

FINAL PRIVATE LETTER RULING

18-002

RESPONSE LETTER

April 10, 2019

Mr. NAME-1
COMPANY-2
Attn: Tax
P.O. Box #####
CITY, STATE AND ZIP CODE

Dear NAME-1:

This letter is in response to your request for a private letter ruling for COMPANY (“Company”), which sells subscriptions. Through the subscriptions, subscribers (“Subscriber(s)”) are entitled to multiple benefits. The Subscribers receive these benefits as they interact with the Company’s internet-based platform (“Platform”). You have asked whether the sales of these subscriptions are subject to Utah sales and use taxes. This private letter ruling concludes that the Company’s sales of subscriptions are *not* subject to Utah sales and use taxes. This conclusion is further explained in Section III. of this private letter ruling request.

I. Facts

You have explained that through the Platform, people (“Viewers”) can watch streaming videos.

Viewers can view these videos without registering with the Company or paying to access or view the videos. Viewers without a subscription will be subject to advertising. Viewers who are Subscribers obtain various levels of ad-free viewing.

You explained that the videos include real-time streaming videos and videos on demand (“VOD”). You explained that the Company obtains licenses for the videos from third parties (“Third Party” or “Third Parties”). These Third Parties often create videos of themselves doing various activities.

While viewing real-time streaming videos, Viewers can type comments using the Platform’s chat function. Third Parties can type comments back. Viewers without a subscription may type comments using basic chat colors and emoticons. Subscribers may type comments using additional emoticons and/or colors, depending on the type of subscription. Subscribers also receive a special icon indicating the type of subscription they purchased. Additionally, for

one of the subscriptions, Subscribers' comments appear more quickly; there is no delay between a Subscriber typing a message and that message appearing in the chat.¹ Furthermore, for that same subscription, Subscribers may access a specialized chat mode for Subscribers only. For a different subscription, Subscribers receive the opportunity to send a custom message to the Platform's community when first subscribing.

The Platform is designed to encourage comments and other interactions among Third Parties and Viewers, instead of having Viewers passively watch videos. Viewers with and without subscriptions can donate to Third Parties using the Platform's chat function. Third Parties participating in gaming activities frequently provide donors with additional playing opportunities. These opportunities include a Viewer playing a video game with the Third Party in a video being streamed on the Platform or a Viewer playing with a particular character, item, or other in-game setting requested by the Viewer. These opportunities motivate Viewers to become Subscribers and donors.

As mentioned previously, Third Parties provide the Company with videos. In addition to providing the Company with *real-time* streaming videos, Third Parties can save their *past* videos and post them to the Platform for Viewers to access as videos on demand ("VOD"). The Third Parties can save their VOD to the Platform without charge, by default, for ### days. If a Third Party becomes a Subscriber of a certain subscription, the Third Party may save their VOD to the Platform for ### days.

You submitted a copy of an agreement ("Agreement") between the Company and its Subscribers. The Agreement is titled "Terms of Service." Under § ### of the Agreement, the Company has the right and absolute discretion to remove any Third-Party videos saved on the Platform at any time for any reason without notice. That section also explains that Third Parties are solely responsible for backing up their videos.

You further explained that Subscribers with a certain subscription receive priority customer support.

The various benefits of the subscriptions have been described above. The exact groupings of benefits for each subscription have not been described above because this private letter ruling ultimately concludes that none of the benefits, if sold separately, would be subject to Utah sales and use taxes.

¹ This private letter ruling does not provide the specific benefits for each type of subscription because this private letter ruling ultimately concludes that all benefits presented, if sold separately, would not be subject to Utah sales and use taxes.

II. Applicable Law

Utah Code Annotated § 59-12-103(1) imposes tax on certain transactions, stating the following in part:²

A tax is imposed on the purchaser . . . on the purchase price or sales price for amounts paid or charged for the following transactions:

- (a) retail sales of tangible personal property made within the state;
.....
- (k) amounts paid or charged for leases or rentals of tangible personal property if within this state the tangible personal property is:
 - (i) stored;
 - (ii) used; or
 - (iii) otherwise consumed;
- (l) amounts paid or charged for tangible personal property if within this state the tangible personal property is:
 - (i) stored;
 - (ii) used; or
 - (iii) consumed; and
- (m) amounts paid or charged for a sale:
 - (i) (A) of a product transferred electronically; . . .
.....
 - (ii) regardless of whether the sale provides:
 - (A) a right of permanent use of the product; or
 - (B) a right to use the product that is less than a permanent use, including a right:
 - (I) for a definite or specified length of time; and
 - (II) that terminates upon the occurrence of a condition.

Utah Code Ann. § 59-12-102 defines various terms, stating in part:

As used in this chapter:

-
- (26) "Computer" means an electronic device that accepts information:
 - (a) (i) in digital form; or
 - (ii) in a form similar to digital form; and
 - (b) manipulates that information for a result based on a sequence of instructions.
- (27) "Computer software" means a set of coded instructions designed to cause:
 - (a) a computer to perform a task; or
 - (b) automatic data processing equipment to perform a task.
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² For purposes of § 59-12-103(1), § 59-12-102(99) defines "purchase price" or "sales price," § 59-12-102(109) defines "retail sale," § 59-12-102(110) defines "sale," and § 59-12-102(125) defines "tangible personal property."

(93) (a) . . . “prewritten computer software” means computer software that is not designed and developed:

- (i) by the author or other creator of the computer software; and
- (ii) to the specifications of a specific purchaser.

.....

(95) (a) Except as provided in Subsection (95)(b), "product transferred electronically" means a product transferred electronically that would be subject to a tax under this chapter if that product was transferred in a manner other than electronically.

(b) "Product transferred electronically" does not include:

- (i) an ancillary service;
- (ii) computer software; or
- (iii) a telecommunications service.

.....

(125)

(b) "Tangible personal property" includes:

.....

- (v) prewritten computer software, regardless of the manner in which the prewritten computer software is transferred.

.....

III. Analysis

As stated previously in this private letter ruling, you have asked whether the Company’s sales of subscriptions are subject to Utah sales and use taxes. This private letter ruling concludes that the Company’s sales of subscriptions are *not* subject to Utah sales and use taxes. The analysis supporting this conclusion is below.

This Section III. includes the following items:

- A list of the subscription benefits divided into four distinct items or categories (Subsection III.A.).
- Analyses of the taxability of each of the four distinct items or categories if sold separately (Subsections III.B. through III.E.).
- A summary of the taxability of the subscriptions (Subsection III.F.).

A. The Benefits of the Subscriptions can be Divided into Four Distinct Items or Categories.

The Company's subscriptions provides Subscribers with the following benefits:

- Ad-free Viewing
- Chat Function Enhancements
- Additional Time to Save VOD on the Platform: ### days instead of ### days
- Priority Customer Support

To analyze the taxability of the purchase price of a subscription, the taxability of the underlying items must be considered. As seen with the Commission's analyses of unrelated memberships in Private Letter Rulings ("PLR(s)") 17-003 and 16-005 and of renewal fees in PLR 15-008, one must "look[] beyond that label [attached to a product] to examine the underlying nature of the transaction."³ This private letter ruling uses this approach to determine the taxability of the Company's subscriptions. When a person purchases a subscription, the person is actually purchasing the four benefits listed above.

Playing games with Third Parties is not part of the subscriptions. The Company does not provide Subscribers with the right to play games with Third Parties. The Third Parties determine with whom they play.

B. If the Ad-Free Viewing Were Sold Separately, the Benefit Would *Not* be Taxable Under § 59-12-103(1).

One of the subscription benefits is ad-free viewing. Viewers without subscriptions can access all streamed content. Thus, when Subscribers purchase ad-free viewing, they are not paying to access the streamed content.^{4,5} The purchase of ad-free viewing is not among the transactions enumerated in § 59-12-103(1) as being taxable. Thus, if the ad-free viewing were sold separately, the benefit would *not* be taxable.

³ Private letter rulings can be accessed through the tax.utah.gov website.

⁴ In general, if a purchaser were to pay to view without downloading videos streamed over the internet, those transactions would not be subject to Utah sales and use taxes. Thus, if the Subscribers were paying for access to streamed content, those transactions would not be subject to Utah sales and use taxes.

⁵ Although you have not inquired about the Multi-Channel Video or Audio Service Tax Act, which is found in Utah Code Annotated, Title 59, Chapter 26, this private letter ruling provides the following comments. In general, if access to streamed videos is sold as part of a multi-channel video or audio service, the amounts paid or charged for that service are subject to the multi-channel video or audio service tax under § 59-26-103. The ad-free viewing of this private letter ruling is not subject to the multi-channel video or audio service tax because Subscribers are not *purchasing* multi-channel video or audio service. Instead, the video content is available free of charge.

C. If the Chat Function Enhancements Were Sold Separately, those Enhancements Would *Not* be Taxable Under § 59-12-103(1).

The chat function enhancements include the following:

- Additional emoticons and/or colors.
- A special icon indicating the type of subscription the Subscriber purchased.
- The ability to comment more quickly, without a delay between a Subscriber typing a message and that message appearing in the chat.
- A specialized chat mode for Subscribers only
- An ability to send a custom message to the Platform's community when first subscribing

You also explained the chat function's importance as follows: the Platform is designed to encourage interactions among Third Parties and Viewers, instead of having Viewers passively watching the videos.

In general, the sale of the ability to participate in an interactive community is not subject to Utah sales and use taxes. PLR 17-003 concerned the taxability of the sale of "the ability to participate in an interactive community comprised of [people holding memberships] of [a] [c]ompany." PLR 17-003 concluded that "[i]f the [c]ompany were to sell this benefit separately, the [c]ompany would be selling a service that is not subject to Utah sales and use taxes." PLR 17-003 provided an "essence of the transaction" analysis supporting its conclusion. In that analysis, PLR 17-003 considered the use of the company's computer software in providing the access to the interactive community. PLR 17-003 concluded the following:

The [c]ompany's software that supports this access to the interactive community is merely incidental to [the] service [of access to the interactive community]. The [c]ompany is using or consuming that software in providing the [m]embers with the service of access to the interactive community.

Applying PLR 17-003 to this private letter ruling, if the Company were to sell access to the chat function, the essence of the transaction would *not* be the use of the Company's software. Instead, the essence of the transaction would be the purchase of the ability to communicate with other Viewers and Third Parties.⁶

The Company does not sell access to the chat function, though; the Company provides the chat function free of charge. Instead, the Company sells chat function enhancements. The essence of the transaction for the sale of the use of the chat function enhancements is for Subscribers to communicate better with other Viewers and Third Parties. As with the use of the

⁶ If the essence of the transaction had been the sale of the use of the Company's software, the sale of that use in Utah would have been taxable. The sale of the use of prewritten computer software in Utah is taxable under § 59-12-103(1)(a), (k), and (l). Prewritten computer software is defined in § 59-12-102(93) and is further defined as being tangible personal property in § 59-12-102(125)(b)(v).

chat function generally, the Company's computer software is involved. The use of the Company's computer software is incidental to the services of both the chat function and the chat function enhancements. The Company is consuming the computer software for the chat function and the enhancements when the Company provides the chat function and the enhancements to the Viewers and Subscribers.

In addition to the sale of the chat function enhancements not being the sale of prewritten computer software, the sale of the chat function enhancements are also not the sale of products transferred electronically, as explained below. The chat function enhancements include emoticons, colors, and special icons. Under § 59-12-102(95)(a), a "product transferred electronically" means a product *transferred* electronically that would be subject to a tax under this chapter if that product was transferred in a manner other than electronically" (emphasis added). The Company does not transfer the emoticons, colors, and special icons to Subscribers; the Subscribers do not download them. The Subscribers can only use the emoticons, colors, and special icons on the Platform.

Overall, the sale of the use of the chat function enhancements is the sale of a service not taxable under § 59-12-103(1).

D. If the Additional Time to Save VOD on the Platform Were Sold Separately, the Benefit Would *Not* be Taxable Under § 59-12-103(1).

Subscribers who are also Third Parties may receive additional time to save VOD on the Platform. They may save their videos ### days instead of ### days. Under the Agreement, the Company has the right and absolute discretion to remove any Third-Party videos saved on the Platform at any time for any reason without notice. Also under the Agreement, the Third Parties are solely responsible for backing up their videos.

Analysis of the essence of the transaction is appropriate for this situation. A Subscriber is storing videos on the Company's Platform, which storage would be on the Company's hardware. There is also a service involved; the Subscriber can have his or her VOD available to Viewers for ### days instead of ### days because he or she can store his or her videos on the Company's Platform longer.

The Utah Supreme Court explained the essence of the transaction as follows:

[T]he essence of the transaction theory[] focuses on the nature of what was sold and whether it primarily entails tangible personal property. . . . This theory examines the transaction as a whole to determine whether the essence of the transaction is one for services or for tangible personal property. The analysis typically requires a determination either that the services provided are merely incidental to an essentially personal property transaction or that the property provided is merely incidental to an essentially service transaction. . . .

B.J.-Titan Services v. State Tax Comm'n, 842 P.2d 822, 825 (Utah 1992) (internal citations removed).

The tangible personal property involved is the Company's hardware used for storage. Under the Agreement, the Company can remove the Subscriber's videos from the Company's hardware at any time for any reason without notice. Additionally, the Agreement instructs Subscribers to store their videos elsewhere. Thus, the Subscribers cannot reasonably rely on the Company's hardware as the Subscribers' primary or backup storage for the Subscribers' videos.

The service involved is the Company's making a Third Party Subscriber's VOD available to Viewers for a longer time period, ### days instead of ### days. This VOD service is the reason Third Parties would store their videos on the Company's Platform.

After considering the Company's computer hardware for storage and the VOD service the Company provides to Third Parties, the essence of the transaction for the additional time to save VOD is the Third Parties' use of the Company's VOD service and not the Third Parties' use of the Company's hardware.

The sale to Third Party Subscribers of the use of the Company's VOD service is not among the taxable transactions listed in § 59-12-103(1). Thus, if the additional time to save VOD on the Platform were sold separately, the benefit would not be subject to Utah sales and use taxes.

E. If the Priority Customer Support Were Sold Separately, the Benefit Would *Not* be Taxable Under § 59-12-103(1).

You have not provided details about what is involved in the priority customer support. This private letter ruling assumes the priority customer support does not involve the Company transferring products transferred electronically to the Subscribers or the Company providing use of tangible personal property, including the Company's software, to the Subscribers. In general, customer support is not subject to Utah sales and use taxes because the sale of that service is not among the transactions enumerated in § 59-12-103(1) as being taxable.

F. Summary

None of the subscription benefits are subject to Utah sale and use taxes if they were sold separately. Likewise, none of the subscription benefits are taxable when they are sold for one non-itemized price. Therefore, the Company's sales of subscriptions that provide the benefits analyzed in this private letter ruling are *not* subject to Utah sales and use taxes.

IV. Conclusion

The Company's sales of subscriptions to Subscribers are *not* subject to Utah sales and use taxes.⁷

The Tax Commission's conclusions are based on the facts as you described them and the Utah law currently in effect. Should the facts be different or if the law were to change, a different conclusion may be warranted. If you feel we have misunderstood the facts as you have presented them, you have additional facts that may be relevant, or you have any other questions, please feel free to contact the Commission.

Additionally, you may also appeal the private letter ruling in the following two ways.

First, you may file a petition for declaratory order, which would serve to challenge the Commission's interpretation of statutory language or authority under a statute. This petition must be in written form, and submitted within thirty (30) days after the date of this private letter ruling. You may submit your petition by any of the means given below. **Failure to submit your petition within the 30-day time frame could forfeit your appeal rights and will be deemed a failure to exhaust your administrative remedies.** Declaratory orders are discussed in Utah Administrative Code R861-1A-34 C.2., available online at <http://tax.utah.gov/commission/effective/r861-01a-034.pdf>, and in Utah Administrative Code R861-1A-31, available online at <http://tax.utah.gov/commission/effective/r861-01a-031.pdf>.

Second, you may file a petition for redetermination of agency action if your private letter ruling leads to an audit assessment, a denial of a claim, or some other agency action at a division level. This petition must be written and may use form TC-738, available online at <http://tax.utah.gov/forms/current/tc-738.pdf>. Your petition must be submitted by any of the means given below, within thirty (30) days, generally, of the date of the notice of agency action that describes the agency action you are challenging.

⁷ This private letter ruling does not address the Company's possible Utah sales and use tax obligations for the Company's consumption of taxable property and services when the Company provides its nontaxable services to its Subscribers. Notably, whether the Company is consuming any property and services in Utah is not explained in the facts of your request letter.

You may access general information about Tax Commission Appeals online at <http://tax.utah.gov/commission-office/appeals>. You may file an appeal through any of the means provided below:

- **Best way**—by email: taxappeals@utah.gov
- By mail: Tax Appeals
USTC
210 North 1950 West
Salt Lake City, UT 84134
- By fax: 801-297-3919

For the Commission,

Lawrence C. Walters
Commissioner

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