Text of Proposed Amendments to California Code of Regulations

Title 18. Public Revenues

Division 2. California Department of Tax and Fee Administration – Business Taxes

Section 1600. Application of Sales and Use Tax to Digital Products.

(*A new regulation to be added to the California Code of Regulations.*)

Regulation 1600. Application of Sales and Use Tax to Digital Products.

(a) Definitions. For purposes of this regulation, the following terms have the following meanings:

(1) "Accessed remotely" has the same meaning as defined in Revenue and Taxation Code section 6016.2.

(2) "Computer" has the same meaning as defined in Revenue and Taxation Code section 6010.9.

(3) "Computer software" has the same meaning as defined in Revenue and Taxation Code section 6010.9.

(4) "Digital product" has the same meaning as defined in Revenue and Taxation Code section 6016.1. This includes, but is not limited to, prewritten computer software with artificial intelligence (AI), and prewritten computer software accessed remotely by users over the internet or by other digital means, such as direct access or non-internet protocols.

"Digital product" excludes:

(A) A digital asset, as defined in Revenue and Taxation Code section 6016.1, such as cryptocurrency or other non-fungible digital assets as specified by the Secretary of the Treasury of the United States.

(B) A digital audio work, as defined in Revenue and Taxation Code section 6016.1, such as music, audio books, spoken recordings, or ringtones.

(C) A digital audiovisual work, as defined in Revenue and Taxation Code section 6016.1, such as movies and videos with sound.

(D) A digital book, as defined in Revenue and Taxation Code section 6016.1, such as electronic books.

(E) Digital infrastructure, defined as a cloud-based service provided remotely that allows a user to create, deploy, scale, or run the user's own computer software on the service

provider's digital platform without managing, operating, or maintaining the user's own infrastructure, including any hardware, software, networks, and facilities that are required to allow the user to create, deploy, scale, or run the user's own computer software, required to complete the task. This includes Infrastructure-as-a-Service (IaaS) that meets the definition of digital infrastructure.

(i) A user's own computer software includes: computer software created by the user; computer software purchased by the user; and computer software leased, licensed, or the right to access to which is otherwise transferred to the user for consideration. A user's own computer software does not include computer software for which the right to access is transferred to the user with the digital infrastructure.

(ii) Prewritten computer software other than that required to allow the user to create, deploy, scale, or run the user's own computer software or that is incidental to providing the digital infrastructure is not considered digital infrastructure.

(iii) Example. Company A sells to a customer cloud-based service provided remotely, which includes data storage and a suite of development tools, which includes prewritten computer software that is required to allow the customer to create, deploy, scale, or run the customer's own computer software. No other prewritten computer software is provided as part of the transaction. The customer does not have to manage, operate, or maintain any hardware, software, networks, or facilities required to allow the data storage or the development tools to be used to create, deploy, scale, or run the customer's computer software. This transaction is a sale of digital infrastructure, which is excluded from the definition of a digital product.

(F) (1) A digital video game product, as defined in Revenue and Taxation Code section 6016.1, such as a digitally downloadable game playable on a video game console or on a computer for entertainment purposes, or a digital in-game purchase.

(2) A digital video game product created, developed, or designed with the intention of the product being used primarily for educational or training purposes is not considered a digital video game product for entertainment purposes.

(G) A digital visual work, as defined in Revenue and Taxation Code section 6016.1, such as computer-generated artwork.

(5) "Prewritten computer software" has the same meaning as defined in Revenue and Taxation Code section 6016.1.

(6) "Purchase" has the same meaning as defined in Revenue and Taxation Code section 6010.

(7) "Sale" has the same meaning as defined in Revenue and Taxation Code section 6006.

(8) "Tangible personal property" has the same meaning as defined in Revenue and Taxation Code section 6016.

(9) “Tangible storage media” has the same meaning as defined in Revenue and Taxation Code section 6016.2.

(10) “Transferred electronically” has the same meaning as defined in Revenue and Taxation Code section 6016.2.

(11) “Use” has the same meaning as defined in Revenue and Taxation Code section 6009.

(b) Application of Tax.

(1) Except as otherwise provided by the amendments made to the Sales and Use Tax Law (commencing with Revenue and Taxation Code section 6001) by Senate Bill No. 122 (Stats. 2026, ch. 23) and any implementing regulations, the rules applicable to the sale and purchase of, and the storage, use, or other consumption of tangible personal property as defined in subdivision (a)(1) of Revenue and Taxation Code section 6016, also apply to the sale or purchase of a digital product.

(2) The exclusions described in subdivision (a)(4) of this regulation do not apply when the product is transferred to the purchaser on tangible storage media.

(3) True Object Test. The true object test set forth in Regulation 1501 applies in determining whether a particular transaction involves a sale of a digital product or the transfer of a digital product incidental to the performance of a service.

When determining the true object of a transaction, a relevant factor includes, but is not limited to, the value of the digital product relative to the value of the service in the transaction.

Examples.

Example 1. Digital Infrastructure with Incidental Software. Company B sells to a customer cloud-based Infrastructure-as-a-Service (IaaS) that meets the definition of digital infrastructure, provided remotely, in the form of data storage and computational power that allows the customer to run the customer’s own computer software. The sale of the IaaS includes a transfer of the right to access prewritten computer software, which allows the customer to connect remotely to the data storage and computational power, to organize the data storage, to manage employee access to the data storage and computational power, and to monitor the remaining data storage and computational power capacity. The prewritten computer software that allows the customer to connect to, organize, manage access to, and monitor data storage and computational power capacity is considered incidental to the true object of the transaction, which is to purchase the IaaS. This transaction is not subject to tax.

Example 2. Digital Infrastructure with Non-Incidental Software. Company C enters into a contract for the sale of IaaS that meets the definition of digital infrastructure and Company C also transfers the right to access prewritten computer software. Company C’s IaaS is required to run the prewritten computer software. The value of the prewritten computer software represents a significantly larger portion of the total cost of the contract

than the value of the IaaS. The true object of the contract is the prewritten computer software. The charge for the entire contract is subject to tax.

(4) Maintenance Contracts.

(A) Mandatory Maintenance Contracts. The purchase of a maintenance contract is mandatory if the purchaser must purchase the maintenance contract in order to purchase or use a digital product.

Amounts charged by a retailer for mandatory maintenance contracts, including consultation charges provided in connection with a mandatory maintenance contract, are taxable as part of the sale or purchase of the digital product.

(B) Optional Maintenance Contracts. The purchase of a maintenance contract is optional if the purchaser is not required to purchase the maintenance contract in order to purchase or use a digital product.

If reasonable charges for services, such as repair, support, or consultation, are separately stated in an optional maintenance contract, the charges for such services are not subject to tax. Digital product updates or enhancements, such as updates or enhancements that add or improve functionalities in that digital product, transferred during the period of the optional maintenance contract, are taxable and are not considered repair, support, or consultation.

If charges for services, such as repair, support, or consultation, and taxable charges for updates or enhancements, are not separately stated and there is a single lump sum charge for the optional maintenance contract, and where the price of the optional maintenance contract does not exceed the price of the digital product to which the optional maintenance contract applies, 25 percent of the lump sum charge is considered to be for the sale of tangible personal property and tax applies to that amount; the remaining 75 percent of the lump sum charge is considered to be nontaxable.

(c) Determining Whether a Transfer of a Digital Product is Subject to Sales Tax or Use Tax.

(1) Notwithstanding Regulation 1600.1, or unless an exemption otherwise applies, the sales tax applies to retail sales of digital products transferred on tangible storage media, transferred electronically, or accessed remotely when the sale occurs in California and there is participation in the sale by a California place of business of the retailer.

A sale occurs in California when the place of sale, as determined by subdivision (d), is in California. Participation in the sale must involve some genuine physical human interaction with the sale from a California place of business of the retailer.

Example 1. A salesperson working out of a retailer’s place of business in California visits a purchaser in California and negotiates the sale of a digital product that is transferred electronically. The purchaser provides a billing address in California. Sales tax applies to this transaction because the place of sale is in California and there is participation in the sale by a California place of business of the retailer.

Example 2. A purchaser visits a retailer's store in California where the retailer is required to hold a seller's permit and purchases a digital product that is transferred electronically. Sales tax applies to this transaction because the place of sale is in California and there is participation in the sale by a California place of business of the retailer.

(2) When sales tax does not apply, use tax applies to the storage, use, or other consumption in this state of digital products transferred on tangible storage media, transferred electronically, or accessed remotely purchased from any retailer for storage, use, or other consumption in this state.

Example 3. A purchaser places an online order with a retailer located out-of-state for a digital product for use in California. Use tax applies to this transaction because there is no participation in the transaction by a California place of business of the retailer.

Example 4. A purchaser places an online order for a digital product for use in California from a retailer with multiple business locations in California for which the retailer is required to hold a seller's permit. The order is placed solely through the retailer's online store, and upon payment through a third-party online payment processing system, the digital product is delivered from a server in California, and the purchaser automatically receives via e-mail an electronic file to digitally download and access the digital product, which the purchaser does download and access from a location in California. Use tax applies to this transaction because there is no participation in the transaction by a California place of business of the retailer.

(d) Place of Sale. The place of sale or purchase of a digital product shall be determined as follows:

(1) For a digital product transferred on tangible storage media, the place of sale or purchase shall be the place the tangible storage media is physically located when the sale or purchase occurs.

(2) If the sale or purchase of a digital product that is not transferred on tangible storage media is an in-person sale or purchase at a location of the seller for which the seller is required to hold a seller's permit pursuant to Revenue and Taxation Code section 6066, the place of the sale or purchase of the digital product transferred electronically or accessed remotely shall be the seller's place of business in this state where the in-person sale or purchase occurs.

(3) If the sale or purchase of a digital product that is not transferred on tangible storage media is not an in-person sale or purchase, the place of the sale or purchase of a digital product transferred electronically or accessed remotely shall be deemed to be the purchaser's known address in this state shown in the seller's records maintained in good faith in the ordinary course of business, determined as follows:

(A) If a purchaser provides an address located in this state to the seller during the consummation of the sale or purchase of a digital product, then that in-state address provided shall be the purchaser's known address.

(B) If the purchaser only provides an out-of-state address to the seller during the consummation of the sale or purchase, and if the seller's records do not show that the purchaser provided the seller with an in-state address within the last 12 months, the purchaser's known address shall be the out-of-the state address.

(C) If the purchaser only provides an out-of-state address to the seller at the consummation of the sale or purchase, and if the seller's records show that purchaser provided the seller with an in-state address within the last 12 months, the seller shall obtain from the purchaser an exemption certificate as described in Regulation 1600.3. If the purchaser provides the exemption certificate, the out-of-state address shall be the purchaser's known address. Obtaining such exemption certificate from the purchaser shall be considered a reasonable effort by the seller to obtain accurate and complete information under Revenue and Taxation Code section 6054. If the purchaser does not provide the exemption certificate, the purchaser's known address shall be presumed to be the in-state address that was most recently provided by the purchaser within the last 12 months. If the purchaser provided more than one in-state address the known address shall be determined as provided in subparagraph (D).

(D) If the purchaser provides more than one address to the seller during the consummation of the sale or purchase, the purchaser's known address shall be determined from those addresses in this state in the following order of priority:

(i) The purchaser's billing address.

(ii) The purchaser's shipping or delivery address.

(iii) The mailing address associated with the purchaser's payment instrument.

(iv) The purchaser's mailing address.

(E) If the purchaser does not provide an address to the seller during the consummation of the sale or purchase, the purchaser's known address in this state shall be determined from the addresses in this state the purchaser previously provided to the seller in the following order of priority:

(i) The purchaser's most recent billing address.

(ii) The purchaser's most recent shipping or delivery address.

(iii) The purchaser's most recent mailing address associated with the purchaser's payment instrument.

(iv) The purchaser's most recent mailing address.

(F) If subparagraphs (A) through (E) do not apply, the place of the sale or purchase of a digital product transferred electronically or accessed remotely shall be deemed to be outside of this state.

(G) Examples.

Example 1. On June 1, 2027, Company A sells to Purchaser B a digital product transferred electronically that was not an in-person sale. Upon completing the order for the digital product, Purchaser B provides an Oregon billing address. Company A's records show that Purchaser B previously purchased a digital product from Company A on January 15, 2027, for which Purchaser B provided a California billing address. Company A requests an exemption certificate from Purchaser B but Purchaser B does not provide one. The place of sale for the June 1, 2027, transaction is the known California address provided by Purchaser B to Company A on January 15, 2027.

Example 2. On January 30, 2027, Company C sells to Purchaser D a digital product transferred electronically that was not an in-person sale. Upon completing the order for the digital product, Purchaser D provides both a Texas billing address and a Nevada delivery address. Company C's records show that Purchaser D previously purchased a digital product from Company C on December 1, 2026, for which Purchaser D provided a California billing address. Because Purchaser D provided more than one address during the consummation of the sale or purchase, but no known address in this state could be determined following the order of priority, the place of sale is deemed to be outside of this state.

(e) Place of Use.

(1) The place of use of a digital product shall be the address of the place or places where any right or power is exercised over the digital product. The right or power to remotely access a digital product is exercised at the place where the person accessing the digital product is located.

(2) Determination of Place of Use by a Seller with Obligation to Collect Use Tax. A seller with an obligation to collect use tax from a purchaser shall, upon sale or purchase of a digital product, make a reasonable effort to obtain accurate and complete address information from the purchaser to determine the place of use. A seller is considered to have made a reasonable effort when:

(A) The seller timely obtains from the purchaser written verification of the addresses of the place or places where the purchaser expects the first use of digital products to occur, and collects use tax on any digital product sold for use in this state; or

(B) If the seller is unable to timely obtain written verification from the purchaser, the seller shall collect use tax based on the purchaser's known address in this state as shown in the seller's records maintained in good faith in the ordinary course of business, as determined in subdivision (d)(3)(A) through (E) of this regulation. If subdivision (d)(3)(A) through (E) of this regulation do not apply, the place of use of a digital product transferred electronically or accessed remotely shall be deemed to be outside of this state.

(C) Written verification is timely obtained before the seller bills the purchaser for the digital product, any time within the seller's normal billing and payment cycle, or any time

at or prior to the digital product being transferred electronically or accessed remotely by the purchaser.

(3) It shall be presumed that a digital product that was purchased outside of this state, as determined pursuant to Revenue and Taxation Code section 6010.5, and used in this state within 90 days from the date of sale or purchase was purchased for storage, use, or other consumption in this state.

(f) Determination of When the Sale Occurs. Tax applies when the retail sale of the digital product occurs.

(1) With regards to sales of digital products transferred on tangible storage media, the rules applicable to sale and purchase of tangible personal property as defined in subdivision (a)(1) of Revenue and Taxation Code section 6016 apply to the determination of when the sale occurs.

(2)(A) When a digital product is transferred electronically or accessed remotely, beginning January 1, 2027, the sale occurs upon any permanent or temporary transfer of the right, in any manner or by any means whatsoever, to open, view, access, download, copy, update, possess, store, manipulate, or otherwise use a digital product, for consideration.

(B) Each transfer of a right, in any manner or by any means whatsoever, to open, view, access, download, copy, update, possess, store, manipulate, or otherwise use a digital product transferred electronically or accessed remotely for consideration is a separate sale. When the sale is subject to tax, the retailer shall report and pay the tax based upon the reporting period within which the transfer of a right is made.

(C) The determination of when a transfer of a right occurs is as follows:

(i) Upon the acceptance of a contract or agreement by the purchaser that grants the immediate right to open, view, access, download, copy, update, possess, store, manipulate, or otherwise use a digital product transferred electronically or accessed remotely for consideration, unless another date in the contract or agreement specifies when that right is granted. If the transfer of a right is subject to a condition, the transfer of the right occurs upon satisfaction of that condition.

(ii) If there is no contract or agreement, upon the completion of the electronic transfer of the digital product; if the digital product is not transferred electronically, upon the receipt of a digital code, password, or other means to access a digital product that resides on the vendor’s server or the server of a third party.

(D) The renewal, extension, or reinstatement of a right to open, view, access, download, copy, update, possess, store, manipulate, or otherwise use a digital product transferred electronically or accessed remotely for consideration beyond the period that the right was initially granted is a sale that occurs on the date the right is renewed, extended, or reinstated.

(E) The modification or expansion of a right to open, view, access, download, copy, update, possess, store, manipulate, or otherwise use a digital product transferred electronically or accessed remotely for consideration beyond the scope of the right that is initially granted is a sale.

(F) Examples. For the examples in this subparagraph, it is presumed that the digital product is transferred electronically or accessed remotely, and that the sale, purchase, or use occurs in California.

Example 1. On December 15, 2026, a purchaser pays consideration to a seller for a user license to access a digital product. However, the agreement specifies that the license is not effective until January 1, 2027. The transfer of the right to access the digital product occurs on January 1, 2027, and the sale is subject to sales or use tax.

Example 2. On December 15, 2026, a seller and purchaser enter into a contract to renew the purchaser's right to access a digital product, effective immediately, through December 14, 2029. The contract specifies that the purchaser may pay in full upon transfer, or the purchaser may enter into a financing agreement and pay monthly installments over three years. The transfer of the right to access the digital product occurs on December 15, 2026, and even if the purchaser pays in monthly installments after January 1, 2027, the sale is not subject to sales or use tax.

Example 3. Same as Example 2, but on November 1, 2029, the seller and purchaser enter into a new contract to renew the purchaser's right to access the digital product, effective December 16, 2029, for another three years. This is a new transfer of the right to access the digital product, which occurs on December 16, 2029, and that sale is subject to sales or use tax.

Example 4. On June 7, 2026, a purchaser pays a fee for the right to access a digital product for a one-month period. The agreement specifies that unless the purchaser cancels the agreement or ceases payment, the right to access the digital product for an additional month will be automatically renewed every 7th day of each subsequent month. The purchaser provides the retailer with the purchaser's credit card information, which is charged on the 7th day of every month until the purchaser cancels the agreement. A sale occurs every 7th day of the month when the right to access the product is renewed. Tax applies to the amounts charged for the right to access the digital product every monthly period beginning with the January 7, 2027, renewal date.

Example 5. On November 1, 2026, a seller and purchaser enter into a contract for the purchase of prewritten computer software that meets the definition of a digital product. The contract specifies that upon payment of the first 50 percent of the total cost of the contract, the seller will transfer to the purchaser the right to access a limited version of the prewritten computer software. It specifies that upon payment of the second 50 percent of the contract, the seller will transfer to the purchaser the right to access the full version of the prewritten computer software. The condition for a transfer of rights is satisfied when the purchaser pays 50 percent of the total cost on November 15, 2026, but the sale is not subject to tax. The condition for a transfer of rights is satisfied when the

purchaser pays the remaining 50 percent of the total cost on January 1, 2027, and that sale is subject to tax.

Example 6. On December 1, 2026, a seller and purchaser enter into a two-year usage-based contract for the license to use a digital product, and the transfer of the right to access is effective immediately and is continuous for the term of the contract. The contract specifies that the amount charged to the purchaser is based on their usage of the digital product in the preceding month, and the applicable rate charged is fixed until December 1, 2028. The purchaser will be invoiced on the first of the month following each month of use, so the January 1, 2027, invoice is based on the purchaser's usage of the digital product between December 1, 2026, through December 31, 2026. The payments made for the entire term of the contract are not subject to tax.

(g) Exemptions. Tax does not apply to the sale or purchase of:

(1) The right to reproduce or copy a digital product in order for copies of the digital product to be distributed for consideration to third parties, even if a copy of the digital product is transferred concurrently with the granting of that right. Any tangible storage media on which the digital product is transferred is merely incidental.

(2) A digital product purchased solely for use outside of this state or in interstate or foreign commerce, pursuant to Regulation 1600.3.

(3) (A) A digital product that represents a service provided in electronic form in which both of the following apply:

(i) The service primarily involves the application of human effort by the service provider.

(ii) The human effort described in subclause (i) originated after the customer requested the service.

(B) This exemption does not apply to the sale or purchase of the right to use the provider's computer software running on a cloud infrastructure or the right to access that software from various client devices through digital means, such as a thin client interface, including a web browser, or a program interface.

(C) Examples.

Example 1. Company A sells personal training sessions, which can be booked through Company A's software application, which shows the available dates and times for specific personal trainers. Customers can have a remote video session with the booked personal trainer on Company A's software application. This service primarily involves the application of human effort by the personal trainer and originates after the customer requested the personal training service. The sale and purchase of the personal training sessions from Company A are exempt from sales and use tax.

Example 2. Company B sells the right to use tax return preparation software remotely accessed by the purchaser or the purchaser's employees through an internet web browser. The tax return preparation software includes a "chat with an agent" option that connects the user to an employee of the Company B, who can explain general features of the tax return preparation software. The exemption does not apply to this sale of the right for the purchaser and the purchaser's employees to access the seller's tax return preparation software. The "chat with an agent" option is incidental to the true object of the contract, which is the tax return preparation software. The sale is subject to sales or use tax.

(h) Operative Date. This regulation is operative as of January 1, 2027.

NOTE: Authority cited: Sections 15570.22 and 15570.24, Government Code; Statutes 2026, chapter 23 (Sen. Bill No. 122), Section 34; and Section 7051, Revenue and Taxation Code. Reference: Sections 6006, 6009, 6009.5, 6010, 6010.5, 6010.5.1, 6010.9, 6016, 6016.1, 6016.2, 6054, 6362.4, 6372 and 6372.1, Revenue and Taxation Code.