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PAUL J. HARTMAN
STATE AND LOCAL TAX FORUM


Short Circuit – Quick Takes on All Things Digital

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Taxation of Technology: Where Have We Been, and Where Are We Going?

Kyle M. Brehm
Fredrikson & Byron



Where Have We Been?

- Indirect Taxes Imposed
 - Sales and Use Tax: Sale or use of tangible personal property and specifically enumerated services (states vary dramatically on how broadly they tax services).
 - Gross Receipts Tax: Gross receipts less exemptions/exclusions/deductions
- Sourcing of Transactions Involving Tangible Personal Property
 - Intrastate: Origin v. Destination Sourcing
 - Interstate: Destination Sourcing
- Sourcing of Service Transactions
 - First use, multiple points of use
 - Services Performed v. Benefit Received

What About Technology Transactions?

- Software
 - Tangible Goods
 - Services
- Digital Goods & Services
 - Specified Digital Products
 - Other Digital Products
 - Digital Services

Software Treated as a Tangible Good

- Single User
 - Delivered via Tangible Media – Almost Always Taxable
 - Delivered Electronically – Taxable in Approximately 80% of States
- Multiple Users
 - Centrally Hosted
 - Distributed to Users – Impact of Multiple Points of Use (“MPU”)

Software Treated as a Service

- SaaS/laaS/PaaS – Taxed in Nearly Half of the States
 - Personal or Business Use?
- Information and Data Processing Services (e.g., Minnesota, Ohio, Texas)
- Telecommunication Services (e.g., Wisconsin)

- Software Related Services
 - Custom Software
 - Implementation v. Installation
 - Maintenance & Support
 - Warranties

What About Digital Goods & Services

- Specified Digital Products (i.e., music, books, and movies)
- Other Digital Products (e.g., video games, photos, greeting cards, etc.)
 - Does this include electronically-delivered software, SaaS, information services, in-app purchases?
- Digital Service Taxes
 - Maryland as a “test case”
 - Impact of ITFA?
- What about Sourcing?
 - Digital Products – Business-to-Business or Business-to-Consumer?
 - Digital Services – “Device accessing digital ads in the state”

Where Are We Going?

- Cryptocurrency
- Non-Fungible Tokens (“NFTs”)
- In-App Purchases
- Metaverse
 - Advertising
 - Loyalty Programs
 - “Product” Sales

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Into the METAVERSE...

Eric M. Anderson
ANDERSEN

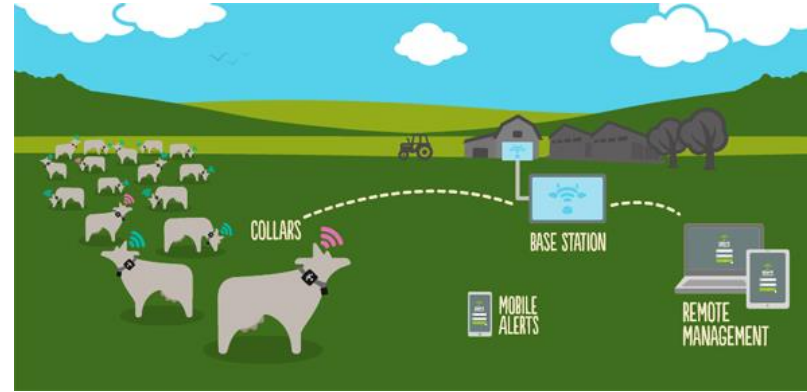


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What can be done in the METaverse?



But is the METaverse for real?

- The Metaverse market is projected to reach a value of US\$74.4bn in 2024.
- Projected annual growth rate (CAGR 2024-2030) of 37.73% resulting in a projected market volume of US\$507.8bn by 2030.
- By 2030, the number of users in the Metaverse market is expected to reach 2.6B users.
- The user penetration is predicted to be 14.6% in 2024 and is expected to increase to 39.7% by 2030.

Based upon public information provided by Statista.com

Taxes have surely caught up...



Try this at home....

...In RIA Checkpoint or your research tool of choice...

Type in “metaverse” and see your results...

Where is tax policy on the METaverse?



Perceptible to the senses?

ADP, LLC vs. Arizona Department of Revenue
(AZ Court of Appeals 1/31/2023)

DirecTV, Louisiana BOA (3/14/2024)

Software just IS tangible personal
property...period?

Akamai Technologies, Inc. v. Comm'r, MA
App. Bd. (12/10/2021)

Use Cases and Use Tax



1. You purchase one in a series of NFTs that is a virtual image of basketball shoes signed by a famous player. As part of the purchase, you also receive a poster of the player wearing the shoes.
2. In your virtual gym, you can pay an extra fee to have the gym transformed into a theme, like being in a Star Wars movie or being in a national park.
3. Your company purchases an inventory management system that scans SKUs when a person wearing a device looks at the item. You pay nothing for the devices but must license the platform for \$10,000 per month.
4. Your company decides to accept BitCoin but charges an extra fee to the buyers for the privilege.



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Into the future...

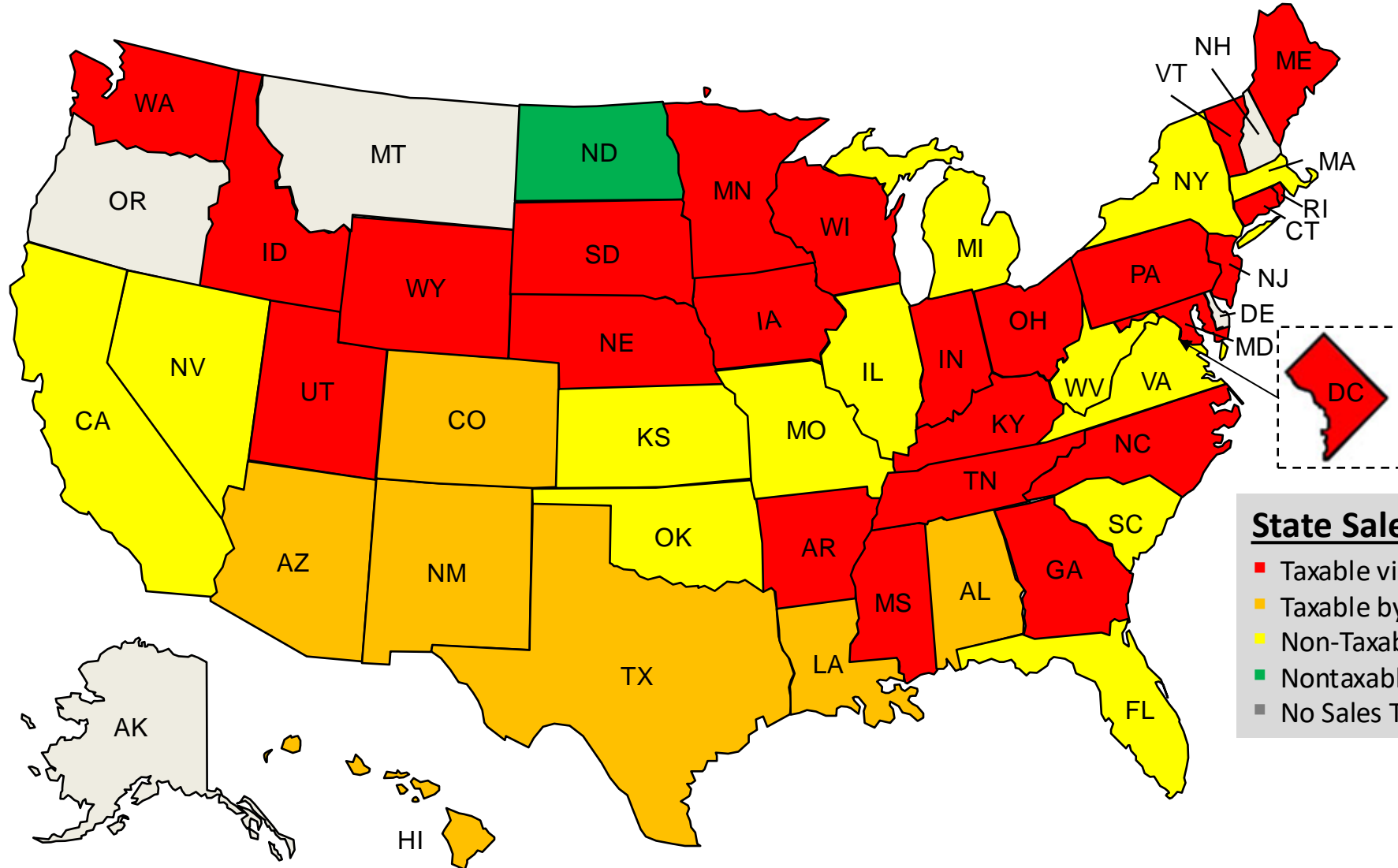


It's Not Taxable Unless The Legislature Says So Expressly.....

Carolynn S. Kranz
Kranz & Associates PLLC / ISTS



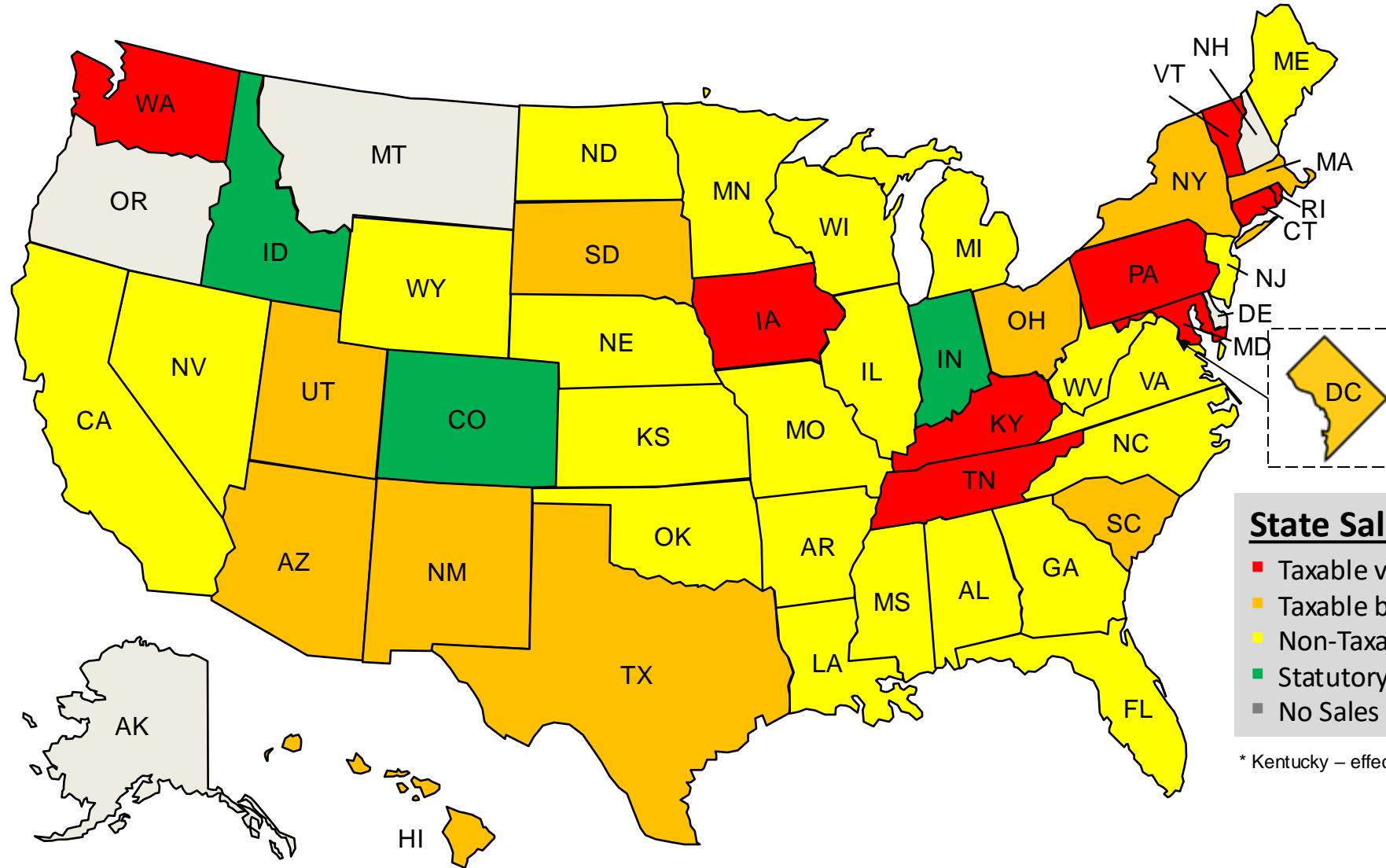
Taxation of Digital Products



State Sales Tax Treatment

- Taxable via Statute (24)
- Taxable by DOR Interpretation (7)
- Non-Taxable by DOR Interpretation (14)
- Nontaxable by Exemption (1)
- No Sales Tax (5)

Taxation of SaaS



State Sales Tax Treatment

- Taxable via Statute* (9)
- Taxable by DOR/Judicial Interpretation (11)
- Non-Taxable by DOR/Judicial Position (23)
- Statutory Exemption (3)
- No Sales Tax (5)

* Kentucky – effective Jan. 1, 2023

Current Issues & Considerations

- Can there an objective standard for determining taxability in states that attempted to legislatively address certain cloud models?
 - Vendor hosted or remotely hosted software falls within the SaaS category, but how will states treat other SaaS models that have traditionally been viewed as services, but involved an accessed software component (i.e., payroll processing)?
- In states that limit the taxation of SaaS to remotely accessed software, the presumption is that all SaaS models are, in fact, prewritten computer software.
 - Should the true object of the transaction control?
 - How do incidental software transfers (i.e., API's, desktop agents and applets) impact the transaction?
 - How will states that do not tax SaaS, but tax electronically delivered software, treat a SaaS transaction where the vendor also provides an incidental free app?

National Efforts for Policy Reform

- Multistate Tax Commission
 - In June 2021, the MTC Uniformity Committee embarked on a project to produce a white paper on the state sales taxation of digital products.
 - The Washington DOR has taken a leading role because that state enacted a broad-based tax on digital automated services.
 - The group has recently drafted a white paper addressing bundling issues.
- SST
- NCSL
 - Preparing a primer for state legislators for the upcoming legislative sessions.