Commenda + Paid.

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The $2.7 Billion Agent Tax Crisis

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Executive Summary

Paid.ai commissioned Commenda Technologies to conduct the first comprehensive study on the taxability of AI agents. The analysis covered 14 leading AI agent companies across multiple categories and included formal Public Letter Ruling requests submitted to state tax authorities.

The research reveals a significant challenge: U.S. sales and use tax systems struggle to classify AI agent transactions, creating uncertainty for companies and regulators alike.

Core Finding

The way an AI agent is structured and priced can mean the difference between being taxable in 22 states versus only 4—an outcome that carries major financial and strategic implications.

The Study: First-of-Its-Kind Analysis

Methodology

Our analysis examined distinct AI agent companies across categories including:

• Sales & Revenue Operations (AI SDRs and sales automation)
• Industry-Specific Solutions (mortgage, healthcare, construction automation)
• Conversational & Voice AI (education, customer service)
• Development Tools (code generation, testing automation)
• Security & Compliance (penetration testing)
• Professional Services (consulting and custom AI development)

The study submitted Public Letter Ruling (PLR) requests to multiple state tax authorities including Iowa, Kentucky, Maryland, Massachusetts, Mississippi, Nebraska, Texas, Utah, Vermont, and Washington, with additional requests to Indiana, Kansas, North Dakota, and Wyoming for specific clarifications.

State Groupings & Tax Impact

The study identified three distinct categories of states:

Group 1: States Generally Taxing Software as a Service (22 States)

- Arizona, Connecticut, District of Columbia, Hawaii, Iowa, Kentucky, Louisiana, Maryland, Massachusetts, Mississippi, New Mexico, New York, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Washington, West Virginia

Group 2: States Generally NOT Taxing Software as a Service (10 States)

- California, Florida, Georgia, Idaho, Illinois, Louisiana, Michigan, Missouri, Nevada, Virginia

Group 3: States with Broad-Based Service Taxes (4 States)

- Hawaii, New Mexico, South Dakota, West Virginia

The Hidden Arbitrage

The U.S. tax system was built for a world where humans do work and companies sell products. It assumes clear boundaries: software is a product you buy, services are performed by people, and employees generate income that gets taxed. AI agents shatter some of these assumptions.

This creates an unprecedented arbitrage opportunity. The same AI agent performing identical functions can be structured as either taxable software or non-taxable professional services. The difference isn't in what the technology does, *but in how companies choose to package, price, and position it*.

Our study reveals that companies are already exploiting this arbitrage, whether intentionally or accidentally.

Two companies in our analysis perform nearly identical mortgage automation functions. One pays sales tax in 22 states. The other pays in just 4 states. The only difference is in how they describe and deliver their service.

It's effectively a tax optimization through structural choices that are entirely legal under current law, but the implications for state revenues are catastrophic.

When companies can choose between being classified as taxable SaaS (affecting millions in tax liability) or non-taxable professional services (paying nothing), rational actors will always choose the latter.

As more companies discover this arbitrage, states face a double hit: they lose income tax from displaced workers AND sales tax from the agents that replace them.

This could result in a $2.7 Billion loss in state and federal revenue per year.

How We Did The Math

Using U.S. Bureau of Labor Statistics data:

- Administrative and clerical workers in the U.S.: 2,496,370[1]
- Mean annual wage: $43,560
- Combined tax burden (income, payroll, state, local): approximately 25% = $10,890

If ~10% of positions are replaced:
- 249,000 jobs eliminated
- Lost revenue per job: $10,890
- **Total annual loss: $2.7 billion**

This calculation assumes:
1. AI agents are classified as non-taxable services (as many are structured per our study findings).
2. No replacement tax mechanism is implemented.
3. Displaced workers don't immediately find new taxable employment.

Case Study: Mortgage Automation Platform

One company in our study offers an AI-agent platform specialized in automating labor-intensive workflows in the residential mortgage industry. They explicitly position themselves as a "fully managed service, not licensed software" with outcome-based pricing.

Tax Treatment:
- Taxable in only: Hawaii, New Mexico, South Dakota, West Virginia
- Exempt in: 46 other states

We note that the 'outcome-based pricing' model strongly supports a service classification, making it exempt in almost all states.

Outcome-based pricing could reduce your offering's price by about 6% on average by being exempt from tax.

[1] https://www.bls.gov/oes/2023/may/oes439061.htm

Case Study: AI Sales Development Platform

Another company positions its offering as an "AI Sales Development Representative" that automates the outbound sales demand generation process. Despite performing similar functions to the mortgage platform, it faces completely different tax treatment.

Tax Treatment:

- Likely taxable in: Arizona, Connecticut, Hawaii, Massachusetts, New Mexico, New York, Ohio, Pennsylvania, South Dakota, Tennessee, Texas, Utah, Washington, West Virginia
- Likely exempt in: California, Florida, Georgia, Idaho, Illinois, Maine, Michigan, Missouri, Nevada, Virginia

Because taxability depends on the 'true object' between software access and non-taxable consultative services, the taxation varies between states.

Case Study: The Downloadable Software Trap

One engineering analytics platform in the study made what seemed like a minor technical decision - offering a downloadable Mac application alongside their cloud service, as an Electron wrapper.

As a result, their "hybrid model, which includes a downloadable Mac application and a cloud backend, makes it clearly taxable as prewritten software.

Result: "Taxable in nearly all states that tax either downloaded software or SaaS."

This finding demonstrates how a simple architectural decision can trigger taxation across the board.

A Decision Framework

Our analysis provides guidance but figuring out if an AI product is taxable is tricky. You must look past the marketing and understand what customers are actually paying for.

The four questions we ask:

1. What are your customers buying?

You have to ignore marketing terms like 'AI Employee'. The key question is: are customers paying to use a tool (software) or are customers paying for a finished result (a service)?

2. How 'custom' is the product?

For tax purposes, you need to know if what you're selling is:
- Changing settings in the existing software for a customer (this is usually taxable).
- Writing brand-new code from scratch, just for the customer (this is often not taxable).

Thus, the word 'customization' can be misleading.

3. Separate your charges on the bill

We recommend that if you sell a package that includes both the AI software (taxable) and services like setup or training (often not taxable), the entire price might get taxed. To avoid this, you as a seller needs to list the charges separately on the invoice.
Paid can help with this.

4. How much are people involved?

We've found that the more that your own employees (as a seller) are actively working on the customer's behalf, the stronger the case that you're buying a non-taxable service. This is the case with FDEs, for example.

Key Tax Classification Principles

The Bundling Problem

Our study highlights a government contract automation platform as a complex case. When sold as a single, non-itemized subscription that includes mandatory onboarding and training – our critical finding is that this makes it taxable.

In states with strict bundling rules like Texas and New York, the presence of the taxable software platform would likely make the entire subscription fee taxable.

However, in states like California, Georgia, Illinois, and Virginia where the 'true object' is the non-taxable managed service component, the entire offering could be exempt.

This single structural decision of bundling vs. itemizing can trigger taxation on 100% of revenue in some states while remaining completely exempt in others.

Custom Software Exemption

We analyzed an omnichannel customer experience platform that is "100% customized for each business", according to their website.

The tax implication: Its taxability depends on whether it is deemed configured (and therefore taxable) SaaS or exempt custom software.

Most states exempt custom software from sales tax, treating it as the result of a non-taxable service.

Key states that DO tax custom software:

- Hawaii
- Connecticut
- South Dakota
- West Virginia

This means 46 states provide an exemption for truly custom AI solutions.

What Professional Services Classification Means

We analyzed services like an autonomous penetration testing platform and concluded: The customer receives the results of a security test, not access to a software tool. This is best characterized as a non-taxable professional service, similar to hiring a human consultant.

Tax result:

- Taxable in: Hawaii, New Mexico, South Dakota, West Virginia
- Exempt in nearly all other states

In most states, professional services are not subject to sales tax.

The True Object Test: Critical for Bundled Services

For bundled offerings containing both taxable and non-taxable components, it is assumed that states will apply a 'true object' or 'dominant purpose' test to classify the entire transaction.

This becomes critical when AI agent companies bundle:

- Software access with professional services
- Platform fees with outcome-based charges
- Technology with human oversight

The "true object" determination can swing tax liability from 0% to 100% of revenue.

Our State-By-State Findings

States with Surprising Exemptions

Our study found these states exempt ALL categories (SaaS, Information Services, Professional Services, Custom Software):

- Arkansas
- California
- Colorado
- Florida
- Georgia
- Idaho
- Illinois
- Maine
- Missouri
- Nevada
- Oklahoma
- Virginia

States Taxing Everything

Per the study, these states tax ALL categories:

- District of Columbia
- Hawaii
- Louisiana ("SaaS, customization, and downloadable software all taxable")
- New Mexico
- South Dakota
- West Virginia

The Gray Areas

The study identified states still awaiting clarification:
In these states, we recommend that a seller asks for a Private Letter Ruling (PLR).

- Pennsylvania
- Connecticut, Rhode Island, South Carolina
- Ohio
- Minnesota (No PLR process)

Recommendation From Our Analysis

Immediate Actions

1. **Understand the distinction:** Think of it like this: paying for a subscription to Microsoft Word is buying a taxable tool. Hiring a person to write a report for you is paying for a non-taxable service.

2. **Document everything:** Check your contracts to clarify if you as a seller are the one managing the AI's work of if the customer is. If the AI just runs on its own, it looks more like taxable software.

3. **Bill strategically:** As a seller, list the charges separately on the invoice. This way, you only collect tax on the taxable parts.

The Outcome-Based Advantage

Our findings strongly support outcome-based pricing. Companies structured as "fully managed services" with outcome-based pricing achieve exemption from sales tax in 92% of states, compared to traditional SaaS models facing taxation in at least 22 states.

Private Letter Rulings

Given the complexity and state-by-state variations revealed in our study, companies should strongly consider obtaining Private Letter Rulings (PLRs) to clarify their specific tax obligations. A PLR provides:

- Definitive guidance from state tax authorities
- Legal certainty for your specific business model
- Protection from unexpected tax assessments
- Clear documentation for investors and auditors

Commenda Technologies specializes in preparing and submitting PLR requests, having already submitted requests to over 10 states as part of this study. They understand the nuances of how to position AI agent offerings for optimal tax treatment.

Conclusion: The Window of Opportunity

As Sachhin Kunjalwar, the author of the Commenda report notes in our research, determining the taxability of AI software and related services is a nuanced process that depends heavily on the unique facts surrounding each offering and the applicable state laws.

As the landscape of AI solutions and tax regulations continues to evolve, it is essential to regularly revisit and update any analysis or conclusions.

This is where Paid, in partnership with Commenda and other tax technology providers, provides essential infrastructure. Companies building AI agents need:

1. Real-time tax classification tracking
2. Outcome-based pricing models that optimize tax treatment
3. Documentation systems that support service classification
4. Multi-state compliance as they scale

The window for establishing tax-efficient structures is open now. Based on our joint analysis, companies have perhaps 3-4 years before regulatory frameworks catch up.

For companies serious about understanding their tax position, the first step is clear: Obtain a Private Letter Ruling (PLR). Commenda can guide you through this process, leveraging their expertise from this groundbreaking study.

For specific tax advice and PLR assistance, contact Commenda (commenda.io) directly. For pricing and monetization infrastructure designed for the agent economy, visit Paid.ai.

About Commenda

Commenda is building the all-in-one platform for global tax and compliance. We enable businesses to seamlessly interface with governments worldwide — managing entities, navigating taxes, and staying compliant across borders.

Our unified suite brings together incorporations, indirect tax automation, transfer pricing, and accounting into one intelligent platform, helping companies expand into new markets without complexity.

Trusted by hundreds of businesses across 30+ countries, Commenda simplifies compliance for everything from startups to publicly listed enterprises — saving thousands of hours and millions in potential penalties.

Founded in 2022, Commenda powers the world's next wave of global businesses with AI-first automation, deep regulatory intelligence, and human expertise.

Learn more at commenda.io

About Paid AI

Paid helps companies monetize AI agents and make the shift from seat-based SaaS to outcome-driven pricing.

Paid track what your agents cost, what value they deliver, and how to price them in ways that actually work. Not just revenue ops. The whole picture: margins, ROI, legal structures, and tax frameworks built for autonomous systems.

Paid gives you the tools to understand true unit economics, transition to outcome-aligned pricing, and navigate the regulatory complexity. You track every agent action, every cost, every outcome. Then you price and bill in ways that capture the value you create without destroying your margins.
We're building the infrastructure to make sure that doesn't happen.

Founded in 2025 by leaders who built Outreach, Salesforce Billing, Pleo, and early Palantir. Backed by Lightspeed Ventures, EQT Ventures, FUSE, and Sequoia.

Learn more at paid.ai

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