

# Kentucky to Begin Taxing Video Streaming Services under Telecom Tax

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Legislators in Frankfort added a new “video streaming service” tax to the omnibus tax bill (HB 354) as part of a closed-door conference committee process before the bill was hastily passed in the House and Senate. Notably, the new video streaming service tax was not previously raised or discussed as part of HB 354 (or any other Kentucky legislation) before it was included in the final conference committee report that passed the General Assembly in March.

Specifically, as passed by the General Assembly, HB 354 will add “video streaming services” to the definition of “multichannel video programming service” subject to the telecom excise tax. This is the same tax imposition that the Department of Revenue argued applied to video streaming services in the *Netflix* litigation—an argument that was rejected by the courts in Kentucky and then subsequently settled on appeal. Under existing law, Kentucky taxes “digital property” under the sales and use tax. The term is broadly defined and applies to audio streaming services, but expressly carves out “digital audio-visual works” (*i.e.*, downloaded movies, TV shows and video; defined consistently with the SSUTA) from the scope of the sales and use tax imposition. HB 354 would not modify the treatment of digital goods and services under the sales and use tax, and changes that would be implemented are limited to the telecom excise tax imposed on the retail purchase of a multichannel video programming service.

As amended by HB 354, the definition of “multichannel video programming service” for purposes of the telecom excise tax would be expanded to mean “live, scheduled, or on-demand programming provided by or generally considered comparable to or in competition with programming provided by a television broadcast station and shall include but not be limited to: (a) Cable service; (b) Satellite broadcast and wireless cable service; and (c) Internet protocol television provided through wireline facilities without regard to delivery technology; and (d) video streaming services.” The legislation defines “video streaming services” as “programming that streams live events, movies, syndicated and television programming, or other audio-visual content over the Internet for viewing on a television or other electronic device with or without regard to a particular viewing schedule.” Thus, the “video streaming services” language in HB 354 would clearly subject over-the-top video streaming service

providers to the excise tax on the retail purchase of a multichannel video programming service. As passed by the General Assembly, the new video streaming services excise tax in HB 354 would “apply to transactions occurring on or after July 1, 2019.”

Governor Matt Bevin signed HB 354 into law on March 26, 2019. The General Assembly subsequently passed a “cleanup bill” (HB 458) that was enacted into law last month, but it did not make any changes to the part of HB 354 that expanded the scope of the tax on multichannel video programming services to include video streaming services.

Kentucky is a member of the Streamlined Sales and Use Tax Governing Board. Taxation of electronically transferred audio-visual works is something specifically dealt with in the Streamlined Sales and Use Tax Agreement (SSUTA). The SSUTA also prohibit the enactment of so-called “replacement taxes” that have the effect of avoiding the provisions of the SSUTA. Kentucky’s inclusion of streamed movies in its tax on multichannel video programming services, a regime outside the sales and use tax, could run afoul of the SSUTA’s prohibition on replacement taxes, potentially putting the state out of compliance with the SSUTA and exposing it to the risk of sanctions by the Governing Board.

**Practice Note:** From an administrability and compliance point of view, enacting a new tax on digital goods and services as part of excise or gross receipts taxes outside the generally applicable sales and use tax poses significant problems. Many businesses that are not telecom providers simply do not have the compliance infrastructure to allow them to collect and remit taxes other than sales and use taxes. In addition, by taxing certain digital goods and services under a tax other than what is applicable to similar content sold via a tangible medium (such as a physical movie rental or viewing a movie in theater), the federal Permanent Internet Tax Freedom Act enacted by Congress may be implicated and pose a litigation risk to the state. Both the compliance nightmare and litigation risk could be easily avoided by imposing the tax under the sales and use tax (as opposed to miscellaneous excise or gross receipts taxes). We will continue to monitor the digital tax climate in Kentucky, and encourage companies impacted by this new imposition to contact the authors to discuss this issue in more detail.

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