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**Issue Paper**  
**Digital Products Sourcing**  
**February 2, 2011**

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**Background**

- **Sourcing provisions:** On November 12, 2002, SSUTA §§ 309, 310.A, and 311 were adopted. *See Appendix A of this Paper.* Together these provisions establish the general framework for sourcing retail sales, subject to certain exclusions.
  - **Digital products definitions:** On September 20, 2007, the Governing Board adopted the digital products definitions in the SSUTA’s Library of Definitions. *See Appendix B of this Paper.* The Governing Board also adopted SSUTA § 332 and § 333 and Governing Board Rule 332.1. *For SSUTA § 332.G and Rule 332.1.G see Appendix C of this Paper.*
  - **First public digital sourcing issue:** During the 2009 Governing Board annual compliance review, Kentucky raised the issue of whether SSUTA § 310.A contemplated place of primary use sourcing, or some other method of sourcing, for certain digitally accessed products. This question was later resolved after statutory changes were made to eliminate place of primary use sourcing for digital products under Kentucky law.
  - **Federal Digital Goods and Services Tax Fairness Act of 2011:** In May 2011, the federal Digital Goods and Services Tax Fairness Act was introduced in Congress (H.R. 1860 and S.971). H.R. 1860 was heard in the House Subcommittee on Courts, Commercial and Administrative Law later that same month. This bill would have created new federal rules for the sourcing of digital goods and services. The 2011 Act was preceded by the Digital Goods and Services Tax Fairness Act of 2010, which contained similar although not identical language.
  - **Second public digital sourcing issue:** During the 2011 Governing Board annual compliance review, the BAC raised an issue related to how sales of remotely accessed prewritten computer software should be sourced. The question arose out of concurrent discussions about whether that prewritten software could be taxed as tangible personal property, computer software, services, or some combination thereof under the SSUTA. These issues remain outstanding with the Governing Board. These issues are outside the scope of this Workgroup.
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**Digital Sourcing Workgroup**

At the Governing Board’s October 2011 meeting in Seattle, the Governing Board directed the State and Local Advisory Council (“SLAC”) to work on digital products sourcing. SLAC then formed the Digital Products Sourcing Workgroup (the “Workgroup”). This document is intended to memorialize the Workgroup’s progress and recommendations, if any.

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**Workgroup scope and process**

- Identify interpretive issues related to the sourcing of specified digital products under SSUTA §§ 309 (application of the sourcing rules and exclusions), 310.A (general sourcing rules), 311 (general sourcing definitions), and 332.G (re: digital codes).
- Develop recommendations for this Issue Paper; and
- Draft interpretive rule language or recommend amendment to the agreement as needed.

*Note: While other products transferred electronically are currently beyond the scope of the Workgroup, this issue could be revisited in future periods.*

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**Issue summary**

- **Issue I: Workgroup process.** Does the Workgroup recommend developing an interpretative rule that generally explains the sourcing of specified digital products together with the development of this Issue Paper?
- **Issue II: Location of receipt:** How does the concept of “receipt” apply for purposes of sourcing specified digital products under SSUTA § 310.A.1 and .2?
- **Issue III: Collecting and maintaining buyer address information:** How does SSUTA § 310.A.3 and 4 and the member states’ recordkeeping requirements apply to the sale of specified digital products where sellers:
  - May not collect and/or maintain purchaser address information, or
  - Do not otherwise collect purchaser address information because of arrangements with third parties?
- **Issue IV: Sourcing allocation:** Is clarification needed with respect to sourcing allocation of specified digital products where the products may be sold in multiple locations to the purchaser? If “yes,” what is the recommended clarification?
- **Issue V: Origin sourcing:** How is SSUTA § 310.A.5 applied in the context of specified digital products? Specifically, what is contemplated by

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the following phrase:

“the location...from which the digital good...was first available for transmission by the seller, or from which the service was provided (disregarding for these purposes any location that merely provided the digital transfer of the product sold).”

**Issue I:  
Workgroup  
process**

**Issue statement:**

Should the Workgroup develop an interpretative rule that generally explains sourcing together with the development of this Issue Paper?

**Workgroup recommendation:**

Yes.

**BAC Subcommittee (Agrees/Disagrees)**

**Rationale:**

This will best help focus the Workgroup in addressing the issues presented. The workgroup had been evenly split on the issue initially and the split was resolved in favor of beginning to draft language.

**SSUTA amendment required (yes/no):**

No.

**Alternative options:**

Develop both the Issue Paper and an interpretive rule.

Develop the Issue Paper first and at the completion of the Issue Paper consider drafting interpretive rule language.

**Discussion:**

On January 9, 2012, the Workgroup discussed whether, in addition to the Issue Paper, it should begin drafting interpretative rule language on sourcing.

Some representatives from the states expressed support for developing both the Issue Paper and interpretative rule language at the same time. The approach has the benefit of providing structure for the group’s efforts, allowing stakeholders to identify issues by working through the SSUTA’s sourcing language, and of contributing to an efficient use of time and resources.

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A representative of the business community expressed concern that the process of drafting rule language may distract from fully vetting the issues for purposes of the Issue Paper. In subsequent discussions there was a recognition that drafting rule language may be helpful

A survey of the states and the BAC was conducted in March 2012 as follows:

<b>Prefer Developing Stand-Alone Issue Paper</b>	<b>Prefer Developing the Issue Paper and Interpretive Rule</b>
IA, MN, WI, MI, BAC	NE, TX, WA, UT, TN

**Issue II:  
Location of  
receipt**

**Issue statement:**

How does the concept of “receipt” apply for purposes of sourcing specified digital products under SSUTA § 310.A.1 and .2?

SSUTA § 310.A.1 and .2 provide:

1. When the product is received by the purchaser at a business location of the seller the sale is sourced to that business location.
2. When the product is not received by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser (or the purchaser's donee, designated as such by the purchaser) occurs, including the location indicated by instructions for delivery to the purchaser (or donee), known to the seller.

**Workgroup recommendation:**

The Workgroup recommends that “receipt” occurs at the physical location of the purchaser at which the specified digital product is viewed, read, or listened to. Examples illustrating this concept of “receipt” and when this location is known are included in proposed Rule 309.6.D.1 and 2.

**BAC Subcommittee (Agrees/Disagrees)**

**Rationale:**

The recommendation results in the sourcing of sales of specified digital products on a destination basis consistent with the purpose contemplated with the adoption of SSUTA § 310.

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**SSUTA amendment required (yes/no):**

No.

**Alternative options:**

None.

**Discussion:**

**Introduction:**

Sourcing pursuant to SSUTA § 310.A.1 and .2 involve two primary questions as follows:

- What does “receipt” and “receive” mean in the context of sourcing specified digital products?
- In the context of sourcing specified digital products, when is receipt “known” to the seller?

*Note: In determining “receipt” the workgroup makes clear its recommendations impact sourcing only and are not intended to impact other issues such as tax imposition.*

**1. What does “receipt” and “receive” mean in the context of sourcing specified digital products?**

*Application of “receipt” to specified digital products generally:*

Section 311 of the Agreement defines the terms “receive” and “receipt” for purposes of the sourcing rules of Section 310.A. The words “receive” and “receipt” appear in §§ 310.A.1 and A.2. Section 311 provides:

“For the purposes of Section 310, subsection (A), the terms “receive” and “receipt” mean:

- A. Taking possession of tangible personal property,
- B. Making first use of services, or
- C. Taking possession or making first use of digital goods, whichever comes first.”

There is no definition in the Agreement for the term “digital goods.” However, discussion among workgroup participants indicate that “digital goods” at a minimum should include specified digital products.

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The Workgroup recommends that “receipt” occurs at the physical location of the purchaser at which the specified digital product is viewed, read, or listened to. Examples illustrating this concept are included in proposed Rule 309.6.D.1 and 2.

## 2. In the context of sourcing specified digital products, when is receipt “known” to the seller?

SSUTA 310.A.2 requires that sales be “sourced to the location where receipt by the purchaser...occurs, including the location indicated by instructions for delivery to the purchaser (or donee), known to the seller.” Based upon the language of Governing Board Rule 311.1, it appears “known to seller” is contemplated as applying to the location of “receipt” possibly as identified in instructions or otherwise.<sup>1</sup>

Unlike with the delivery of tangible personal property, it may be more difficult for the seller to know the location where specified digital products are received. That is, the seller is transmitting the specified digital product electronically and it may be challenging to know with certainty the physical location where the purchaser is actually taking possession or making first use.

Proposed Rule 309.6.D.1 and .2 are examples of where the seller may reasonably know the location of receipt because in cases where the purchaser comes to the seller’s place of business and the seller actively facilitates the electronic transmission of the specified digital product or where seller provides the specified digital and the method of delivering that product to fixed service known location. The examples are not intended to be exhaustive of all the situations where “receipt” may be known. However, outside this specific context, sellers may face greater challenges in knowing the location of receipt and may at times need to default to the sourcing rules in SSUTA § 310.A.3, .4, .5.

<sup>1</sup> A. Except as otherwise provided in the Streamlined Sales and Use Tax Agreement, sellers of services are to source the sales of those services under the general destination sourcing regime of section 310.A of the Agreement. Section 310.A.1 provides that in cases where the service is received by the purchaser at a location of the seller, the seller is to source the service to that location under section 310.A.1 of the Agreement. If the purchaser receives the service at any other location, and that location is known to the seller, the sale of the service is sourced to that location. If the location of receipt by the purchaser is unknown to the seller of the service, the seller should source the sale of the service according to the provisions of section 310.A.3, .4 or .5 of the Agreement as appropriate. *Governing Board Rule 311.1 – Receipt of Services Generally.*

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Additionally, similar to transactions involving tangible personal property, purchasers may provide sellers with instructions indicating where they expect to take possession or make first use of a specified digital product at a specified physical location. However, unlike with tangible personal property, it may be more difficult for the seller to know with certainty that the instructions correspond with the location of receipt. **The workgroup recommends that instructions for delivery language do/does not apply to specified digital products.**

**See Rule 309.2 Sourcing of Prewritten Computer Software Ex. 2 as follows: “Seller electronically delivers copies of the prewritten computer software to multiple locations of the Purchaser. The Seller has the information identifying the multiple locations for the electronic delivery of the prewritten computer software. The Seller sources the retail sale to each jurisdiction where the Purchaser receives the prewritten computer software.”**

*Example 3: SSUTA 310.A.2 - Other location...instructions to the seller.*

- Facts: Company Y purchases a video from Company Z. The video qualifies as a specified digital product. Company Z maintains an address for Company Y in its books and records in State 1. Company Z electronically transmits the video to a server. At the time of purchase, Company Y provides instructions to Company Z indicating a “ship-to” address in State 3 where it intends to take possession or make first use of the video.
- Conclusion:

**How do the “receipt” based sourcing rules relate products sold by mobile telecommunications services providers? Are these products sourced to the customer’s place of primary use?**

**Issue III:  
Collecting and  
maintaining  
location  
information**

**Issue statement:**

How does SSUTA§ 310.A.3 and .4 and the member states’ recordkeeping requirements apply to the sale of specified digital products where sellers:

- Collect and/or maintain purchaser address information,
- May not collect and/or maintain purchaser address information, or
- Are otherwise not collecting purchaser address information due to arrangements with third parties?

**Workgroup recommendation:**

**BAC Subcommittee (Agrees/Disagrees)**

**Rationale:**

**SSUTA amendment required (yes/no):**

**Alternative options:**

**Discussion:**

**Introduction:**

SSUTA § 310.A.3 and .4 provide alternative sourcing rules where the seller cannot source to the place of “receipt” under SSUTA§ 310.A.1 and .2. Under these alternative methods the seller must either:

- Source sales to the location indicated by an address for the buyer that is available from the business records of the seller that are maintained in the ordinary course of the seller's business when use of this address does not constitute bad faith; or
- Source sales to the location indicated by an address for the buyer obtained during the consummation of the sale, including the address of a purchaser's payment instrument, if no other address is available, when use of this address does not constitute bad faith.

Electronic commerce’s continues to evolve and in some instances purchaser information may not always be collected. This raises questions relating to sourcing under SSUTA § 310.A.3 and .4.

*Example 3: SSUTA 310.A.4 - Purchasers address information not obtained or maintained by the seller.*

- **Basic facts:** Seller A, located in State XYZ, offers movie files for sale. Purchasers in any state may buy the movie files. Seller A electronically transfers the movies to purchasers.
  - *Example 1:* Seller A, as a matter of internal policy and practice, does not obtain the purchasers’ address information or zip codes.
  - *Example 2:* Seller A collects only an address for the purchaser at the consummation of sale for authentication and security purposes.
  - *Example 3:* Seller A contracts with a third party to collect and process payments from its purchasers. The third party remits to the seller only the



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purchasers' payments and not the purchasers' location information.

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**Issue IV:  
Sourcing  
allocation**

**Issue statement:**

Is clarification needed with respect to sourcing allocation of specified digital products where the products may be sold in multiple locations to the purchaser? If "yes," what is the recommended clarification?

*Note: This Issue is not intended to address or implicate the "multiple points of use" concept as contemplated under former SSUTA § 312.*

**Workgroup recommendation:**

**BAC Subcommittee (Agrees/Disagrees)**

**Rationale:**

**SSUTA amendment required (yes/no):**

**Alternative options:**

**Discussion:**

Some digital products may be offered for sale to purchasers at multiple locations. SSUTA § 310.A does not expressly address such situation with respect to specified digital products.

The federal Digital Goods and Service Tax Fairness Act of 2011 sought to address a similar issue. In particular, the Act provided:

- If the sale of digital goods or digital services is made to multiple locations of a customer, whether simultaneously or over a period of time, the seller may determine the customer's tax address or addresses using the address or addresses of use as provided by the customer.

The Governing Board addressed this issue in the prewritten computer software and computer related services context under Governing Board Rules 309.2 and 309.3.

Rule 309.2 provides:

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**Example 2:** Seller electronically delivers copies of the prewritten computer software to multiple locations of the Purchaser. The Seller has the information identifying the multiple locations for the electronic delivery of the prewritten computer software. The Seller sources the retail sale to each jurisdiction where the Purchaser receives the prewritten computer software.

Rule 309.3 provides:

- If receipt occurs in multiple locations and the purchaser and seller agree to allocate the retail sale to multiple locations based on a reasonable and consistent method, the seller shall source the retail sale to those locations using such method. The locations and allocation must be provided by the purchaser by the time of the invoice.
- **Example 1:** Purchaser, headquartered in State A, and Seller enter into a data processing services agreement. Under the agreement, Seller will conduct the data processing services from its facility located in State P. Purchaser has employees evenly distributed in States A, B, C, and D who will be accessing Seller's facility remotely using a communications network and making use of Seller's data processing services. Purchaser requests that Seller's invoice reflect the fact that it will be receiving the data processing services equally in States A, B, C, and D. Seller agrees to the Purchaser's request and sources the transaction between the four states where the Purchaser will be receiving the services. Seller has satisfied its responsibility for sourcing the transaction under Section 310.A.2.

**Issue V: Origin sourcing**

**Issue statement:**

How is SSUTA § 310.A.5 applied in the context of specified digital products? Specifically, what is contemplated by the following phrase: “the location...from which the digital good...was first available for transmission by the seller, or from which the service was provided (disregarding for these purposes any location that merely provided the digital transfer of the product sold).”

**Workgroup recommendation:**

**BAC Subcommittee (Agrees/Disagrees)**

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**Rationale:**

**SSUTA amendment required (yes/no):**

**Alternative options:**

**Discussion:**

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**Appendix A-  
SSUTA general  
sourcing  
provisions**

**SSUTA § 311: GENERAL SOURCING DEFINITIONS**

For the purposes of § 310, subsection (A), the terms "receive" and "receipt" mean:

- A. Taking possession of tangible personal property,
- B. Making first use of services, or
- C. Taking possession or making first use of digital goods, whichever comes first.

The terms "receive" and "receipt" do not include possession by a shipping company on behalf of the purchaser.

**SSUTA § 310: GENERAL SOURCING RULES**

A. Except as provided in § 310.1, the retail sale, excluding lease or rental, of a product shall be sourced as follows:

1. When the product is received by the purchaser at a business location of the seller the sale is sourced to that business location.
2. When the product is not received by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser (or the purchaser's donee, designated as such by the purchaser) occurs, including the location indicated by instructions for delivery to the purchaser (or donee), known to the seller.
3. When subsections (A)(1) and (A)(2) do not apply, the sale is sourced to the location indicated by an address for the purchaser that is available from the business records of the seller that are maintained in the ordinary course of the seller's business when use of this address does not constitute bad faith.
4. When subsections (A)(1), (A)(2), and (A)(3) do not apply, the sale is sourced to the location indicated by an address for the purchaser obtained during the consummation of the sale, including the address of a purchaser's payment instrument, if no other address is available, when use of this address does not constitute bad faith.
5. When none of the previous rules of subsections (A)(1), (A)(2), (A)(3), or (A)(4) apply, including the circumstance in which the seller is without sufficient information to apply the previous rules, then the location will be determined by the address from which tangible personal property was shipped, from which the digital good or the computer software delivered electronically was first available for transmission by the seller, or from which the service was provided (disregarding for these purposes any location that merely provided the digital transfer of the product sold)..[.]

**SSUTA § 310.1: ELECTION FOR ORIGIN-BASED SOURCING**

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A. A member state that has local jurisdictions that levy or receive sales or use taxes may elect to source the retail sale of tangible personal property and digital goods pursuant to the provisions of this section in lieu of the provisions of subsection A (2), (3) and (4) of § 310 if they comply with all provisions of sub§ C of this § and the only exception to § 310 is the exception provided for in subsection B of this §..[.]

**SSUTA § 309: APPLICATION OF GENERAL SOURCING RULES AND EXCLUSIONS FROM THE RULES**

A. Each member state shall agree to require sellers to source the retail sale of a product in accordance with § 310 or § 310.1. Except as provided in § 310.1, the provisions of § 310 apply to all sales regardless of the characterization of a product as tangible personal property, a digital good, or a service. Except as otherwise provided in this Agreement, the provisions of § 310 and § 310.1 only apply to determine a seller's obligation to pay or collect and remit a sales or use tax with respect to the seller's retail sale of a product. These provisions do not affect the obligation of a purchaser or lessee to remit tax on the use of the product to the taxing jurisdictions of that use.

B. Sections 310 and 310.1 do not apply to sales or use taxes levied on the following:

1. The retail sale or transfer of watercraft, modular homes, manufactured homes, or mobile homes. These items must be sourced according to the requirements of each member state.
2. The retail sale, excluding lease or rental, of motor vehicles, trailers, semi-trailers, or aircraft that do not qualify as transportation equipment, as defined in § 310, subsection (D). The retail sale of these items shall be sourced according to the requirements of each member state, and the lease or rental of these items must be sourced according to § 310, subsection (C).
3. Telecommunications services and ancillary services, as set out in § 315, and Internet access service shall be sourced in accordance with § 314.
4. Florist sales as defined by each member state. Such sales must be sourced according to the requirements of each member state.
5. The retail sale of products and services qualifying as direct mail shall be sourced in accordance with § 313.

**SSUTA, Appendix C, Library of Definitions, Part I Administrative Definitions**

“Retail sale or Sale at retail” means any sale, lease, or rental for any purpose other than for resale, sublease, or subrent.

**Appendix B –  
Digital  
products  
definitions**

**SSUTA, Appendix C, Library of Definitions, Part II Product Definitions  
DIGITAL PRODUCTS DEFINITIONS**

“Specified digital products” means electronically transferred:

“Digital Audio-Visual Works” which means a series of related images which, when shown in succession, impart an impression of motion, together with accompanying sounds, if any,

“Digital Audio Works” which means works that result from the fixation of a series of musical, spoken, or other sounds, including ringtones, and

“Digital Books” which means works that are generally recognized in the ordinary and usual sense as “books”.

For purposes of the definition of “digital audio works”, “ringtones” means digitized sound files that are downloaded onto a device and that may be used to alert the customer with

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respect to communication.

For purposes of the definitions of “specified digital products”, “transferred electronically” means obtained by the purchaser by means other than tangible storage media.

**Appendix C –  
SSUTA Digital  
products  
provisions**

**SSUTA § 332: SPECIFIED DIGITAL PRODUCTS**

A. ...

G. The tax treatment of a “digital code” shall be the same as the tax treatment of the “specified digital product” or product “transferred electronically” to which the “digital code” relates. The retail sale of the “digital code” shall be considered the transaction for purposes of the Agreement. For purposes of this section, “digital code” means a code, which provides a purchaser with a right to obtain one or more such products having the same tax treatment. A “digital code” may be obtained by any means, including email or by tangible means regardless of its designation as “song code”, “video code”, or “book code.”

**Governing Board Rule 332.1 – Products Transferred Electronically**

A...

G. 1. Section 332 G provides that the tax treatment of a “digital code” shall be the same as the tax treatment of the “specified digital product” to which the “digital code” relates and that the retail sale of the “digital code” shall be considered the transaction for purposes of the Agreement. Under this section, whether or not the sale of a “digital code” is taxable will depend on whether the “specified digital product” which the “digital code” allows the purchaser to obtain is taxable. Additionally, the transfer of the “digital code” to the customer is the taxable event; no taxable event occurs when the purchaser later exercises the “digital code” and takes electronic delivery of the “digital product.”

2. “Digital Code” means a code that provides a purchaser with a right to obtain one or more digital product(s) within one or more of the “specified digital product” subcategories having the same tax treatment.

3. A “digital code” may be transferred electronically or it may be transferred on a tangible medium such as piece of paper, plastic card, invoice or certificate or imprinted on another product.

4. If the code permits the purchaser to obtain a product from more than one subcategory of “specified digital products”, it is a “digital code” only if all of the subcategories have the same tax treatment. For instance, if the code allows the purchaser to obtain either a “digital audio visual work” or a “digital book” (each of which meets the definition of a “specified digital product”), it would be a “digital code” only if the taxing state either tax or exempts both “digital audio works” and “digital books”; if the state taxes one subcategory and exempts the other, then the code is not a “digital code.” Only if the taxable or nontaxable nature of the underlying “specified digital product” or products is ascertainable at the time the code is purchased does the code qualify as a “digital code.”

5. A code that represents a stored monetary value that is deducted from a total as it is used by the purchaser is not a “digital code.” Nor is a code that represents a redeemable card, gift card or gift certificate that entitles the holder to select “specified digital products” of an indicated cash value a “digital code.” Only if the code may be used to obtain one or more identifiable products within one or more subcategories of “specified digital products” having the same tax treatment does the code qualify as a “digital code.”

6. The placement of a time restriction on the redemption of a “digital code” in no way

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impacts whether the right to use the underlying digital product is temporary or permanent.

7. Examples:

**Example 1:** State A does not tax any of the subcategories of “specified digital products.” Customer in State A purchases a “digital code” that allows the electronic delivery of a single song. The sale of the “digital code” is not subject to tax and no taxable event occurs when the customer uses the “digital code” to download a song.

**Example 2:** State B imposes its sales tax on “digital audio works.” Customer in State B purchases a “digital code” that allows the electronic delivery of a single song (which constitutes a “digital audio work”). The purchase of the “digital code” is subject to tax because State B taxes “digital audio works.” However, when the customer takes electronic delivery of the “digital audio work”, no taxable event occurs; the customer has already paid the tax due with respect to the sale of the “digital audio work.”...[.]”

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