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incurring use tax obligations on those expenditures. These purchases are for services that are "consumed" to further your firm's operations and are typically not bought ...

Shane Ratigan • Apr. 03, 2018



For accounting professionals and many of their clients, the software or other digital services they use daily are no longer stored on local hard drives or overheated servers stuffed in a back closet. Instead, these programs, applications and products are accessed from remote servers where the software code that powers them resides. Access is made via the internet by multiple simultaneous users, providing several efficiencies of scale: complex and helpful tools are available at a competitive price, less investment is required in hardware and IT services by individual companies and

firms, and instantaneous availability of solutions on multiple device types across the

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That is not to say many states haven't developed ingenious, if not exactly intuitive, theories about how to apply existing rules to the new cloud world. Yet, beware! Even if a state does not address cloud-based services, it may still demand the services are taxed under some patched together legal logic.

Buying and Selling Cloud-Based Services

In dealing with sales tax, one of the principal tasks for any vendor is to determine the proper tax treatment for the items or services it sells in the jurisdictions where it is obligated to comply. This process is rarely simple, even with established products or services, the U.S. sales and use tax universe of 46 states and several localities often prefer to put their own twist on the taxation of specific transactions. Cloud-based services have certainly established themselves in the marketplace, but they remain identified as specifically taxable or exempt in less than a quarter of the sales tax states.

The dearth of direct guidance on the treatment of cloud-based services for sales and use tax affects sellers and buyers. Vendors struggle to determine with certainty whether these services should be taxed at all, while purchasers are left wondering if they are being overcharged or, especially in the case of business consumers, is there a use tax obligation that must be accrued?

Some States are Helping, so How are They Doing it?

As alluded to above, there are really three varieties of states in this area: they affirmatively identify cloud-based services, use existing rules to shoehorn some cloud services into existing categories of other taxable goods or services, or seem to ignore the existence of the cloud all together.

Since lack of clarity creates fear, uncertainty and doubt, we commend the minority of

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More commonly, states have addressed only limited factual circumstances with regards to the cloud, and most of the states in this category have only addressed SaaS. Connecticut finds a service that provides remote access to information is taxable as a data processing service. In West Virginia, where most services are taxable generally, the delivery of cloud-based services enjoys no specific exemption and likely are taxable at the general rate.

Finally, a portion of states do not define cloud services, but have yet to apply existing rules to determine taxability. For example, in Nevada, almost no services are taxed at all, the state's silence on the cloud implies these services are exempt as well.

A Friendly Use Tax Reminder to Cloud-Loving Accountants and Other Professionals

As your firm adopts more and more cloud based solutions, it also runs the risk of incurring use tax obligations on those expenditures. These purchases are for services that are "consumed" to further your firm's operations and are typically not bought for resale. Use tax compliance should not be a new thing, but use tax obligations regarding cloud-based services are often tinged with a twist: many providers of cloud-based services are not collecting sales tax, even when the services are taxable in your state.

Cloud-based or not, we can all agree that vendors don't collect sales taxes for their own reasons, but with cloud-based services, the reason is typically related to the nature of the cloud itself: the delivery of these services can be made without the traditional indicia of sales tax nexus. Recall sales tax 101: without a physical presence, a vendor is not obligated to collect sales tax, leaving the purchaser to self-remit use tax. One of the main selling points of the cloud is its lack of physicality in the hands of its users.

The Take-Away

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of the sales tax band is not your thing, consider finding a specialist who can help you and your clients avoid tripping over their own feet on the dance floor.

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Sales Tax

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