

Taxing Cloud Services and Digital Goods in Washington

Caleb Allen, JD

Washington State Dept of Revenue
(Interpretations and Technical Advice)

September 8, 2014

Introduction

- With respect to digital transactions (including digital goods and cloud services):
 - Why did Washington update its law?
 - How did Washington update its law?
 - What are some of the continuing challenges?

Prior to 2007

- Trends:
 - Increased Internet usage.
 - Increased bandwidth available.
 - Increasing number of products and services offered/delivered over the internet.
 - Increasing number of disputes between DOR and taxpayers about taxability of transactions.

Tipping Point?

- A taxpayer requested a specific exemption for its industry
- Information electronically delivered
- Raises Questions
 - What other transactions and industries need exemptions?
- Focuses industry, DOR and legislature

Legislature Takes Initial Action

- Legislature requests that the DOR form a committee to study digital transactions taxation
 - Committee included industry, government and academia
 - Two year process looking at other states and countries treatment of digital transactions etc

Report and Recommendation

- Some findings:
 - Antiquated tax law creates ambiguity
 - Risk of erosion to tax base as products and services move online
 - Need to be in compliance with SSUTA if taxing digital goods (can't be TPP)
- Some principles:
 - Simplicity
 - Conformity to SSUTA
 - Competitiveness
 - Durability of solution

The Legislation

- Comprehensive legislation effective in July of 2009
- Clarifying legislation effective in June of 2010
- A working frame work for addressing digital transactions including digital goods and cloud services
- Continuing tweaks?
 - e.g. exemptions, exclusions etc

Washington Law

- Digital products are subject to retail sales tax:
 - Digital goods
 - Digital automated services (DAS)
 - Digital codes
 - Remote access software (RAS)

Digital Goods

- Digital goods:
 - SSUTA: (“specified digital goods”) digital books, music, and video.
 - Washington: sounds, images, data, facts or information or any combination thereof
 - E.g. digital picture, engine schematic, PDF file etc.

Remote Access Software (RAS)

- Washington taxes prewritten software:
 - Tangible media (sale of TPP)
 - Downloaded (sale of TPP)
 - Accessed remotely (retail service = RAS)
 - Charges for the right to access and use prewritten software where possession is maintained by seller
 - Regardless of how charged.

Digital Automated Services (DAS)

- Beyond software and digital goods.
- Digital automated service (DAS) is unique:
 - “...any service transferred electronically that uses one or more software applications...”
 - Broad imposition but lots of exclusions (e.g. advertising, hosting etc)
- Examples: online information services, litigation support, web crawling (gathers information) etc.
- With DAS category WA addressed:
 - Rapid change in business models and technology.
 - Changes could make digital good and RAS categories obsolete (see next slide).

Software/RAS & Digital Good Morph

- Software/RAS:
 - CD with software/game in store
 - Access to software/game online
 - Access to software/game online PLUS service:
 - Real time multiplayer functionality
 - Chat rooms
 - World wide tournaments
- Digital Good/Music:
 - Music on CD purchased in store
 - Access to streaming “album” online
 - Access to streaming “album” online PLUS service:
 - Ability search history of music group and related groups
 - Ability to buy concert tickets
 - Chat with other music lovers
 - Software tools to compose songs and create digital files

Digital Codes

- Have not been an issue.
- Provides purchaser the right to obtain a digital good or DAS.
 - Example: digital code inside bottle cap allows the purchaser the right to obtain an MP3 file.

How it Fits Together

Remote Access
Software

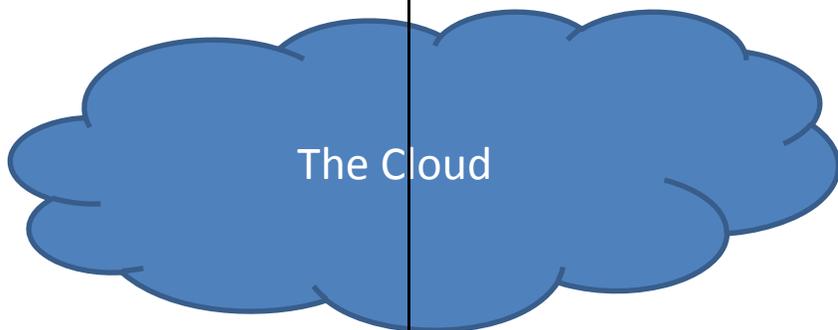
Digital Automated Service

Digital Good

Software

Service that use software

Books,
music,
video,
data, facts,
information



The Cloud

Significant Digital Transaction Issues

- Three significant issues for digital transactions:
 - Taxability
 - Is it one of the enumerated taxable categories?
 - Is it excluded or exempt?
 - Sourcing
 - SSUTA rules and digital transactions
 - Blind forms of payment
 - Marketplace transactions may lack of information
 - Nexus
 - Safe harbors provisions
 - Software on servers in Washington
 - Marketplace service providers