



MULTISTATE TAX COMMISSION

## MEETING NOTES

### MTC Work Group – Sales Taxation of Digital Products September 5, 2024

#### **I. Welcome and Opening Remarks, Including Review of Notes from July 11, 2024 Work Group Meeting**

Tim Jennrich (Washington), Chair of the Work Group, convened the meeting. He also noted that the process guidelines and notes from the July 11 meeting were posted and that anyone with changes to those notes should contact Nancy Prosser, at [NProsser@MTC.gov](mailto:NProsser@MTC.gov).

#### **II. Initial Public Comment**

Jennrich invited any initial public comments. There were none.

#### **III. Update on NCSL SALT Task Force Digital Primer Project**

Nancy Prosser, MTC, gave a report on the National Conference of State Legislatures' (NCSL's) decision to develop a primer for the upcoming legislative sessions on taxation of digital products. She noted that she and Jonathan White, MTC, will be part of the group working on that primer and that Steve Kranz of McDermott, Will & Emery will be the chief drafter for the group.

#### **IV. Discussion of Digital Products Definitions**

Jennrich summarized the past discussion and work of staff and the work group on the definitions of digital products and raised the question of whether it would be useful now to begin to develop possible definitions—given that states are taxing digital products more and more. He noted that this was discussed this spring and that Ray Langenberg (Texas), had proposed an outline for possible definitions—from a broad standpoint. He asked the work group to consider returning to this issue, look at the research that White and others had done, and the broad and narrow approaches that had been outlined in that research. He noted that he also believed it would make sense for this work group to work on the broader definitions while asking Streamlined to work on more specific definitions. Jennrich noted that while the objection to this has been that defining products will only lead to taxation of those products, states were already taxing other digital products but doing it differently. He asked that the group return to this issue at the next meeting and be ready to discuss this approach.

Jennrich also noted that he had asked Craig Johnson, Streamlined, and Langenberg to weigh in on this idea. Johnson commented that he believed uniform, standard definitions were important and that he was especially concerned about the fact that prewritten software is generally considered tangible property under Streamlined and by the states and that it might be problematic to change that. He also agreed with Jennrich that it was important to get

ahead of the issue so that states can take a more uniform approach and it made sense for Streamlined to work on the more specific or narrow definitions.

Langenberg noted that states are currently allowed to tax products beyond those defined by Streamlined and that he supported the idea of having a system of definitions so that lawmakers can effectively choose the extent to which they wish to impose tax on a range of items and do it consistently.

Prosser also noted that the Tax Foundation has put out a document summarizing the issues related to taxing digital products and has raised the concern about adequate definitions.

Mark Nebergall, SofTec, noted that in most states sales taxes are limited to tangible personal property and enumerated services and that when taxing digital products there needs to be some consideration of both similar tangible property as well as similar services that may not be taxed in order to avoid violating the Internet Tax Freedom Act.

#### **V. Update on Staff Draft of Bundling White Paper**

Jennrich then introduced the discussion of the draft bundling white paper. He noted this was a first draft and that input was welcome. He then turned it over to Prosser and White, who noted that the draft is posted on the project page. Prosser noted that there has already been some feedback and more is welcomed. She gave a brief overview of the structure of the white paper and that if there any ultimate findings or recommendations—they would also be included.

White then reviewed the research section of the white paper. He noted that he was particularly interested in feedback on how much detail should be included. He then reviewed the different parts of the research including the Streamlined rule and how states have implemented that rule. He also noted that the white paper includes examples to illustrate the rules but does not include all the state examples that might be available. The examples also help to show the application of the rules to particular circumstances. Also, states should review to see if there are any mistakes or corrections to be made.

White noted that the Streamlined rule appears to be the most extensively developed and other state rules are generally not as developed. He also noted that while states may have addressed particular issues, the rules may not be entirely formal, but instead based on particular questions or rulings about certain transactions. The white paper also includes examples of where non-streamlined states have addressed the bundling issue more fully.

Jennrich echoed the idea that if the white paper does not include rules that a state considers to be important or that are otherwise not sufficiently covered to reach out and provide that information.

Mia Strong (Louisiana), Work Group Vice Chair, noted that if it is decided that the white paper should include more detail—it would probably be better to include that detail in an appendix, to keep the document more readable and reasonable.

White noted that the other issues covered by the white paper include the true object test and variants on that test. He expressed the concern that while this issue is related to bundling, it may not be appropriate to cover in as much detail. He also noted that the same thing was true of the section on “mixed” transactions. This is where the true object test does not apply and so, is more related to that issue. White then reiterated the desire to get feedback on the amount of detail to be included, and turned it back to Prosser.

Prosser then reviewed the section of the white paper on the stakeholder meetings and the input that was obtained from those meetings with staff. She noted that one of the big issues for taxpayers is whether their products can be properly coded for the use of the reporting software. Also, taxpayers want to know what kinds of information will need to be kept in order to show that they have treated their sales properly. She asked anyone who participated in the stakeholder meetings to speak up if there was something missed by that summary.

Prosser then noted that ITFA has provisions that may address bundling with internet access which are summarized in the white paper, and there is also information on the Mobile Telecommunications Sourcing Act. There is also a summary of the issues raised by states that they think may need to be addressed more fully.

Prosser explained that the goal of this white paper is to determine whether taxing digital products may create issues that are not sufficiently addressed by the current rules, especially the Streamlined rules which are the most developed. She asked whether the group might be willing to put together a study group to take some of the examples that have been raised and walk through the application of the rules to see if those examples create any issues. Jennrich commented that this idea was important and he agreed that this would perhaps be good as a study group exercise to see if states agree as to whether the rules work and are detailed enough.

Johnson also agreed that he supported this kind of exercise—running the examples through the Streamlined bundling rule to see if states agree on results—to see if there are any new issues that should be addressed by Streamlined. He invited members of the public to weigh in as well.

Prosser also noted that the white paper includes some approaches that have been raised by stakeholders and others as being important to addressing bundling issues—including de minimis and tainting rules. Also, she noted that there are sections, including findings and conclusions, that are still to be developed.

Nebergall also asked whether the proposed federal legislation on digital goods and services might contain any bundling-related rules and Prosser noted that was a question that could be addressed in the white paper.

Prosser reviewed some other approaches that had been suggested—including a hierarchy or decision-tree approach to the various rules or using a percentage rule that is applied as a presumption, which might be easier to comply with. While these approaches are not in use generally, they may be helpful.

Langenberg asked whether we have potentially overstated the significance of the true object test and its relationship to the bundling issue and rules used to address that issue. He agreed that the decision tree or hierarchy is a good idea and could also be used to summarize the rules set out in the white paper and how they may relate. He argued that there is an order to the application of the rules and this could be useful to focus on. Prosser noted that part of this will also have to be coordinated with how certain products, especially telecom-related products, are treated.

Brad Heller (California) mentioned that his view on bundling has changed and that he sees the problem as one that requires considering the equity in taxing items that would not otherwise be taxable, because of how they are sold. He noted that, in particular, there may

be an approach to subscriptions and similar bundled transactions that may have a number of both taxable and non-taxable products. Prosser noted that this is the kind of example that may help to show whether the rules are complete or different types of products need slightly different rules.

**VI. Other Business – Next work group meeting is October 3, 2024**

Jennrich asked if there was any other business to raise. There was none.

**VII. Adjourn**

Jennrich concluded the meeting.