State Tax Alert
January 2023

State Sales and Use Tax Quarterly Update – January 2023

Ernst & Young LLP's Sales and Use Tax Quarterly Update provides a summary of recent major legislative, administrative and judicial sales and use tax developments.

Are we there yet? A recent spate of state court rulings might mean that the issue of sales and use tax nexus is finally settled…or not

The U.S. Supreme Court's 2018 decision in *South Dakota v. Wayfair*[1] was meant to settle the issue of nexus for sales and use tax purposes; however, issues remain. Among them: whether the legacy state nexus provisions remained valid; whether the states would enforce them – either prospectively and retroactively; and whether physical presence still mattered, in light of the Court's approval of an economic nexus standard. With respect to physical presence, it is safe to say that it is still a factor in determining nexus – it is just no longer "the" factor. With respect to the pre-*Wayfair* nexus provisions enacted in a number of states, there are still questions that are slowly being resolved; namely, whether they are still valid and/or necessary.

Two recent developments involving the Online Merchants Guild (discussed *below*) sought to address whether nexus could be created by the in-state storage of inventory by a third-party fulfillment entity. Another case, from North Carolina (also discussed *below*), examined the effect that *Wayfair* had on applying old nexus precedent to current matters. None of these matters shared a common outcome, except that in no instance was pre-*Wayfair* nexus deemed to exist absent some legitimate physical presence.

Finally, in Massachusetts, on December 22, 2022 the Supreme Judicial Court (SJC) ruled on the validity of that state's legacy (pre-*Wayfair*) nexus provision, 830 Code Mass. Regs. § 64H.1.7.[2] That regulation deemed cookies and apps owned by a remote seller and stored on the device of an in-state purchaser as constituting physical presence for sales and use tax nexus purposes. The regulation also deemed the use of content delivery networks (CDNs) that stored a seller's computer code and delivered such code to website users, thereby enabling these users to access the sellers' websites stored on the CDNs' servers rather than on the websites' host servers, as creating nexus. Under the regulation, any out-of-state seller with such in-state "presence," who also had more than $500,000 in Internet sales to Massachusetts customers,

[1] 585 U.S. __ (2018).
[2] *U.S. Auto Parts Network, Inc. v. Commissioner*, No. SJC-13283 (Mass. Sup. Jud. Ct. December 22, 2022).

resulting in at least 100 transactions, was required to register and collect and remit sales and use taxes on such sales.

The Commissioner claimed that these "electrons" that were "existing in the Commonwealth" constituted physical presence and, thus, nexus under the regulation. This concept, generally referred to as "cookie nexus," was pioneered by Massachusetts in 2017 and was gaining popularity among the states, pre-*Wayfair*.

In concluding that the in-state presence of "electrons" and cookies did not satisfy the *Quill*[3] physical presence standard, the SJC declined to apply *Wayfair* retroactively, citing the *Wayfair* Court's emphasis on the South Dakota's statute's non-retroactivity provision and in the Wayfair amicus brief filed by a coalition of States, including Massachusetts, in which the States "assured the Court that retroactivity was not a concern" and "represented that 'other legal and pragmatic safeguards' would prevent them from applying any new rule retroactively." In short, the SJC applied pre-*Wayfair* legal standards to pre-*Wayfair* controversies, as the *Wayfair* Court directed.

So, while the controversies may not be fully at their end, if nothing else, these developments do provide some degree of certainty with respect to any remaining pre-*Wayfair* open periods that, absent some legitimate physical presence, there can be no substantial nexus.

Our Observation: In a post-*Wayfair* world, taxpayers that ignore nexus precedent under *Quill* and its progeny do so at their own peril. While open periods from pre-*Wayfair* times are rapidly closing,[4] the concept of physical presence as a nexus standard remains. For many remote sellers that do not meet current economic nexus sales thresholds, physical, tangible presence must still be considered. And, based on these recent developments – all these years later – we continue to get a better sense of what is ***not*** physical presence for sales and use tax purposes.

Other Recent Sales and Use Tax Developments

Nexus

California: The Ninth Circuit Court of Appeals affirmed a district court's dismissal of a federal lawsuit brought by a trade association for e-commerce merchants seeking to enjoin California from requiring its members to obtain a seller's permit from California to facilitate sales tax collection. In so holding, the Ninth Circuit agreed with the district court that the Tax Injunction Act bars federal jurisdiction in this matter because the injunction sought by the association would stop, to some degree, the assessment or collection of state sales tax in California and because an adequate state remedy — California's tax refund procedures — already exists. *Online Merchants Guild v. Maduros*, No. 21-16911 (US Ct. App., 9th Cir. Dist. Ct., November 9, 2022).

[3] *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).
[4] It is important to note that, absent a filing, periods and statutes of limitations do not close.

North Carolina: The North Carolina Supreme Court (Court), reversing a trial court ruling, has held that an out-of-state printer that shipped goods to in-state customers via common carrier and maintained an in-state sales representative had sufficient nexus with the state for sales and use tax purposes. According to its sales contracts, possession, legal title, and risk of loss for any ordered materials passed from the printer to its customers when the materials were delivered to the common carriers outside of North Carolina. The lower court had held that the sales at issue lacked transactional nexus to North Carolina under the Commerce Clause since title and possession of the printed materials transferred outside the state. Citing U.S. Supreme Court precedent in *McLeod v. J.E. Dilworth Co*.[5] and *General Trading Co. v. State Tax Comm'n.*,[6] companion cases that prohibited imposition of a state sales tax on an interstate transaction (*Dilworth*) while permitting imposition of a state use tax on a similar transaction (*General Trading*), the lower court concluded that a sufficient nexus to impose the sales tax was absent. In reversing, the Court applied the four-factor *Complete Auto Transit*[7] test, concluding that the printer had substantial nexus with the state, and that the North Carolina's sales tax regime was fairly apportioned, nondiscriminatory, and fairly related to services provided by the state. The Court also determined that assessment of the tax did not violate Due Process. With respect to its nexus analysis, the Court based its determination on the in-state presence of the printer's representative, the fact that North Carolina is a destination-based sales tax state, and the volume of the printer's North Carolina sales. Although it did not apply the 2018 U.S. Supreme Court *Wayfair* decision retroactively, the Court did note that the decision did not draw any distinction between the sales tax and the use tax. *Quad Graphics, Inc. v. North Carolina Dep't. of Revenue*, No. 407A21, 2022-NCSC-133 (N.C. S. Ct. December 16, 2022).

Pennsylvania: The Pennsylvania Department of Revenue will not appeal the Pennsylvania Commonwealth Court's ruling in *Online Merchants Guild v. Hassell*, in which the court ruled that an out-of-state business that sells merchandise through an online marketplace's fulfillment program, and whose only connection to Pennsylvania is the storage of its inventory at the online marketplace's in-state warehouse, is not required to collect and remit Pennsylvania sale tax on such sales because it does not have sufficient contacts with Pennsylvania. *Online Merchants Guild v. Hassell*, No. 179 M.D. 2021 (Pa. Commw. Ct. September 9, 2022).

Tax Base and Taxability

Colorado: In response to a ruling request, the Colorado Department of Revenue (CO DOR) determined that state and state-administered sales tax does not apply to: (1) a company's sales of credits that can be used on its internet-based platform (platform credits) on which viewers can watch streaming videos; or (2) to the redemption of these credits by viewers, both with and without third-party enhancements. The CO DOR found the platform credit is akin to gift cards, "which evidence the issuer's agreement to provide goods and services when redeemed", and as such sales of the credit are not subject to tax. Redemption of the platform credits also is not taxable because the credits are not being used to acquire taxable tangible personal property or services. Rather, when a viewer redeems the credit, the viewer is purchasing special recognition of earning badges or having their chat messages emphasized on the platform. These enhancements, the CO DOR said, are not taxable services. Colo. Dept. of Rev., PLR 22-005 (July 22, 2022).

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[5] 322 U.S. 327 (1944).
[6] 322 U.S. 335 (1944).
[7] *Complete Auto Transit Inc. v. Brady*, 430 U.S. 274 (1977).

Louisiana: In response to a ruling request, the Louisiana Department of Revenue (LA DOR) determined that sales of electricity at electric vehicle charging stations are subject to sales and use tax and that consumers purchasing this electricity are responsible for paying the tax on these purchases. The LA DOR noted that because the electricity sold at charging stations is not for residential use or being purchased as a business utility, neither the constitutional exclusion nor the statutory exemption for sales of electricity apply. In addition, the LA DOR found that the separately stated fee for idle time is not subject to sales and use tax as the fee has no connection to the sale of the electricity and it can be avoided if the vehicle is promptly disconnected from the charging station after the vehicle is charged. La. Dept. of Rev., Revenue Ruling No. 22-004 (December 6, 2022).

Minnesota: Recently issued Rev. Notice #22-04, states the Minnesota Department of Revenue's (MN DOR) position on when the charge for a service must be included in the price of a taxable good or service when the service is necessary to complete the sale. This notice provides a broad clarification of the MN DOR's position, and it revokes and replaces the industry specific Rev. Notice #06-06, which only pertained to interior design services. (Revocation of Notice #06-06 also removes the one-year lookback period for interior design services.) The MN DOR's position on "services necessary to complete the sale" is that services not otherwise subject to sales tax are included in the sales price of a taxable good or service if they are necessary to complete the sale of the taxable good or service. The MN DOR explained that "[a] service is necessary to complete the sale of a taxable good or service if it is an essential part of the transaction such that purchase of the service results in [such sale] from the same retailer." The MN DOR said the service is necessary to complete the sale if it meets any of the following conditions: (1) the retailer, in conjunction with the sale of taxable goods or services, requires or otherwise does not permit the purchaser to opt out of the service; or (2) the purchaser receives a credit for the purchase of the service against the purchase of the goods or services from the same retailer. The MN DOR further stated that contract for or stating a service separately from the taxable goods or services does not control whether the service is necessary for the completion of the sale. Notice #22-04 includes illustrative examples. Revocation of Notice #06-06 is effective for sales and purchases made after December 19, 2022, except revocation of the lookback period is effective for purchases of interior design services made after March 31, 2023. Minn. Dept. of Rev., Notice #22-04 (December 19, 2022) (revokes and replaces Rev. Notice #06-06).

Mississippi: On October 1, 2022, the Mississippi Taxation of Remote and Internet-Based Computer Software Products and Services Study Committee (Committee) submitted its report to the Mississippi Legislature. The Committee's general recommendations regarding sales and use taxation of software and related services are to exclude from sales and use tax: (1) all sales of software to business consumers and used as a business input, and (2) all software-related services to business consumers and used as a business input. The Committee did not make any recommendations related to sales of software and related services to non-business consumers. The Committee also did not propose specific language to codify regarding definitions and examples of taxable and nontaxable items; however, the Committee reasoned that consensus on the following topics could be reached during the legislative process: (1) define "computer software" and "computer software sales and services"; (2) exclude from the definition of "computer software" data or databases, apps or similar programs, platform-as-a-service or infrastructure-as-a-service; (3) exclude from the definition of "computer software sales and services" data processing services; (4) include a non-exclusive list of non-taxable items such as research databases, credit reports, real estate listings, rating reports and services, title abstracts, wire services, consumer banking; and (5) include a general statement that if there any ambiguities or uncertainties as

to whether an item, service or transaction is taxable or nontaxable it is presumed nontaxable unless the legislature acts to clarify the statute. A copy of the report and exhibits are available here.

Mississippi: A company's sales of photography services and copyrights to digital still images are not subject to Mississippi sales tax because capturing and selling digital images is neither the sale of taxable tangible personal property nor a taxable business activity. In so holding, the Mississippi Supreme Court (Court) found that photography is not a taxable service and still digital images do not fall within the definition of taxable digital product. Further, since the company only used digital photography it is not providing taxable film development activities. The Court also rejected the Mississippi Department of Revenue's alternative argument that the company engaged in the taxable business activity of photo finishing, reasoning that while the Legislature has amended certain provisions in the tax code "to reflect the digital revolution", it has not amended Miss. Code § 27-65-23 to specifically include the editing of purely digital images. Accordingly, the Court vacated the sales tax assessment against the company. *Mississippi Dept. of Rev. v. EKB, Inc.*, No. 2021-SA-00441-SCT (Miss. S.Ct. October 6, 2022).[8]

Nevada: Adopted regulation (R052-21) provides guidance on taxation of peer-to-peer car (P2P) sharing program. If requested by the Nevada Department of Taxation (NV DOT), a person operating a P2P car sharing program must submit proof that the person has obtained or attempted to obtain from each shared vehicle owner who places a vehicle on the digital network or software application of the P2P car share program the required electronic certification for each shared vehicle. (The regulation lists the information that must be included in the electronic certification.) Shared vehicles owners that have paid sales and use tax on the purchase of a shared vehicle must retain documentation showing proof of the payment. (The regulation lists what the documentation must set forth.) Persons operating a P2P car sharing program on a quarterly basis must submit to the NV DOT a report that includes information on each shared vehicle placed on the P2P car sharing program's digital network or software application during the prior calendar quarter. (The regulation lists what information must be included in the report.) The regulation also provides P2P car sharing program record retention guidance. Nev. Tax Comm. LCB File No. R052-21 (filed September 28, 2022).

Ohio: New law, House Bill 223 (HB 223), allows vendors to deduct sales tax remitted for bad debts on private label credit cards when the debt is written off as uncollectible by the credit card account lender or by a person succeeding to such accounts. The expansion of the bad debt deduction is effective July 1, 2023. Under existing law, Ohio Rev. Code 5739.121 allows a vendor to take a deduction from sales tax owed when it makes a sale on credit, collects and remits the applicable sales tax, and where the purchaser defaults on payment. The debt must have been uncollected for at least six months and is only available for debts that have become worthless or uncollectible (i.e., deductible for federal income tax purposes) during the most recent sales tax reporting period. The deduction is applied against the sales tax remitted by the vendor for the applicable reporting period with a refund available if the bad debt exceeds the vendor's taxable sales for the reporting period. If the vendor subsequently collected the debt the vendor has to repay the tax previously deducted. Only a vendor was allowed to claim the deduction and no deduction was allowed for bad debts on another person's books. In 2009, the Ohio Supreme Court

[8] The Mississippi Supreme Court noted that "this Court abandoned its 'old standard of review giving deference to agency interpretations of statutes' and established that we now will conduct a de novo review without giving such deference." *HWCC-Tunica, Inc. v. Miss. Dept. of Rev.*, 296 So. 3d 668, 673 (Miss. 2020), (quoting *King v. Mississippi Military Dept.*, 245 So. 3d 404, 407-08 (Miss. 2018)).

held[9] that a vendor that used an unrelated finance company to handle its private label credit card transactions was not entitled to the deduction for defaulted accounts because it did not charge off the debts as uncollectible on its own books as Ohio Rev. Code 5739.121 then required. HB 223 *signed by the Governor* December 22, 2023.

South Carolina: In response to a ruling request, the South Carolina Department of Revenue said that separately stated "inflation fees", "convenience fees", "non-cash adjustment fees" or similar types of fees charged by a retailer as part of a retail sale of tangible personal property are included in "gross proceeds of sales" or "sales price" subject to the state's sales and use tax. Such fees, however, are not taxable if the retail sale of tangible personal property is otherwise exempt from sales and use tax or the transaction is not subject to tax (e.g., sale of a nontaxable service). S.C. Dept. of Rev., SC Rev. Ruling #22-10 (October 20, 2022).

Texas: The Texas Comptroller of Public Accounts is providing additional time for businesses that sell, rent or lease motor vehicles to deduct the fair market value (FMV) of a retired vehicle titled in Texas from the total consideration paid for a replacement vehicle. Generally, the FMV deduction must be used within 18 months of a retired vehicle's removal from service and offered for sale. The Comptroller said that because of "the current difficulty in finding replacement vehicles" it is providing such businesses with an additional 12 months to purchase a replacement vehicle for vehicles retired in 2022. The Comptroller noted that businesses need to maintain records documenting when the vehicle was retired, its FMV and when the FMV deduction was used. Tex. Comp. of Pub. Accts., Tax Policy News "Extension of the Fair Market Value Deduction (FMVD)" (October 2022).

Wisconsin: The Wisconsin Department of Revenue (WI DOR) issued guidance on the application of the state's sales and use tax on non-fungible tokens (NFT), stating that taxability of the sale or purchase of an NFT depends on the taxability of the underlying product, good or service. The WI DOR provided the following examples: (1) NFTs that entitle the purchaser to download music or movies are sales of a taxable specified digital good; (2) NFTs that entitle the purchaser admission into a sporting event are sales of taxable admission; and (3) NFTs that entitle the purchaser to tangible artwork are sales of taxable tangible personal property. Wis. Dept. of Rev., Wis. Tax Bulletin 219 "Non-Fungible Tokens" (October 2022).

Sales and Use Tax Exemptions, Exclusions and Refunds

Missouri: The Missouri Supreme Court (Court) affirmed the administrative hearing commission's (AHC) determination that a Missouri not-for-profit corporation, which provides a wide range of services to predominantly low-income communities, and its wholly owned single-member Missouri not-for-profit limited liability company (LLC) that is helping with the Phase IV development, qualify for sales and use tax exemptions as charitable organizations. The Court found that the entities' primary purposes in the Phase IV development was to benefit person with low incomes in a specific area, which reflected a charitable purpose, and not as the Missouri Department of Revenue (MO DOR) asserted that it was for the benefit of the general welfare of the community. The Court also rejected the MO DOR's argument that the AHC erred in determining that the entities are charitable organization when one of them was previously granted civic exemptions because the statutory categories of charitable and civic exemptions

[9] *Home Depot USA, Inc. v. Levin*, 2009 Ohio 1431 (2009).

are mutually exclusive classifications and preclude such a determination. Rather, the Court determined that "separate designations for civic and charitable organizations justify only the conclusion that such categories are not coextensive and there is some differences between the two …" Moreover, in comparing the definitions of civic and charitable organizations, the Court found overlap between them, noting that activities of a civic organization also could be characterized as humanitarian activities of a charitable organization and that some organization could qualify as a civic organization but not a charitable organization (and vice versa) as a legal element may not be met. *Beyond Housing, Inc. and Pagedale Town Center II v. Missouri Dir. of Rev.*, No. SC99051 (Mo. S.Ct. September 13, 2022).

South Carolina: In response to a ruling requestion, the South Carolina Department of Revenue (SC DOR) said that retail sales of injectable medicine or injectable biologic for use in hospitals or in independent surgery centers are not exempt from South Carolina's sales and use tax under S.C. Code § 2-36-2120(80). The SC DOR noted, however, that such sales may be exempt from tax under another provision of S.C. Code § 2-36-2120, explaining that certain injectable medicines or injectable biologics that are prescription medicine and therapeutic radiopharmaceutical used to treat (1) cancer, leukemia, lymphoma, rheumatoid arthritis or related disease, or (2) the side effects of such treatment, may qualify for a sales and use tax exemption under S.C. Code § 2-36-2120(28)(a). S.C. Dept. of Rev., SC Rev. Ruling #22-9 (October 20, 2022).

Texas: On September 30, 2022, the Texas Supreme Court denied review in *Hegar v. Texas Westmoreland Coal Co.*,[10] in which the Third Court of Appeals (Appeals Court) held that a mining company was entitled to a refund of sales and use tax paid on the lease of three excavators, which the company used to extract and break apart lignite coal ore. The company argued that the sales and use tax manufacturing exemption in Tex. Tax Code § 151.318(a)(2)(A) applied because the excavators were used in processing lignite coal. The Texas Comptroller of Public Accounts (Comptroller) disagreed arguing that the lignite coal extracted from the ground was real property, not tangible personal property. The Comptroller also asserted that "processing" did not encompass extracting minerals from the ground. The Appeals Court rejected the Comptroller's arguments, holding that Section 151.318(a)(2)(A) does not require raw materials or inputs in the manufacturing process to be tangible personal property, only that the output at the end of the process differ from one or more inputs along the way. Additionally, the Appeals Court held that the excavators undeniably made physical changes to the lignite coal by extracting it from the ground. For more on this development, including the ruling's implications, *see* EY Tax Alert 2022-1564 (October 14, 2022).

Washington: The Washington Department of Revenue (WA DOR) said that it will not appeal the Washington Board of Tax Appeals (BTA) decision in *Terrapower LLC*,[11] in which the BTA held that a manufacturer is not required to manufacture items for sale in order for the manufacturer's purchases of qualifying machinery and equipment used in its research and development operation to qualify for the retail sales tax exemption, provided that all other requirements are met. The WA DOR said that it is developing further clarification or guidance, which will be issued at a later date. Wash. Dept. of Rev., Special Notice: "Notice regarding manufacturers' retail sales and use tax exemption for purchases of machinery and equipment used in a research and development operation" (November 9, 2022).

[10] 636 S.W.3d 61 (Tex. App. 2021), *review denied* (Tex. S.Ct. September 30, 2022).
[11] *Terrapower LLC v. Wash. Dept. of Rev.*, BTA Dkt. No. 19-065 (WA BTA July 25, 2022).

Transactions and Services

Federal: The U.S. Government Accountability Office (GAO) issued a report on states' remote sales tax provisions. The GAO estimated that remote sales tax collections were around $30 billion in 2021. According to the report, businesses, as a result of having to comply with remote sales tax legislation, reported increased costs related to software to expand multistate tax collection capabilities, audits and assessments, and staying current with legal requirements in multiple jurisdictions. Businesses also reported increased tax exposure. Further, the GAO found the overall remote sales system raised the following concerns as compared to a good tax system: (1) remote sellers having to devote significant time to understand various state requirements in states they have economic nexus; (2) remote sellers diverting resources away from business operations and investments toward tax compliance; and (3) understanding the various state requirements and remote sales tax obligations increased administrative costs for businesses selling remotely. The GAO recommended "that Congress consider working with states to establish nationwide parameters for state taxation of remote sales," and suggested that the parameters (1) balance state interest while addressing multistate complexities, (2) improve the overall system's alignment with a good tax system and address existing uncertainties related to taxing remote sales. GAO-23-105359 "Remote Sales Tax: Federal Legislation Could Resolve Some Uncertainties and Improve Overall System" (November 14, 2022).

Iowa: The Iowa Department of Revenue (IA DOR) has adopted various non-substantive revisions and substantive changes to rules related to services subject to the state's sales and use tax. According to the rule's "Purpose and Summary", non-substantive changes include the rescission of ch. 26, the "longstanding" rules on taxation of services, and replacement with new ch. 211. The rules also have been reorganized to include more subject-focused chapters. The substantive changes include modifications to current rules and the adoption of new rules to implement recently taxable services. Rule 701-211.17(423), regarding machine operators, excludes language from the prior rule that created confusion (i.e., use of the word "primary") and includes examples that describe when a person is a machine operator based on the person's use of a computer to perform job functions. The IA DOR also adopted as binding administrative rules, the nonbinding guidance it had issued on the imposition of sales tax on digital-based services. The new and amended rules[12] were adopted on November 9, 2022, and they take effect January 4, 2023.

Kentucky: The Kentucky Department of Revenue (KY DOR) has added new frequently asked questions (FAQs) on some of the 34 services that will become taxable on January 1, 2023, under legislation (HB 8) enacted in 2022. The FAQs address: employer recruitment services, lobbying, product testing, photography and photo finishing services, residential utility exemption changes, cosmetic surgery procedures, motor vehicle rental/ride share excise tax, parking services, rental space, transient room tax. The KY DOR said the website will be updated regularly.

New York: A company's subscription fees for tracking emails its customers send to prospective clients and analyzing that information and providing customers with reports on what activity occurred when the email was sent — such as whether the email was read, whether links were clicked, whether attachments were downloaded or emailed replied to — are nontaxable information services. In so holding, the New York Division of Tax Appeals (NY DTA) found that the reports are nontaxable because they consists solely

[12] The new rules include ch. 211 and ch. 218. Amended rules: ch. 203, ch. 213 through ch. 16, ch. 19, ch. 20, ch. 25.

of the customer's own data, are personal/individual in nature and are not furnished to other customers. The NY DTA also determined that the customer's use of software provided through a browser extension in email platforms to share templates and the download of a plugin to sync with an email platform and Salesforce was incidental to the primary purpose of proving reports and, as such, the company was not selling prewritten software. *Matter of Yesware, Inc., Matter of Bellows, and Matter of Andrus*, DTA Nos. 829638, 829639 and 829640 (N.Y. Div. of Tax App. September 29, 2022).

Tennessee: In response to a ruling request, the Tennessee Department of Revenue (TN DOR) found that a data and technology company's sales of its license and credential verification and compliance monitoring services are not subject to the state's sales and use tax because they are sales of nontaxable information and data processing services. The TN DOR determine that using various sources of information to build a proprietary database that customers can access is a type of information service. Further, while customer access to the services through the company's online portal or an application programming interface could be seen as taxable computer services, the TN DOR found that use of such was "merely incidental" to the non-taxable information and data processing services. The TN DOR reasoned that there is no additional charge for use of the application, both the portal and application are only used to gain access to the nontaxable services, and they are worthless without the nontaxable services. Tenn. Dept. of Rev., Letter Ruling #22-08 (October 12, 2022).

Tennessee: In response to a ruling request, the Tennessee Department of Revenue (TN DOR) determined that a company's subscription-based online platform and mobile application (collectively, "product") used to create and manage rental property advertising listings is computer software that users can use to generate and manage their own advertising content, and not advertising services. Accordingly, the company's sales of subscriptions the product are subject to the state's sales and use tax. In contrasting this ruling with TN DOR Rev. Rul. 19-01 (May 2019), the TN DOR noted that while there are similarities between the two rulings, in Ruling 19-01 the taxpayer's customers used the taxpayer's product to create event listings that were posted on the taxpayer's platform; they did not use software tools to create reports or manage data. In Ruling 19-01, the true object of the transaction was the non-taxable platform and listing services. Here, the company's product does not provide a platform for users to list their advertisements. Rather, the product allows users to create advertisements and publish them on other platforms, collects communications data, and contacts prospective buyers through automated emails and texts. In this instance, the TN DOR determined that the true object of the transaction is access to computer software. Tenn. Dept. of Rev., Letter Ruling #22-07 (October 5, 2022).

Texas: The Texas Comptroller of Public Accounts (Comptroller) in STAR Accession No. 202210014L (October 20, 2022) determined that charges for designated doctor exams ordered by the Texas Department of Insurance, Division of Workers' Compensation (TDI-DWC) are "insurance services" subject to Texas sales and use tax. The Comptroller acknowledged that STAR Accession No. 202210014L addressed policy issues related to workers' compensation insurance that it had not previously addressed. Given this, the Comptroller said it would delay implementation of that policy until after the 2023 legislative session concludes; this delay provides the TDI-DWC and participants in the workers' compensation system to seek legislative change. Given the delayed implementation, the Comptroller said doctors are not required to collect sales or use tax on designated doctor exams performed before October 1, 2023. Tex. Comp. of Pub. Acct., STAR Accession No. 202211002L (November 10, 2022).

Technology and Digital Taxes

Maryland: On October 17, 2022, Anne Arundel County (MD) Circuit Court Judge Alison Asti ruled that the Maryland's Digital Advertising Services Tax (DAT), [13] which took effect on January 1, 2022, violates: (1) the Internet Tax Freedom Act (ITFA) and Supremacy Clause because it "constitutes a discriminatory tax"; (2) the Commerce Clause as it discriminates against interstate commerce; and (3) the First and Fourteenth Amendments because it singles out the plaintiff for selective taxation and is not content-neutral.[14] Accordingly, the DAT is invalid. A similar challenge to the DAT brought in federal court was largely dismissed on March 4, 2022 on grounds that the suit was barred by the federal Tax Injunction Act.[15] The federal challenge was declared moot on December 2, 2022.[16] Nevertheless, Judge Asti's bench ruling does not settle the issue. Despite stating that "the incoming governor and the incoming legislature should be given the opportunity to revisit the law," the Comptroller, on November 21, 2022, gave notice that he was appealing Judge Asti's decision. And, on December 27, 2022, the Maryland Attorney General simultaneously filed with the Maryland Supreme Court a writ of certiorari, asking the court to consider the matter, and a motion requesting that enforcement of the tax be stayed pending appeal. It should be noted that the ruling calls into question whether similar legislation introduced in other states will move forward or be reworked in the upcoming 2023 state legislative sessions.

Controversy and Compliance

National: Businesses paid more than $951 billion in state and local taxes in fiscal year 2021, an increase of 13.6% from fiscal year 2020, according to a study prepared by Ernst & Young LLP (EY US) for the Council On State Taxation (COST) and its affiliate, the State Tax Research Institute (STRI). The report, titled "Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2021," shows that in 2021, business tax revenue accounted for 43.6% of all state and local tax revenue. In all, state business taxes increased by 17%, and local business taxes grew by 10.2%. The study provides estimates of state and local business taxes that reflect tax collections from July 2020 through June 2021. The strong growth in corporate income taxes and individual income taxes on business income is in part due to the extension of the April 15 filing deadline to July, which shifted revenues from FY20 to FY21. The data presented in this study is for each state's fiscal year, which differs by state. The study reports that general sales taxes on business inputs and capital investments totaled $194.5 billion, or 20.4% of state and local business taxes. Visit here for the full study.

Arizona: The Arizona Department of Revenue (AZ DOR) said that it has sent 2023 Transaction Privilege Tax (TPT) renewal letters to businesses. Taxpayers selling products or engaging in taxable business activity should have renewed their Arizona TPT license by January 1, 2023. The renewal is good from January 1 to December 31, 2023; the renewal must be made annually. Renewals received by the AZ DOR after January 1 are subject to penalties and/or late fees. Taxpayers with multiple business locations

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[13] Maryland's DAT is imposed on the annual gross revenue derived from digital advertising in the state. The tax applies at a graduated rate that increases in increments based on the taxpayer's global annual revenues. For more on the DAT, see Tax Alerts 2021-0343 and 2021-0788.
[14] *Comcast of California/Maryland/Pennsylvania/Virginia/West Virginia LLC et al. v. Comptroller of the Treasury of Maryland*, Case No. C-02-CV-21-000509 (October 17, 2022 Md. Cir. Ct. Anne Arundel Cty.).
[15] See *Chamber of Commerce of the United States of America et al. v. Franchot*, Civ. No. 21-cv-410 (U.S. Dist. Ct. Md. N. Div.).
[16] *Id.* Memorandum Opinion and Order (U.S. Dist. Ct. Md. N. Div. December 2, 2022).

must renew their license electronically. Ariz. Dept. of Rev., 2023 Transaction Privilege Tax License Renewals Notice (November 8, 2022).

Colorado: In September 2022, the Colorado Department of Revenue (CO DOR) released for public comment draft rule on the state's new retail delivery fee – new Rule 43-4-218 "Retail Delivery Fee". The general rule, as described by the draft retail delivery fee rule is that on or after July 1, 2022, retailers making retail delivers must impose, collect and remit the retail delivery fee. The fee is added to the price of the retail delivery. These requirements do not apply to retailers not doing business in Colorado. The draft rule provides guidance on (1) imposition of the fee and how it is sourced, with focused discussions on (a) subscriptions, recurring purchase programs, leases and installment sales; (b) delivery by a motor vehicle; and (c) determining delivery location; (2) deliveries of tangible personal property not subject to, or exempt from, the retail delivery fee, with specific guidance on wholesale sales, drop shipments, complimentary tangible personal property, discounts, and burden of proof; (3) contractors and repair services (e.g., time and materials contractor, lump-sum contractor, suppliers to contractors); (4) deliveries of marijuana; (5) registration; (6) collection of the retail delivery fee, with specific guidance on displaying retail delivery fees on an invoice, failure to collect the fee, retail sales made through an online marketplace, and direct payment permit holders; (7) filing and remitting the retail delivery fee; (8) refunds and credits, including claims for refund, credit for refunded fees collected in error, disputes, returned retail deliveries, canceled retail deliveries, bad debts charged-off; and (9) penalties and interest, statute of limitations, power of collection and enforcement, and calculation and publication of the retail delivery fee. The CO DOR accepted comments and held a public rulemaking hearing on the draft rule on November 3, 2022.

Colorado: The Colorado Department of Revenue (CO DOR) adopted Rule 40-10.1-607.5, which provides guidance on collecting, administering and enforcing prearranged ride fees imposed on transportation network companies (TNCs). TNCs required to collect and remit the fee must register with the CO DOR and create a prearranged ride fee account. TNCs that fail to register with the CO DOR are still liable and responsible for the full amount of the fees due plus any applicable interest. The return must be filed by, and the fee remitted on or before, the last day of the month following the close of each reporting period. The amount remitted to the CO DOR equals the product of the fee in effect for the reporting period and the number of prearranged rides requested and accepted through the company's digital network in the reporting period. Refunds for overpayment of the fee must be filed not later than three years after the date of payment. TNCs must keep and preserve for a period of at least three years it books, accounts, and records necessary to determine the amount of the fee. If a TNC does not timely file a return or remit the correct amount of fee due, the CO DOR can estimate the amount of fees due; the estimate becomes a notice of deficiency which a TNC can protest. The rule takes effect December 30, 2022. The rule was adopted on November 16, 2022.

Indiana: The Indiana Department of Revenue (IN DOR) issued guidance describing the state's various sales and use tax sourcing rules. Under Indiana law, whether a transaction is considered made in Indiana or another jurisdiction primarily depends on where the purchaser receives the goods or services. Indiana's sourcing rules differ for transactions that are sales or leases/rentals as well as for various types of tangible personal property. The guidance includes: (1) general sourcing rules, which explain the order in which retail sales of a product are sourced; (2) general sourcing rules for rentals and leases; (3) sourcing of rentals and leases of motor vehicles, trailers, semitrailers and aircraft; (4) sourcing of transportation equipment; and (5) sourcing of floral products. In regard to the sourcing rules for rentals and leases requiring recurring period payments, the first payment is sourced the same as a retail sale

and subsequent payments are sourced to the primary property location for each period covered by the payment (the property location is not altered by intermittent use at different locations). For rentals and leases that do not require periodic payments, the payment is sourced the same as a retail sale. The bulletin took effect upon publication. Ind. Dept. of Rev., Sales Tax Information Bulletin #96 "Sourcing Rules" (October 2022).

Kansas: The Kansas Department of Revenue issued guidance on the phase-out of the state's sales and use tax on food and food ingredients. Under law enacted in 2022 (HB 2106), the current 6.5% tax rate will be reduced to 4% on January 1, 2023, and to 2% on January 1, 2024. The rate is reduced to zero as of January 1, 2025. Food and food ingredients remain subject to local sales and use taxes imposed by cities and counties. The guidance includes definitions of food and food ingredients. Kan. Dept. of Rev., Notice 22-15 "Kansas Food Sales Tax Rate Reduction" (December 1, 2022).

Missouri: The Missouri Department of Revenue (MO DOR) posted frequently asked questions (FAQs) on the state's remote seller and marketplace facilitator provisions that take effect on January 1, 2023. A remote seller must register with the MO DOR if its gross receipts from taxable sales of tangible personal property (TPP) into Missouri exceeds $100,000 in a year. A marketplace seller does not have to register with the MO DOR or collect and remit vendor's use tax if it only sells through a marketplace facilitator. A marketplace seller, however, will have to register, collect, and remit tax, if it has taxable sales in excess of $100,000 in Missouri that are not through a marketplace facilitator. The tax is remitted to the MO DOR separately from what is reported by the marketplace facilitator. Similar to remote sellers, a marketplace facilitator must register with the MO DOR and file a vendor's use tax return if its gross receipts from taxable sales of TPP into Missouri exceed $100,000 in a year. The MO DOR explained that the $100,000 threshold is based on all sales of TPP made to Missouri customers and shipped into the state, including through a marketplace facilitator. At the end of each calendar quarter, if the entity's gross receipts from taxable sales into Missouri exceed $100,000 in the preceding 12-month period, it must collect and pay Missouri vendor's use tax effective no later than three months following the close of the quarter (e.g., if on July 1, 2024, the threshold was met, the entity would collect and pay vendor's use tax by October 1, 2024). The entity must continue to collect and remit vendor's use tax as long as it is engaged in business in Missouri. The FAQs explain how to register with the MO DOR and how a marketplace facilitator should report its retail sales. Lastly, the MO DOR said that marketplace facilitators are eligible for the 2% timely discount if they remit tax owed on or before the tax return's due date. Mo. Dept. of Rev., "Remote Seller and Marketplace Facilitator FAQs" (last accessed December 9, 2022).

New Mexico: The New Mexico Taxation and Revenue (NMTR) issued guidance on the gross receipts tax collection and remittance requirements for marketplace providers selling lodgings or accommodations. Under New Mexico law, a business that through its online marketplace lists and books lodgings or accommodations in New Mexico on behalf of third parties is a marketplace provider and will owe gross receipts tax on the receipts from sales it facilitates if it is "engaging in business" in New Mexico. A business is "engaging in business" in New Mexico if it is physically present in the state or, if in the prior calendar year, it had over $100,000 in taxable gross receipts sourced to New Mexico. The over $100,000 threshold is based on sales made by the entity; if a marketplace provider, the threshold determination includes receipts received on behalf of marketplace sellers, but does not include sales of the entity's affiliates or its parent company. The tax rate includes the state gross receipts tax rate and any applicable local option gross receipts tax. Taxable gross receipts include all money received from the buyer, including amounts received on behalf of marketplace sellers and fees charged to the buyer for the accommodation such as service fees and fees associated with using the property's facilities.

Taxable gross receipts also include fees the marketplace provider receives as compensation for listing the accommodation for the seller when the fee is charged as a separate transaction and not as a percentage of the receipts received from the buyer (which would already be included in the reported gross receipts). Marketplace sellers are responsible for reporting gross receipts from the sales of the accommodation on the online marketplace. Marketplace sellers, however, may deduct these receipts on the gross receipts return. Even though the seller taking the deduction may owe no tax, they still need to report the receipts in order to comply with reporting requirements. The NMTR's guidance includes illustrative examples. The NMTR noted that marketplace provides also may be subject to other taxes administered by municipalities and counties such as lodgers' tax. N.M. Taxn. and Rev., Bulletin B-200.37: Marketplace Providers and the Sale of Lodgings or Accommodations (October 12, 2022).

Oklahoma: The Oklahoma Tax Commission adopted amendments to the rules for the rental tax on motor vehicle rentals – Okla. Admin. Rules §§ 710:95-4-2, -3 and -4 – to add information on peer-to-peer car sharing programs and shared vehicles. Amendments to Rule § 710:95-4-2 add definitions of "applicable taxes", "peer-to-peer car sharing program", "peer-to-peer car sharing program agreement", "rental agreement", "shared vehicle" and "shared vehicle owner". Taxes that apply to shared vehicles purchased in Oklahoma include the motor vehicle excise tax and sales tax. Taxes that apply to such vehicles purchased outside the state include sales, use, excise or other tax generally due upon the purchase of a motor vehicle in the jurisdiction in which the shared vehicle was purchased. An amendment to Rule § 710:95-4-3 makes clear that the rental tax on motor vehicles does not apply to any shared vehicle for which applicable taxes were paid upon the vehicle's purchase. An amendment to Rule § 710:95-4-4 requires peer-to-peer car sharing programs to collect the rental tax when the rental agreement is paid. The amended rules took effect September 11, 2022. Okla. Tax Comm., amendments to Okla. Admin. Rules §§ 710:95-4-2, -3 and -4 (39 Okla. Reg 2303, adopted September 1, 2022).

Texas: The Texas Comptroller of Public Accounts determined that for purposes of the optional single local use tax rate for remote sellers, the estimated average rate of local sales and use taxes imposed in Texas during the preceding state fiscal year ending August 2022 is 1.75%. This rate will be in effect for the period from January 1, 2023 to December 31, 2023. Tex. Comp. of Pub. Accts., Texas Register "In Addition" (47 TexReg 7443 November 4, 2022).

Wyoming: The Wyoming Department of Revenue (Department) issued guidance on the application of the state's sales, use and lodging taxes to various types of lodging transactions, including using an online platform to make a reservation. The Department considers online travel companies (OTCs) to be marketplace facilitators under Wy. Stat. §39-15-502; as the marketplace facilitator, the OTC is responsible for collecting and remitting sales, use and lodging taxes. Marketplace facilitators must collect and remit sales tax on all sales made on its own behalf and on behalf of marketplaces sellers – in this case the hotel is the marketplace seller. When an OTC is not involved in the reservation process the entire lodging services provided by the hotel is subject to sales and lodging tax, which must be reported and remitted by the hotel. When a travel agent is used, the hotel charges the customer for the room; the entire cost of the room rental includes tax on the travel agent's commission. If lodging services are reserved partially through an OTC and partially through the hotel, the OTC is responsible for collecting taxes associated with the goods and services related to the online transaction, while the hotel should collect any additional taxable fees that are not covered by the OTC transaction (e.g., when the guest request a rollaway bed or makes a purchase from the hotel store). When a customer reserves a room through an OTC but directly pays the hotel for the lodging service (and at a later time the hotel pays the OTC a commission), the hotel is responsible to report the total cost of the room and taxes. The guidance

is effective January 1, 2023. Wy. Dept. of Rev., Bulletin: Lodging Services and Marketplace Facilitators (October 1, 2022).

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