



MULTISTATE TAX COMMISSION

# **SALES TAX ON DIGITAL PRODUCTS WORK GROUP MEETING**

**JANUARY 8, 2026**

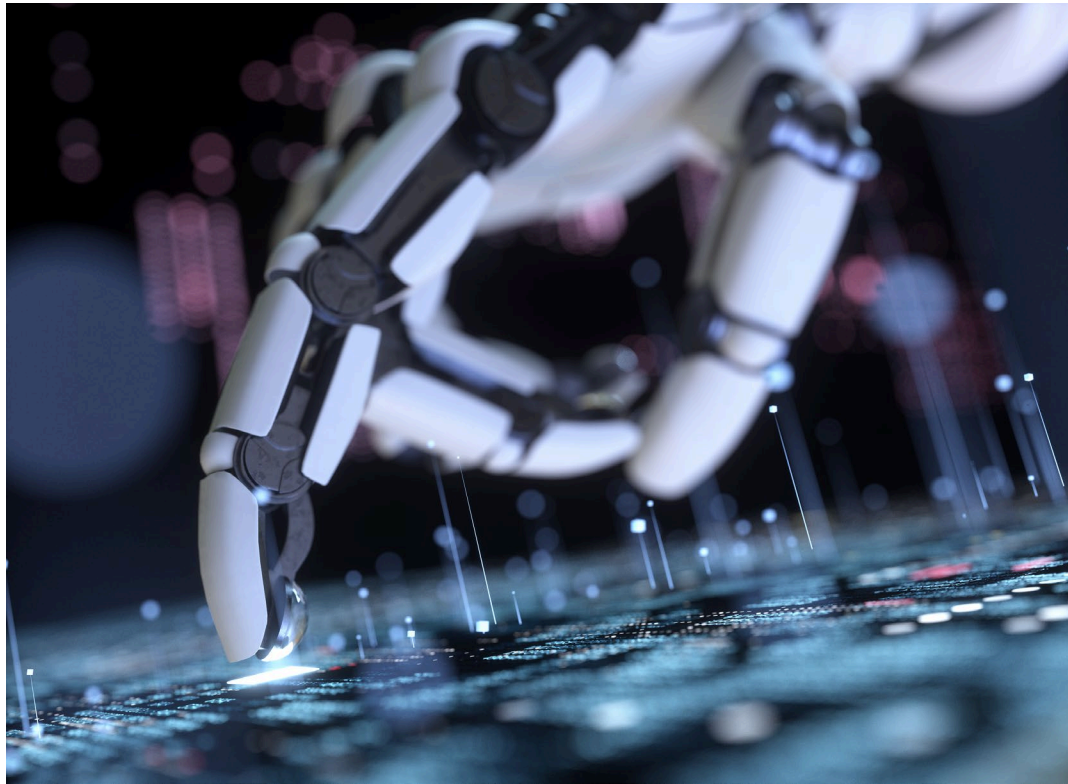


# **EXCLUSIONS AND EXEMPTIONS**

**DIGITAL PRODUCTS PROJECT**



## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE



**IMPORTANT NOTE** – The way in which certain transactions or items are removed from the tax base—whether through narrow definitions, exclusions, or exemptions varies by state. Some states may exclude things that are exempted by other states and vice versa.

## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

### I. Sales Tax Base & Related Terms

The ultimate sales tax base is typically determined as follows:

#### A. Definitions –

Definitions of items form the starting point for imposition of the tax by:

- a. **Generally defining** some items (e.g. tangible personal property),
- b. **Specifically defining** other items (e.g. certain specified digital goods).

## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

### I. Sales Tax Base & Related Terms

The ultimate sales tax base is typically determined as follows:

...

#### B. Exclusions Generally –

Exclusions narrow the general application of the tax by providing for:

- a. Limitations on or exceptions to the defined items or amounts to which tax applies—which may be included in the definitions themselves.
- b. General exclusions based on easily verifiable criteria (e.g., sales by government).

## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

### I. Sales Tax Base & Related Terms

The ultimate sales tax base is typically determined as follows:

....

#### C. Exemptions Generally –

Exemptions carve out from the tax base certain specific transactions based on various criteria which often have to be verified in some way, including:

- Definitions of specific items,
- Who the seller is (e.g. hospitals),
- Who the buyer is (e.g. government),
- Use of the item by the buyer (e.g. resale, manufacturing, agriculture, etc.),
- Other criteria (e.g. sales tax holidays).

## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

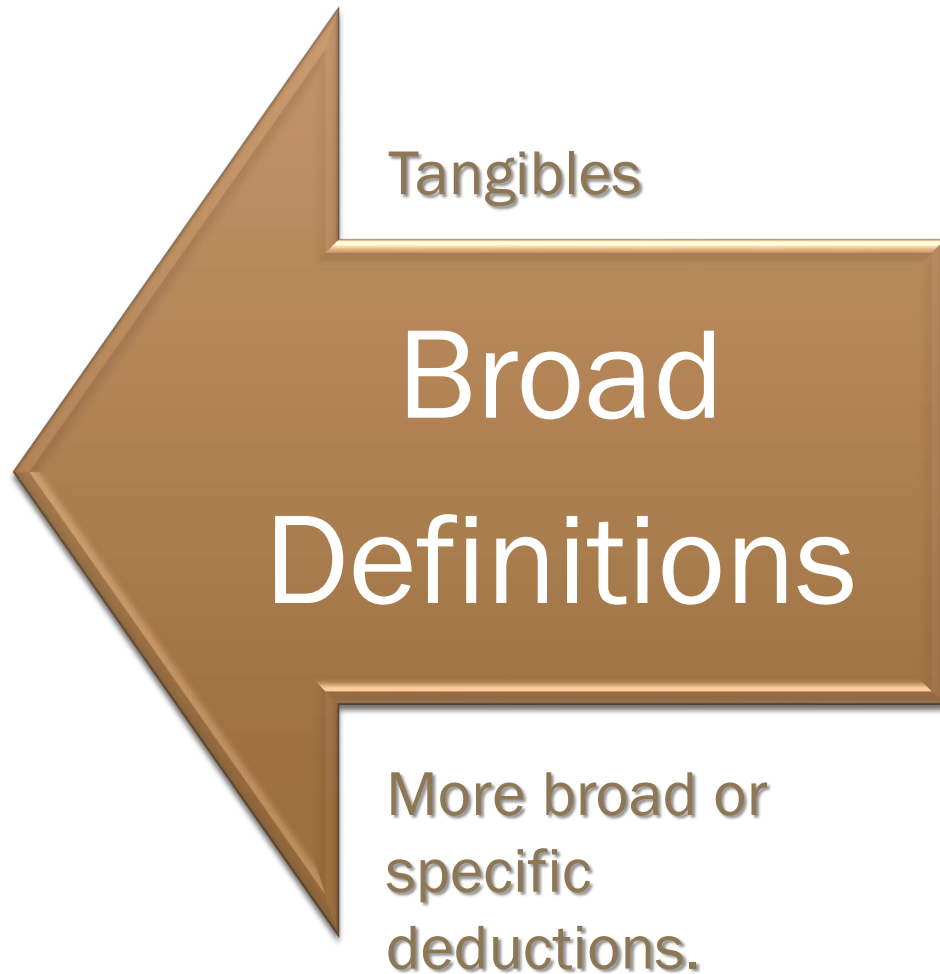
## II. Relationship of Exemptions to Definitions of Taxable Items:

States have typically taken two different approaches to determining the sales tax base:

- A. **Broad definition with a number of specific exemptions:**  
States generally tax tangible personal property broadly defined, with a number of exclusions or exemptions, or
- B. **Narrow definition with fewer specific exemptions:**  
States generally tax services and intangible or digital items by narrowly defining specific services or items, with some additional exclusions or exemptions

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**HERE'S A WAY TO THINK ABOUT IT:**



Services & Digital Products



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## **REPORT OF STUDY GROUP – PROPOSED BROAD DEFINITION & BROAD EXEMPTION**

“Related Exemption: A product is exempt from taxation as an automated digital product if the product will be used **predominantly for a trade or business.**”

“Existing exemptions and exemption procedures should be reviewed to determine applicability. **If a state has other exemptions that are limited to tangible personal property or taxable services, the state should consider expanding the exemptions** to explicitly cover automated digital products.”

## **CONSIDERATIONS FOR POLICY-MAKERS**

- **Effect of Specific Digital Product Definitions –**  
Do specific definitions effectively address all exemption-related issues?
- **Effect of Broad B2B Exemption –**  
Does the broad B2B exemption address all exemption-related issues?
- **Other Policy Choices –**  
How important are parity and simplicity?
- **Particular Digital Issues –**  
How difficult will line-drawing be with digital products?

## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

### III. Specific Exclusions and Exemptions – Common Criteria

- A. Value (fees, interest, etc.) not included in the taxable price.
- B. Most common criteria:
  1. Definition of the item (e.g., food, clothing, prescriptions, etc.)
  2. Identity of the seller or the buyer (e.g., government, charity, etc.)
  3. Use by the buyer (e.g., resale/lease, use in certain activities, etc.)
- C. Multiple criteria

**EXCLUSIONS AND  
EXEMPTIONS –  
PROPOSED  
OUTLINE**

**III. Exclusions and Exemptions –  
Application of Common Criteria**

- A.** Value (fees, interest, etc.) not included in the taxable price.

It appears the same exclusion /exemptions that generally apply to sales would also apply to sales of digital products.

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**EXAMPLES –  
EXEMPTION BASED ON  
DEFINITION OF ITEM**

- Food
- Fuel
- Items subject to other excise taxes (e.g., vehicles)
- Real property

# EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

## B. Common Single Criteria –

### 1. Based on **Definition of Item**

- Effect of Specific Digital Product Definitions – **Incomplete**, given that common exemptions may apply criteria not found in the definition itself or may apply only to tangible goods and not digital equivalents.
- Effect of Broad B2B Exemption – **Incomplete**, given that common exemptions apply to items that are not business inputs.
- Other Policy Choices – If the digital item is a substitute or equivalent to the non-digital item that is currently exempted then policymakers might include it in the exemption or create an equivalent,
- Particular Digital Issues – **Equivalency may be difficult to determine in some cases.**

**EXAMPLES –  
EXEMPTION BASED ON  
IDENTITY OF SELLER OR  
BUYER**

- Sales by or to government
- Sales by or to charitable organizations
- Isolated and occasional sales



## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

### B. Common Single Criteria –

#### 2. Based on **Identity of Seller or Buyer**

- Effect of Specific Digital Product Definitions – **Incomplete**, given that some exemptions may apply criteria not found in the definition itself.
- Effect of Broad B2B Exemption – **Incomplete**, given that some exemptions apply to items based solely on the identity of the seller or based on the identity of non-business buyers.
- Other Policy Choices – Unless there is a reason to treat sales of digital products differently, then policy-makers might apply these exemptions to digital products.
- Particular Digital Issues – It would appear **fairly simple** to address these single-criteria type exemptions.

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## **EXAMPLES – EXEMPTION BASED ON USE BY THE BUYER**

- Resale/re-lease
- Educational use
- Use in providing healthcare services

NOTE: Exemptions that incorporate use-based criteria often include (implicitly or explicitly) other criteria—such as who the buyer is. See multiple criteria below.

## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

### B. Common Single Criteria –

#### 3. Based on Use by Buyer

- Effect of Specific Digital Product Definitions – **Incomplete**, given that some exemptions may apply criteria not found (**or difficult to include**) in the definition itself.
- Effect of Broad B2B Exemption – **May be broader** than other limited exemptions applicable to other products.
- Other Policy Choices – Unless there is a reason to treat sales of digital products differently, then policy-makers might apply these exemptions to digital products.
- Particular Digital Issues – **The most common example is resale/lease to the purchaser's customer (and no other use by the purchaser). This is fairly straight-forward.** Other use-based criteria may be somewhat more complex.

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## **EXAMPLES – EXEMPTION BASED ON MULTIPLE CRITERIA**

- Certain items purchased by certain buyers and/or for certain uses.
- The most common examples are items purchased for use in producing other products.
  - Ingredients or component parts
  - Consumables
  - Production-related tools and equipment

## EXCLUSIONS AND EXEMPTIONS – PROPOSED OUTLINE

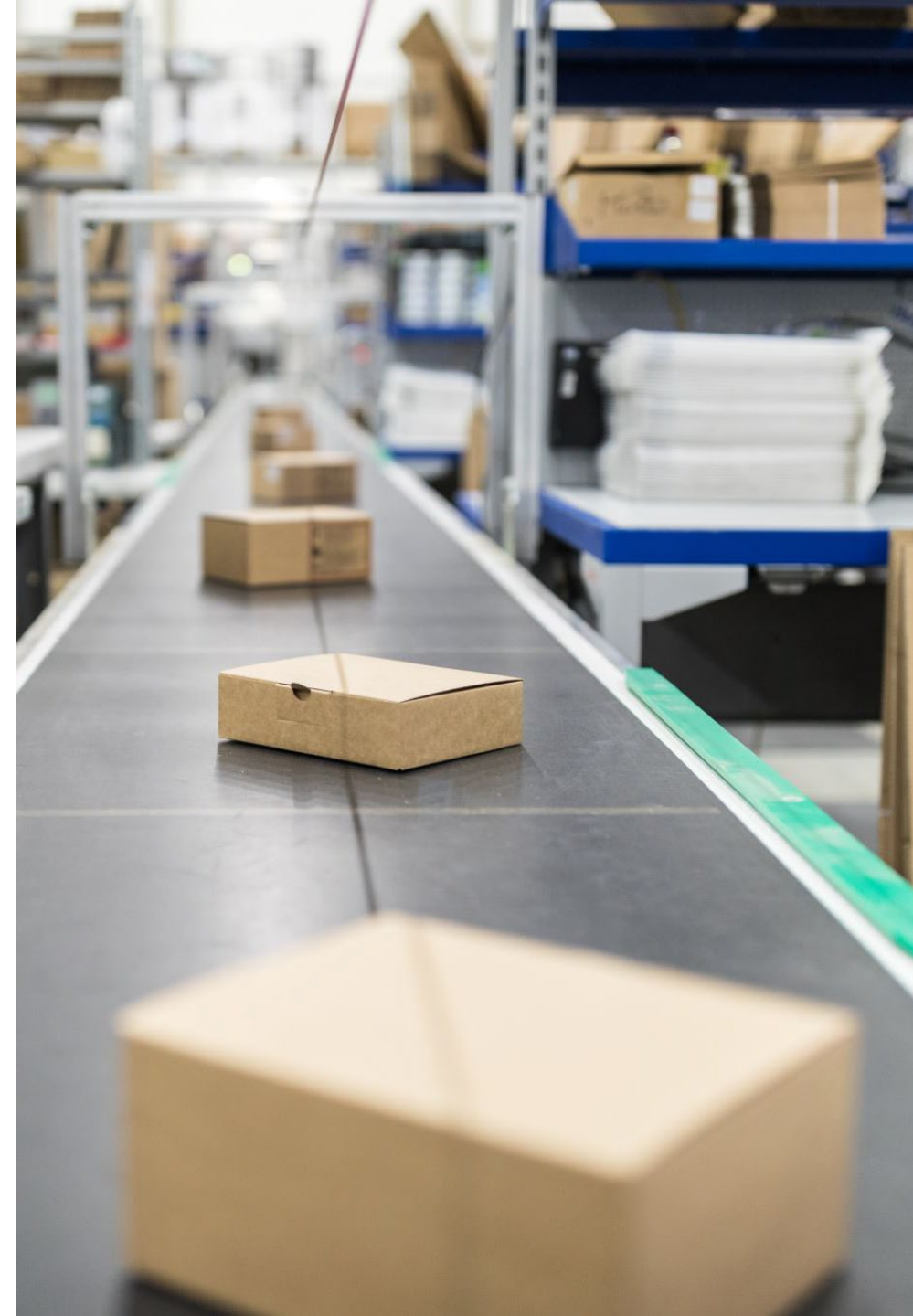
### C. Multiple Criteria – Particularly “production” type inputs.

- Effect of Specific Definitions – **Incomplete**, given the difficulty of including certain, multiple criteria in a single specific definition, and also because this would not address tangible products used in the production of digital products.
- Effect of Broad B2B Exemption – **Incomplete** to the extent the exemption pertains to **tangible products consumed or used in production** of digital products.
- Other Policy Choices – The comparison to manufactured goods would have to be considered and how parity might be reached with respect to tangible products used to produce digital products. **Not only digital products used to produce tangible products, but vice versa.**
- Particular Digital Issues – **What is a “component part” or a “consumable” or a production “tool” or “equipment” when it comes to producing digital products?**

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## **MOST STATES HAVE MANUFACTURING EXEMPTIONS**

- May or may not define a “qualified manufacturer.”
- May define what is “manufacturing” or “processing” – with some similar terms defined more broadly or more narrowly.
- May provide exemptions for ingredients and component parts but only certain consumables and production-related tools and equipment.
- May not address digital products used in producing tangibles or tangibles used in producing digital products.



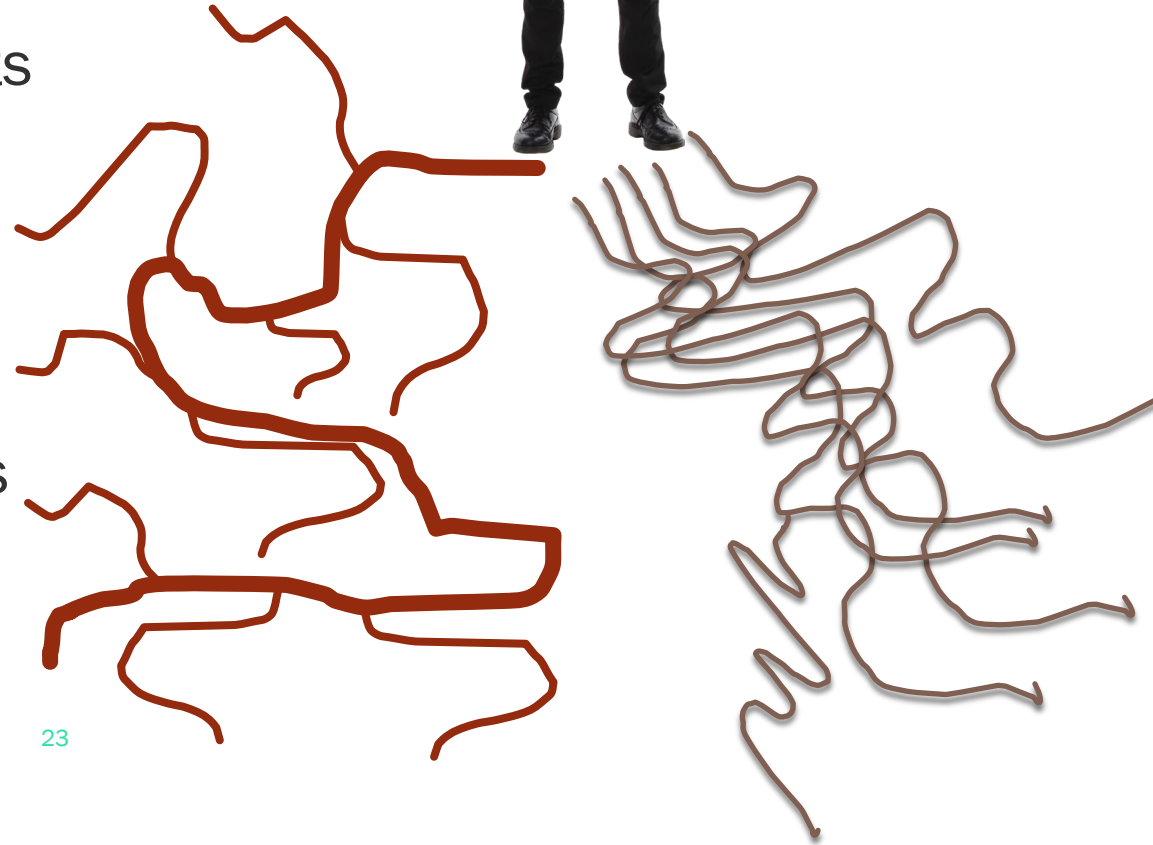
## CURRENT TREATMENT –

- In general, states that treat some digital goods as tangible property may already apply certain exemptions to those products.
  - But that doesn't mean the simple thing to do is just include all digital products under the definition of tangible products.
- Only a handful of states have addressed production-related exemptions.
- To the extent the final product is not taxed, states may be more inclined to tax certain inputs.

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## GENERAL CONCLUSION

- Providing for a straight-forward approach to exemptions for broadly defined digital products is not necessarily more difficult than for specifically defined digital products, and may even be simpler over time.
- The particular issues for both are:
  - Creating parity in treatment of similar items or uses, and
  - Treatment of production activity





# **QUESTIONS – DISCUSSION?**