

May 17, 2024

NCSL Executive Committee Task Force of State and Local Taxation

# Exploring State Approaches to Taxing Digital Goods

## Virginia Overview

Presenter

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Revenue estimates are in millions and were generated by Virginia Department of Taxation in producing Fiscal Impact Statements for HB889 and HB1281 in the 2024 General Assembly Session or in response to Budget Conferees as found on page 10 of "Summary of Major Items in Conference Report" dated March 8, 2024.

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### Digital retail sales tax in Governor's budget if taxed at 5.787% effective retail sales tax rate

	Software Apps (businesses)	Apps other services (consumers)	Streaming Music & Video	Digital Downloads	Consumer Digital tax Total
FY2026	0	\$586.5	\$111.2	\$57.2	\$754.8
% of digital		78%	15%	8%	
		100%			

Definition in Governor's Budget:

"Digital personal property" means **digital products delivered electronically**, including software, digital audio and audiovisual products, reading materials, and other data or applications, **that the purchaser owns or has the ability to continually access**, whether by downloading, streaming, or otherwise accessing the content, **without having to pay an additional** subscription or usage fee to the seller after paying the initial purchase price."

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Definitions in Governor’s budget con'd

**"Taxable service"** means any of the following services used or consumed in the Commonwealth:

1. Software application services;
2. Computer-related services;
3. Website hosting and design;
4. Data storage; and
5. Streaming services.

Governor proposed applying sales tax to all 5 categories of services defined above only to **consumer** digital purchases. **Business** purchases would be exempt.

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**Digital retail sales tax in Reg Session Conf Report** taxed at 5.787% effective retail sales tax rate

	Software Apps {businesses}	Apps other services {consumers}	Streaming Music & Video	Digital Down-loads	Digital Tax including business apps Total
FY2026	\$360.5	\$586.5	\$111.2	\$57.2	\$1,115.3
% of digital	32%	53%	10%	5%	
	~ 1/3		~ 2/3		

The Conference Report accepted the Governor's definitions of digital services. However, **the Legislature regarded** the definition of "digital personal property" as **"products delivered electronically ... after paying the initial purchase price" to be a definition of tangible property.**\*

Since Virginia does not exempt most business purchases of tangible property from the sales tax,\*\* the Legislature applied the tax to business purchases of software applications.

\* ie, NY Tax Appeals Tribunal 5/2/24 decision that software that helped businesses manage temporary employees were sales of tangible personal property not nontaxable services.  
(\*\*§ 58.1-609.2 exempts agriculture; § 58.1-609.3 exempts manufacturing and specific carve-outs, ie, data centers, transportation services, natural gas.)

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Resolution as of May 13, 2024

- The Governor had proposed the digital tax – along with raising the retail sales tax rate – as a package to lower income tax rates.
- Legislature rejected the rest of Governor’s package.
  - Income tax rate cut was 3 times greater for 5.75% bracket than for 2% bracket.
  - There was no legislative support for raising general sales tax rate.
- The Governor rejected only enacting a digital sales tax.
  - He pledged to cut taxes.
  - Business reacted to not being exempt.
- It was agreed to use current higher than anticipated revenues – rather than enacting an ongoing digital sales tax – to fund K-12 funding increases and other priorities.
- Legislature noted that taxation of digital goods needed to be considered as part of comprehensive modernization of tax structure.

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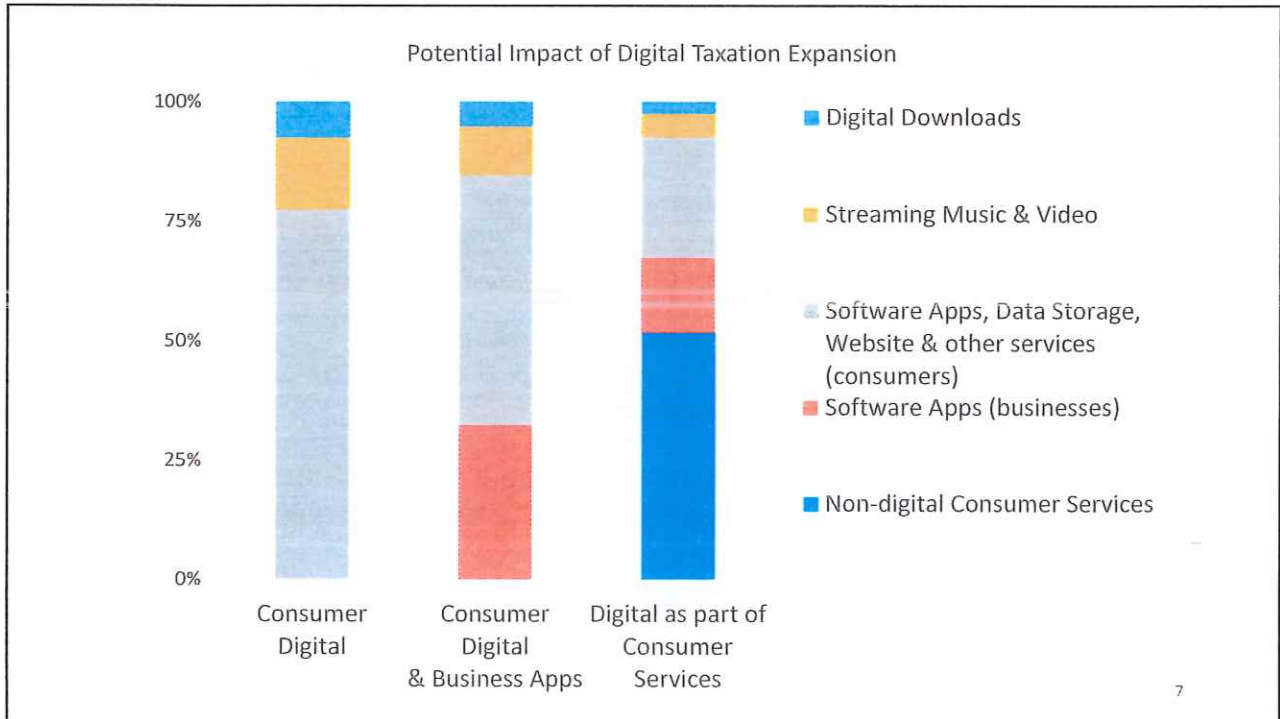
**Option: Extend sales tax broadly to services and digital goods**

	Select non-digital Consumer Services	Software Apps (businesses)	Apps, Data Storage, Website & other services (consumers)	Streaming Music & Video	Digital Down - loads	Total
FY2026	\$1,200.7	\$360.5	\$586.5	\$111.2	\$57.2	\$2,316.0
% of "services"	52%	16%	25%	5%	2%	

Virginia essentially does not tax services and in 2015 was ranked 44th by Tax Foundation in sales tax breadth. Therefore, "select" consumer services includes most services that might be taxed in other states. The following services are excluded:

1. Healthcare requiring state licensure or certification of the practioner or the facility and veterinarian care;
2. Professional services such as provided by attorneys, accountants, and real estate agents;
3. Business to business services not including tangible property separately billed;
4. Building trades and construction work that requires a permit; and
5. Home and grounds services not performed by a person employed by or contracted through a third party.

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Revenue estimates are for the total revenue generated. Expanding the sales tax base applies to all sales taxes enacted in Virginia; therefore, the revenue would be split and approximately

- 38% would go to the **state** General Fund for appropriation;
- 23% is the 1-cent **local** sales tax;
- 16% is allocated to localities based on **school-age population**;
- 14% is the 0.05-cent **state transportation tax**;
- 7% is **regional transportation** authority taxes; and
- 1% are **voter-approved local** sales taxes for school bonds or tourism.

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