

Draft Language for Major Provisions of a Digital Goods Bill

Key definitions

The following definition section would be a new statute in the B&O tax chapter. The definitions would also apply to the sales and use taxes. This section defines the terms “digital code,” “digital goods,” “digital automated services,” and “transferred electronically/electronically transferred.” Digital goods and digital automated services are defined very broadly. This is done so that the definitions can capture changes in technology and business models over time. Because the definitions are so broad, specific sales and use tax exemptions will need to be provided for those digital goods and digital automated services for which there is no desire to tax, such as personal e-mail communications.

Proposed bill language for a new section defining key terms:

(1) “Digital code” means a code that provides a purchaser with the right to obtain one or more digital goods, digital automated services, or both, if all of the digital goods and digital automated services to be obtained through the use of the code have the same sales and use tax treatment. A digital code may be obtained by any means, including e-mail or by tangible means regardless of its designation as song code, video code, book code, or some other term.

(2)(a) “Digital automated service,” except as provided in (b) of this subsection (2), means any service furnished via a computer network that involves an automated process and that utilizes one or more software applications.

(b) “Digital automated service” does not include:

(i) Any service that primarily involves the application of human effort, and the human effort originated after the customer requested the service;

(ii) The loaning or transferring of money or the purchase, sale, or transfer of financial instruments. For purposes of this subsection (2)(a)(ii), “financial instruments” include cash, accounts receivable and payable, loans and notes receivable and payable, debt securities, equity securities, as well as derivative contracts such as forward contracts, swap contracts, and options;

(iii) Dispensing cash or other physical items from a machine;

(iv) Payment processing services;

~~(v) Parimutuel wagering and handicapping contests as authorized by chapter 67.16 RCW;~~

~~(vi) Telecommunications services and ancillary services as those terms are defined in RCW 82.04.065;~~

~~(vii) The internet and internet services as those terms are defined in RCW 82.04.297; and~~

~~(viii) The service [of providing consumers with access to prewritten computer software] described in RCW 82.04.050~~

(3)(a)(i) “Digital goods,” except as provided in (b) of this subsection (3), means sounds, images, data, facts, or information, or any combination thereof, in electronic form, made available for the use or enjoyment of consumers. For

Deleted: (v) Any lottery game administered by the lottery commission, including any shared game lottery as defined in RCW 67.70.010; ¶

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purposes of the definition of “digital goods,” it is immaterial whether the consumer receives possession of the sounds, images, data, facts, or information, or merely has the right to access, view, or listen to the sounds, images, data, facts, or information.

(ii) The term “digital goods” includes audio and video programming, when the audio or video programming is provided on a pay-per-program basis or allows customers to access a library of programs at any time for a specific charge for that service.

(b) The term “digital goods” does not include:

(i) Sounds, images, data, facts, or information, or any combination thereof, in electronic form and obtained by the purchaser by means of tangible storage media;

(ii) Audio and video programming services not included within (a)(ii) of this subsection (3);

(iii) Telecommunications services and ancillary services as those terms are defined in RCW 82.04.065;

(iv) Computer software as defined in RCW 82.04.215;

(v) Internet services as defined in RCW 82.04.297;

(vi) The representation of a professional service in electronic form, such as an electronic copy of an engineering report prepared by an engineer;

(vii) Digital automated services and services excluded from the definition of digital automated services in subsection (2)(b) of this section; and

(viii) Television and radio broadcasting.

(4) “Electronically transferred” or “transferred electronically” means obtained by the purchaser by means other than tangible storage media. It is not necessary that a copy of the product be physically transferred to the purchaser. So long as the purchaser may access the product, it will be considered to have been electronically transferred to the purchaser.

Sales and use tax imposition statutes

RCW 82.04.050, which defines the term “retail sale” for purposes of B&O, sales, and use taxation, would be amended to include the sale of digital goods, digital codes, and digital automated services to consumers who are end users, regardless of the user rights received by the buyer and method of payment. RCW 82.04.050 would also be amended to define retail sale to include the service of providing consumers with access to prewritten computer software, which will be referred to as “on-demand software services” throughout this document.

The retail sales tax imposition statute (RCW 82.08.020) would not need to be amended, because that statute simply imposes sales tax on all “retail sales” as defined in RCW 82.04.050. The use tax imposition statute (RCW 82.12.020) needs to be amended to specifically impose use tax on the use of digital goods, digital codes, digital automated services, and on-demand software services.

Proposed bill language to make the sale of digital goods, digital codes, and digital automated services a retail sale by amending RCW 82.04.050:

(a) The term [retail sale] also includes the following sales to consumers of digital goods, digital codes, and digital automated services:

(i) Sales to end users;

(ii) Sales in which the seller has granted the purchaser the right of permanent use;

(iii) Sales in which the seller has granted the purchaser a right of use that is less than permanent;

(iv) Sales in which the purchaser is not obligated to make continued payment as a condition of the sale; and

(v) Sales in which the purchaser is obligated to make continued payment as a condition of the sale.

(b) A retail sale of digital goods or digital codes under this subsection includes any services provided by the seller exclusively in connection with the digital goods or digital codes, whether or not a separate charge is made for such services.

(c) For purposes of this subsection, the following definitions apply:

(i) "End user" means any purchaser other than a purchaser who receives by contract a digital good, digital code, or digital automated service for further commercial broadcast, rebroadcast, transmission, retransmission, licensing, relicensing, distribution, redistribution or exhibition of the product or service, in whole or in part, to another person or persons. A person that purchases digital goods, digital codes, or digital automated services for the purpose of giving away such products or services will not be considered to have engaged in the distribution or redistribution of such products or services and will be treated as an end user.

(ii) "Permanent" means perpetual or for an indefinite or unspecified length of time. A right of permanent use is presumed to have been granted unless the agreement between the seller and the purchaser specifies or the circumstances surrounding the transaction suggest or indicate that the right to use terminates on the occurrence of a condition subsequent.

Proposed bill language to make on-demand software services a retail sale by amending RCW 82.04.050:

The term [retail sale] also includes the charge made to consumers for the right to access and use prewritten computer software, where possession of the software is maintained by the seller or a third party, regardless of whether the charge for the service is on a per use, per user, per license, subscription, or some other basis.

Proposed bill language to impose use tax on the use of digital goods, digital codes, digital automated services, and on-demand software services by amending RCW 82.12.020:

(1) There is hereby levied and there shall be collected from every person in this state a tax or excise for the privilege of using within this state as a consumer any:

(a) ~~((Any))~~ Article of tangible personal property purchased at retail, or acquired by lease, gift, repossession, or bailment, or extracted or produced or manufactured by the person so using the same, or otherwise furnished to a person engaged in any business taxable under RCW 82.04.280 (2) or (7), including tangible personal property acquired at a casual or isolated sale, and including byproducts used by the manufacturer thereof, except as otherwise provided in this chapter, irrespective of whether the article or similar articles are manufactured or are available for purchase within this state¹;

(b) ~~((any))~~ Prewritten computer software, regardless of the method of delivery, but excluding prewritten computer software that is either provided free of charge or is provided for temporary use in viewing information, or both; ~~((or))~~

(c) Service defined as a retail sale in RCW 82.04.050 (2)(a), (3)(a), or [on-demand software services, excluding on demand software services that are provided free of charge];

(d) ~~((any))~~ Extended warranty; or

(e) Digital good, digital code, or digital automated service.

Business inputs and other key exemptions and exclusions from the tax base

Sales and use taxes on digital goods, digital codes, digital automated services, and on-demand software services only apply to transactions involving consumers. For purposes of B&O, sales, and use taxes, the term “consumer” is defined in RCW 82.04.190. Business inputs are excluded from the tax base through an exclusion from the definition of consumer.

Proposed bill language to exclude certain business inputs from the tax base by amending the definition of consumer in RCW 82.04.190:

(10) ~~[Consumer means]~~ Any person who purchases, acquires, or uses a digital good, digital code, digital automated service, or [on-demand software], other than for the purpose of:

(a) Further commercial broadcast, rebroadcast, transmission, retransmission, licensing, relicensing, distribution, redistribution or exhibition of the product or service, in whole or in part, to others. A person that purchases, acquires, or uses digital goods, digital codes, digital automated services, or [on-demand software] for the purpose of giving away such products or services will not be considered to have engaged in the distribution or redistribution of such products or services;

Deleted: [Consumer means] Any person who purchases, acquires, or uses [on-demand software] other than for resale in the regular course of business; and¹
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¹ This underlined language is not new to the statute. Moving the language to subsection (1)(a) will improve the readability of the statute.

(b) Consuming the digital good, digital code, digital automated service, or [on-demand software] in producing for sale a new product, where the digital good, digital code, digital automated service, or [on-demand software] becomes an ingredient or component of the new product. A digital code becomes an ingredient or component of a new product if the digital good or digital automated service acquired through the use of the digital code becomes an ingredient or component of a new product; or

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(c) Making the digital good or digital automated service, including a digital good or digital automated service acquired through the use of a digital code, or the [on-demand software] available free of charge for the use or enjoyment of others on that person's website, if that website generates advertising revenue for that person.

There are certain digital goods that are not bought and sold, such as personal e-mail communications and internal business memoranda. Similarly, there are many kinds of digital automated services that are provided free of charge, such as the Department of Revenue's E-file service. These types of digital goods and digital automated services would not be subject to sales tax because they are not sold. However, the use of these kinds of digital goods and digital automated services would be subject to use tax, absent an exemption.

Proposed bill language to provide a use tax exemption for certain digital goods for which no charge is made:

(1) The provisions of this chapter do not apply in respect to the use of digital goods that are:

- (a) Of a non-commercial nature, such as personal e-mail communications;
- (b) Created solely for an internal audience; or
- (c) Created solely for the business needs of the person who created the digital good and is not the type of digital good that is offered for sale, including business e-mail communications.

(2) This section does not apply to the use of any digital goods purchased by the user, the user's donor, or anybody on the user's behalf.

Proposed bill language to provide a use tax exemption for digital automated services for which no charge is made:

The provisions of this chapter do not apply in respect to the use of digital automated services provided free of charge.

Bundling of products and/or services to be obtained through the use of a code that doesn't meet the definition of digital code

The definition of "digital code" does not include a code that that allows the purchaser to obtain more than one digital good and/or digital automated service that do not have the same sales and use tax treatment. One way to clarify the tax treatment of the sale of these types of codes is to

treat them similar to a bundled transaction. A bundled transaction, with certain exceptions, is the retail sale of two or more distinct products and/or services for one nonitemized price. The tax treatment of bundled transactions is governed by RCW 82.08.195. Generally, a bundled transaction is subject to sales tax if any of the component products or services are subject to sales tax. However, in the case of a bundled transaction that includes telecommunications service, ancillary service, Internet access, or audio or video programming service and the price is attributable to services that are taxable and services that are not taxable, sales tax does not apply to the portion of the price attributable to nontaxable services if that portion of the price can be identified by reasonable and verifiable standards from the seller's books and records that are kept in the regular course of business for other purposes.

Proposed bill language amending RCW 82.08.195 to address the sales tax treatment of the sale of codes for multiple digital goods and/or digital automated services, and any other products and/or services, where the goods and services do not have the same sales and use tax treatment:

(6) In the case of the sale of a code that provides a purchaser with the right to obtain more than one digital good or digital automated service, or both, including a code that also provides the purchaser with the right to obtain other products or services, and all of the products and services, digital or otherwise, to be obtained through the use of the code do not have the same sales and use tax treatment, for purposes of the tax imposed by RCW 82.08.020:

(a) The transaction is deemed to be the sale of the products and services to be obtained through the use of the code; and

(b)(i) The tax imposed by RCW 82.08.020 applies to the entire selling price of the code, except as provided in (ii) of this subsection (6)(b).

(ii) If the seller can identify by reasonable and verifiable standards the portion of the selling price attributable to the products and services that are not subject to the tax imposed by RCW 82.08.020 from its books and records that are kept in the regular course of business for other purposes including, but not limited to, nontax purposes, the tax imposed by RCW 82.08.020 does not apply to that portion of the selling price of the code attributable to the products and services that are not subject to the tax imposed by RCW 82.08.020.

Value of digital goods, digital codes, digital automated services, and on-demand software services for use tax purposes:

Under current law, use tax is calculated by multiplying the tax rate by the value of the product or service. Generally, the value of the product or service will correspond with its purchase price. However, where the purchase price does not reflect the true value of the product or service, or when the product or service was not acquired by purchase, value is determined based on the retail selling price at place of use of similar products or services of like quality and character.

Under this proposal, the definition of "value of the service used" in RCW 82.12.010(3) would be amended to clarify that the definition applies to digital automated services and on-demand

software services in addition to other services. RCW 82.12.010 would also be amended to add a definition of “value of the digital good or digital code used.”

Proposed bill language to provide a definition of “value of the digital good or digital code used”:

(5) “Value of the digital good or digital code used” means the purchase price for the digital good or digital code, the use of which is taxable under this chapter. If the digital good or digital code is acquired other than by purchase, the value of the digital good or digital code must be determined as nearly as possible according to the retail selling price at place of use of similar digital goods or digital codes of like quality and character under rules the department may prescribe;

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