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Sales Tax Corner

Sales Tax Incentives for Data Centers

By Ilya A. Lipin and Jordan B. Mottram

With artificial intelligence, cryptocurrencies, and the digitization of the physical world accelerating at an unprecedented pace, the demand for data centers and supporting infrastructure has also reached new heights. In a competitive bid to attract technology investment, states are ramping up efforts to offer data center incentives and tax exemptions.

Data center incentives are intended to drive major investments and job creation in local communities, typically requiring substantial capital outlays and specific employment commitments and salary levels, with benefits typically lasting five to 20 years (or even more) depending on the jurisdiction. In return for investment and jobs, qualifying data centers may be eligible for sales tax exemptions; income, franchise, and property tax incentives; cash; and grants based on meeting and complying with specific requirements.

This column examines sales tax incentives for data centers, highlighting recent developments in Arkansas, Kentucky, Louisiana, and New Jersey. It provides practical guidance on taking full advantage of the benefits of sales tax incentives, maintaining compliance with their requirements, and understanding the nuanced provisions specific to each program.

Types of Data Centers

A data center is a physical facility that is used to store critical applications and data. There are several types of data centers, each designed to meet different business needs, operational requirements, and levels of security and scalability:

- An enterprise data center is owned and operated by a single organization to support its internal information technology (IT) requirements. The market share of enterprise data centers is on the decline: In 2018, approximately 60 percent of data center capacity was on premises *versus* 37 percent in 2024. By 2029, that number is projected to decline to 20 percent.[1]
- Hyperscale data centers are advanced facilities managed by major technology companies such as Amazon and Google and designed to provide large-scale cloud computing and data storage solutions. These expansive, highly customized centers have become the dominant type of data center, accounting for 37 percent of the market as of July 2024.[2]

- Cloud data center is infrastructure owned and operated by a cloud services provider such as Amazon Web Services (AWS), Google Cloud, or Microsoft Azure to support customers' IT needs.
- A managed services data center is owned and managed by a third party. Instead of purchasing IT physical assets outright, the business leases the equipment and infrastructure from a third-party service provider.
- Co-location data centers are third-party facilities where businesses can rent physical space to house their servers and other IT equipment. For organizations that do not require or prefer not to operate their own data center, co-location offers a flexible and cost-effective solution.
- Edge data centers are small, decentralized facilities located closer to end-users or devices, enabling faster data processing and reduced latency by handling information locally.

Overview of Available Tax Incentives

Data center incentives vary by jurisdiction and may include sales tax exemptions; income or franchise tax credits, exemptions, or favorable sourcing methodologies; and property tax abatements.[3] Each jurisdiction has its own procedures for obtaining an exemption—which must be carefully followed—as well as specific requirements regarding the equipment eligible for exemption. While this column focuses on sales tax exemptions, it is also important to consider what additional benefits should be reviewed during the negotiation process.

The remainder of this section surveys incentives available by tax type.

Sales Tax Incentives

Sales tax incentives typically include exemptions for purchases of specified tangible personal property to be installed or incorporated into the data center. This may include ancillary equipment, such as heating, ventilation, and cooling equipment and security equipment, that will help the data center operate. Some states also provide exemptions for purchases of electricity, backup generators, and energy sources to assist with the cost of operating the data centers.

When the exemption is claimed determines whether the purchaser can obtain the exemption at the time of purchase—thus avoiding being temporarily out of pocket for sales tax—or must pay the tax and then file for a refund. For example, Pennsylvania provides owners, operators, or qualified tenants of data centers with a certificate of exemption (Form REVK-704) that must be presented to the vendor along with Pennsylvania exemption certificate (Form REV-1220) within 60 days of the purchase or lease of exempt computer data center equipment.[4] The option of using the exemption certificates at the time of purchase allows the purchaser to preserve cash flow.

Minnesota provides a 20-year sales tax exemption on computers, servers, cooling and energy equipment, energy use, and software for companies that build new data centers of at least 25,000 square feet with a $30 million investment over 48 months or refurbish existing centers with a $50 million investment within 24 months.[5] However, sales tax must be paid upfront by the purchaser, and after the Minnesota Department of Employment and Economic Development approves the certification of a facility, the owner of the qualifying business may apply for a sales tax refund on eligible purchases within three and a half years from the invoice date. If the contractor, subcontractor, or builder paid the tax, then that person must furnish to the owner of the qualifying business a statement that includes the cost of the exempt items and the taxes paid on them, so that the owner may apply for the available refund within the limitations period.[6]

Income Tax Incentives

Incentives that exempt income or franchise taxes are generally less prevalent than those available for sales and property taxes. Where such incentives do exist, they are most often structured as job creation credits that can be used to offset tax liabilities. However, incentive programs offered in states such as Mississippi provide substantial income tax exemptions and franchise tax benefits, representing an alternative approach to encouraging investment within their jurisdictions.

For certified business enterprises, Mississippi exempts earnings from income tax and the value of capital used, invested, or employed from franchise tax.[7] To qualify, a business enterprise must own or operate a data center with a minimum capital investment of $20 million and create a minimum of 20 new full-time jobs with a specified average wage.[8]

The state also offers sales and use tax exemptions for the purchase or lease of component building materials and equipment for initial construction of facilities or expansion of facilities that are certified by the Mississippi Development Authority, as well as replacement hardware, software, and other technology necessary to operate a data center.[9]

Other states such as Texas offer benefits through favorable sourcing methodologies. For example, while Texas generally applies a cost-of-performance approach for sourcing receipts for franchise tax purposes, it has amended its administrative rules to adopt a market-based sourcing method specifically for Internet hosting service receipts.[10] Under this amended sourcing approach, receipts are sourced to Texas only if the customer consuming the service is physically located in the state.[11] Under this sourcing rule, gross receipts derived from out-of-state customers accessing the center for data storage and retrieval, database search services, or processing of data in Texas do not count toward the sales tax numerator in the apportionment factor, which affects the provider's tax liability.

Property Tax Incentives

Data center property tax incentives generally provide for abatements against the taxable value of real and personal property over a specific period (generally 10–20 years). Property taxes are typically administered and negotiated at the local level, even when authorized by state law. Consequently, engaging professionals with strong local connections and expertise with data centers is essential to securing favorable terms and positive recognition for a company's anticipated investment in the community.

For example, Montana provides for a partial personal property tax abatement of 75 percent of the tax due for 10 or 20 years dependent on the terms sought by the applicant.[12] If abatement is granted, the executive director of the Office of Economic Development notifies the county assessor of each county where a data center is located of the approval of the partial abatement, including the duration and percentage of the partial abatement granted.

As another example, Maryland has statutory programs under which local taxing authorities can exempt or reduce the taxation of data center property for centers that meet qualified data center criteria: depending on the location, investing at least $2 million or $5 million of qualified personal property into the facility.[13]

In jurisdictions that allow property tax assessments, facility owners may use cost-segregation analyses to distinguish between real and personal property assets. This process can enable accelerated depreciation deductions for shorter-lived components, support alternative valuation methodologies, or result in reduced property tax assessments.

Overview of Qualification Requirements

While incentive requirements vary by state, applicants seeking data center incentives generally must contractually commit during the precertification process to meeting statutory criteria. Those criteria typically include minimum financial investment, creation of new jobs, investment in specified types and sizes of infrastructure, and other state-specific requirements. Those requirements and their corresponding benefits should be reviewed in the project's planning stages to understand which program best fits the company's objectives.

The minimum capital investment varies widely across state incentive programs, ranging from $2 million to $500 million. For example, Maryland allows sales tax incentives for up to 10 years based on a $2 million dollar investment in specified areas, whereas Arkansas requires that $500 million be invested over the first five years from the date of the certificate of occupancy.[14] Various factors can affect the amount of investment required to meet state thresholds, including location in the state, renovation *versus* new construction, technology and sustainability requirements, and operational efficiency and lifespan.

More than 15 states require that a qualifying company create a minimum number of jobs related to the data center. Qualifying jobs are usually measured based on the wage relative to the median income at the location of the data center and sometimes must be created within a prescribed period. For example, Alabama requires data processing centers to create at least 20 new jobs with a minimum annual wage of $40,000, although the statute does not specify the period over which those jobs must be created. Notably, the incentives associated with such projects can extend from 10 to 30 years.[15] In comparison, Illinois requires 20 jobs with wages at 120 percent of the median county wage over five years.[16]

Some states require that companies pay a minimum amount in payroll (for example, Arkansas requires at least $1 million in the state over two years; Ohio requires at least $1.5 million at the project site annually), while others do not have a set income requirement (Idaho).[17]

Some states impose facility size requirements to qualify. Iowa requires that the facility be at least 5,000 square feet in the aggregate and comply with the sustainable design and construction requirements established by the state building code commissioner.[18] Minnesota requires data centers to be at least 25,000 square feet.[19]

Clean energy also affects requirements. For instance, Arizona requires data centers to attain certification under energy star or green globes standards, and Illinois requires facilities to be carbon neutral or certified under a variation of green building standards.[20]

Energy requirements may also become part of the conditions. For example, Florida's definition of a data center property subject to sales tax exemption requires the facility to have a critical IT load of at least 15 megawatts and a critical IT load of at least 1 megawatt dedicated to each individual owner or tenant of the data center within five years of the commencement of construction of the center.[21]

The primary use of a data center could affect the center's eligibility for incentives. For example, Arkansas excludes data centers primarily engaged in cryptocurrency mining operations from the exemption.[22]

The requirements do not always have to be met by a single entity, particularly in co-location environments where qualifying tenant investments and job creation can be combined with the owner's and operator's investments to reach the minimum standards.

Survey of Select States with New Data Center Sales Tax Incentives

Arkansas

Effective October 1, 2025, Arkansas amended its sales and use tax exemption for qualified data center costs to support the purchase of data center equipment; eligible data center costs; services purchased in conjunction with developing, acquiring, constructing, expanding, renovating, refurbishing, and operating a qualified data center; and electricity used by a qualified data center.[23]

The new law reduces the investment requirement for a qualified data center from $500 million to $100 million.[24] The compliance period for the investment is five years and begins on commencement of facility construction.[25] Also, the annualized minimum compensation requirement of $1 million must be met and may include indirect payments to individuals performing services in Arkansas over the two calendar years following the calendar year in which the facility commenced operations.[26] The data center structure and equipment can now be located on adjacent tracts of land in Arkansas and may include additions to or expansions of the facility.[27] Lastly, the project must receive a positive cost–benefit analysis from the Arkansas Economic Development Commission.[28]

Eligible data center costs subject to exemption include expenditures for the development, acquisition, construction, expansion, renovation, refurbishment, and operation of a qualified data center. That includes costs of land, buildings, site improvements, modular data centers, computer data center equipment acquisition and permitting, lease payments, site characterization and assessment, engineering, and design used directly and exclusively in a qualified data center.[29]

Arkansas also created an exemption for a qualified large data center that needs to meet the investment of at least $2 billion within 10 years of the commencement of facility construction.[30] Similarly, there is the annualized minimum compensation requirement of $3 million that must be met along with similar terms, as noted above.[31]

Kentucky

On July 15, 2024, Kentucky began offering a sales tax exemption on data center equipment purchased for use in a qualified data center project.

The term "data center equipment" includes a broad scope of items, including servers, routers, connections, monitoring and security systems, fiber optic cabling and network equipment, computer software, and other tangible personal property essential for operating a data center that may be purchased exempt from sales and use tax following preliminary project approval. Construction equipment, building and construction materials intended for permanent incorporation as improvements to real property, electricity used by the facility, and administrative office equipment do not fall under the exemption.[32]

To qualify for the sales tax exemption, the data center must meet the requirements set by the Kentucky Economic Development Finance Authority (KEDFA). On approval, KEDFA will issue a certificate of exemption, which the company can use when making qualified purchases. Beginning September 1, 2025, and annually on or before every September 1 thereafter, a preliminarily approved company must report to the Department of Revenue on a fiscal-year basis an itemized schedule of data center equipment claimed and purchased tax-free.[33]

- To be eligible for exemption, a qualified data center project must meet minimum capital investment requirements on or before the fifth anniversary of preliminary approval. Owners, operators, or co-location tenants must invest at least $450 million, and project organizers must invest at least $150 million. The project also must be located in a consolidated local government having a population of at least 500,000, as determined by census data.

A qualified data center project provides infrastructure through acquiring, leasing, rehabilitating, expanding, or constructing at least one building that:

- Houses a group of networked server computers to centralize the storage, management, and dissemination of data and information for a single project; and
- Contains dedicated cooling equipment for the computing machines and related infrastructure; extra capacity for data redundancy, including the ability to maintain or replace equipment without a system shutdown; and physically isolated systems to avoid disruption from both planned and unplanned events.

A data center project will not meet qualification requirements if it results in the replacement of existing data centers in Kentucky, applies for or accepts any other economic development incentives under Kentucky law, or benefits from the sales and use tax exemption for the sale or purchase of electricity used in commercial cryptocurrency mining.[34]

Louisiana

Act 730, enacted in June 2024, provides a state and local sales and use tax exemption on data center development and related services and qualified data center equipment.[35]

Data centers include a facility, campus of facilities, or interconnected facilities in Louisiana with the primary business purpose of processing, storing, retrieving, or communicating data and are developed to power, cool, secure, or connect its own equipment or the equipment of its customers.[36]

The term "data center equipment" includes a broad scope of equipment or software purchased or leased for the processing, storing, retrieving, or communicating data.[37] Excluded from the exemption are office equipment or supplies, equipment or supplies used primarily in sales activities or transportation activities, non-qualified tangible property that is incorporated into real property, and tangible personal property that is rented or leased for one year or less.[38]

To qualify as an approved data center by the Department of Economic Development, the facility operator must confirm that the project will create at least 50 new direct, permanent jobs in Louisiana and intends to invest a minimum of $200 million in new capital in the state between July 1, 2024 and July 1, 2029.[39] On approval, the data center will issue a direct payment number that can be used to make purchases without the payment of sales tax. The initial term of the rebate is 20 years with the possibility of a 10-year extension. However, the Department of Economic Development may terminate the agreement if the recipient is unable to fulfill its obligations.[40]

Sales tax overpayments found on an approved data center's exempt purchases are not eligible for interest on any refunded amounts *via* the rebate.[41]

New Jersey

New Jersey provides a tax credit to businesses that are primarily engaged in the artificial intelligence (AI) industry or the large-scale AI data center industry. A business is considered to be primarily engaged in an industry if more than 50 percent of its employees are engaged in AI-related activities or more than 50 percent of its revenue is generated from AI-related activities.[42] The use of AI applications in the furtherance of a company's own business operations does not count toward this engagement threshold.[43]

AI-related activities include developing new AI algorithms and techniques such as machine learning, natural language processing, and computer vision; creating AI-powered software and hardware products for various applications; medical AI modelling or programming; developing AI chatbots for customer service; AI development for vehicles; and collecting, storing, and managing the vast amount of data needed to train and use AI models.[44]

Eligible businesses must make a minimum capital investment of at least $100 million and create at least 100 new full-time jobs in the state.[45]

The tax credits are awarded on a first-come, first-served basis up to the lesser of:

- The product of 0.1 percent of the eligible business's total capital investment multiplied by the number of new full-time jobs,
- 25 percent of the eligible business's total capital investment, or
- $250 million.[46]

The amount of credit allowed may be applied against New Jersey tax liability. Eligible companies may also sell or assign the tax credit for not less than 85 percent of the transferred credit amount.[47]

Recommended Best Practices

For businesses planning to establish data centers, navigating the complex landscape of state and local tax incentives is essential. The availability of and ability to obtain such incentives are crucial in the data center selection process, alongside other considerations such as access to power infrastructure and grid reliability, connectivity to network and cooling infrastructure, security, and community support. These incentives can offer significant financial advantages but require a strategic approach to take full advantage of benefits and maintain compliance.

Below are key practical recommendations for reviewing and navigating data center sales tax benefits and mitigating areas that could lead to noncompliance:

- Identify and compare tax incentives across jurisdictions to determine if they align with the company's short- and long-term objectives. In addition to sales tax considerations, the review should include property tax abatements and income tax credits specifically for data centers. Assess qualification criteria, certification steps, and ongoing compliance requirements to ensure sustained benefits. Nontax considerations should also be weighed.
- Engage with local economic development agencies and tax professionals who understand the nuances of regional incentive programs and can assist in navigating the application process before executing contracts or making a public announcement about the chosen site for the data center. Local incentives may be negotiated separately and in addition to state benefits.
- Carefully review the terms and conditions associated with any tax incentives to comply with and understand any long-term commitments.
- Understand the scope of the exemption. For instance, while purchases of data center equipment may be

exempt under state law, purchases of general equipment for on-site offices are frequently excluded from sales tax exemptions. Equipment with mixed-use purposes—such as laptops, handheld devices, and motor vehicles used both inside and outside the data center—might be excluded from the exemption.[48]

- Understand the timing of the exemption. If sales tax must be paid upfront and later recovered through a refund claim following government approval or certification (such as in Minnesota), the responsible party for filing such a claim should be familiar with the process, expected timelines, and the speed with which refunds are typically processed. When expenditures have been made but project certification does not occur within the statutory window, a company should consider filing protective refund claims to preserve eligibility before the statute of limitations expires. Knowing whether the clock starts with preliminary approval or when construction begins can affect the viability of any claims.
- Similarly, in the pre-payment and refund states, be wary of the ability to obtain interest on refund payments. Some states, including Louisiana, prohibit payment of interest on refund claims related to exempt data center purchases.
- In states where purchases made during the construction of a data center are exempt from sales tax through the issuance of exemption certificates to vendors, there is a risk that, on audit, the purchaser may become liable for unpaid use tax or be subject to a clawback of benefits if the project fails to meet the prescribed requirements. Therefore, the party responsible for claiming the sales tax exemption should monitor the progress in meeting the requirements to ensure compliance and avoid creating potential sales tax exposure. If any potential exposure is significant, the company should consider the impact for financial statement reporting purposes.
- Be aware that some uses of data centers may disqualify the centers from exemption. For example, several states, including Arkansas and Kentucky, specifically exclude cryptocurrency mining operations from their exemptions. As a result, purchases that were initially exempt may become subject to tax if the intended use of the data center changes to include crypto mining activities.

ENDNOTES

1 Neal Weinberg, "5 Reasons the Enterprise Data Center Will Never Die" (Jan. 30, 2025) *www.cio.com/article/3808734/5-reasons-the-enterprise-data-center-will-never-die.html*.

2 Tania Tsoneva and John Affleck, CBRE, "Decoding Data Centers: Opportunities, risks, and investment strategies" (Jul. 17, 2024), available at *www.cbreim.com/insights/articles/decoding-data-centers*.

3 Some jurisdictions also offer negotiated credits, cash grants, or favorable financing options, which are outside the scope of this column.

4 72 Pa. Stat. §9931-D; *See* Computer Data Center Equipment Exemption Program (Feb. 2024), available at *www.pa.gov/content/dam/copapwp-pagov/en/revenue/documents/incentivescreditsprograms/computerdatacenterequipprog/documents/computer_data_center_equip_exemption_program_guidelines.pdf*. If the vendor refuses to accept the Exemption, the certified data center owner, operator or qualified tenant must pay the sales tax. The certified data center owner, operator or qualified tenant may seek a refund of the tax through a Petition for Refund filed with the Board of Appeals.

5 Minn. Stat. §§297A.68(42)(b), (c), (d), & (f).

6 *See* Revenue Notice #16-07: Sales and Use Tax—Exemptions—Qualified Data Centers; Revocation of Revenue Notice #12-11 (published Oct. 10, 2016).

7 Miss. Code Ann. §57-113-21.

8 Miss. Code Ann. §57-113-21(a).

9 Miss. Code Ann. §57-113-21(d).

10 34 Tex. Admin. Code §3.591(e)(13)(A). Texas defines the term "Internet hosting service" as providing an unrelated user Internet access to computer services using property that is owned or leased and managed by the provider and on which the user may store or process its own data or use software that is owned, licensed, or leased by the user or provider.

11 34 Tex. Admin. Code §3.591(e)(13).

12 NRS 360.754(4)(c); NRS 361.0683(2)(a).

13 Md. Code Ann. Tax-Gen. §11-239 & Tax-Prop. §7-248.

14 Md. Code Ann. Tax-Gen. §11-239(d); Ark. Code Ann. §26-52-456(a)(4).

15 Ala. Code §40-9B-3; Ala. Dept. of Rev., Summary of Alabama Taxes and Tax Incentives, *www.revenue.alabama.gov/wp-content/uploads/2025/05/summary.pdf*.

16 20 Ill. Comp. Stat. 605/605-1025(c), -(d).

17 Ark. Code Ann. §26-52-456(a)(4); Ohio Rev. Code Ann. §122.175(A); Idaho Code 63-3622VV(2)(j).

18 Iowa Code Ann. §423.3.95.b.(2); Iowa Department of Revenue, Data Center Sales and Use Tax Incentives, *revenue.iowa.gov/taxes/tax-guidance/sales-use-excise-tax/data-centers*.

19 Minn. Stat. §297A.68(42)(c).

20 Ariz. Rev. Stat. §41-1519.O.13 & 20 Ill. Comp. Stat. 605/605-1025(c)(5).

21 Fla. Stat. §212.08(5)(r)1.c.(III).

22 Ark. Code Ann. §26-52-456(a)(4)(B)(iii).

23 Ark. Cd. §26-52-456(b).

24 Ark. Cd. §26-52-456(a)(2).

25 Ark. Cd. §26-52-456(a)(4)(A)(i).

26 Ark. Cd. §26-52-456(a)(4)(A)(ii).

27 Ark. Cd. §26-52-456(a)(3).

28 Ark. Cd. §26-52-456(a)(4)(C).

29 Ark. Cd. §26-52-456(a)(2).

30 Ark. Cd. §26-52-456(a)(7).

31 Ark. Cd. §26-52-456(a)(7)(B).

32 Ky. H.B. 8, §§37-42.

33 Ky. Dept. of Rev., "Sales Tax Facts" (Jun. 1, 2024), available at *revenue.ky.gov/News/Publications/Sales%20Tax%20Newsletters/Sales%20Tax%20Facts%202024%20-%20Jun.pdf*.

34 *Id.*

35 La. H.B. 827, enacted on Jun. 19, 2024.

36 La. Rev. Stat. Ann. §47:305.73(A)(2).

37 La. Rev. Stat. Ann. §47:305.73(A)(3)(a).

38 La. Rev. Stat. Ann. §47:305.73(A)(3)(b).

39 La. Rev. Stat. Ann. §47:305.73(B)(2).

40 La. Rev. Stat. Ann. §47:305.73(B)(3).

41 La. Rev. Stat. Ann. §47:305.73(C).

42 N.J. Rev. Stat. §34:1B-397(a)(3).

43 *Id.*

44 *Id.*

45 N.J. Rev. Stat. §§34:1B-397 (b) and (c).

46 N.J.S.A. 34:1B-400.

47 NJ Rev Stat §34:1B-401.

48 72 Pa. Stat. §9931-D(c)(3).