

Digital products including digital goods

What digital products are subject to tax?

Sales or use tax apply to all digital products, regardless of how they are accessed (downloaded, streamed, subscription service, networking, etc.). (See exclusions from the definitions and exemptions from retail sales and use tax below)

Digital products subject to sales or use tax include:

- Downloaded digital goods (music and movies, etc.)
- Streamed and accessed digital goods
- Digital automated services (DAS)

The laws also cover remote access software ("RAS") which is also subject to sales and use tax.

It does not matter if the purchaser obtains a permanent or nonpermanent right of use.

Questions and answers

- Definition of terms
- How these laws apply
- Exclusions and exemptions
- Questions
- References

Definition of terms

What is a digital product?

- It is transferred electronically.
- Digital goods (movies and music, etc.)
- Digital automated services (services that have been automated)

What is a digital good?

- Data
- Facts
- Information
- Sounds (music)
- Images (movies, pictures)
- Any combination of the above.

When these are transferred electronically, they are digital goods.

Digital goods do not include:

- The representation of a personal or professional service primarily involving the application of human effort
- Internet access
- Computer software
- Digital automated services (DAS)
- Remote access software (RAS)

What are digital automated services (DAS)?

DAS are services that use one or more software applications and are transferred electronically. DAS includes software, but it is not merely software. A DAS will frequently include data, information or additional functionality/services (e.g. chat rooms, multiplayer capabilities etc).

Examples include:

- Photo sharing services
- Car history report services
- A service that crawls the internet and gathers, categorizes and stores information

Note: Services that are primarily the result of human effort performed in response to a customer request are not considered DAS.

DAS also does not include:

- Internet access
- Payment processing
- Data processing services
- Telecommunications

- Live interactive presentations
- Advertising services
- Web hosting, storage, and back up

For the definition and a complete list of exceptions, see RCW 82.04.192(3)(b). Also, for a more detailed discussion on what a DAS, see WAC 458-20-15503(203).

What are data processing services?

Data processing services are primarily automated services 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. Charges for data processing services are subject to service and other activities B&O tax as a professional service (sales tax does not apply).

What are web site development services?

"Web site development service" means the design and development of a web site provided by a web site developer to a customer. Charges for web site development services are subject to service and other activities B&O tax as a professional service (sales tax does not apply).

What is digital data storage, hosting and back-up?

"The mere storage of digital products, digital codes, computer software or master copies of software is excluded from the definition of DAS. This exclusion includes the provision of space on a server for web hosting or backing up data or other information. Charges for digital storage, hosting and back-up services are subject to B&O tax under the service and other activities classification (sales tax does not apply).

What are online advertising services?

"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 search engine 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. Charges for online advertising services are subject to B&O tax under the service and other activities classification (sales tax does not apply).

Note: Services that are primarily the result of human effort performed in response to a customer request are not considered DAS.

DAS also does not include:

- Any service that primarily involves the application of human effort by the seller, and the human effort originated after the customer requested the service
- Internet access
- Payment processing
- Data processing services
- Telecommunications
- Live interactive presentations
- Advertising services
- Web hosting, storage, and back up
- Online marketplace related activities

For the definition and a complete list of exclusions, see RCW 82.04.192(3)(b).

What are online marketplace related activities?

Online marketplace related activities, which are services that allow the person receiving the services 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 either to:
 - (A) Create or host the service recipient's web site; or
 - (B) Process orders from customers using the service recipient's web site.

What is remote access software (RAS)?

RAS is prewritten software provided remotely. In other words, the buyer pays the seller for the right to access and use the prewritten software, which resides on the seller's server or the server of a third party. (An Application Service Provider is an example of a business that may provide RAS.) RAS is classified as a retail sale for B&O tax purposes and is subject to sales or use tax. The purchase of prewritten software is exempt if the purchaser uses the software to provide RAS.

What is a digital code and how is it taxed?

Digital code provides purchasers with the right to obtain one or more digital products.

If all the digital products available through the code are digital and have the same tax treatment, the code is considered a **digital code**. Digital codes are taxed the same way as the underlying digital product.

If the digital code provides the purchaser digital products that do not have the same tax treatment, it is not a digital code.

How these laws apply

How are prewritten remote access software keys or activation codes taxed?

The sale of prewritten software subject to sales or use tax includes the sale or charge made for a key or an enabling or activation code.

What is the value of the digital product for use tax purposes?

The value is the purchase price of the digital product. If the digital product is acquired by means other than a purchase, the value of the digital product is determined by the retail selling price of a similar digital product.

Are there any common digital goods that are exempt from tax?

Yes. Digital goods that are not offered for sale are exempt from tax when they are:

- Noncommercial (such as personal e-mail communications).
- Created solely for an internal audience.
- Created solely for the business needs of the person who created the digital good and is not the type of digital good that is offered for sale, such as business e-mail communications.

When is a digital product, digital code, or RAS used in the state of Washington for purposes of use tax?

A digital good or digital code is used within this state when the consumer first accesses, downloads, possesses, stores, opens, manipulates, or otherwise uses it within this state. A DAS is used within this state when the consumer first uses, enjoys, or otherwise receives the benefit of the service in this state. RAS is used in this state when the consumer first accesses the prewritten software in this state.

How are sales of digital products, digital codes, and remote access software sourced?

The standard sourcing rules from the Streamlined Sales and Use Tax Agreement (SSUTA) apply to the sourcing of digital products, digital codes, and RAS. Washington's implementation of the SSUTA rule is in RCW 82.32.730.

The sales of digital products, digital codes, and RAS are sourced the same as other sales according to the following hierarchy:

- The seller's place of business if the purchaser receives the digital product at the seller's place of business;
- If not received at the seller's place of business, the location where the purchaser receives the digital product, digital code, or RAS;
- If the location where the purchaser receives the digital product, digital code, or RAS is not known, the purchaser's address available in the seller's business records;
- If no address is available in the seller's business records, the purchaser's address obtained at the time of sale (e.g., purchaser's payment instrument); and
- If no address is obtained at the time of sale, the address where the digital product, digital code, or RAS is first made available for transmission by the seller.

Does placing digital products, digital codes, or software on a server in Washington establish nexus?

Putting a digital product on a server in Washington does not establish nexus. If an out-of-state person owns, rents, or leases server equipment, then ownership interest of the server equipment may be considered as a factor in determining nexus.

How does B&O tax apply to sales of digital products, digital codes, and RAS?

Taxpayers with nexus in Washington who sell digital products, digital codes, or remote access software sourced to Washington are subject to the B&O tax under the Retailing classification on the gross proceeds of retail sales and the B&O tax under the Wholesaling classification on the gross proceeds for wholesaling receipts. If digital products are licensed to someone who is not an end user, then those gross receipts are likely subject to the Royalties B&O tax.

Is the production of digital goods classified as manufacturing?

No. The production of digital goods is not manufacturing.

Exclusions and exemptions

Exclusions, including telecommunications and internet access, are not considered digital products even though they are transferred electronically. These activities and items are excluded from the definition of digital products. Their tax treatment is not changed by these laws. (See the Definition of Terms section above for more examples of activities that are not considered digital goods and digital automated services.)

Digital products purchased for resale or to become a part of a new product

Purchases of digital products for resale or to be used as components of a new product for sale are not subject to sales and use tax, but are subject to wholesaling B&O tax on the seller. The purchaser must provide a reseller permit or an exemption certificate.

Digital products given away for free

There is a use tax exemption for the recipient of digital products obtained free of charge. There is also a sales and use tax exemption for the person purchasing digital products, digital codes, or remote access software to give it away for free. The purchaser must provide an exemption certificate to the seller. The seller is also still subject to the Retailing B&O tax.

Digital goods purchased for a business purpose

If a business purchases a digital good (only digital goods, NOT digital automated services or remote access software) for business purposes, then the purchase is exempt from sales tax. Digital codes can be purchased exempt from sales tax as well, as long as only digital goods are obtained

through the use of the code and the digital goods will be used solely for business purposes. The seller is still subject to Retailing B&O tax on these sales.

For use within and outside Washington

Businesses purchasing digital products that may be used concurrently within and outside Washington are entitled to the multiple points of use (MPU) sales tax exemption. The buyer must provide the exemption certificate and pay use tax as explained below. The MPU exemption does not apply to purchases for personal use. The seller is still subject to Retailing B&O tax on sales.

Based on the buyer's records, the buyer may apportion the use tax in proportion to the in-state to out-of-state users.

1. Number of users (e.g. employees or agents) in this state
2. Divide it by the number of users (e.g. employees or agents) everywhere.
Thus, even if delivery of the product occurs in Washington, a person eligible for the MPU exemption owes use tax only on the apportioned value. The Department may authorize or require an alternative method of apportionment, supported by the taxpayer's records, that fairly reflects the proportion of in-state to out-of-state use.

Remote access software

There is an exemption for the purchase of prewritten software by the person who will provide the software remotely. The seller is still subject to Retailing B&O tax on these sales.

M&E exemption of digital goods

"Machinery and equipment" (M&E) includes digital goods. Digital goods used directly in a manufacturing operation are exempt under the M&E exemptions, provided all of the requirements of the exemption are met.

Television or radio broadcasts

Television and radio broadcasts of regular programming are not subject to sales or use tax and are subject to the Service & Other Activities B&O tax. However, if a broadcaster sells programming on a pay-per-program basis that allows the buyer to access a library of programs at any time for a specific charge, then sales tax and Retailing B&O tax applies.

There is an exemption for cable companies' sales of pay-per-program programming if cable companies are subject to a franchise fee on the gross revenue from the sale. Satellite providers have a federal exemption only from the local portion of the sales and use tax when they sell programming on a pay-per-program basis. Satellite providers do not have a state sales and use tax exemption because they do not pay franchise fees and therefore their sales are subject to the state portion of the sales tax rate. RCW 82.04.192(11).

Questions?

If you have tax questions about digital products, e-mail us or call 360-705-6705.

References

RCWs

- 82.04.192 - Digital products definitions
- 82.04.257 - Tax on digital products and services
- 82.04.258 - Digital products - Apportionable income
- 82.08.0208 - Digital codes
- 82.08.02082 - Digital Products - Ingredient or component - Made available for free
- 82.08.02088 - Digital products - Business Buyers - Concurrently available for use within and outside state
- 82.08.0273 - Exemptions -- Sales to nonresidents of tangible personal property, digital goods, and digital codes for use outside the state -- Proof of nonresident status -- Penalties.
- 82.12.0208 - Exemptions -- Digital codes.
- 82.12.0255 - Exemptions -- Nontaxable tangible personal property, warranties, and digital products.
- 82.12.0259 - Exemptions -- Use of personal property, digital automated services, or certain other services by federal corporations providing aid and relief.
- 82.12.0284 - Exemptions -- Use of computers or computer components, accessories, software, digital goods, or digital codes donated to schools or colleges.
- 82.32.532 - Digital products -- Nexus.
- 82.32.533 - Digital products -- Amnesty.

WACs

- 458-20-15501 Taxation of computer systems and hardware
- 458-20-15502 Taxation of computer software
- 458-20-15503 Digital Products

ETAs

- ETA 3176 Digital Products - General Implementation
- ETA 3177 Digital Products - General Analysis of Tax Liability

More information

Special Notice - Online Searchable Databases are Digital Automated Services
(pdf)

Special Notice - Digital Products (pdf)

Photography Tax Guide

Forms

Digital Products and Remote Access Software Exemption Certificate



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