

# Washington's Tax on Digital Products: What Every Seller and Buyer Should Know.

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## I. BACKGROUND

As technology converted (and continues to convert) valuable tangible personal property into valuable intangible property, states became paranoid that a significant part of the sales and use tax base would disappear. Indeed, the sales and use tax constitutes a large portion of a state's revenue.<sup>1</sup> As a wise tax lawyer<sup>2</sup> once said: "Just because I'm paranoid doesn't mean that they are not out to get me!" The states had good reason to be paranoid because their sales and use tax structures were not designed with intangibles, like digital products, in mind. As the digital technology converts more valuable tangible personal property into valuable intangible property, the sales and use tax base will become smaller and smaller if changes to the taxing system are not made.

Many states struggled to retard the erosion of the sales and use tax base by defining intangible property as tangible property. When the Streamline Sales and Use Tax (SSUTA) Agreement prohibited member states from defining a digital product as tangible personal property, it made the fight against the erosion more difficult.

Washington State took the initiative to study the area of digital products and then enacted legislation. After the state studied the issues, there was no agreement as to how digital products should be taxed. There was, however, agreement that it was a complex matter. In the study, it said that the legislature could (1) do nothing, (2) tax discrete components of digital products or (3) tax the universe of digital products, selectively exempting certain digital products when tax policy made sense to do so.

The Association of Washington Business argued against the option to tax the universe of digital products.<sup>3</sup> There is a good tax policy reason for **not** taxing in that overbearing way. By

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<sup>1</sup> Using Washington as an example, in the 2011 Fiscal Year, of the total collection for major taxes, Washington collected 44.9 % from the sales and use tax. See

[http://dor.wa.gov/Docs/Reports/2011/Tax\\_Statistics\\_2011/chart1.pdf](http://dor.wa.gov/Docs/Reports/2011/Tax_Statistics_2011/chart1.pdf)

<sup>2</sup> Sam Saracino (former Davis Wright Tremaine tax partner) ... he gets credit for this though he may have heard this from another wise individual.

<sup>3</sup> AWB Presentation on Digital Goods, Section I.D. page 1, see

<http://dor.wa.gov/docs/reports/digitalgoods/awbpresentationondigitalgoods.pdf>

selectively identifying each kind of digital product to tax as option 2 would require, careful thought would be given to the merits of taxing the specific digital product. In this way, the state would not inadvertently and accidentally impose tax on digital products that should not be taxed but deliberately and intentionally add them to the sales and use tax base upon merit.

Yet, others believed that such an approach coupled with the continuing evolution of digital products would inadvertently exclude too many digital products that should be taxed. Taxing the universe of digital products, in their minds, was a better course because if it turned out to be bad tax policy to tax a particular digital product, then the legislature could always exempt it. Of course, in theory, that is correct. However, there are a few problems with that view. Once the tax collection from such products become part of the revenue forecast, exemptions --- no matter what the laudable merits of the exemption might be --- are difficult to approve when the tax is used to fund education, healthcare and other laudable and demanding social needs. Another problem is that cost prohibitive for small businesses adversely affected by bad tax policy to fund a lobbying campaign to secure an exemption.

What we are left with is a tax on the universe of digital products with select exclusions and exemptions.

## **II. FUNDAMENTALS OF THE TAX ON DIGITAL PRODUCTS**

### **A. To whom does the tax on digital products apply?**

The Business and Occupations (B&O) tax applies to sellers of digital products and digital codes.<sup>4</sup> The rate is .471% for retail sales and .484% for wholesale sales.<sup>5</sup> For businesses that sell digital automated services, the good news is that the B&O tax rate changes from 1.8% (currently) in the service category to .471% or .484%, depending on whether the sale is retail or wholesale.

The sales and use tax applies to buyers of digital products. There is no specific imposition of retail sales tax on digital products. Rather, digital products and digital codes are incorporated into the definition of a “retail sale”.<sup>6</sup> However, for use tax purposes, there is a specific imposition of tax on digital products.<sup>7</sup>

The state sales and use tax rates are 6.5%.<sup>8</sup> The total sales and use tax rates vary by local government (from 7.5% to 9.5%).<sup>9</sup> The Department of Revenue provides these local rates on its website.<sup>10</sup>

Determining if one is selling a retail service is critical, because if the seller makes the wrong determination and the sales tax was due, then the seller will have under-collected sales tax by roughly 7.5% to 9.5% of the gross selling price, depending upon the location of the buyer.

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<sup>4</sup> RCW 82.04.257

<sup>5</sup> RCW 82.04.257(1)

<sup>6</sup> RCW 82.04.050(8)(a) and (b)

<sup>7</sup> RCW 82.12.020(1)(e)(i), (ii) and (iii)

<sup>8</sup> RCW 82.05.020(1) and RCW 82.12.020(4)(a)

<sup>9</sup> RCW 82.14.030

<sup>10</sup> [http://dor.wa.gov/content/findtaxesandrates/SalesAndUseTaxRates/LocalSales\\_Use.aspx](http://dor.wa.gov/content/findtaxesandrates/SalesAndUseTaxRates/LocalSales_Use.aspx)

While the B&O rate will go down, the decrease will not be sufficient to offset the un-collected sales tax liability.

Making the determination as to whether the seller is selling a digital product subject to sales tax is tedious, so some sellers might be tempted to default to treating all sales as subject to sales tax. Why not? The B&O tax rate is more than 1% lower and the economic burden is really the buyer's problem. However, that strategy maybe more dangerous than defaulting to treating all sales as a service ... at least as far as digital automated services is concerned. Over-collecting sales tax when it is not due could leave the seller open to a class action lawsuit.<sup>11</sup> Consequently, a seller must knowingly collect the sales tax when it is due to appease the state and not collect it when it is not due to avoid a possible class action lawsuit.

## **B. What is a digital product under Washington law?**

A digital product means either a “digital good” or “digital automated service.”<sup>12</sup>

### **1. What is a digital good?**

A “digital good” means<sup>13</sup>

- sounds,
- images,
- data,
- facts, or
- information, or
- any combination thereof, that is transferred electronically,
- including, but not limited to,
  - specified digital products and
  - other products transferred electronically not included within the definition of specified digital products.

The final category is vague, making for a very broad definition that taxes the universe of digital goods, even ones that are not yet in existence.

### **2. What is a digital automated service?**

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<sup>11</sup> For example, AT&T was forced to defend a class action because it continued to collect and remit sales tax on data plans when it allegedly knew that the states involved did not require collection of tax. See <http://wirelesscontractsinfo.blogspot.com/2010/11/at-settles-in-class-action-suit-over.html>.

<sup>12</sup> RCW 82.08.192(7)

<sup>13</sup> RCW 82.04.192(6)(a)

A digital automated service is where there will be the most confusion. It means “any service transferred electronically that uses one or more software applications.” RCW 82.04.192(2). That is a very broad definition that taxes the universe of services, potentially including activities that might not occur to a seller or buyer that it actually a retail sale.

**3. What is a “digital code”?**

A "digital code" is a code that gives the buyer the right to buy digital products, but is a taxable digital code only if all of the digital products to be obtained through the code are also subject to the sales and use tax.

**4. What does it mean to be “electronically transferred”?**

"Electronically transferred" or "transferred electronically" means the digital product was obtained by the purchaser by means other than tangible storage media. Access to the digital product is sufficient; physical transfer is not required.<sup>14</sup>

**5. General rule ... the Take Away from these Fundamentals Principles**

Embracing the “taxation of the universe of digital products,” sellers and buyers should consider every digital product as subject to the sales or use tax, including merely accessing a digital product.

### **III. EXCLUSIONS**

Exclusions are better than exemptions because any ambiguity in tax-imposing sections is construed against the taxing authority.<sup>15</sup> Thus, whether the tax applies is determined by inclusions and exclusions, and any ambiguities in construing them are construed against taxation.

**A. Digital Goods**

The term “digital goods” excludes<sup>16</sup> certain activities or items:

- 1 Telecommunications services and ancillary services as those terms are defined in RCW 82.04.065;
- 2 computer software as defined in RCW 82.04.215; or
- 3 the internet and internet access as those terms are defined in RCW 82.04.297.

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<sup>14</sup> RCW 82.04.192(8)

<sup>15</sup> *MAC Amusement Co. v. State Dept. of Revenue*, 95 Wash.2d 963, 633 P.2d 68 (1981), *Foremost Dairies, Inc. v. Tax Commission*, 75 Wash.2d 758, 453 P.2d 870 (1969) and *In re Ehlers' Estate*, 53 Wash.2d 679, 335 P.2d 825 (1959)

<sup>16</sup> RCW 82.04.192(6)(b)

## **B. Digital Automated Services**

The term “digital automated services” also has exclusions. The statute<sup>17</sup> tried to anticipate circumstances when certain services should be exempted. These 16 exempted services (which include a good) are:

- 1 Any service that primarily involves the application of human effort by the seller, and the human effort originated after the customer requested the service;
- 2 The loaning or transferring of money or the purchase, sale, or transfer of financial instruments. For purposes of this subsection ... [2], "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;
- 3 Dispensing cash or other physical items from a machine;
- 4 Payment processing services;
- 5 Parimutuel wagering and handicapping contests as authorized by chapter 67.16 RCW;
- 6 Telecommunications services and ancillary services as those terms are defined in RCW 82.04.065;
- 7 The internet and internet access as those terms are defined in RCW 82.04.297;
- 8 The service described in RCW 82.04.050(6)(b);
- 9 Online educational programs provided by a:
  - (A) Public or private elementary or secondary school; or
  - (B) An institution of higher education as defined in sections 1001 or 1002 of the federal higher education act of 1965 (Title 20 U.S.C. Secs. 1001 and 1002), as existing on July 1, 2009. For purposes of this subsection ... [9(B)], an online educational program must be encompassed within the institution's accreditation;
- 10 Live presentations, such as lectures, seminars, workshops, or courses, where participants are connected to other participants via the internet or telecommunications equipment, which allows audience members and the

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<sup>17</sup> RCW 82.04.192(3)(b)

presenter or instructor to give, receive, and discuss information with each other in real time;

- 11 Travel agent services, including online travel services, and automated systems used by travel agents to book reservations;
- 12 (A) A service that allows the person receiving the service to make online sales of products or services, digital or otherwise, using either: (I) The service provider's web site; or (II) the service recipient's web site, but only when the service provider's technology is used in creating or hosting the service recipient's web site or is used in processing orders from customers using the service recipient's web site.  
  
(B) The service described in this subsection ... [12(B)] does not include the underlying sale of the products or services, digital or otherwise, by the person receiving the service;
- 13 Advertising services. For purposes of this subsection ... [13], "advertising services" means all services directly related to the creation, preparation, production, or the dissemination of advertisements. Advertising services include layout, art direction, graphic design, mechanical preparation, production supervision, placement, and rendering advice to a client concerning the best methods of advertising that client's products or services. Advertising services also include online referrals, search engine marketing and lead generation optimization, web campaign planning, the acquisition of advertising space in the internet media, and the monitoring and evaluation of web site traffic for purposes of determining the effectiveness of an advertising campaign. Advertising services do not include web hosting services and domain name registration;
- 14 The mere storage of digital products, digital codes, computer software, or master copies of software. This exclusion from the definition of digital automated services includes providing space on a server for web hosting or the backing up of data or other information;
- 15 Data processing services. For purposes of this subsection ... [15], "data processing service" means a 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. Data processing services include check processing, image processing, form processing, survey processing, payroll processing, claim processing, and similar activities. Data processing does not include the service described in RCW 82.04.050(6)(b); and
- 16 Digital goods.

## C. Digital Codes

Excluded from "digital code" is a code that represents a stored monetary value that is deducted from a total as it is used by the purchaser (e.g., coupon codes). It also excludes a code that represents a redeemable card, gift card, or gift certificate that entitles the holder to select digital products of an indicated cash value.<sup>18</sup>

## IV. EXEMPTIONS

As mentioned above, there are certain statutory construction rules that apply to exclusions and exemptions. Unlike tax-imposing sections, exemptions are narrowly construed in favor of taxation.<sup>19</sup>

### A. Digital Goods

#### 1. Free to the General Public

The law exempts businesses<sup>20</sup> from sales and use tax if the business makes digital goods available free for the use and enjoyment of the general public.<sup>21</sup> "General public" means all persons not a discrete class of persons except classes of persons who

- Reside or own property within a state, political subdivision or municipal corporation or
- Are authorized library patrons.<sup>22</sup>

The exemption must be documented by an exemption certificate.<sup>23</sup>

#### 2. Business Purpose

The law exempts sales and use of digital goods (or services rendered in respect to digital goods<sup>24</sup>) if the digital goods and services rendered in respect to such digital goods are purchased solely for business purposes.<sup>25</sup> "Business purpose" means "any purpose" that is relevant to the business needs of the purchaser.<sup>26</sup> The exemption must be documented by an exemption

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<sup>18</sup> RCW 82.04.192(5)

<sup>19</sup> *Budget Rent-A-Car of Wash.-Or, Inc. v. Department of Rev.*, 81 Wash.2d 171, 500 P.2d 764 (1972), *Evergreen-Washelli Memorial Park Co. v. Department of Revenue*, 89 Wash.2d 660, 574 P.2d 735 (1978).

<sup>20</sup> Ordinarily, sales and use tax exemptions apply to specific kinds of transactions or uses but in this case, the exemption actually applies to a taxpayer as opposed to the taxpayer's transaction or use.

<sup>21</sup> RCW 82.08.02082(1) and RCW 82.12.02082

<sup>22</sup> See footnote 21

<sup>23</sup> RCW 82.08.02082(2)

<sup>24</sup> This service is not the same as "digital automated services"; this service repairs to labor that is related to installing, repairing, altering or improving a digital good for consumers. RCW 82.04.050(g)

<sup>25</sup> RCW 82.08.02087(1)

<sup>26</sup> RCW 82.08.02087(3)(a)

certificate.<sup>27</sup> Similarly, the law also exempts digital goods (or services rendered in respect to digital goods) from the use tax.<sup>28</sup>

### 3. Concurrent Use

The law exempts sales of digital goods, digital codes and digital automated services if the buyer will employ them in multiple points of use in concurrent use both within and without the state.<sup>29</sup> The exemption must be documented by an exemption certificate.<sup>30</sup>

Concurrent use means that the employees (or purchaser's agents) may use the digital goods and digital automated services simultaneously from more than one location within and without the state.<sup>31</sup> It does not include multiple uses within only Washington.

However, for use tax purposes, the buyer must determine how much of the concurrent use occurs in Washington.<sup>32</sup> The use is apportioned; it is determined by counting the users within Washington and the total employees everywhere using the digital product.<sup>33</sup> The number of Washington users is the numerator and the total is the denominator. The resulting percentage is multiplied times the tax that would have been charged as if the entire charge was subject to use tax.<sup>34</sup> The taxpayer must keep records in the ordinary course of business that reflects which employees use the digital products from multiple locations within and without Washington.<sup>35</sup>

### 4. Use by students

Digital goods may be used by students in public or private primary or secondary schools or certain institutions of higher education and exempt from for use tax.<sup>36</sup> There is no corresponding sales tax exemption.

### 5. Non-residents

Sales of digital goods to non-residents are exempt from sales tax if

- The digital goods will be used out of state
- The non-resident is a bona fide resident of a Canadian province or territory, possession of the United States and any other state except Washington.<sup>37</sup>

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<sup>27</sup> RCW 82.08.02087(2)

<sup>28</sup> See footnote 25

<sup>29</sup> RCW 82.08.02088(1) and (2)

<sup>30</sup> *Id.*

<sup>31</sup> RCW 82.08.02088(4)

<sup>32</sup> RCW 82.12.02088(1)

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*

<sup>35</sup> RCW 82.12.02088(2)

<sup>36</sup> RCW 82.12.02084

<sup>37</sup> RCW 82.08.0273(1)

To be a qualified state or province of residency, the state has no sales, use, value added, gross receipts (on retailing activities) or similar taxes of three percent or more.<sup>38</sup> The qualified state must have a reciprocal exemption for Washington residents.<sup>39</sup>

**6. Non-commercial use**

Use of digital goods are exempt from use tax if they are non-commercial in nature, created solely for an internal audience or created solely for the business needs of the creator and is not of the type of digital good that the creator offers for sale.<sup>40</sup>

**7. Distributed “free of charge”**

Use of a digital product by a user that the user received for free is exempt from the use tax.<sup>41</sup>

**8. Donated**

Donated digital goods or digital codes are exempt from use tax when irrevocably donated to any public or private school.<sup>42</sup>

**B. Digital Automated Services**

**1. Free to the General Public**

The law exempts businesses<sup>43</sup> from the sales and use tax if the business makes digital automated services available free for the use and enjoyment of the general public.

**2. Business purpose**

The law failed to exempt digital automated services used solely for business purposes.

**3. Concurrent use**

See discussion in sub-paragraph 3 on page 8.

**4. Use by students**

The law failed to exempt digital automated services from use tax used solely for use by students.

**5. Organizations incorporated under any act of Congress**

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<sup>38</sup> RCW 82.08.0273(1)(b)(i)

<sup>39</sup> RCW 82.08.0273(1)(b)(ii)

<sup>40</sup> RCW 82.12.02085

<sup>41</sup> RCW 82.12.02086

<sup>42</sup> RCW 82.12.0284

<sup>43</sup> See footnote 20

Exempt is the use of digital automated services by corporations that have been incorporated under any act of the Congress. The taxpayer must have as its principal purposes to furnish volunteer aid to members of the armed forces of the United States and also to carry on a system of national and international relief and to apply the same in mitigating the sufferings caused by pestilence, famine, fire, flood, and other national calamities and to devise and carry on measures for preventing the same.<sup>44</sup>

**6. Non-residents**

See discussion in sub-paragraph 5 on page 8.

**7. Non-commercial use**

Use of digital goods are exempt from use tax if they are non-commercial in nature, created solely for an internal audience or created solely for the business needs of the creator and is not of the type of digital good that the creator offers for sale.<sup>45</sup>

**8. Distributed “free of charge”**

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**C. Digital Codes**

**1. Access to digital products that are exempt**

Digital codes are exempt from sales and use tax if the digital products purchased are also exempt from sales and use tax.<sup>48</sup>

**2. Business purpose**

See discussion in sub-paragraph 2 on page 7.

**3. Concurrent use**

See discussion in sub-paragraph 3 on page 8.

**4. Non-residents**

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<sup>44</sup> RCW 82.12.0259

<sup>45</sup> RCW 82.12.02085

<sup>46</sup> RCW 82.12.02086

<sup>47</sup> RCW 82.12.0284

<sup>48</sup> RCW 82.08.0208 and RCW 82.12.0208

See discussion in sub-paragraph 5 on page 8.

5. Distributed ‘free of charge’

See discussion in sub-paragraph 7 on page 9.

**V. BUNDLED TRANSACTIONS ... DOES THIS AID IN DETERMINING THE PROPER TAX CLASSIFICATION?**

The legislature enacted laws regarding bundled transactions to conform to SSUTA. The law recognizes that transactions can be bundled to include a mixture of components that may or may not be subject to sales or use tax. This is not really an exemption but more in the nature of a tax-imposing section. The laws define “bundled transactions” and how to impose tax on bundled transactions.<sup>49</sup>

“Bundled transaction” is defined to mean a transaction that includes distinct and identifiable products but are sold in a single price.<sup>50</sup> As for the taxability of the transaction, the general rule is that a bundled transaction is subject to sales or use tax.<sup>51</sup>

However, the law also permits the seller and buyer, in the case of a retail sale, and the buyer in the case of use tax, to determine the bundle by the “true object”.<sup>52</sup> Thus, if a seller sold digital goods that were properly exempt under the business purpose exemption, as well as digital automated services, then the transaction or use should be classified by the “true object”. If the “true object” was to purchase the exempt digital goods, then the entire transaction should be exempt from sales or use tax and the digital automated services should not cause the transaction to be subject to the sales or use tax. However, DOR has signaled a rejection that the bundled transaction rules will apply in this way.

**VI. SOURCING THE SALE TO A LOCATION**

Once a sale has been made, the seller must determine at what rate tax must be collected. Under SSUTA, sales are sourced to the destination.<sup>53</sup> The sourcing rules are:

- If the purchaser receives the digital good, digital automated services or digital code at the seller’s place of business, then the **seller’s place of business** is the place of sale.<sup>54</sup>
- If receipt is not at the seller’s business location, then the sale of the digital good, digital code, digital automated service, is sourced **to the location where receipt by the purchaser** or the purchaser's donee, designated as such by the purchaser, **occurs**,

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<sup>49</sup> RCW 82.08.190 and RCW 82.08.195

<sup>50</sup> RCW 82.08.190(1)(a)(i) and (ii)

<sup>51</sup> RCW 82.08.195(1) and RCW 82.12.195(1)

<sup>52</sup> RCW 82.08.195(2) and RCW 82.12.195(2)

<sup>53</sup> RCW 82.32.730

<sup>54</sup> RCW 82.32.730(1)(a)

including the location indicated by instructions for delivery to the purchaser or donee, known to the seller.<sup>55</sup>

- If the receipt still cannot be sourced, then the sale is sourced to **the buyer’s address that is kept in the seller’s business records**, so long as such records are maintained in the ordinary course of the business and the use of the address is not in bad faith.<sup>56</sup>
- If the receipt still cannot be sourced, then the sale is sourced to the **buyer’s address obtained during the consummation of the sale**, including the address of a purchaser's payment instrument, if no other address is available and the use of the address is not in bad faith.<sup>57</sup>
- If the receipt still cannot be sourced, then the location shall be determined by the address from which the digital good or digital code or the computer software delivered electronically was first available for transmission by the seller, or where digital automated service was provided, disregarding for these purposes any location that merely provided the digital transfer of the product sold.<sup>58</sup>

The terms, “receive” and “receipt,” are statutorily defined.<sup>59</sup> They mean where buyer makes first use of a digital automated service or where the buyer takes first possession or makes first use of digital goods or digital codes, whichever first occurs.

## VII. THE RULE’S APPROACH TO THE ANALYSIS

The draft rule actually provides a fairly good approach to analyzing digital products. The rule is structured in parts with each part captioned with a question:

Part 1: Are the Products or Services Transferred Electronically?<sup>60</sup>

Part 2: Does the Product or Service meet the General Definition of Digital Product or Digital Code?<sup>61</sup>

Part 3: Are There Applicable Exclusions from the General Definitions of Digital Product and Digital Code?<sup>62</sup>

Part 4: Are the Sales of the Digital Product or Digital Code Sourced to Washington?<sup>63</sup>

Part 5: Are there Applicable Retail Sales or Use Tax Exemptions for the Purchase or Use of the Digital Product or Digital Code?<sup>64</sup>

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<sup>55</sup> RCW 82.32.730(1)(b)

<sup>56</sup> RCW 82.32.730(1)(c)

<sup>57</sup> RCW 82.32.730(1)(d)

<sup>58</sup> RCW 82.32.730(1)(e)

<sup>59</sup> RCW 82.32.730(9)(f)

<sup>60</sup> Draft WAC 458-20-15503, page 1

<sup>61</sup> Draft WAC 458-20-15503, page 2

<sup>62</sup> Draft WAC 458-20-15503, page 6

<sup>63</sup> Draft WAC 458-20-15503, page 13

Of course, there are several nuances in the way in which DOR interprets the statutes, and the draft rule tries to demonstrate the principles with many examples. Until DOR finalizes the rule, however, there is no assurance that the principles and examples will be DOR's final interpretation.

## VIII. LIST OF RESOURCES

### A. Report on Digital Products, December 5, 2008<sup>65</sup>

In 2007, the Washington Legislature required the Washington Department of Revenue to conduct a study of the potential sales and use taxation of digital goods. The study committee consisted of members from industry, the Department of Revenue and the legislature. The report did not recommend any course of action but identified issues.

According to the study, the following problems lead to the study:

1. Current excise tax law lacks specificity, which leads to a lack of transparency and certainty, and results in disagreements between the Department of Revenue, taxpayers, and those charged with the collection and remittance of the tax. This could result in class action lawsuits being filed by customers of those charged with collecting and remitting the tax;
2. Application of current law may not be durable in the face of changing technology;
3. Developing a tax policy that treats conventional and digital goods equally in all instances will be difficult;
4. As new digital goods and existing conventional goods are digitized, Washington and local governments may face a reduction of the retail sales and use tax base if digital goods are removed from the retail sales and use tax base;
5. Many digital activities can be easily moved to other jurisdictions to avoid tax liability; and
6. To continue to tax products delivered electronically while remaining in conformity with the SSUTA, Washington must adopt a statute specifically authorizing the taxation of such items.

Points 1 and 2 are directed at confusion in the taxation of digital produces, both current and future. Point 3 is directed at equality between functional equivalents that results in different tax results based only on form. Points 4, 5 and 6 are directed at preserving the tax revenue from existing sales and use tax sources in the pre-digital world.

With regard to Point 6, the Streamline Sales and Use Tax Agreement (SSUTA) prohibited a state from concluding that a digital product was the same as tangible personal

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<sup>64</sup> Draft WAC 458-20-15503, page 15

<sup>65</sup> See [http://dor.wa.gov/Docs/Reports/DigitalGoods/Digital\\_Goods\\_Study\\_Final\\_Report.pdf](http://dor.wa.gov/Docs/Reports/DigitalGoods/Digital_Goods_Study_Final_Report.pdf)

property, and therefore subject to sales and use tax. However, SSUTA did permit states to define “digital products” and choose whether to impose tax on such products. Under SSUTA, DOR could impose no tax, selectively impose tax or generally impose tax.

**B. Engrossed Substitute House Bill 2075, Chap. 535, Laws of 2009 (ESHB 2075)<sup>66</sup>**

This bill is the by-product of the work done by the Study Committee, enacting provisions to tax Digital Products.

**C. Substitute House Bill 2620, Chap. 111, Laws of 2010 (SHB 2620)<sup>67</sup>**

This bill added clarification language to the 2009 law.

**D. Excise Tax Advisory 9002 (July 24, 2009)**

This advisory addresses taxing digital songs, movies, books and online games transferred electronically.

**E. Special Notices June 29, 2010 and November 2, 2010**

The June special notice explains that SHB 2620’s clarified of the ambiguities in ESHB 2075.

The November 2, 2010 special notice *retreats* from earlier agency guidance that online searchable databases (OSD) were exempt if used solely for business purposes.

**F. Excise Tax Advisory 9003 (November 30, 2010)**

This advisory sets up a decision tree to help taxpayers determine whether a digital product is subject to the sales or use tax.

**G. Excise Tax Advisory 9001 (June 30, 2011)**

This advisory generally describes the law changes in 2009 and 2010.

**H. Excise Tax Advisory XXXX (draft, adoption pending)**

This advisory is intended to provide guidance for sourcing digital products and digital codes.

**I. Drafts of Proposed WAC 458-20-15501 (Taxation of Computer Systems and Hardware), -15502 (Taxation of Computer Software) and -15503 (Taxation of Digital Products)**

These draft rules are proposals to implement ESHB 2075 and SHB 2620.

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<sup>66</sup> See <http://apps.leg.wa.gov/billinfo/summary.aspx?bill=2075&year=2009>

<sup>67</sup> See <http://apps.leg.wa.gov/billinfo/summary.aspx?bill=2620&year=2009>