

## **A motion by Kentucky to amend Article III of the Streamlined Sales Tax Governing Board's Rules and Procedures**

### **Rule 336.1. Redemption Codes**

- A.** Section 336.A. provides that the tax treatment of a “redemption code” shall be the same as the tax treatment (including sourcing) of the “product or service” to which the “redemption code” relates.
- B.** Section 336.E. provides that the retail sale of the “redemption code” shall be considered the transaction for purposes of the Agreement. Additionally, the transfer of the “redemption code” to the purchaser is the taxable event; no taxable event occurs when the purchaser later exercises the “redemption code” and receives the product or service.
- C. Sourcing.--**
1. If the seller, at the time of the sale of the redemption code, **does not know** the location where the purchaser will receive any of the related products or services, the sale of the redemption code is sourced using the sourcing hierarchy of Section 310.A of the Agreement.
  2. If the seller, at the time of the sale of the redemption code, **knows** the location where the purchaser will receive one or more of the related products or services, the sale is sourced to that location using the sourcing hierarchy of Section 310.A.1 or A.2 of the Agreement.
- D.** The term “voucher,” as used in Section 336.D.2. shall be interpreted in a manner consistent with how that term is used in Disclosed Practice 1.
- E.** The following examples illustrate the application of Section 336.

#### **Example 1A: Downloaded Prewritten Computer Software**

SoftwareCo sells prewritten computer software on its website. When software is purchased on SoftwareCo's website customers receive a code to use to download and install the software purchased. Once the software is downloaded and installed, the code is no longer needed, and the customer retains a license granting perpetual rights of possession and use of the software.

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Scenario: Customer Z selects and purchases prewritten computer software on SoftwareCo's website using a credit card. Customer Z receives a code for the software purchased. Customer Z enters the code on SoftwareCo's website to download and install the software at any time and location they choose. SoftwareCo does not know where or when Customer Z will download and install the software and no additional charge is made to Customer Z when the code is used.

Conclusion: The code for the prewritten computer software is a redemption code. Since SoftwareCo makes no additional charge nor obtains additional payment from the customer when the code is entered online and used to download and install the software, there is no opportunity for SoftwareCo to collect sales tax at that time. If sales of downloaded prewritten computer software are taxable at the location indicated by the customer credit card address, SoftwareCo must collect sales tax on the sale of the code.

### **Example 1B: Downloaded Prewritten Computer Software**

SoftwareCo sells various products including prewritten computer software on its website. Customers can purchase codes for various monetary increments to be applied to the purchase of any product sold by SoftwareCo. The codes are sold on SoftwareCo's website and by third-party sellers.

Scenario 1: Customer G purchases a code valued at \$100 that may be used towards the purchase of SoftwareCo products. Customer G applies the \$100 code towards the purchase of SoftwareCo prewritten computer software costing \$250.

Conclusion 1: There are two transactions taking place.

1. Customer G's purchase of the code for \$100 is not a redemption code. This is a "gift card" because it represents a monetary value and is specifically excluded from the

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definition of redemption codes by Section 336.D.1. No tax is due at the time the gift card is purchased.

2. Customer G purchases \$250 of SoftwareCo prewritten computer software using the \$100 code and paying an additional \$150 with her credit card. If sales of downloaded prewritten computer software are taxable at the location determined by application of the sourcing rules, SoftwareCo must collect tax on the full \$250 sale of the software.

Scenario 2: Customer H purchases a code valued at \$300 that may be used towards the purchase of SoftwareCo products. Customer H applies the \$300 code towards the purchase of SoftwareCo prewritten computer software costing \$175.

Conclusion 2: There are two transactions taking place.

1. Customer H's purchase of the code for \$300 is not a redemption code. This is a "gift card" because it represents a monetary value and is specifically excluded from the definition of redemption codes by Section 336.D.1. No tax is due at the time the gift card is purchased.
2. Customer H purchases \$175 of SoftwareCo prewritten computer software using the \$300 code. The full cost of Customer H's purchase is covered by the \$300 code and does not require any additional payment. If sales of downloaded prewritten computer software are taxable at the location determined by application of the sourcing rules, SoftwareCo must collect tax on the full \$175 sale of the software. SoftwareCo deducts the sale price of \$175 plus any applicable tax due from Customer H's gift card and the credit remaining can be used at a later date.

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### **Example 2A: Game Tokens – Downloaded Prewritten Computer Software**

GameCo develops computer games for downloading and playing on gamers' devices. Gamers can purchase codes from third-party sellers that entitle the purchaser to GameCoTokens. These tokens have no monetary value and can only be used within GameCo games. When used, the tokens unlock additional game enhancements. No additional charges are made at the time the tokens are used. The basic game and additional game enhancements are prewritten computer software included in the original download.

Scenario: Customer C purchases a card at a third-party retailer's business location with a code that gives Customer C 100 GameCoTokens. GameCo has no knowledge of the price the third-party retailer charged Customer C for the code. The retailer has no knowledge of where the customer will use the code and obtain the tokens. Customer C uses the code and adds the 100 GameCoTokens to his account for use within the GameCo game. The GameCoTokens are deducted from Customer C's account as Customer C uses the tokens to unlock enhancements to the game.

Conclusion: The GameCoTokens have no monetary value and therefore are not gift cards. The code for the 100 GameCoTokens is a redemption code because it provides the purchaser with a right to unlock additional game enhancements, which are prewritten computer software. If sales of downloaded prewritten computer software are taxable at the retailer's business location, the retailer must collect sales tax on the sale of the card containing the code.

### **Example 2B: Game Tokens – Downloaded Prewritten Computer Software**

Same facts as in Example 2A except the GameCo prewritten computer software, in addition to allowing the gamers to play the game on the downloaded version, also allows them to interact

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online with other gamers remotely for no additional charge. In addition to using the codes to obtain higher levels of play and other enhancements to the downloaded version of the software, the gamers may also use the codes to obtain the same higher levels of play and other enhancements when interacting with other players in the interactive online version.

Scenario 1: In State 1, neither downloaded prewritten computer software nor interactive online game playing is subject to sales tax.

Conclusion 1: The code that allows gamers to obtain higher levels of play and other enhancements to both the downloaded and the online, interactive versions of the prewritten computer software is a redemption code because neither element of the code is subject to tax in the state such that all the elements have the same tax treatment. Because neither element is subject to sales tax, the retailer would not collect tax on the sale of the code to Customer C. The code is included in the definition of "redemption code" under Section 336.B.

Scenario 2: In State 2, both downloaded software and interactive online game playing are subject to sales tax.

Conclusion 2: The code that allows gamers to obtain higher levels of play and other enhancements to both the downloaded and the online, interactive versions of the software is a redemption code because both elements of the code are subject to tax in the state such that all the elements have the same tax treatment. Because both elements are subject to sales tax, the retailer would collect tax on the sale of the code to Customer C. The code is included in the definition of "redemption code" under Section 336.B.

Scenario 3: In State 3, downloaded software is subject to sales tax and interactive online game playing is not subject to sales tax.

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Conclusion 3: The code that allows gamers to obtain higher levels of play and other enhancements to both the downloaded and the online, interactive versions of the software is not a redemption code because one element of the code is subject to tax in the state and the other element of the code is not subject to tax such that all the elements do not have the same tax treatment. The code is excluded from the definition of "redemption code" by Section 336.D.3.

### **Example 3: Symphony Performance Ticket**

The local symphonic orchestra holds concerts during the concert season. Concert tickets can be purchased on a website. The concert tickets sold on the website are for concerts on a specific date and are for a specific seat in the concert hall. When a patron buys a ticket from the website, the patron receives a "QR" code that the patron can either print or have available for display on a smart phone. The patron receives the service when the QR code is used to enter the concert hall.

Scenario: Upon arrival at the concert hall, the patron displays the QR code and the ticket taker scans the code and lets the patron into the concert. The patron enters the concert hall and proceeds to his or her assigned seat. The patron is not obligated to make any additional payment.

Conclusion: The QR code is a redemption code. Since neither the seller of the QR code nor the ticket taker charges or obtains payment from the patron when the QR code is presented there is no opportunity for the seller or ticket taker to collect sales tax. If sales of concert tickets are taxable at the concert location, the seller must collect sales tax on the sale of the "QR" code.

### **Example 4: Haircut (services)**

A barber charges \$50 for a haircut. The barber, through a social media website, pre-sells haircuts at her barbershop. The social media website transmits money received from purchasers to the barbershop. The barber has only one location. Customers have the option of purchasing a

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redemption code entitling the customer to (1) a certain dollar amount towards the purchase of a haircut or (2) a \$50 haircut without any further charge.

Scenario 1: Customer Y buys a code that allows Customer Y to receive \$30 towards the cost of a haircut. Customer Y gets a \$50 haircut. Customer Y uses the \$30 code and pays the \$20 difference.

Conclusion 1: The code is not a redemption code for at least two reasons. First, it is a "gift card" because it represents a monetary value and is specifically excluded from the definition of redemption codes by Section 336.D.1. Second, the barber charges Customer Y for the difference between the price of the code and the price of the haircut at the time the barber service is provided giving the barber an opportunity to collect sales tax at that time. The code is excluded from the definition of "redemption code" by Section 336.D.4.

The social media website that Customer Y bought the code through is not obligated to collect sales tax on the sale of the code because it is the sale of a gift card. The barber is obligated to collect the sales tax on the \$50 price of the haircut at the time the customer receives the haircut if barber services are subject to tax in the barber's state.

Scenario 2: Customer Y buys a code through a social media website that allows Customer Y to receive a haircut from the barber for no additional charge. Customer Y gets the haircut, uses the code and pays nothing to the barber shop.

Conclusion 2: The code is a redemption code because the barber does not charge Customer Y when the haircut is provided. The barber is obligated to give the haircut for no additional charge and Customer Y is not obligated to make any additional payment upon receipt of the haircut.

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Customer Y receives the service at the barber's shop. The social media website that Customer Y purchased the code through is obligated to collect sales tax on the sale of the code based upon where the barber services will be received if barber services are subject to tax in the barber's state.

### **Example 5: Flat screen TV (TPP)**

TV Shop, with a single location, maintains a website where customers can buy codes redeemable for a flat screen TV. Customers have the option of purchasing a code that entitles the holder to receive either (1) a specific dollar amount for the purchase of a flat screen TV; or (2) a specific model flat screen TV without any further payment. Customers must go to TV Shop's business location to redeem the code.

Scenario 1: Customer X buys a code for \$300 towards the cost of any flat screen TV from TV Shop. Customer X gives the code to his son as a birthday present. Customer X's son takes the code to TV Shop and shops for a new flat screen TV. Customer X's son selects the model he wants which retails for \$700, uses the \$300 code and pays the \$400 difference.

Conclusion 1: The code in Scenario 1 is not a redemption code. This is a "gift card" because it represents a monetary value and is specifically excluded from the definition of redemption codes by Section 336.D.1. No Tax is due at the time the gift card is purchased.

Because TV Shop charges Customer X for the difference between the price of the code and the price of the TV at the time the TV is delivered to Customer X such that there is an opportunity to collect sales tax at that time, the code is excluded from the definition of "redemption code" by Section 336.D.4.

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TV Shop is not obligated to collect sales tax on the sale of the code at the time the code was sold.

TV Shop is obligated to collect the sales tax from Customer X's son on the \$700 sales price of the flat screen TV, if sales of flat screen TVs are subject to tax in the state of the TV Shop's business location.

Scenario 2: Customer Y buys a code that allows the holder of the code to receive a specific flat screen TV from TV Shop. Customer Y gives the code to his son as a birthday present. Customer Y's son takes the code to TV Shop, uses the code and receives the specific flat screen TV without making any additional payment.

Conclusions 2: The code in Scenario 2 is a redemption code because it is for a specific item and there is no opportunity for TV Shop to collect sales tax at the time of delivery of the flat screen TV. TV Shop is obligated to give Customer Y's son the flat screen TV for no additional charge to either Customer Y or his son.

The flat screen TV must be picked up at TV Shop's location. The TV Shop is obligated to collect sales tax on the sale of the code based on the location of the TV Shop and if sales of flat screen TVs are subject to tax in the state of TV Shop's business location.

### **Example 6: Preorder for Pickup**

StoreCo is a retailer of general merchandise and grocery products with storefronts in various states. StoreCo maintains their own website where customers can purchase items for pick up. Customers place orders on the website, provide payment information, and selects an available day and time to pick up the order at a store location. Customers authorize the payment, but the customer is not charged by StoreCo until the order is picked up. At the time the order is placed, customers receive a barcode that must be presented at the time the order is picked up.

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Scenario: Customer A places an order for products on StoreCo's website. Customer A selects location, date and time to pick up the products ordered. Customer A provides their payment information when they place the order. StoreCo sends Customer A a barcode for the order that is placed, acknowledging the location, date and time for pickup. Prior to Customer A's designated pickup day and time, StoreCo employees will select the items from the store shelves making any necessary adjustments for out-of-stock or weight-based products. Customer A arrives at the selected location, date and time and receives the products ordered. Once the order is picked up, Customer A's payment method is charged for the adjusted total.

Conclusion: The barcode is not a redemption code because StoreCo did not charge the customer at the time the barcode was issued. Customer A is charged when the order is picked up. StoreCo is obligated to collect sales tax on the products that are subject to tax in the state where the products are picked up by Customer A.

### **Example 7: Parking Pass**

ParkingCo manages several public parking garage facilities in multiple states. Customers can purchase ParkingCo parking passes for a specific parking facility or for access to multiple facilities managed by ParkingCo. Passes are purchased online and, at the time of purchase, the customer receives a QR code which allows entry to the parking facility. The customer must provide the QR code to the parking attendant to access the parking facility.

Scenario 1: Customer B purchases a 12-month parking pass from ParkingCo for use at a **specific parking facility** located in State 5, which imposes sales tax on parking services. The customer purchases the pass online using a credit card.

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Conclusion 1: The parking pass QR code is a redemption code because the purchase is for parking services at a specific parking facility and no further payment is made when the QR code is used to access the facility. Applying the general sourcing rules of Section 310, ParkingCo charges State 5 sales tax on the 12-month parking pass because:

the location of the parking facility is known to the seller,

the parking pass is for use only at that specific facility located in State 5, and

State 5 taxes parking services.

Scenario 2: Customer C resides in State 6 and purchases a parking pass from ParkingCo which allows for use in **any parking facility** in States 5, 6 and 7 for a 12-month period. Customer C purchases the pass online using a credit card and provides ParkingCo with the card holder's State 6 billing address. Parking services are subject to sales tax in State 5 but not in States 6 or 7.

Conclusion 2: The parking pass QR code is a redemption code because the purchase is for parking services, a single product, and no further payment is made at any of the facilities when the QR code is used to access the facilities. Applying the general sourcing rules of Section 310, the sale is sourced based upon Customer C's credit card billing address (State 6) and no sales tax is charged because:

Parking Co does not know the state where Customer C will make first use of the parking service,

The only address known by ParkingCo for the purchaser is State 6, the credit card billing address, and

State 6 does not tax parking services.