

## Sales tax for Digital Products in the U.S.

You're all excited about opening your online business and are ready to start selling digital products to your customers in the US. If only digital taxes weren't so overwhelmingly complex! American sales tax follows one of the most complicated systems on the planet, but don't worry: You don't need to know the ins and outs of it all, a working knowledge of the most important concepts will do the trick. We have prepared an easy primer for you to help you cut through the maze.

Today, media goods such as music, video, and books, can be delivered electronically to customers. Digital sales of these goods have greatly increased while sales of similar products in physical form have experienced a sharp decline.

Historically, customers only purchased physical items such as CDs, VHS cassettes, or paper books, that could be weighed, packaged, mailed, carried, or driven. The majority of today's sales tax law is still based on old and outdated models focused exclusively on sales of physical goods. No one envisioned the possibility of a future where products and services could be delivered online.

### Sales Tax By States – Where are Digital Products Taxable?

#### State vs. the States

There is no uniform sales tax in the US. It is up to each individual state whether or not it wants to charge sales tax, and how much. This means that for any sales your business makes in the US, you need to look at sales tax on a state level, i.e. at the tax regulations for each state relevant to you.

The sales tax laws have been updated to include digital goods and services in different ways across the different US states, and the application of these laws has been troublesome for most state and local governments.

Quick Stats:

- There are 27 states that tax digital products.
- There are 23 states that do not tax digital products.
- 5 states do not have a retail sales tax at all; these include, Alaska, Delaware, Montana, New Hampshire and Oregon.
- For the states that tax digital products, the tax rate varies from 1% to 7%, depending upon the state and the type of digital good.

Please note that in the U.S., you are only required to collect sales tax in states where you have "sales tax nexus". This occurs when your business has some kind of "physical presence" in a state, for instance; an office, employees, inventory, affiliates, a drop shipping relationship or selling products at a tradeshow or other event. If you have nexus in a state, then you have to apply sales tax to buyers in that state.

#### What Are Digital Products?

So which items are considered digital products? With all of the recent technological advances, this is not an easy question to answer.

In general, digital products, or digital goods, are defined as intangible (= non-physical) goods that exist in electronic or digital format. They are delivered to the end customer electronically, such as through email or online download.

Examples include: digital media, downloadable music, internet radio, internet television and streaming media, webinars and online courses, fonts and graphics, digital subscriptions, online ads, internet coupons, electronic tickets, online casino credits, downloadable software and mobile applications and online games.

From a tax perspective, there are 6 types of digital goods:

- Online data processing services.
- Downloaded software.
- Downloaded books, such as eBooks and Kindle.
- Downloaded music, digital audio files such as iTunes and podcasts.
- Downloaded movies or digital video, such as Netflix and Amazon Prime.
- Other downloaded electronic goods.

## Definitions by State

Do all US states apply these categories uniformly? No! Hang in there, we'll break this down for you. There are basically three scenarios:

- **States using their own definition** – In addition to the general categories listed above, many states have their own definition of digital goods and services. These include: Arkansas, Connecticut, Georgia, Illinois, Iowa, Kansas, Louisiana, Maine, Michigan, Minnesota, Mississippi, North Carolina, Ohio, Oklahoma, Texas and West Virginia.
- **States not using any definition at all** – There are 18 states (Alabama, Arizona, California, Colorado, D.C., Florida, Hawaii, Idaho, Maryland, Massachusetts, Missouri, New Mexico, New York, Pennsylvania, South Carolina, South Dakota, Utah and Virginia) that do not specifically define digital goods.
- **States using a standard definition** – The remaining states utilize a standardized definition of digital goods: Indiana, Kentucky, Nebraska, New Jersey, Nevada, North Dakota, Rhode Island, Tennessee, Vermont, Washington, Wisconsin and Wyoming. This definition is called the Streamlined Sales Tax (SST) Definition of Digital Goods; further information about this is available online, e.g. on the Streamlined Sales Tax Governing Board, Inc.'s [website](#). (Please also see "Digital Taxes Resources" below).

## Sales Tax on Digital Goods by State

Ok, so now we know that digital products are defined differently in the individual US states. But which states actually tax them and how? Let's have a look at each state:

State	Taxable Note
<a href="#">Alabama</a>	YES Digital downloads are generally considered tangible personal property and are taxable at the same rate as other tangible personal property.
<a href="#">Alaska</a>	NO No sales tax in the state.

<u>Tennessee</u>	YES	Digital products are tax exempt in Tennessee.
<u>Texas</u>	YES	Taxable as long as the item also taxable if sold in physical format.
<u>Utah</u>	YES	Digital products are taxable in Utah.
<u>Vermont</u>	YES	Digital products are taxable in Vermont, whether transferred electronically for permanent or temporary use.
<u>Virginia</u>	NO	No sales tax in the state.
<u>Washington</u>	YES	Digital products are taxable in Washington. This includes downloaded digital goods like music and movies, streamed and accessed digital goods, and digital automated services.
<u>West Virginia</u>	NO	No sales tax in the state.
<u>Wisconsin</u>	YES	Digital goods are taxable in Wisconsin. This includes audio works, audiovisual works, books and codes used to purchase works (digital or physical) by digital means.
<u>Wyoming</u>	YES	Digital products are taxable in Wyoming. This includes digital audio works, audio visual works and books.

## Federal and State Legislation

Not the easiest system to understand, right? Many people think so, too, and there have been attempts by the US government as well as individual state governments to make this easier for everyone.

In 2011, the US Congress enacted The Digital Goods and Services Tax Fairness Act. This law provided a federal framework for digital taxes, but didn't go far enough in providing guidance and direction for the individual states.

More recently, there have been several attempts by federal and state legislators to create a more homogenous digital tax, but there has been fierce resistance. This means that so far, the system has remained rather complex.

## Digital Taxes Resources

Since you will need to deal with this state-based structure for the foreseeable future, it is important for you to know where you can get more information about the specific tax regulations in each state relevant to you.

Your most important source is each state's tax authority or Department of Revenue, but there are numerous other resources that can be used to determine if a digital tax applies to you.

The Streamlined Sales and Use Tax Agreement (SSUTA) assists states as they administer a similar and more uniform sales and use tax. Their [website](#) provides a useful online taxability matrix broken down by each state.

The [Federation of Tax Administrators \(FTA\)](#) is an organization of state tax authorities and administrators which surveys sales tax rates and provides regularly updated reports. If you have additional questions, check with a sales tax specialist or a Certified Public Accountant (CPA).

## Conclusion

And voilà! Now you have a solid understanding of the foundations of sales tax laws in the United States, and you also know how and where to obtain any further information for your individual business needs.

If you have any questions about how Quaderno makes handling US sales tax easier for you, check out our [website](#) or shoot us an email at [support@quaderno.io](mailto:support@quaderno.io).