

State Ruling

204-756, Interim Statement Regarding the Taxability of Non-Fungible Tokens (NFTs)-- Sales and use-- Taxability of persons and transactions-- Internet/Electronic commerce-- Taxability of NFTs

¶204-756. Interim Statement Regarding the Taxability of Non-Fungible Tokens (NFTs), Washington Department of Revenue, July 1, 2022.

Sales and use: Taxability of persons and transactions: Internet/Electronic commerce:

Taxability of NFTs.— The Washington Department of Revenue has provided interim guidance on the application of excise taxes to non-fungible tokens (NFTs). The tax treatment of various transactions involving NFTs is as follows:

- When the object of the purchase is a standalone digital product (i.e., the NFT itself), the sale is subject to sales tax and retailing B&O tax.
- When the object of the purchase is a standalone good or service classified as a retail sale, the sale is subject to retail sales tax and retailing B&O tax.
- When the object of the purchase is a standalone good or service not classified as a retail sale, no sales tax is due but the seller may be subject to B&O tax or some other excise tax.
- When the sale of an NFT includes a royalty payment to the NFT creator, or other party who retains the right to royalties for future sale or distribution of the NFT, the gross income from royalties is subject to royalties B&O tax.

Interim statement regarding the taxability of non-fungible tokens (NFTs)

July 1, 2022

Scope

This Interim Guidance Statement is intended to provide general information related to the taxability of certain transactions involving non-fungible tokens (NFTs) and does not intend to address any exemptions, exclusions, deductions, credits, or other incentives that may apply. This statement is not intended to be comprehensive, and the Department anticipates conducting future stakeholder efforts with the goal of developing more permanent and comprehensive guidance.

This statement does not address NFTs or factual scenarios that differ from the information and examples provided below. There are many types of NFTs available today, and not all are discussed. If you have recently purchased (or sold) an NFT and your situation differs from what is discussed here, we encourage you to request a binding letter ruling to assist you in determining your tax obligations.

What are non-fungible tokens?

Non-fungible tokens (NFTs) are digital code on a blockchain comprised of unique identification codes and metadata that distinguish them from one another. The following terms, which are used throughout this statement, are not legal definitions but are rather functional descriptions that the Department has developed based on how the terms are used by industry participants:

Token

“Token” refers to a digital unit supported by a blockchain. Blockchain refers to a digital ledger of transactions that are duplicated and distributed across an entire network of computing systems. A blockchain uses a decentralized network of computing systems to verify, record, and distribute transactions [1], rather than using a centralized database. In the process, the system creates a

foundation of what are often described as immutable ledgers.

A blockchain can be used to create tokens that are unique (see “Non-fungible” below). These tokens use blockchain technology to verify their uniqueness and facilitate the transaction.

Non-fungible

“Non-fungible” means “not capable of being interchanged.” The tokens discussed in this guidance are non-fungible, meaning they cannot be copied, substituted, or subdivided. Generally, the term “fungible” refers to something, such as money or a commodity, that is replaceable in equal part or quantity as payment for settling a debt or account, or capable of mutual substitution. [2]

Non-fungible token (NFT)

A non-fungible token (NFT) is a unique digital identifier that cannot be copied, substituted, or subdivided, that is recorded in a blockchain, and that is used to certify authenticity and ownership of a specific type of product. [3] NFTs are distinguishable from cryptocurrency, which is fungible, based in part on the unique nature of NFTs.

In addition to the NFT itself, purchasers of an NFT may also be entitled to receive other types of products or services, including (but not limited to): a) digital products, such as music, visual, video works, or video games, b) admissions to non-retail sales taxable events, such as tickets to clubs, sporting events, or concerts, c) prepared foods and beverages served by restaurants, or d) tangible personal property, such as memorabilia, collectibles, or apparel. NFTs are taxed based on the character of the underlying products (goods and services) included in the sale. [4]

Relevant Legal Definitions

“**Digital automated services**” means services transferred electronically that use one or more software applications. (RCW 82.04.192(3); WAC 458-20-15503(203)).

“**Digital code**” means a code that provides a purchaser with the right to obtain one or more digital products, if all of the digital products to be obtained through the use of the code have the same sales and use tax treatment. “Digital code” does not include a code that represents a stored monetary value that is deducted from a total as it is used by the purchaser... A digital code may be obtained by any means, including email or by tangible means regardless of its designation as song code, video code, book code, or some other term. (RCW 82.04.192(5); WAC 458-20-15503(204)).

“**Marketplace**” means a physical or electronic place, including, but not limited to, a store, a booth, an internet website, a catalog or a dedicated sales software application, where tangible personal property, digital codes and digital products, or services are offered for sale. (RCW 82.08.010(14)).

“**Marketplace facilitator**” means a person that: (a)(i) Contracts with sellers to facilitate for consideration, regardless of whether deducted as fees from the transaction, the sale of the seller's products through a marketplace owned or operated by the person; (ii) Engages directly or indirectly, through one or more affiliated persons, in transmitting or otherwise communicating the offer or acceptance between the buyer and seller. For purposes of this subsection, mere advertising does not constitute transmitting or otherwise communicating the offer or acceptance between the buyer and seller; and (iii) Engages directly or indirectly, through one or more affiliated persons, in any of the following activities with respect to the seller's products: (A) Payment processing services; (B) Fulfillment or storage services;(C) Listing products for sale; (D) Setting price;(E) Branding sales as those of the marketplace facilitator; (F) Taking orders; or (G) Providing customer service or accepting or assisting with returns or exchanges. (RCW 82.08.010(15)).

How are NFTs taxed?

The Department understands there is an emerging industry in which NFTs are being produced for sale to end consumers, speculative investors, and resellers. In order to determine the proper tax treatment of a given transaction involving an NFT, it is critical to consider: a) whether the transaction is comprised of multiple components or merely a digital code which grants the owner access to a digital good, b) the taxability of each underlying component, and c) the identity of the parties to the transaction (e.g., is the purchaser a consumer or reseller?). [5] (See RCW 82.04.250, 82.04.257, 82.04.290, 82.04.050, 82.08.010, 82.08.020.)

How to determine the selling price of an NFT?

Generally, the selling price of an NFT is measured by the consideration received by the seller, whether from the purchaser or a third party. The Department anticipates that, in some cases, consideration will be received in the form of cryptocurrency. If a seller receives cryptocurrency in exchange for an NFT, the value of the cryptocurrency tendered must be converted to US dollars as of the time of the sale. [6] [7]

What records should an NFT seller retain?

Taxpayers are responsible for retaining appropriate documentation pursuant to WAC 458-20-254 and RCW 82.32.070. NFT sellers must retain documentation to substantiate the nature and character of each sale. Sellers must retain documentation indicating the time and place of a sale, the consideration received, and any other records necessary to establish the taxability (or non-taxability) of each transaction and the proper measure of the tax.

The Department has identified the following basic types of arrangements involving NFTs [8]:

- The object of the purchase is a standalone digital product (i.e., the NFT itself). Examples include digital artwork, photographs, video clips, autographs, etc. Sales of digital products are generally subject to retail sales tax. The seller is also subject to retailing B&O tax measured by the gross proceeds of the sale.
- The object of the purchase is a standalone good or service (other than a digital product) classified as a retail sale under RCW 82.04.050. The NFT itself is not the object of the customer's purchase. Sales of goods or services defined as retail sales under RCW 82.04.050 are subject to retail sales tax. The seller is also subject to retailing B&O tax measured by the gross proceeds of the sale.
- The object of the purchase is a standalone good or service not classified as a retail sale under RCW 82.04.050. The NFT itself is not the object of the customer's purchase. Sales of goods or services not defined as retail sales under RCW 82.04.050 are not subject to retail sales tax. The seller may be subject to B&O tax, use tax, or some other excise tax measured by the gross proceeds of the sale. Frequently, income from a service not defined as retail sale under RCW 82.04.050 is subject to the service and other activities B&O tax.
- The sale of an NFT includes a royalty payment to the NFT creator, or other party who retains the right to royalties for future sale or distribution of the NFT. The gross income from royalties subject to royalties B&O tax. (RCW 82.04.2907).

Mixed Transactions

The Department anticipates sales of NFTs that entitle the purchaser to a digital product (i.e., the NFT itself) and one or more other products or services. In these situations, the seller must determine the taxability of each good or service included in the sale and also whether the sale constitutes a "bundled transaction." When considering transactions that involve the sale of products that do and do not constitute a "retail sale," for one nonitemized price, the "bundled

transaction” statutes — codified at RCW 82.08.190 and RCW 82.08.195 — control whether the entire sale price is subject to retail sales tax or whether each item provided is taxed separately. RCW 82.08.190 defines a “bundled transaction” as follows:

(1)(a) “Bundled transaction” transaction means the retail sale of two or more products, except real property and services to real property, where:

- (i) The products are otherwise distinct and identifiable; and
- (ii) The products are sold for one nonitemized price.

(b) A bundled transaction does not include the sale of any products in which the sales price varies, or is negotiable, based on the selection by the purchaser of the products included in the transaction.

Sales that include an NFT may be a “bundled transaction”. A “bundled transaction” is generally subject to retail sales tax and retailing B&O tax unless the transaction meets one of the exceptions in RCW 82.08.190(4).

If a bundled transaction involves a code that provides a purchaser with the right to obtain more than one digital product or one or more digital products and other products or services, and all of the products and services, digital or otherwise, to be obtained are subject to retail sales tax, then either the transaction is deemed to be entirely subject to retail sales tax or may be unbundled assuming the requirements of RCW 82.08.195(7)(b)(ii) are met. (RCW 82.08.195(7)).

Marketplace Facilitator

Marketplaces that facilitate retail sales of NFTs may qualify as market facilitators for Washington tax purposes. (RCW 82.08.010(15)). NFT marketplaces may need to register with the Department of Revenue if they meet substantial nexus standards. (WAC 458-20-19401.) Marketplaces *must* collect and remit sales or use tax on all taxable retail sales sourced to Washington on behalf of any marketplace seller making retail sales through the marketplace facilitator's marketplace. (WAC 458-20-282). Marketplaces that qualify as marketplace facilitators must provide sellers within their marketplace with the seller's monthly Washington sales information. (RCW 82.08.0531(4)(a)). Marketplace facilitators must report their own sales and sales made on behalf of other sellers within their marketplace. (RCW 82.08.0531(7).) If a marketplace takes commissions from retail sales of NFTs that are sourced to Washington, they are subject to service and other activities B&O tax. (RCW 82.04.290.) [9]

How are retail sales of NFTs sourced?

Sourcing refers to the place where a sale is deemed to take place for purposes of retail sales tax. Retail sales of digital products are sourced according to the following hierarchy in RCW 82.32.730(1):

1. When received by the purchaser at a business location of the seller, the sale is sourced to that business location. (RCW 82.32.730(1)(a)).
2. When not received by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser occurs, including the location indicated by instructions for delivery to the purchaser, known to the seller. (RCW 82.32.730(1)(b)).
3. When the first two steps 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. (RCW 82.32.730(1)(c)).
4. When the first three steps 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. (RCW 82.32.730 (1)(d)).
5. When the first four steps of this subsection do not apply, including the circumstance where the seller is without sufficient information to apply those provisions, then the location shall be determined by the address from which the digital code was first available for transmission by the seller, or from which the digital automated service or other service defined as a retail sale under RCW 82.04.050 was provided, disregarding for these purposes any location that merely provided the digital transfer of the product sold. (RCW 82.32.730(1)(e) (“origin sourcing”).

For purposes of the above sourcing hierarchy, “receive” and “receipt” mean taking possession of tangible personal property, making first use of digital automated services or other services, or taking possession or making first use of digital codes, whichever comes first. (RCW 82.32.730(9)(f)).

How is gross income from the sale of NFTs sourced or apportioned?

Retailing B&O tax for retailing activities

Gross income from a retail sale is subject to retailing B&O tax if the sale is sourced to Washington according to RCW 82.32.730(1). (RCW 82.04.250 and 82.04.257).

Service and other activities B&O tax for apportionable activities

Gross income from apportionable activities is generally attributed to Washington according to where the benefit of the service is received. (RCW 82.04.462 and WAC 458-20-19402). Apportionable activities include activities subject to the service and other activities B&O tax classifications under RCW 82.04.290.

Royalty B&O tax for intangibles

Royalty income is generally attributed to Washington according to where the intangible property will be used by the customer. (RCW 82.04.2907, 82.04.460 and WAC 458-20-19403).

Examples

In this section the Department provides a number of examples that identify facts and then state a conclusion. These examples should be used only as a general guide. The tax results of other situations must be determined separately after a review of all of the facts and circumstances. [10]

Taxpayers are encouraged to contact the Department for guidance in cases where the facts and circumstances comprising their business activities are not covered in this statement.

Example 1 — Sale of an NFT that provides ownership of a digital code

Facts:

- Zoe lives in Friday Harbor, Washington.
- Zoe creates highly coveted puffin NFTs, Peculiar Puffins, which are marketed for sale through an online NFT marketplace.
- Zoe sells a Peculiar Puffin NFT, which provides ownership of a digital code to Norika, who resides in Seattle, Washington.
- Zoe obtains and maintains business records for Norika, including Norika's address in Seattle, Washington.

Result:

- Zoe sold a digital code (which grants access to a digital image) to an end consumer (Norika).
- The sale is subject to retail sales tax and retailing B&O tax.

- While Zoe does not know where Norika first received the NFT, the sale is sourced to Seattle according to RCW 82.32.730(1)(c).
- Zoe is subject to retailing B&O tax and must collect retail sales tax from Norika at the combined state and local rate for Seattle. The sale is deemed to have occurred at the time the NFT transfer from Zoe to Norika was recorded to the blockchain.

Example 2 — Sale of an NFT that provides ownership of a digital code and a right to obtain a non-retail service (admission to a spectator event)

Facts:

- Iggy Richards, *South Capitol* rock band member, resides in Olympia.
- Iggy sells NFTs of the band's songs, which provide ownership of a digital code (digital music).
- As part of the single nonitemized selling price, the buyer obtains a concert ticket to the band's upcoming performance at the Gorge Amphitheatre in Grant County.
- Louisa who resides in Olympia purchases an NFT package from Iggy.
- Iggy obtains and maintains business records of Louisa's address in Olympia.

Result:

- The sale is comprised of two distinctly taxable components, a digital code (digital musical recording) and a non-retail service (admission to a live concert).
- If sold separately, the sale of the digital code is subject to retail sales tax and retailing B&O tax, while the gross income for admission to a concert is subject to service and other activities B&O tax.
- This transaction is a bundled transaction under RCW 82.08.190, which should be treated as the sale of a code under RCW 82.08.195(7). The facts do not indicate that the products can be unbundled, so the entire selling price is subject to retail sales tax and retailing B&O tax. The sale is deemed to have occurred at the time the NFT transfer from Iggy to Louisa was recorded to the blockchain.
- While South Capitol does not know where receipt of the NFT occurs, the sale is sourced to Olympia following RCW 82.32.730(1)(c).
- Iggy must collect retail sales tax from Louisa at the combined state and local rate for Olympia.

Example 3 — Sale of an NFT where a royalty is received

Facts:

- Meghan lives in Bellingham, Washington.
- Meghan creates highly coveted puffin NFTs, Peculiar Puffins.
- When Meghan created the Peculiar Puffin NFTs, she retained a 10 percent royalty on all subsequent sales of her NFTs.
- Zoe, who lives in Friday Harbor, Washington purchased ownership rights to several of Meghan's Peculiar Puffin NFTs.
- When Zoe sells a Peculiar Puffin NFT, Meghan automatically receives a 10 percent royalty on the sale.
- Zoe sells one of the Peculiar Puffin NFTs to Norika who resides in Seattle, Washington.

Result:

- Zoe sold a digital code (which grants access to a digital image) to an end consumer (Norika).

- The sale is subject to retail sales tax and retailing B&O tax.
- While Zoe does not know where Norika first received the NFT, the sale is sourced to Seattle according to RCW 82.32.730(1)(c).
- Meghan is subject to royalties B&O tax on the 10 percent commission she received on Zoe's sale to Norika. (RCW 82.04.2907).
- The royalty income is sourced Seattle, the location where Norika first received the NFT.

Upcoming plan for converting this interim guidance into permanent guidance

The Department will continue to review this issue for purposes of developing permanent guidance. The Department anticipates that this interim statement will continue in effect until permanent guidance is issued or the interim statement is cancelled. The Department anticipates engaging external stakeholders on this topic, with the goal of developing more comprehensive and permanent guidance. If you are interested in participating in future stakeholder work in this area, please contact Nikki Bizzarri at (360) 534-1582 or nikkib@dor.wa.gov.

If you need to request a binding letter ruling, please do so here: <https://dor.wa.gov/contact/request-tax-ruling>.

Footnotes

[1]	E.g., financial transactions, smart contracts, NFTs. An example is the conveyance of cryptocurrency from one wallet to another.
[2]	See "Fungible." Merriam-Webster.com Dictionary, Merriam-Webster, https://www.merriam-webster.com/dictionary/non-fungible%20token . Accessed 14 Jun. 2022.
[3]	See "Non-fungible token." Merriam-Webster.com Dictionary, Merriam-Webster, https://www.merriam-webster.com/dictionary/non-fungible%20token . Accessed 9 Jun. 2022.
[4]	This Interim Guidance Statement does not purport to address all transactions, including those that deal with virtual real property, real property, or tangible personal property.
[5]	This Interim Guidance Statement does not purport to address transactions involving casual or isolated sales or sales for resale. Future guidance may be developed to address these areas.
[6]	An example of a cryptocurrency pricing index is the WorldCoinIndex (website). WorldCoinIndex is an online pricing index for hundreds of cryptocurrencies. The index tracks cryptocurrency values by computing their average (weighted) value across the world's cryptocurrency exchanges.

	[7]	<p><i>See also</i>, Washington State Department of Revenue, <i>Interim Guidance Statement Regarding Bitcoin, Payments, Minting, and Investment Income</i>: https://dor.wa.gov/interim-statement-regarding-bitcoin-payments-mining-and-investment-income.</p>
	[8]	Assumes no exemptions or exclusions apply, the sales are properly taxable in Washington, and nexus exists.
	[9]	For more information, see Washington State Department of Revenue, <i>Marketplace facilitators</i> : https://dor.wa.gov/taxes-rates/retail-sales-tax/marketplace-fairness-leveling-playing-field/marketplace-facilitators .
	[10]	To obtain Department advice that you may rely upon, you may request a binding letter ruling from the Department: https://dor.wa.gov/contact/request-tax-ruling .