

TENNESSEE DEPARTMENT OF REVENUE  
REVENUE RULING # 20-03

**Revenue rulings are not binding on the Department. This ruling is based on the particular facts and circumstances presented and is an interpretation of the law at a specific point in time. The law may have changed since this ruling was issued, possibly rendering it obsolete. The presentation of this ruling in a redacted form is provided solely for informational purposes and is not intended as a statement of Departmental policy. Taxpayers should consult with a tax professional before relying on any aspect of this ruling.**

**SUBJECT**

The application of the Tennessee sales and use tax to on-hold messaging services, VideoCast programming services, and overhead music services.

**SCOPE**

Revenue Rulings are statements regarding the substantive application of law and statements of procedure that affect the rights and duties of taxpayers and other members of the public. Revenue Rulings are advisory in nature and are not binding on the Department.

**FACTS**

The Taxpayer is a Delaware corporation engaged in the business of selling customized On-Hold Messaging ("OHM") Services, VideoCast Programming ("VCP") Services, and Overhead Music Services. The Taxpayer describes its business as providing "custom marketing and sales solicitation services by promoting additional products and services offered by its customers." The Taxpayer's specific revenue streams and billing methods are discussed in more detail below.

*On-Hold Messaging Services*

The Taxpayer provides custom marketing messaging services for customers' telephone systems. To the extent the Taxpayer's customers' callers are interested in additional information about a certain product or service, the OHM Services allow the customers' systems to direct call traffic to customers' sales departments.

The charge for OHM Services includes the production of customized recorded messages, including script (advertising/marketing/copyrighting), consultation services, any music licensing fees the Taxpayer incurs in production of the messaging, and professional talent options the Taxpayer uses to produce the messages. The customer is provided, via electronic delivery, an audio commercial message similar to a commercial aired by a radio station. Customers also have access to custom messages previously provided to them during the contract period.

A typical contract includes a set number of custom messages per month, consisting of written script with up to [REDACTED] messages totaling approximately [NUMBER OF] words and the associated recorded voice and/or music material. All written and recorded material remains the property of the Taxpayer and may not be used by a customer beyond the expiration date of the agreement. The

customer agrees not to retransmit, reproduce, or duplicate in any manner the productions provided by the Taxpayer.

The Taxpayer may provide equipment<sup>1</sup> necessary for its customers to utilize the Taxpayer's audio messages. Such equipment is invoiced as a separate line item reflecting no charge. Title to the equipment remains with the Taxpayer. Customers are prohibited from altering, tampering with, or disassembling the equipment. Customers also are prohibited from using the equipment beyond the expiration date of the agreement and must return the equipment to the Taxpayer within 30 days from the end of the agreement. If a customer fails to return the equipment, the Taxpayer charges the customer a [AMOUNT] fee.

The Taxpayer provides its OHM Service through one of five packages based on customer site types as described below:

- Primary Site: This facility will have its own entirely custom program which can include new custom audio productions each month.
- Custom Specific Site: This facility will generally have the same custom monthly content that is selected for the Primary site, but will receive static, customized facility-specific messages in place of those heard at the Primary site.
- Duplicate Site: This facility will have an exact duplicate program of what is selected for the Primary site.
- Modified Primary Site: This facility will have a new program each month with messages that all Modified Primary sites must use and custom messages specific to the individual site.
- Primary Bi-Monthly Site: This facility will have its own entirely custom program. The service includes a new, professionally produced custom program every other month.

In addition to purchasing one of the five packages, customers may order separately-stated additional services such as Spanish language programming; pre-recorded radio ad audio conversion, which requires editing/re-recording; on-site interview sessions, which include audit introduction and wrap by a professional voice; and voice prompts, which include professional writing, voice over, wraps and production.

#### *VideoCast Programming Services*

The Taxpayer provides customized VCP Services to the customer's location. The VCP Service allows custom promotional content to be played on video screens at the customer's location. In addition to custom promotional content, the customer may also purchase generic content such as weather feeds, news feeds, and/or a stock market ticker feed. A menu board or other content, such as the status of an order, may also be displayed. All content is generally delivered electronically.

The VCP Service requires a Digital Signage Media Player that the Taxpayer provides to the customer. The Digital Signage Media Player is invoiced as a separate line item reflecting no charge. The customer may use its own TV monitors and equipment to display the content or may purchase these items from the Taxpayer.

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<sup>1</sup> The sample contract provided indicates the equipment is [REDACTED].

Charges for VCP Services include the following services involved in producing the custom video content:

- Development of initial custom layout and design
- Production of elements and motion segments
- Access to historical static and video content
- Remotely managed content updates
- A set number of hours monthly for custom digital creative updates
- Portal access for each location, which offers the ability for local content updates
- Weather feeds, news feeds and stock ticker feeds (these are optional and are only included in the charges when provided)

The custom video content is licensed to the Taxpayer's customers as a non-exclusive, non-transferrable, non-assignable, limited license in the content for the term of the agreement. Customers agree not to make copies of the content in any format, not to create derivative works from the content or make any changes to the content, and not to use the content at any other location, trade show or marketing event. The content is the Taxpayer's copyrighted, proprietary information and is protected by applicable copyright laws, and all rights to license, market, or otherwise develop or dispose of the content are the exclusive property of the Taxpayer.

Additionally, the invoice states that any Digital Signage Media Players provided as part of the services will remain the property of the Taxpayer and customers may not sell, dispose of, or otherwise encumber these items. Any television monitors or mounting equipment purchased by a customer will remain the customer's property.

#### *Overhead Music Services*

The Taxpayer provides pre-programmed channels of advertising-free music in a variety of genres. The Taxpayer's Overhead Music Services are generally provided by third-party producers. Such music is licensed by the Taxpayer and subsequently licensed to the Taxpayer's customers for a fee. Customers are not permitted to record, modify, edit, reproduce, transmit or alter any licensed music.

As an additional service and for an additional fee, customers may choose to have customer-specific promotional messages (the "promotional messages") inserted into the music playlist. The promotional messages direct shoppers to a current sale item or remind them about seasonal specials. Approximately 60%-70% of the Taxpayer's customers purchase this additional service. All written and recorded material provided as part of the additional service remains the property of the Taxpayer and may not be used by customers beyond the expiration date of the agreement. Customers agree not to retransmit, reproduce, or duplicate in any manner the promotional messages provided by the Taxpayer.

The Taxpayer usually sells overhead music equipment to customers in order to facilitate its Overhead Music Services. However, the Taxpayer may, on occasion, provide equipment to customers at no charge.

For all three services, the Taxpayer may charge customers a service activation fee that includes labor and materials for the installation and configuration of any necessary equipment. If a site survey is necessary, the Taxpayer will perform one for an additional fee.

The Taxpayer separately itemizes all fees on its invoices. The Taxpayer acknowledges that all charges for the provision of tangible equipment and the installation and configuration of such equipment for all three services, including charges for site surveys and service activation fees, are subject to Tennessee sales and use tax.<sup>2</sup>

## RULINGS

1. Are the Taxpayer's OHM Services subject to Tennessee sales and use tax?

Ruling: Yes, the Taxpayer's OHM Services are subject to Tennessee sales and use tax under TENN. CODE ANN. § 67-6-233 (2018).

2. Are the Taxpayer's VCP Services subject to Tennessee sales and use tax?

Ruling: Yes, the Taxpayer's VCP Services are subject to Tennessee sales and use tax under TENN. CODE ANN. § 67-6-233. However, the optional weather feeds, news feeds, and stock ticker feeds that may be sold with the VCP Services are exempt information services under TENN. CODE ANN. § 67-6-233(d).

3. Are the Taxpayer's Overhead Music Services subject to Tennessee sales and use tax?

Ruling: Yes, the Taxpayer's Overhead Music Services are subject to Tennessee sales and use tax under TENN. CODE ANN. § 67-6-233.

4. Is the Taxpayer required to pay Tennessee use tax on the equipment it provides to Tennessee customers for no charge?

Ruling: Yes. When the Taxpayer provides equipment to its Tennessee customers at no cost, the Taxpayer is using the equipment to transfer specified digital products and is subject to Tennessee use tax on the equipment.

## ANALYSIS

Under the Retailers' Sales Tax Act (the "Act"),<sup>3</sup> retail sales of tangible personal property and specifically enumerated services<sup>4</sup> are subject to the sales tax, unless an exemption applies. The term "sale" includes "the furnishing of any of the things or services" taxable under the Act.<sup>5</sup> One of the "things"

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<sup>2</sup> This includes the [AMOUNT] fee charged for equipment provided to OHM Service customers that is not returned. The Taxpayer is not currently collecting and remitting Tennessee sales and use tax; it must do so. TENN. CODE ANN. § 67-6-501 places the liability for sales tax on the dealer selling tangible personal property. While the dealer may charge the consumer the appropriate tax, as between the dealer and the consumer, it is the dealer that is ultimately liable to the state. *Sam Carey Lumber Co. v. Sixty-One Cabinet Shop, Inc.*, 773 S.W.2d 252 (Tenn. Ct. App. 1989). The Taxpayer cannot transfer this responsibility to its customers by contract or otherwise. Thus, the Taxpayer must register for sales and use tax and may do so through the Department's Tennessee Taxpayer Access Point ("TNTAP") at: <https://tntap.tn.gov/eservices/>.

<sup>3</sup> Tennessee Retailers' Sales Tax Act, ch. 3, §§ 1-18, 1947 Tenn. Pub. Acts 22, 22-54 (codified as amended at TENN. CODE ANN. §§ 67-6-101 to -907 (2018)).

<sup>4</sup> TENN. CODE ANN. § 67-6-205 (Supp. 2019) (listing services subject to tax).

<sup>5</sup> TENN. CODE ANN. § 67-6-102(78)(C) (Supp. 2019).

specifically taxable under the Act is the “retail sale, lease, licensing or use of specified digital products transferred to or accessed by subscribers or consumers” in Tennessee.<sup>6</sup> Specified digital products include “electronically transferred digital audio-visual works, digital audio works and digital books.”<sup>7</sup>

The transactions at issue involve multiple components, some of which are not subject to tax. When a sale consists of taxable and nontaxable components, the transaction’s true object or its crucial,<sup>8</sup> “essential,”<sup>9</sup> “necessary,”<sup>10</sup> “consequential,”<sup>11</sup> or “integral”<sup>12</sup> element determines its taxability.<sup>13</sup> If the true object of the transaction is not independently subject to sales tax and the taxable components are “merely incidental” to the true object of the transaction, the transaction is not subject to sales tax.<sup>14</sup> However, if the true object is taxable, the entire transaction is taxable. If the transaction is taxable, the tax base is its “sales price” or “purchase price,” which is defined to include the total amount of consideration for which property or services are sold.<sup>15</sup>

### **ON-HOLD MESSAGING SERVICES**

The customized recorded messages licensed for use under the Taxpayer’s OHM Services are specified digital products. As such, the Taxpayer’s OHM Services, including the separately stated additional services, are subject to the Tennessee sales and use tax under TENN. CODE ANN. § 67-6-233.<sup>16</sup>

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<sup>6</sup> TENN. CODE ANN. § 67-6-233(a) (2018).

<sup>7</sup> TENN. CODE ANN. § 67-6-102(27), (28), (29), and (86) (defining the types of specified digital products).

<sup>8</sup>See, e.g., *Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621, 624 (Tenn. 1987) (holding that a transaction involving the sale of non-taxable intangible advertising concepts was nevertheless subject to sales tax on the entire amount of the transaction because advertising models, which were tangible personal property, were an “essential,” “crucial,” and “necessary” element of the transaction).

<sup>9</sup>*Id.*; see also *AT&T Corp. v. Johnson*, No. M2000-01407-COA-R3-CV, 2002 WL 31247083, at \*8 (Tenn. Ct. App. Oct. 8, 2002) (holding that a transaction involving the sale of engineering services along with separately itemized tangible telecommunications systems was subject to sales tax on the entire amount of the contract because “equipment, engineering, and installation combine in this instance to produce BellSouth’s desired result: a functioning item of tangible personal property assembled on the customer’s premises,” and further describing the engineering services as “essential” and “integral” to the sale of tangible personal property).

<sup>10</sup> See *supra* note 8.

<sup>11</sup> See *Rivergate Toyota, Inc. v. Huddleston*, No. 01A01-9602-CH-00053, 1998 WL 83720, at \*4 (Tenn. Ct. App. Feb. 27, 1998) (holding that a transaction involving the commission and distribution of advertising brochures was subject to sales tax on the “entire cost of the transaction” because, although the transaction involved a number of services, the brochures themselves “were not inconsequential elements of the transaction but, in fact, were the sole purpose of the contract”).

<sup>12</sup> See *AT&T Corp. v. Johnson*, 2002 WL 31247083, at \*8.

<sup>13</sup> See generally Tenn. Dept. of Rev. Ltr. Rul. 14-10 (Oct. 14, 2014) (discussing Tennessee law regarding bundling and the “true object” test), available at <https://www.tn.gov/content/dam/tn/revenue/documents/rulings/sales/14-10.pdf>.

<sup>14</sup> See generally *id.*

<sup>15</sup> TENN. CODE ANN. § 67-6-102(72) and (79)(A).

<sup>16</sup> See also TENN. CODE ANN. 67-6-102(86).

OHM Services are sold with rights of less than permanent use to the recorded messages and such rights are conditioned upon continued payment by the customer. The contract for the OHM Services provides that all written and recorded material remains the property of the Taxpayer and may not be used by the customer beyond the expiration date of the agreement. The customer agrees not to retransmit, reproduce, or duplicate in any manner the productions provided by the Taxpayer. A taxable retail sale includes the sale of an audio digital work with rights of less than permanent use.<sup>17</sup> The customized recorded messages are digital audio works, which are a type of specified digital product, and the customer's purchase constitutes a taxable retail sale as described in TENN. CODE ANN. § 67-6-233(b)(1)-(3).

OHM Services also include a sales and marketing aspect. Advertising services are not among those services listed as taxable in Tennessee.<sup>18</sup> While advertising services are not subject to tax, final artwork sold by an advertising agency to a customer pursuant to an agreement for advertising services is subject to sales tax. The sales price of the final artwork, however, does not include fees paid for advertising services.<sup>19</sup>

The Taxpayer has not provided facts that support that it is an advertising agency as defined in TENN. CODE ANN. § 67-6-102(1), nor do its contracts appear to be for advertising services. Under TENN. CODE ANN. § 67-6-102(3)(B), advertising services do not include the production of final artwork or advertising materials.<sup>20</sup> While advertising materials are subject to tax, they are defined to exclude "original sound recordings produced by recording studios, television studios, video production studios or by or for advertising agencies, or masters produced from the original recordings, regardless of whether the original recordings or masters are produced in a tangible medium or a digital equivalent."<sup>21</sup> The Taxpayer's facts do not suggest that these services are included in its sales. In summary, the Taxpayer's facts do not support a finding that the crucial element of the transaction is advertising services. Instead, the Taxpayer's facts and contracts support a conclusion that the true object of the sale is the recorded messages, which are subject to Tennessee sales and use tax as described above.

Although other separately-stated additional services are available under the OHM Service, some of which may not be otherwise subject to tax, all of the additional services are a part of or are further customization of the customized recorded messages (e.g. Spanish language programming, radio ad audio conversion, voice prompts, professional writing, etc.). Without being able to obtain the customized recorded messages, none of the other service offerings would be of any value to the customer. These services, therefore, are part of the sales of the digital audio work (the customized recorded messages) and subject to tax under the definition of "sales price".<sup>22</sup> Consequently, charges

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<sup>17</sup> TENN. CODE ANN. § 67-6-233(a) and (b)(1)-(3) (stating that the "retail sale, lease, licensing or use of specified digital products transferred to or accessed by subscribers or consumers" in Tennessee is subject to sales and use tax and include: "[s]pecified digital products sold with rights of less than permanent use; [s]pecified digital products sold with rights of use conditioned upon continued payment by the subscriber or purchaser; and [s]ubscriptions to, access to or the purchase of a digital code for receiving or accessing specified digital products." Emphasis added.)

<sup>18</sup> TENN. CODE ANN. § 67-6-205.

<sup>19</sup> See TENN. CODE ANN. § 67-6-312(b) (2018).

<sup>20</sup> Advertising materials are specifically subject to Tennessee sales and use tax pursuant to Tenn. Code Ann. § 67-6-312(c) (2018).

<sup>21</sup> TENN. CODE ANN. § 67-6-102(2).

<sup>22</sup> TENN. CODE ANN. § 67-6-102(79)(A)(iii).

for the Taxpayer's OHM Service are subject to the sales and use tax under TENN. CODE ANN. § 67-6-233 as the licensing for use of specified digital products.

### **VIDEOCAST PROGRAMMING SERVICES**

The VCP Service allows custom promotional content and generic feeds to be played on video screens at the customer's location. The custom video content licensed for use under this service is a specified digital product. As explained in the previous section, specified digital products are subject to tax under TENN. CODE ANN. § 67-6-233. However, as explained below, the optional weather feeds, news feeds, and stock ticker feeds are exempt information services.<sup>23</sup>

Sales of specified digital products are subject to Tennessee's sales and use tax. Here, the Taxpayer's customers pay a fee in exchange for the custom video content. The custom video content is a digital audio-visual work, which is a type of specified digital product as defined by statute. The sale, lease, or licensing of audio-visual works is subject to tax as set forth in TENN. CODE ANN. § 67-6-233(b)(1)-(3).<sup>24</sup>

Although there are itemized charges for the VCP Services, some of which may not otherwise be subject to sales and use tax, all of the itemized charges except the charges for weather feeds, news feeds, and stock ticker feeds are a part of or are additional customization of the custom video content (e.g., custom layout and design, production of elements and motion segments, access to historical video content, managing updates, custom digital creative updates, etc.). Without being able to obtain the customized video content, none of the itemized VCP Service charges would be of any value to the customer. These services, therefore, are included in the sales price of the digital audio-visual work and subject to tax.<sup>25</sup> Other than the exception described below, charges for the Taxpayer's VCP Services are subject to sales and use tax under TENN. CODE ANN. § 67-6-233 as the sale of access to specified digital products.

Information services are exempt under TENN. CODE ANN. § 67-6-233(d), which excludes certain items from tax, including "subscriptions to data processing and information services that allow data to be generated, acquired, stored, processed or retrieved and delivered by electronic transmission to a purchaser." Information services include weather feeds, news feeds, and stock ticker feeds. The Taxpayer's customers purchase the weather feeds, news feeds, and stock ticker feeds for the information contained therein. Accordingly, if the Taxpayer separately states the charges for the weather feeds, news feeds, and stock ticker feeds, the charges for these information services will not be subject to sales and use tax.

### **OVERHEAD MUSIC SERVICES**

Customers purchasing the Overhead Music Services pay a monthly fee in exchange for the pre-programmed advertising-free music, which may consist of only music or may include optional promotional messages. The licensing terms are the same as the licensing arrangements for the

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<sup>23</sup> TENN. CODE ANN. § 67-6-233(d).

<sup>24</sup> Consistent with the analysis of the customer audio messaging, the true object of the VPC Service is the digital audio-visual work.

<sup>25</sup> TENN. CODE ANN. § 67-6-102(79)(A)(iii).

products described above. The pre-programmed advertising-free music, including, if any, promotional messages licensed for use under this service offering also falls within the definition of a “specified digital product” as a “digital audio work.”<sup>26</sup> Like the previously discussed services, the Taxpayer’s Overhead Music Services are subject to the sales and use tax under TENN. CODE ANN. § 67-6-233.

The purchase of the Overhead Music Services, alone, or including the optional promotional messages, constitutes a retail sale of a specified digital product. Although there are other itemized charges such as activation fees or site survey fees, some of which may not be otherwise subject to Tennessee sales and use tax, those additional charges are for services that are part of the sale of the Overhead Music Services. These services have no value to the customer without the music and optional promotional messages. Under these facts, charges for these services are part of the sale of the digital audio work.<sup>27</sup> Accordingly, charges for the Taxpayer’s Overhead Music Services and optional promotional messages are subject to the sales and use tax as sales of access to specified digital products.<sup>28</sup>

### **APPLICABILITY OF USE TAX**

Tennessee imposes a sales tax on retail sales of tangible personal property.<sup>29</sup> Tennessee also imposes a use tax on the purchase price of each item of tangible personal property “when the same is not sold but is used, consumed, distributed, or stored for use or consumption in this state.”<sup>30</sup> The tax is paid by the person who “uses” the property in Tennessee. In this context, “use” is defined as “the exercise of any right or power over tangible personal property incident to the ownership thereof.”<sup>31</sup>

The Taxpayer stated that it may provide equipment to customers at no charge. In such circumstances, the Taxpayer is using tangible personal property to transfer specified digital products to its customers. Accordingly, the Taxpayer is the user and consumer of the equipment provided at no charge to its Tennessee customers and is liable for use tax on these items.

APPROVED: David Gerregano  
Commissioner of Revenue

DATE: 5/4/2020

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<sup>26</sup> TENN. CODE ANN. § 67-6-102(27) and (86).

<sup>27</sup> TENN. CODE ANN. § 67-6-102(79)(A)(iii).

<sup>28</sup> TENN. CODE ANN. § 67-6-233.

<sup>29</sup> TENN. CODE ANN. § 67-6-202(a) (2018).

<sup>30</sup> TENN. CODE ANN. § 67-6-203(a) (2018).

<sup>31</sup> TENN. CODE ANN. § 67-6-102(94)(A).