receive either a copy of the software program or any part of the program’s computer code. Reciprocity and credit for tax due and paid to another state may be applicable.”).

<sup>169</sup> Mich. Comp. Laws Ann. section 205.92(p).

<sup>170</sup> Michigan Department of Treasury, “Notice to Taxpayers Regarding *Auto-Owners Insurance Company v. Department of Treasury*” (Jan. 6, 2016).

## Minnesota

Minnesota<sup>171</sup> is a SSUTA state. Its DOR offers easy-to-locate and easy-to-follow guidance for digital goods.<sup>172</sup> Minnesota taxes pre-written computer software but not SaaS. Minnesota also taxes digital products accessed online. In its online guide, Minnesota clarifies that online hosted software accessed through the internet is not taxable. However, this is not the case with specified digital products (videos) — those are deemed taxable when they are “transferred electronically” and not just “delivered electronically,” as the term “transferred electronically” includes the ability to access the products. As such, streaming digital content appears taxable, but access to software in the cloud does not. Also, per Sales Tax Fact Sheet 199:

Pay television service is taxable. Beginning July 1, 2013, pay television service replaces the terms cable television service and direct satellite service. Pay television service includes all “pay” television services regardless if delivery is via cable, direct satellite, or otherwise.

## Mississippi

Mississippi<sup>173</sup> is not a SSUTA state. The guidance available on the DOR’s website is in the form of FAQs and is very basic. Mississippi has a somewhat lengthy definition of tangible personal property that refers to it not merely being “perceptible to the human senses” but also to “chemical analysis.” Mississippi does not distinguish between the types of software and taxes both software and specified digital products. From the statutes it is not clear if the tax on software and specified digital products applies only if they are downloaded as opposed to merely accessed. Yet in its rules, Mississippi clarifies that

<sup>171</sup> Minn. Stat. Ann. sections 297A.61 (Definitions), 297A.66 (Jurisdiction to require collection and remittance of taxes).

<sup>172</sup> Minnesota Department of Revenue, “Sales Tax Fact Sheet 134, Computer Software” (rev. Sept. 2018); “Sales Tax Fact Sheet 177, Digital Products” (rev. Sept. 2018); and “Sales Tax Fact Sheet 199, Telecommunications, Pay Television, and Related Services” (rev. Aug. 2017).

<sup>173</sup> Miss. Code Ann. sections 27-65-3 (Definitions), 27-65-17 (Sale of tangible personal property, farming and logging equipment and parts), 27-65-26 (Specified digital products), 27-65-19 (Public utilities; telecommunications services); and 35 Miss. Admin. Code Pt. IV, R. 4.10 (Specified digital products), R. 5.06 (Computer equipment and services).

while all software is taxable, “software maintained on a server located outside the state and accessible for use only via the Internet is not taxable.”<sup>174</sup>

However, the rules apply a broader taxability coverage for specified digital products, which are considered “electronically transferred” — the term includes “delivery via internet or network, or access via internet or network to a server where the product is stored, regardless of the location of the server.”<sup>175</sup>

## Missouri

Missouri<sup>176</sup> is not a SSUTA state and does not have easy-to-find guidance, other than its rules for software.<sup>177</sup> Missouri taxes only canned software sold in a tangible medium — no taxation on digital goods otherwise. The rule provides:

In general, the sale of canned software is taxable as the sale of tangible personal property. The sale of customized software, where the true object or essence of the transaction is the provision of technical professional service, is treated as the sale of a nontaxable service.<sup>178</sup>

SaaS is nontaxable in Missouri.<sup>179</sup>

## Nebraska

Nebraska<sup>180</sup> is a SSUTA state, so taxability of its items is presented in a uniform way in the SSUTA matrix. Under the matrix, every type of software and related contract and digital good is taxable in Nebraska, except for digital goods that are “sold to other than the end-user.” As of January 1, the Nebraska DOR is working on publishing its guidance for digital goods. The website states that

<sup>174</sup> 35 Miss. Admin. Code Pt. IV, R. 5.06.

<sup>175</sup> 35 Miss. Admin. Code Pt. IV, R. 4.10.

<sup>176</sup> Mo. Ann. Stat. sections 144.010 (Definitions), 144.020 (Rate of tax — tickets, notice of sales tax), 144.605 (Definitions), 144.610 (Tax imposed, property subject, exclusions, who is liable); and 12 Mo. Code of State Reg. section 10-109.050.

<sup>177</sup> Mo. 12 CSR 10-109.050.

<sup>178</sup> Mo. 12 CSR section 10-109.050(1).

<sup>179</sup> Mo. 12 CSR section 10-109.050(3)(H) (“The sale of software as a service is not subject to tax. The service provider must pay sales or use tax on any tangible personal property used to provide the service that is purchased or used in Missouri.”).

<sup>180</sup> Neb. Rev. Stat. sections 77-2701.16 (Gross receipts, defined).

its guidance on computer software is being updated.<sup>181</sup>

The definition of tangible personal property is narrow in Nebraska and only includes property that has a physical existence or form. Nonetheless, Nebraska expressly taxes intellectual property and entertainment property being sold, leased, or otherwise provided, including production of any software, or the activities of providing satellite programming, television, and so forth. Thus, Nebraska, like a handful of states, does not differentiate between customized and pre-written software.<sup>182</sup> SaaS is not expressly addressed in the statutes, but based on the broad taxability, SaaS must be taxable because the tax is on the act of furnishing the properties of software to the buyer (no mention is made of how the software is delivered) as long as the properties are made available and furnished.

Separately, Nebraska taxes:

the retail sale of digital audio works, digital audiovisual works, digital codes, and digital books delivered electronically if the products are taxable when delivered on tangible storage media. A sale includes the transfer of a permanent right of use, the transfer of a right of use that terminates on some condition, and the transfer of a right of use conditioned upon the receipt of continued payments.<sup>183</sup>

The services of a community antenna television service operator, or a satellite service operator are taxable and treated as a public utility.<sup>184</sup>

## Nevada

Nevada<sup>185</sup> is a SSUTA state and does not tax products delivered electronically because they are not considered tangible personal property. The Nevada Department of Taxation states on its website that “software, electronic magazines, clipart, program code, or other downloaded materials” are not taxable. “Products delivered electronically or by load and leave” are similarly not taxable. “However, products ordered via the internet and shipped into Nevada are taxable, as well as any software transferred via a disk or other tangible media. A box of software or other product shipped to customers in this state is physical, tangible personal property and subject to sales tax.”<sup>186</sup>

Nevada has separate sections for custom and pre-written computer software, which is only taxable as if not delivered electronically or via load and leave. Specified digital products are separate from tangible personal property (specifically excluded) and therefore are not taxed. Nonetheless, Nevada taxes hosting and data processing services.

## New Jersey

New Jersey<sup>187</sup> is not a SSUTA state. It taxes information services, pre-written software, and specified downloadable digital products. New Jersey provides thorough guidance through publications and technical bulletins. Its definition of tangible personal property includes pre-written computer software delivered electronically.<sup>188</sup> Because SaaS only provides the customer access to the software and the software is not delivered electronically, it is not the sale of tangible personal property. However, SaaS that meets the definition of an information service and is used to provide information to customers by an

<sup>181</sup> Nebraska Department of Revenue, Sales and Use Tax Information Guides.

<sup>182</sup> See Neb. Rev. Stat. section 77-2701.16(3)(a) (stating that the tax applies to gross receipts of every person engaged in selling, leasing, or otherwise providing intellectual or entertainment property, meaning “the furnishing of computer software . . . including the charges for coding, punching, or otherwise producing any computer software and the charges for the tapes, disks, punched cards, or other properties furnished by the seller.”)

<sup>183</sup> Neb. Rev. Stat. section 77-2701.16(9).

<sup>184</sup> Neb. Rev. Stat. section 77-2701.16(2).

<sup>185</sup> Nev. Rev. Stat. Ann. sections 360B.415 (Computer software), 360B.483 (Specified digital products), 372.105 (Imposition and rate), 363C.430 (Publishing, software and data processing), 372.085 (Tangible personal property), Nev. Admin. Code 372.875 (Applicability of tax to custom computer software and custom programming services).

<sup>186</sup> Nevada Department of Taxation, Sales Tax Information and FAQs.

<sup>187</sup> N.J. Stat. Ann. section 54:32B-2 (Definitions), 54:32B-3 (Imposition of sales tax; definitions).

<sup>188</sup> N.J. Stat. Ann. section 54:32B-2(g).

information service provider is a sale of information services.<sup>189</sup>

Regarding its information services, New Jersey explains:

A business which charges a fee for access to any type of information other than personal or individual information (e.g., stock quotes, financial, legal research, property values, and marketing trends) through any means (e.g., an electronic database, subscription to a hard copy report) is selling an information service, because the true object of that transaction is the information itself. As such, these transactions are subject to tax.<sup>190</sup>

Yet, New Jersey makes clear that:

Receipts from sales of a specified digital product that is accessed but not delivered electronically to the purchaser are exempt from tax. Nor is tax imposed on other types of property that are delivered electronically, such as digital photographs, digital magazines, etc.<sup>191</sup>

### New Mexico

New Mexico<sup>192</sup> is not a SSUTA state. It taxes tangible personal property and most services. Digital goods are not specifically addressed but are considered taxable.

### New York

New York<sup>193</sup> is not a SSUTA state. The Department of Taxation and Finance provides guidance on its website stating that:

Prewritten computer software is taxable as tangible personal property whether it is sold as part of a package or as a separate component, regardless of how the software is conveyed to the purchaser.

Therefore, prewritten computer software is taxable whether sold: on a disk or other physical medium; by electronic transmission; or by remote access.<sup>194</sup>

New York further explains that the basis for taxing remotely accessed software is the constructive possession, stating, “When a purchaser remotely accesses software over the Internet, the seller has transferred possession of the software because the purchaser gains constructive possession of the software and the right to use or control the software.”<sup>195</sup> Otherwise, digital products are not subject to sales tax in New York.

### North Carolina

North Carolina<sup>196</sup> is a SSUTA state, and its DOR offers guidance on sales and use tax in a 300-plus-page compilation of bulletins.<sup>197</sup> North Carolina views access to software remotely as a service and does not impose sales or use tax on charges for such services. North Carolina reaches a different conclusion regarding digital products or digital content, which is not considered tangible personal property and is nonetheless taxed whether delivered or accessed electronically. North Carolina makes clear that video programming and satellite digital audio radio services are also taxable.

### North Dakota

North Dakota<sup>198</sup> is a SSUTA state. North Dakota provides clear guidelines for application of sales tax to computers.<sup>199</sup> It taxes pre-written software that is electronically transferred via load and leave, but not SaaS or specified digital products that are specifically exempt.

<sup>189</sup> New Jersey Division of Taxation, Technical Bulletin TB-72 (July 3, 2013).

<sup>190</sup> New Jersey Division of Taxation, Publication ANJ-29.

<sup>191</sup> New Jersey Division of Taxation, Publication ANJ-27.

<sup>192</sup> N.M. Stat. Ann. sections 7-9-3 (Definitions), 7-9-7 (Imposition and rate of tax; denomination as “compensating tax”), 7-9-57.2 (Deduction; gross receipts tax; sale of software development services).

<sup>193</sup> N.Y. Tax Law sections 1101 (Definitions); 1105 (Sales tax).

<sup>194</sup> N.Y. Department of Taxation and Finance, Tax Bulletin ST-128 (TB-ST-128) (Aug. 5, 2014).

<sup>195</sup> *Id.*

<sup>196</sup> N.C. Gen. Stat. sections 105-164.3 (Definitions), 105-164.4 (Tax imposed on retailers and some facilitators).

<sup>197</sup> N.C. Department of Revenue, Sales and Use Tax Bulletins (Jan. 1, 2020).

<sup>198</sup> N.D. Cent. Code sections 57-39.2-01 (Definitions), 57-39.2-02.1 (Sales tax imposed), 57-39.2-04 (Exemptions).

<sup>199</sup> N.D. Office of State Tax Commissioner, Sales Tax — Computers (Sept. 2006).

## Oklahoma

Oklahoma<sup>200</sup> is not a SSUTA state. It provides guidance through various private letter rulings. Oklahoma is limited in its taxation of digital goods — only pre-written software that is delivered via load and leave or tangible medium is taxable.

## Ohio

Ohio<sup>201</sup> is a SSUTA state and taxes most digital goods, including software and “specified digital products” and even information services like access to data and databases. The only nontaxable items are custom software and related update and upgrade contracts (mandatory and optional) and those audio and audiovisual products that are not sold to the end-users. The Ohio Department of Taxation provides its guidance through numerous FAQs.<sup>202</sup> While SaaS is not expressly addressed, it is likely taxed because Ohio also taxes data processing services, computer services, and e-information services that include “providing access to database information, and providing access to electronic mail systems.”<sup>203</sup> For tangible personal property, the sale constitutes the transfer of title, possession or both, and the granting of a license to use is sufficient.

Regarding digital products that are electronically transferred, they are taxable when provided for use. Ohio has gone as far as to provide on its website examples of taxpayers who must pay tax. An FAQ states:

32. What is taxed under R.C. 5739.01(B)(12), “specified digital products”? — Items, including but not limited to, audiovisual products (such as

movies), audio products (such as songs), and books delivered electronically. Tax applies to both temporary and permanent transfer (i.e., need not purchase the product for ownership). Examples are Netflix, HULU, I-Tunes, e-books for Kindle and other electronic readers.

Similarly, Ohio separately identifies tangible personal property and pre-written software; specified digital products; and automatic data processing. Like Massachusetts, Ohio taxes satellite broadcasting but not cable services.

## Pennsylvania

Pennsylvania<sup>204</sup> is not a SSUTA state and has a distinctly simple approach to its digital goods taxation framework. It offers a one-page guidance document stating that digital products include canned software, video, and so forth, and that these products are all taxable whether accessed or streamed.<sup>205</sup> The guidance provides that examples of electronically transferring a product include “downloading a product from the internet. Viewing a product that is streamed over the internet. Receiving a product by email from the retailer.” Further, the website guidance provides:

Common purchases of digital products that are taxable include, but are not limited to: E-books or a subscription to download e-books. Digital video that is downloaded or streamed or a subscription to a streaming service, such as Netflix or Hulu. Digital audio that is downloaded or streamed including songs, ringtones, and audio books from iTunes, Google Play and other services, as well as subscriptions to satellite radio and other streaming services.

To achieve broad coverage, Pennsylvania defines tangible personal property to include not only corporeal personal property but items that are digital, including their maintenance and updates, “whether electronically or digitally delivered, streamed or accessed and whether purchased singly, by subscription or in any other

<sup>200</sup> Okla. Stat. Ann. tit. 68 sections 1352 (Definitions), 1354 (Tax levy).

<sup>201</sup> Ohio Rev. Code sections 5739.02 (Levy of tax; purpose; rate), 5739.01 (Definitions).

<sup>202</sup> Ohio Department of Taxation, Frequently Asked Questions.

<sup>203</sup> Ohio could be clearer regarding taxability of SaaS. The tax applies to software delivered electronically — defined as “delivery of computer software from the seller to the purchaser by means other than tangible storage media.” Since remotely hosted software is not “delivered,” it may be argued that SaaS is not taxable unless the intent was the delivery of software functionalities only, not the code, or ability to control the software itself. While Ohio has some guidance on its website in the form of FAQs, it does not clarify the issue. One question asks: “Is prewritten computer software taxable as specified digital products?” The answer is “Yes, prewritten computer software is taxable, whether purchased in CD form or received electronically via download or otherwise.”

<sup>204</sup> Pa. Stat. Ann. sections 7201 (Definitions), 7202 (Imposition of tax).

<sup>205</sup> Pennsylvania Department of Revenue, Tax on Digital Products.

manner.<sup>206</sup> The state also taxes video programming. This approach eliminates a lot of possibly unnecessary guidance or distinctions. However, public television is not taxable.<sup>207</sup>

### Rhode Island

Rhode Island<sup>208</sup> is a SSUTA state. Like Kentucky and Ohio, Rhode Island taxes most digital products (canned software and specified digital goods for end-users) that are transferred electronically, or by means other than tangible property, with no mention of transfer through access or stream in the law. On October 1, 2018, Rhode Island announced that the sale, storage, use, or other consumption of vendor-hosted pre-written computer software, or SaaS, will be subject to Rhode Island's 7 percent sales and use tax. The statutes refer to software "delivered electronically, by load and leave," or "vendor-hosted."<sup>209</sup>

One interesting aspect of Rhode Island's framework is that its law presumes that tangible personal property, pre-written software, and digital products are taxable unless proven otherwise to the satisfaction of the tax administrator.<sup>210</sup> "The term 'specified digital products' (sometimes called 'digital downloads') generally means digital movies, TV shows, books, music, and related items — including subscriptions to streaming audio and visual products (such as films, shows, and music), streamed or downloaded to computers, phones, and other devices."<sup>211</sup>

### South Carolina

South Carolina<sup>212</sup> is not a SSUTA state and taxes pre-written software and customer software if delivered on a tangible medium. South Carolina is unique in how it stretches its definition of tangible personal property to include services such as communications,<sup>213</sup> but also excludes transmission of computer database information. The guidance is not clear and is generally based on private letter rulings. So while not taxing SaaS, South Carolina taxes streaming under communications, and there are authorities suggesting that SaaS is software sold via application service provider and is therefore taxable if it meets that criteria.<sup>214</sup> The DOR explains that software delivered from a remote location is not subject to the sale and use tax, but the service provider is allowed to charge customers for database access services.<sup>215</sup> And "charges paid by a customer for streaming television programs, movies, music, and other similar content are charges for communication services and are therefore subject to South Carolina sales and use tax whether paid for as part of a subscription service, per item, or per event."<sup>216</sup>

<sup>206</sup> Pa. Stat. Ann. 72 P.S. section 7201 (m)(2).

<sup>207</sup> Pa. Stat. Ann. 72 P.S. section 7201 ("The term shall not apply to transmissions by public television, public radio services or official Federal, State or local government cable services.").

<sup>208</sup> R.I. Gen. Laws sections 44-18-7 (Sales defined), 44-18-8 (Retail sale or sale at retail defined), 44-18-16 (Tangible property), and 44-18-7.1 (Additional definitions).

<sup>209</sup> R.I. Gen. Laws section 44-18-7(14), (15). Rhode Island Department of Revenue, ADV2018-38, "Tax Change Takes Effect on Monday, October 1" (Sept. 4, 2018).

<sup>210</sup> R.I. Gen. Laws section 44-18-25.

<sup>211</sup> R.I. Department of Revenue, "Summary of Legislative Changes" (Aug. 5, 2019).

<sup>212</sup> S.C. Code Ann. sections 12-36-60 (Tangible personal property), 12-36-70 (Retailer and seller).

<sup>213</sup> Note the term "communication services" is defined broadly to include satellite and other programming services of television, radio or music; database access transmission (e.g., legal research); and streaming services for television programs, movies, music, and other similar content.

<sup>214</sup> South Carolina Department of Revenue FAQs. "Software delivered via an Application Service Provider, whereby the seller maintains the software on a website and the purchaser pays to access the software on that website, is subject to the sales and use tax."

<sup>215</sup> S.C. Code Ann. sections 12-36-910(B)(3) and 12-36-1310(B)(3). South Carolina Department of Revenue, Revenue Ruling No. 03-5 (Dec. 9, 2003).

<sup>216</sup> South Carolina Department of Revenue, Revenue Ruling No. 18-1 (Apr. 10, 2008).



## South Dakota

South Dakota<sup>217</sup> is a SSUTA state that has had long-standing guidance on products transferred electronically.<sup>218</sup> In 2011, using a “fact sheet” format, South Dakota announced that it would not treat digital goods differently, pointing out that the method of delivery should not matter, but, to avoid confusion South Dakota would clarify that these goods are taxed — both software (even custom) and music and videos as follows:

In South Dakota the receipts from the sale of tangible personal property have been subject to sales tax since 1935. Since that time methods of delivering products has expanded to include transferring products electronically. Products transferred electronically are taxed as a sale of tangible personal property. However some states do not tax products transferred electronically which creates confusion as to whether or not these products are tangible personal property. To remove any confusion as to whether or not products transferred electronically are taxable, South Dakota has defined products transferred electronically and created a specific statute imposing tax on these products. The new law and definition of products transferred electronically does not change any tax liability. Sellers that sell products transferred electronically will continue to owe sales tax on receipts of products delivered to customers in South Dakota. Consumers using products delivered electronically will continue to owe use tax on their cost of the products, if sales tax was not collected by the seller.

...

<sup>217</sup>S.D. Codified Laws sections 10-46-2 (Tax on tangible personal property purchased for use in state), 10-45-2.4 (Tax on products transferred electronically), 10-45-1.9 (Bundled transaction defined), 10-45-1.17 (Telecommunications service defined), 10-45-1. (Lease or rental defined — exclusions), 10-45-1.1 (Gross receipts not to include late charge fees).

<sup>218</sup>South Dakota Department of Revenue, Tax Fact Sheet, Products Transferred Electronically (Mar. 2011); and Tax Fact Sheet, Telecommunication Services (June 2016).

A product transferred electronically is any product obtained by the purchaser by means other than tangible storage media such as a cd, dvd, disk or tape. A product transferred electronically does not include any intangible such as a patent, stock, bond, goodwill, trademark, franchise, or copyright. Temporary or Permanent Use Sales tax applies to products transferred electronically when the purchaser has temporary use of the product and when the purchaser has permanent use of the product. Example: Access to a downloaded movie for three days is a temporary use of a product and is subject to sales tax. Purchasing a movie that is downloaded to a computer for permanent use is also subject to sales tax.

In a later fact sheet, the DOR wrote that “Web hosting services are subject to state sales tax, plus applicable municipal sales tax based on the customer’s location.”<sup>219</sup> However, it is unclear whether South Dakota would tax SaaS. The statute provides a separate definition of tangible personal property that includes pre-written software and a separate definition for products transferred electronically.

For the products transferred electronically, the tax is on the gross receipts of all sales, leases, or rentals of any product transferred electronically if:

- the sale is to an end user;
- the sale is to a person who is not an end user, unless otherwise exempted by this chapter;
- the seller grants the right of permanent or less than permanent use of the products transferred electronically; or
- the sale is conditioned or not conditioned on continued payment.<sup>220</sup>

However, these are not the circumstances applicable to software or tangible personal property. The term “retail sale” applicable to tangible personal property includes the term “lease or rental,” which is separately defined as “any transfer of possession or control of tangible

<sup>219</sup>South Dakota Department of Revenue, Tax Fact Sheet, Internet (Jan. 2019).

<sup>220</sup>S.D. Codified Laws section 10-45-2.4.

personal property or any product transferred electronically for a fixed or indeterminate term for consideration.”<sup>221</sup> Because there must be transfer of control, South Dakota does not appear to tax purchases of software or e-products that merely require access and that are not actually electronically obtained. Even in its 2011 fact sheet, South Dakota provides examples of “downloaded” movie. Unlike Massachusetts, that exempts cable television but not broadcasting, South Dakota taxes cable television but not broadcasting.<sup>222</sup>

### Tennessee

Tennessee<sup>223</sup> is not a SSUTA state. It provides a detailed, 79-page guide for its taxpayers, which has sections addressing taxability of digital goods.<sup>224</sup> Tennessee taxes computer software (all types) and digital products, including access to television and satellite service, except data processing, which is excluded. Tennessee states that tangible personal property does not include signals broadcast over airwaves. Tennessee expressly addresses taxation of SaaS<sup>225</sup> and states that the taxable use of computer software includes the access and use of software that remains in possession of the seller and is remotely accessed by a customer for use in the state. This provision ensures that software remains subject to sales and use tax regardless of a customer’s method of use.<sup>226</sup>

<sup>221</sup> S.D. Codified Laws sections 10-45-1; 10-45-1.5.

<sup>222</sup> S.D. Codified Laws sections 10-45-5; 10-45-12.1.

<sup>223</sup> Tenn. Code Ann. sections 67-6-221 (Interstate telecom. serv. tax); 67-6-201 (Declaration of privilege); 67-6-102 (Definitions).

<sup>224</sup> Tenn. Department of Revenue, Tennessee Sales and Use Tax Guide (Sept. 2019).

<sup>225</sup> Tenn. Code Ann. section 67-6-231(a) (“The retail sale, lease, licensing or use of computer software in this state, including prewritten and custom computer software, shall be subject to the tax levied by this chapter, regardless of whether the software is delivered electronically, delivered by use of tangible storage media, loaded or programmed into a computer, created on the premises of the consumer or otherwise provided.”); section 67-6-231(b) (“use of computer software” includes the access and use of software that remains in the possession of the dealer who provides the software or in the possession of a third party on behalf of such dealer).

<sup>226</sup> Tennessee Department of Revenue, *supra* note 224, at 33.

### Texas

Texas<sup>227</sup> is not a SSUTA state. Texas sets the tone of its statutory regulation of digital goods when it states that the electronic form of a taxable item as opposed to its physical media does not alter the tax status. Similarly, Texas taxes the digital distribution of video programming to purchasers by any means now in existence or that may be developed.<sup>228</sup> Texas does not use the term software; instead it refers to a “computer program.” However, the definitions are similar. Texas defines a computer program as “a series of instructions . . . to permit the computer system to process data and provide results and information.” Other states define the term “computer software” as “a set of coded instructions designed to cause a computer or automatic data processing equipment to perform a task.”<sup>229</sup>

Texas, like Alabama, Washington, D.C., Hawaii, Iowa, Mississippi, Nebraska, Tennessee, and West Virginia, does not distinguish between canned or pre-written software and customized software, so it is all taxable. Texas addresses taxability of SaaS under the category of “data processing services,” which includes data storage and manipulation and cable television services (any video streaming) as taxable items that are defined broadly to accommodate any technological changes. One interesting aspect of Texas’s statutory framework is the detailed list of its taxed cable television services including direct broadcast satellite service; subscription television service; satellite master antenna television service; master antenna television service; multipoint distribution service; multichannel multipoint distribution service; fixed programming; any audio portion of a video program; streaming video programming provided via the internet or other technology, regardless of the type of device used by the purchaser to receive the service; video-on-demand services or subscription services that allow purchasers to choose from a library of available content; and any other video

<sup>227</sup> Tex. Tax Code Ann. sections 151.0035 (Data processing service); 151.0101 (Taxable services).

<sup>228</sup> 34 Tex. Reg. section 3.313.

<sup>229</sup> See, e.g., Mich. Comp. Laws Ann. section 205.92b(c); and Wis. Stat. Ann. section 77.51(1p).

programming provided in exchange for consideration.<sup>230</sup>

## Utah

Utah<sup>231</sup> is one of the SSUTA states. Utah provides some guidance in Publication 25 (Sales and Use Tax General Information),<sup>232</sup> Publication 64 (Sales Tax Information for Computer Service Providers), and private letter rulings, but not all guidance is entirely clear. Utah defines and taxes tangible personal property, which includes pre-written computer software. Utah does not use the terms “specified digital products” or “specified digital goods,” but, like several other states it uses the term “product transferred electronically.” SaaS is taxable if it is “used” — no transfer of possession or control required. On its website, the tax commission explains:

Remotely accessed software includes hosted software, application service provider (ASP) software, software-as-a-service (SaaS), and cloud computing applications. License fees for remotely accessed prewritten software are taxable if the purchased software is used in Utah. If remotely accessed software is used at more than one location and at the time of the transaction, the buyer provides the seller a reasonable and consistent method for allocating the transaction between those locations, the seller must source the transaction to those locations. If the buyer does not provide the seller with a method of allocating a transaction that is used in multiple locations, the seller must source the transaction to the buyer’s address.<sup>233</sup>

Utah’s approach is practical and may be helpful. However, for the product transferred electronically, Utah requires some transfer; that is, the product must be downloaded. A private letter ruling states that “in general, if a purchaser were

to pay to view without downloading videos streamed over the internet, those transactions would not be subject to Utah sales and use taxes. Thus, if the Subscribers were paying for access to streamed content, those transactions would not be subject to Utah sales and use taxes.”<sup>234</sup>

There are proposals to make the definition even more clear to include streaming. Note, however, that Utah imposes a separate tax on multichannel video service providers.

## Vermont

Vermont<sup>235</sup> is a SSUTA state and provides two pages of easy-to-follow guidance to simplify taxation of digital goods.<sup>236</sup> Vermont’s statute is basic: software that is pre-written and obtained or downloaded only is taxable, and so are specified digital products. One twist is that Vermont separately taxes access to cable television or broadcasting. Hence, it appears that Vermont taxes streaming — just like Washington, D.C., Iowa, and Pennsylvania.

## Virginia

Virginia<sup>237</sup> is not a SSUTA state. It taxes tangible pre-written computer software and communications services. The definition of tangible personal property does not refer to software.<sup>238</sup> Virginia’s communications sales and use tax applies to more than 10 services, including cable television, landline and wireless telephone, and satellite television and radio. Yet it does not apply to many other services, including but not limited to electronically delivered digital products (for example, music, reading materials, software), information services, internet access, or prepaid calling.

Under Virginia law, only pre-written computer software delivered in tangible form is subject to sales and use tax. SaaS is nontaxable in

<sup>234</sup> Utah PLR 18-002.

<sup>235</sup> Vt. Stat. Ann. Tit. 32 sections 9701 (Definitions), 9771 (Imposition of sales tax).

<sup>236</sup> Vermont Department of Taxes, Prewritten Software Accessed Remotely.

<sup>237</sup> Va. Code Ann. sections 58.1-648 (Imposition of sales tax; exemptions), 58.1-3500 (Defined and segregated for local taxation), 58.1-3523 (Definitions).

<sup>238</sup> Va. Code Ann. section 58.1-3500.

<sup>230</sup> 34 Tex. Reg. section 3.313. Texas taxes information services and data processing. Tex. Tax Code Ann. section 151.0101(a)(10), (12).

<sup>231</sup> Utah Code Ann. sections 59-12-102 (Definitions), 59-12-102.3 (Authority to enter into agreement—Delegates), 59-12-103 (Sales and use tax base — Rates — Effective dates — Use of sales and use tax revenues).

<sup>232</sup> Utah State Tax Commission, Publication 25 (revised June 2019).

<sup>233</sup> Utah State Tax Commission, Publication 64 (revised May 2012).

Virginia.<sup>239</sup> Lastly, the Virginia Department of Taxation provides guidance on taxable telecommunication services as follows:

Services subject to the tax include, but are not limited to: . . . cable television (including but not limited to basic, extended, premium, pay-per-view, video on demand, digital, high definition, video recorder, music services and fees for additional outlets); and satellite television and satellite radio.<sup>240</sup>

## Washington

Washington<sup>241</sup> is a SSUTA state. The Washington DOR website provides a detailed guidance, with definitions, FAQs, examples, and references.<sup>242</sup> The definition of tangible personal property includes prewritten computer software.<sup>243</sup> Washington separates the definition of digital products to include digital goods<sup>244</sup> and digital automated services.<sup>245</sup> In its online guidance, the DOR states that “digital products subject to sales or use tax include: downloaded digital goods (music and movies, etc.), streamed and accessed digital goods, and digital automated services.”<sup>246</sup>

The definition of the term “electronically transferred” is broad, stating: “so long as the

purchaser may access the product, it will be considered to have been electronically transferred to the purchaser.” While it has a special exclusion from retail sales and use tax for radio or television broadcast providers as to their sale of audio or video programming, Washington does not exempt those programs offered on a pay-per-program basis or for an arrangement that allows the buyer to access a library of programs at any time for a specific charge for that service.<sup>247</sup> Also, income received from the sale of regular audio or video programming by a radio or television broadcaster is generally subject to service and other business and occupation tax and therefore not subject to retail sales tax.

The DOR recently prevailed in *Gartner Inc.*<sup>248</sup> The court of appeals explained that Washington imposes a business and occupation tax on both digital goods and digital automated services. The administrative rule distinguished a digital good from digital automated services as follows: “A digital good is not a service involving one or more software applications. A digital good consists solely of images, sounds, data, facts, information or any combination thereof. Clear examples of digital goods are digital books, digital music, digital video files, and raw data.”<sup>249</sup>

In contrast, digital automated services consist of software that facilitates access to a stand-alone digital good.<sup>250</sup> Gartner argued that Washington incorrectly classified its services as digital automated services and not professional services. The appellate court disagreed, finding that Gartner’s clients purchased access to digital goods that was enhanced by a customized client portal — an automated feature. The appellate court also found that Gartner’s services did not involve “human effort.”

<sup>239</sup> Virginia Department of Taxation, Ruling 12-191 (Nov. 29, 2012).

<sup>240</sup> Virginia Department of Taxation, Communications Taxes.

<sup>241</sup> Wash. Rev. Code Ann. sections 82.04.192 (Digital products definitions); 82.08.020 (Tax imposed); Wash. Admin. Code 458-20-15503.

<sup>242</sup> Washington Department of Revenue, *supra* note 21.

<sup>243</sup> Wash. Rev. Code Ann. section 82.08.010, but not customized software or digital products.

<sup>244</sup> Digital goods means “sounds, images, data, facts, or information, or any combination thereof, transferred electronically, including, but not limited to, specified digital products and other products transferred electronically not included within the definition of specified digital products.” Wash. Rev. Code Ann. section 82.04.192(6)(a). Specified digital products include “electronically transferred digital audiovisual works, digital audio works, and digital books.” Wash. Rev. Code Ann. section 82.04.192(9).

<sup>245</sup> Wash. Rev. Code Ann. section 82.04.192(7). Digital automated services means “any service transferred electronically that uses one or more software applications.” Wash. Rev. Code Ann. section 82.04.192(3)(a). Note that data processing services are excluded from digital automated services. Section 82.04.192(3)(b)(xv). They are defined as “primarily automated service provided to a business or other organization where the primary object of the service is the systematic performance of operations by the service provider on data supplied in whole or in part by the customer to extract the required information in an appropriate form or to convert the data to usable information.” *Id.*

<sup>246</sup> Washington Department of Revenue, *supra* note 21.

<sup>247</sup> Wash. Admin. Code section 458-20-15503 (Rule 15503).

<sup>248</sup> *Gartner Inc. v. Department of Revenue*, 455 P.3d 1179 (Wash. App. 2020).

<sup>249</sup> Wash. Admin. Code section 458-20-15503(203)(a)(i).

<sup>250</sup> *Id.*

## West Virginia

West Virginia<sup>251</sup> is a SSUTA state and does not offer much guidance on its website. West Virginia imposes consumer sales and services tax on all software (customized or canned), and SaaS is likely considered a taxable service in West Virginia. The state does not tax digital goods; however, it taxes television and broadcasting services — either sales or use, depending on whether the broadcaster is in or out of state.<sup>252</sup> Also, “to encourage computer software developers, computer hardware designers, systems engineering firms, electronic data processing companies and other high-technology companies to locate and expand their businesses in West Virginia,” the state exempts from tax some sales of computer hardware and software directly incorporated into manufactured products; some leases; sales of electronic data processing service; sales of computer hardware and software directly used in communication; and sales of educational software.<sup>253</sup>

## Wisconsin

Wisconsin<sup>254</sup> is a SSUTA state and its DOR provides detailed guidance.<sup>255</sup> In addition to pre-written computer software, which is taxed as “tangible personal property,”<sup>256</sup> Wisconsin imposes sales and use tax on specified digital goods;<sup>257</sup> additional digital goods (greeting cards, finished artwork, periodicals, video or electronic

games, and newspapers or other news or information products);<sup>258</sup> and digital codes.<sup>259</sup>

Wisconsin’s taxation of software appears more limited than its taxation of digital goods. While Wisconsin statute provides that Wisconsin imposes tax on “prewritten computer software, regardless of how it is delivered to the purchaser,”<sup>260</sup> on its website, the state addresses cloud computing and SaaS and indicates that software accessed in that manner would not be taxable unless the employees were on premises and controlled it.<sup>261</sup>

However, when clarifying whether the delivery of specified digital goods makes a difference, Wisconsin’s website provides that electronic transfers include uploading, streaming, and emailing, and that retaining a copy is not indicative of whether there is electronic transfer. A digital good is transferred electronically regardless of whether the purchaser can make or retain a copy of the good.<sup>262</sup> Wisconsin taxes cable television.

## Wyoming

Wyoming<sup>263</sup> is a SSUTA state. Its DOR provides guidance in the form of the vendor manual. It does not address the specifics of taxation of SaaS or digital goods,<sup>264</sup> generally imposing tax on the sales price of every retail sale of tangible personal property in the state, the gross rental paid for the lease or contract transferring possession of tangible personal property, intrastate telecommunications services,

<sup>251</sup> W. Va. Code sections 11-15-1 (General consumers sales and service tax imposed) and 11-15-3 (Amount of tax; allocation of tax and transfers).

<sup>252</sup> West Virginia State Tax Department, TSD 372, Radio and Television Broadcasters and Sales and Use Tax (rev. Dec. 2014).

<sup>253</sup> W. Va. Code section 11-15-9h.

<sup>254</sup> Wis. Stat. section 77.51 (Definitions) and 77.52 (Imposition of retail sales tax); and *Wisconsin Department of Revenue v. Menasha Corp.*, 754 N.W.2d 95 (Wis. 2008).

<sup>255</sup> Wisconsin Department of Revenue, What is Taxable (listing cable television services as taxable); Digital Goods; Publication 240, “Digital Goods: How Do Wisconsin Sales and Use Taxes Apply to Sales and Purchases of Digital Goods?” (May 2016); “Sales and Use Tax Treatment Computer — Hardware, Software, Services (October 1, 2009 and thereafter);” Publication 247, “Commercial Radio and Television Stations — How Do Wisconsin Sales and Use Taxes Affect Your Operations?” (Dec. 2014).

<sup>256</sup> Wis. Stat. section 77.51(20).

<sup>257</sup> Wis. Stat. section 77.51(17x).

<sup>258</sup> Wis. Stat. section 77.51(1a).

<sup>259</sup> Wis. Stat. section 77.51(3pc).

<sup>260</sup> Wis. Stat. sections 77.51(20), 77.52(1)(a).

<sup>261</sup> Sales and Use Tax Treatment Computer — Hardware, Software, Services (Oct. 1, 2009, and thereafter) (“Charges for accessing prewritten computer software located on the vendor’s server, if the customer does not operate the vendor’s server, or control its operation and does not have physical access to the vendor’s server, are not taxable. This assumes the service provider is not providing a taxable service (for example, a telecommunications message service) in the transaction.”).

<sup>262</sup> Wisconsin has been described as one of the most aggressive states in the pursuit of digital product taxation because it treats the transfer of digital goods as a taxable sale regardless of whether a customer has the right to upload the digital content and play the recording or merely enjoys it once. See Publication 240 at 8 (“It is not necessary for the purchaser of the digital good to record the digital good on tangible storage media for the product to be considered a digital good.”).

<sup>263</sup> Wyo. St. Ann. sections 39-15-101 (Definitions) and 39-16-103 (Imposition).

<sup>264</sup> Wyo. Department of Revenue, Vendor Manual.

and the sales price of every retail sale of specified digital products in the state.<sup>265</sup> Tangible personal property means all personal property that can be seen, weighed, measured, felt or touched, or that is in any other manner perceptible to the senses. The term includes pre-written computer software.<sup>266</sup> Regarding specified digital products: “A sale of specified digital products is only subject to the tax under this section if the purchaser has *permanent use* of the specified digital product.”<sup>267</sup> Thus, Wyoming requires permanent use as the criteria that determines whether software or specified digital products are taxable. The terms “lease” and “rent” require transfer of possession or control. ■

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<sup>265</sup> Wyo. Stat. Ann. section 39-15-103.

<sup>266</sup> *Id.*

<sup>267</sup> *Id.* (emphasis added).