



MULTISTATE TAX COMMISSION

MEETING NOTES

MTC Work Group – Sales Taxation of Digital Products

January 8, 2026

I. Welcome, Review of Notes from Previous Call, and Initial Public Comment

Mia Etienne Strong (Louisiana), vice-chair of the Work Group, convened the meeting and stated the notes from the previous meeting were online. Mia invited initial public comment.

There was no public comment.

II. Exclusion/Exemption Issues – Issues for Policy-Makers, Taxpayers/Practitioners, and Administrators

Mia then moved to the topic of sales tax exemptions and turned to Helen Hecht (MTC). Helen shared slides and provided an update. She stated the overall focus was determining whether adding digital products to the tax base will be effective and administrable and that one topic is the effect on exemptions.

Helen started by describing two major options for determining the tax base: narrow imposition definitions and broad imposition definitions. She noted that each of these will affect the scope and size of exemptions in different ways.

Helen then introduced different categories of carveouts to the tax base. She first distinguished exemptions and exclusions, stating that exemptions are based on criteria-based excisions from the tax base whereas exclusions are usually areas where no imposition is ever made. She provided an example of an exclusion: the carveout of expenses or certain costs from the definition of gross proceeds.

She described the relationship between exemptions and definitions, saying that if a broader definition is used for impositions, more exemptions will be needed, whereas if narrow definitions are used for imposition, less exemptions will be needed.

Helen mentioned the report of the definitions study group, which included a broad business-to-business (B2B) exemption to accompany the broad imposition outlined in the report. The exemption is based on whether the automated digital product is used predominantly for a trade or business. Helen noted the report provides that other exemptions should be considered separately. The question being whether those should be altered to ensure they apply to digital products.

According to MTC staff research, there are several categories of exemptions based on the criteria they are based on. The criteria include the definition of the item; the identity of the seller or buyer; the use by the buyer; and a blend of multiple criteria.

Helen stated that examples of exemptions based on the definition of an item include food; fuel; items subject to other taxes, like vehicles; and real property. She then considered how these types of exemptions would interact with a tax base built on specific definitions. She noted this type of exemption and definition system would be incomplete, as many exemptions would rely on criteria not found in the definitions. She also noted these might apply only to tangibles and not to digital products. Policymakers might want exemptions based on criteria not easily added or practically added to the definitions themselves.

Helen then considered whether the broad B2B exemption would adequately capture these exemptions. Her conclusion is that the broad B2B exemption would only incompletely address these due to the possibility of transactions with a nonbusiness purchaser that policymakers might still want to exempt.

Helen identified the other policy choices or priorities as equity or parity; in other words, whether one product is a substitute or equivalent for another.

Mia asked whether we should consider exemption certificates along with the exemptions. She noted the legislature is focused on policy and not always on how the Department will deal with the exemption. She suggested considering how exemptions are being administered. Helen responded that we should consider documentation and its role in administering exemptions.

Helen next addressed exemptions based on the identity of the seller or buyer. Helen noted that definitions of specific items cannot also be expected to limit tax only to certain buyers and sellers, at least not practically. She said the broad imposition with a B2B exemption has a similar issue: a purchaser that does not qualify as a business purchaser, like a nonprofit, might buy the product and be subject to tax. Policymakers might want that purchase to be untaxed.

Helen stated that this type of exemption might be simpler because the intricacies of the product do not matter. The identity of the buyer or seller is the only issue.

Josh Pens (Colorado) raised an issue with the purchaser identity question. Josh stated that nonprofits are often operating trades or businesses. Helen said we would need more specificity on that and how we use the term 'trade or business' or 'business' for purposes of the broad B2B exemption or other exemptions.

Helen next addressed exemptions based on the use by the buyer. She provided a sale for resale exemption as an example. Helen noted similar issues with this one, stating that specific definitions would not work. She said the definitions would become too long and complicated if they were intended to both define the term and exclude things for resale all in one.

She then addressed the broad B2B exemption, noting that it is broader than this exemption category because it covers things that are predominantly used in the business rather than just things 'resold' by the business. She said the broad B2B exemption would probably cover this criterion.

Helen next addressed exemptions based on multiple criteria. As examples, she provided ingredients or component parts; consumables; and production-related tools and equipment. Helen stated that to the extent a broader manufacturing exemption exists, the question would be whether that applies to digital products.

Helen noted the use of specific definitions was not satisfactory because with multiple criteria, the definitions would get even longer and could also have multiple definitions for very similar items. For the broad B2B exemption, Helen said this might be an area where it would need to be amended to add tangibles that go into the process of creating a digital product.

Helen noted one issue was the task of identifying component parts and the relative difficulty of that task with digital products compared to physical products.

Most states have manufacturing exemptions. Some manufacturing exemptions define a “qualified manufacturer” and provide criteria of what products can be bought without tax. Others define the process, for example, “manufacturing” or “processing,” and then provide that anyone that does that activity qualifies. Other times the exemption may be for component parts or ingredients. Helen stated these typically include certain consumables and production-related equipment.

Helen noted that some states already treat digital products as tangible property. In that case, many exemptions may already apply, but that if the base starts expanding, some may not. Helen pointed out that only a few states have addressed production-related exemptions. She also noted the tendency to tax inputs if the final product is not taxed and to not tax the inputs if the final consumer good is taxed.

In conclusion, Helen said that it is not necessarily easier to do specific definitions; it could be just as doable to have a straightforward approach to exemptions given a broadly defined imposition through a broad definition.

Josh Pens raised concern about the report suggesting policymakers consider the broad B2B exemption. Josh called this an “absolute” B2B exemption, noting it was beyond broad. Addressing the policy, Josh stated that even though sales tax is meant to be a personal consumption tax and should address pyramiding, it is imperfect, always will be, and will involve tradeoffs. Josh stated the broad B2B exemption is much broader than anything done in Colorado. For example, it is much broader than Colorado’s manufacturing machinery exemption. Josh stated this only applies to machinery, not office supplies used in the accounting office. He noted the proposed B2B exemption would apply to software used in the accounting office.

Josh then noted that many existing exemptions in fact mitigate pyramiding but that mitigation of pyramiding was never the reason for them. He stated Colorado’s manufacturing exemption was not justified as anti-pyramiding but as an economic development tool. Josh cautioned against going too far with anti-pyramiding efforts.

Addressing practicality, Josh asked how the seller would know the purchaser is in a trade or business and will use it in a trade or business. He stated in some cases even the buyer will not know at the time of purchase. Josh said this will put pressure on consumers’ use tax, which is notoriously difficult and low compliance. He also stated it would put pressure on refund claims. Josh also asked about timing, asking whether the predominant use by a trade or business was meant to be in the first year or over the entire life of the product.

Mia stated the broad B2B exemption may be part of the draft the study group developed but not a full recommendation from the work group. Helen said that the B2B exemption and whether it is broad should factor into the equity considerations also. Helen said the difficulty she was raising is determining whether digital products are real inputs.

Josh offered a couple ways to narrow the broad B2B exemption. One option was to identify classes of automated digital products that, categorically, are not inputs, and therefore not exempt. Another was identifying categories of business that are not the target of the exemption.

Karl Frieden (COST) responded that the sales tax should apply to final consumption and not to intermediate consumption. He acknowledged that if you fully exempt digital business inputs it will create an inequity with other sectors where there is no general business inputs exemption. Karl then said he would frame the question as whether we can do better. He noted that the United States has the only tax that heavily applies to intermediate consumption. Karl also noted that exemptions for business inputs must be created up front because once tax is imposed it becomes more difficult to create B2B exemptions. He said that getting a framework in place for exempting digital business inputs that is better than what exists is important. Finally, Karl noted that practicality suggests allowing a broad B2B exemption to reduce opposition from the business community.

Helen acknowledged that the broad B2B exemption contained in the study group report is not a perfect match between digital and physical inputs. She noted that addressing that inequity will be hard because identifying the components of a digital product is more difficult than for physical products. She noted, however, that if the exemption is based on (1) being digital and (2) purchased by a business, that gets some pyramiding relief and avoids the difficult task of identifying the components of a digital product.

III. Comments on the Draft Bundling Section of White Paper

Mia invited any comments on the bundling white paper draft, noting that it was posted on the project webpage. She requested readers to note the draft's format as that format is likely to be the template for other sections of the white paper.

Mia then asked if there was any new business. There was none.

IV. Adjourn

Mia adjourned the meeting.