California SB 122: Preparing for SaaS Sales Tax in 2027

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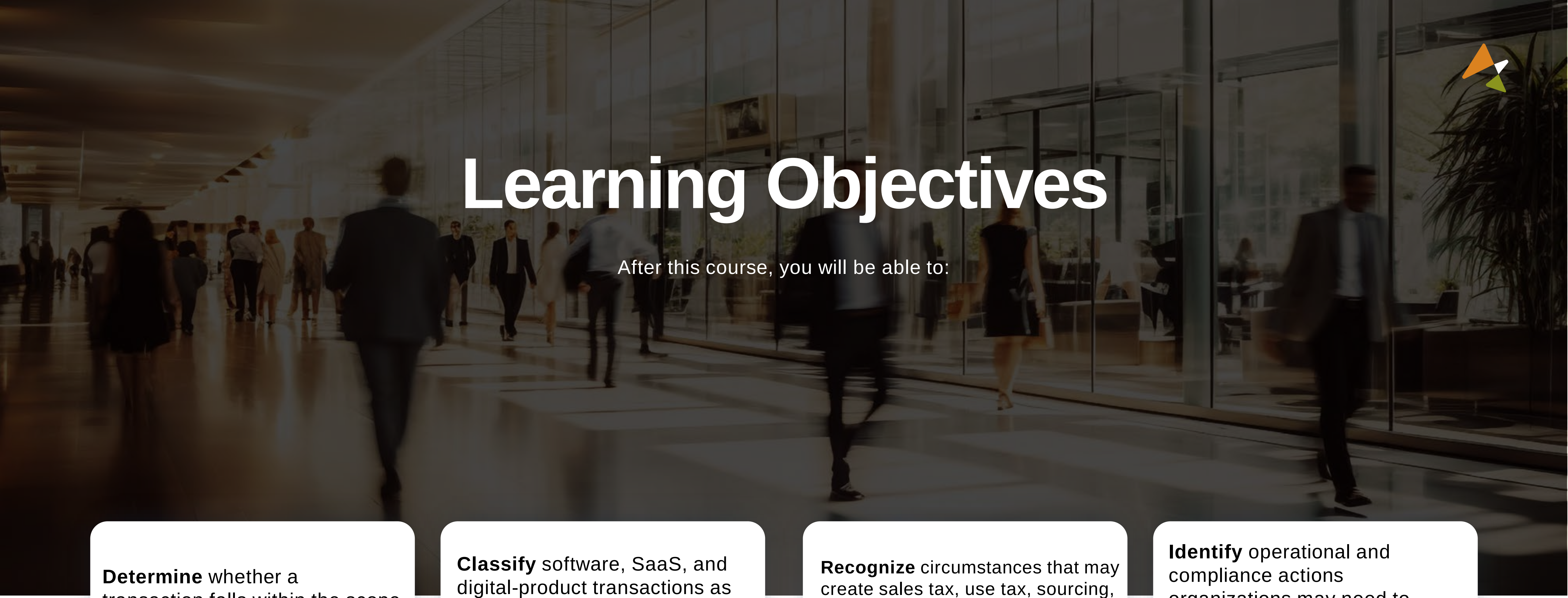

Learning Objectives

After this course, you will be able to:

Determine whether a transaction falls within the scope of California SB 122.

Classify software, SaaS, and digital-product transactions as taxable, excluded, or potential exempt.

Recognize circumstances that may create sales tax, use tax, sourcing, or nexus considerations under SB 122.

Identify operational and compliance actions organizations may need to address before the January 1, 2027 effective date.

WEBINAR

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Why This Matters

- Why California enacted SB 122
- Effective date and implementation timeline
- Why organizations should start planning before year-end

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SB 122 Timeline

- **June 29, 2026**
  Governor Newsom signs SB 122 into law
- **July 21, 2026**
  First CDTFA interested parties workgroup
- **September 1, 2026**
  CDTFA issues draft emergency regulations
- **September 10, 2026**
  Second CDTFA interested parties meeting
- **January 1, 2027**
  Tax on digital products takes effect

What Is Now Taxable (as of 1/1/2027)

- “Tangible personal property” now includes “[a] digital product and any copyright or patent interests associated therewith.” (RTC § 6016(2))
- “Digital product” means “prewritten computer software transferred on tangible storage media, transferred electronically, or accessed remotely.” (RTC § 6016.1(a))
- “Accessed remotely” means software accessed for consideration by code, password, or other means “that resides on the vendor’s server or the server of a third party.” (RTC § 6016.2)
- A taxable sale includes “any permanent or temporary transfer of the right … to open, view, access, download, copy, update, possess, store, manipulate, or otherwise use a digital product.” (RTC §§ 6006(i), 6010(g))
- SaaS called out by name: a digital product “includes, but is not limited to, prewritten software transferred to or accessed remotely by, Software as a Service (SaaS), a computer and other computer applications.” (Draft Reg. 1600(a)(6))

TAXABLE UNDER SB 122

What's In

Prewritten software accessed remotely as SaaS

Electronically delivered software — downloads and access keys

Licenses, subscriptions, and renewals

Add-ons, modules, and upgrades tied to software use

Bundled software plus services arrangements

POLL 2: READINESS

Polling Question #2

What's Out - Not a "Digital Product"

- Digital infrastructure
  - Draft Reg. 1600(a) excludes "cloud-based Infrastructure as a Service (IaaS) and Platform as a Service (PaaS) that allow customers to create, deploy, or run their own software application."
  - RTC § 6016.1(c)(8) defines it 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."
  - The statute adds a condition: the service must do this "without managing, operating, or maintaining the user's own infrastructure," including hardware, software, networks, and facilities.
- Digital books
- Digital audio and audiovisual works
- Digital video game products and digital visual works

What's Out - Statutory Exemptions

- Human effort exemption — RTC § 6372.1
  - Exempts a digital product "that represents a service provided in electronic form" where "the service primarily involves the application of human effort by the service provider."
  - Timing matters: "the human effort originated after the customer requested the service."
  - The catch (§ 6372.1(b)): if the customer is really buying access to your software — cloud-hosted, reached by browser or API — the exemption is off, even when people are involved.
    - *Statute: the 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 either a thin client interface, including a web browser, or a program interface."*
- Right to reproduce or copy a digital product for distribution to third parties (RTC § 6362.4)
- Digital products bought solely for use outside California or in interstate or foreign commerce (RTC § 6372)
- Custom computer software (RTC § 6010.9; proposed Reg. 1502.2)

The $5 Million Threshold

- Retailer relief at $5 million — RTC § 6052 (proposed Reg. 1600.1)
  - Once digital-product gross receipts to one purchaser exceed $5,000,000 in a calendar year, the retailer is relieved of sales tax liability on sales to that purchaser.
  - From 2028 the test looks to the current or preceding calendar year; CPI-adjusted from October 2031.
  - Insurers are excluded.
- Liability flips to the purchaser
  - The purchaser self-assesses and remits use tax on those purchases (RTC § 6201.55).
  - To do so, the purchaser must hold a use tax direct payment permit or obtain a CDTFA waiver.

When the Vendor Doesn’t Collect

- **Sales tax is the vendor’s liability — use tax is yours**
  - If the vendor charges tax and you have the receipt, you are done. If it never turns tax on, the liability does not disappear — it moves to you (RTC § 6201.55).
- **Below the $5 million threshold**
  - The retailer is supposed to collect. If it does not — unregistered vendor, or it treats the product as exempt — you must self-assess use tax.
  - A use tax direct payment permit is not available at this level; that route is tied to the threshold.
- **Above the $5 million threshold**
  - The retailer is relieved of liability, so you self-assess and remit regardless of what the invoice shows.
- **In Practice:** review SaaS and digital invoices for uncollected tax and accrue where it is missing — vendor misclassification becomes your audit exposure.

Multiple Points of Use

- **The problem: one license, users in several states**
  - You buy once, but the team uses it inside and outside California, so taxing the full price here overstates California’s share.
- **The fix: an MPU certificate (proposed Reg. 1600.2)**
  - You give the seller a certificate saying the product will be used in more than one state, and the seller collects tax only on the California share.
  - The certificate protects the seller — you own the allocation and the records behind it.
  - CDTFA has already blessed the basis: Reg. 1600.2 defines “computer,” “multiple points of use,” and “user,” so allocating by user or computer location is an accepted method.
- **Where the statute allows it — RTC § 6372(e)**
  - Permitted for licenses “concurrently available for use in multiple locations” — but you give up the § 6406 credit.
- Sourcing underneath it all (§ 6010.5.1): for remote access, use occurs where the user sits.

WHAT TO DO NOW

Planning Ahead

- Inventory your offerings — software accessed remotely vs. services
- Review contracts and pricing — unbundle software from services
- Map where customers use the product — it drives sourcing
- Ready your systems — billing, tax engine, and exemption certificates
- Register and build the compliance calendar before January 1, 2027
- Model the impact on margins and pricing
- Comment on the draft regulations while they are still open
- Assign ownership across tax, finance, legal, and product

Contracts Signed Before 1/1/2027

- What controls is when access transfers — not signing or payment (Draft Reg. 1600(f)(2)(A))
- Illustrative examples from CDTFA (Draft Reg. 1600(f)(2)(C))
  - Not taxable — Example 3: product transferred electronically on December 15, 2026 with immediate access; payment arrives January 1, 2027. The sale is not subject to sales or use tax.
  - Not taxable — Example 5: a December 15, 2026 sale financed over 12 months with immediate access. The sale “occurs on December 15, 2026, and is not subject to sales or use tax, regardless of the time payment is received.”
  - Taxable — Examples 1 and 2: a December 2026 contract where access starts January 1, 2027
  - Subscriptions split by period: “Tax does not apply to payments received for subscription periods prior to January 1, 2027. Tax applies to payments received for subscription periods on or after January 1, 2027.”
  - Example 4: a December 2026 monthly subscription is taxed only on the 2027 months
- Planning point: switching on access before January 1, 2027 is what preserves nontaxable treatment

Parting Thoughts

- **Start the conversation now**; document positions
- **Revisit your footprint** — SB 122 moves the line
- A **nexus study is the easiest place to start** — we can run one with you
  - Economic nexus from newly taxable receipts
  - Where users sit, not where contracts are signed
  - Registration status in every state you serve
- Other states will follow California

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