Sales and Use Tax:

How the Wayfair decision impacts your business

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WKBOSS

Business Owners' Strategy Series

Sales Tax vs. Use Tax

Sales tax

- Generally, in-state to in-state transaction
- Imposed on the buyer, but collected by the seller
- Example: You purchase computers from an in-state seller

Sales Tax vs. Use Tax

Vendor's Use Tax

- Out-of-state to in-state transaction
- Imposed on the buyer, but collected by the seller
- Typically this is what generates most nexus arguments
- Example: You purchase computers from an out-of-state seller who does have nexus in your state

Sales Tax vs. Use Tax

Consumer's Use Tax

- Out-of-state to in-state transaction
- Imposed on the buyer, and remitted by the buyer
- Example: You purchase computers from an out-of-state seller who doesn't have nexus in your state
- Just because you aren't charged use tax, doesn't mean you don't have to pay it. Remittance rules differ by state. Missouri requires filing with at least $2,000 in annual purchases subject to tax.

Sales Tax vs. Use Tax

- Sales and use tax may have different rates in each state or locality
  - For example:
    - Many Missouri localities (including Columbia and Jefferson City) don’t have a use tax
    - MO has exemptions for manufacturing that apply for local use tax, but not local sales tax

Taxability

- What is typically taxable?
- Physical goods sold at retail
- Rentals of personal property (sometimes exempt if lessor paid tax on the purchase)
- Some services
- Some entertainment
- Watch out for delivery, handling and surcharges, these depend on the state and situation
- Depends on the state so best practice is to assume the sale is taxable until proven otherwise

Exemptions

- Resale – usually requires a resale certificate
- Manufacturing – could be full, partial, or not exempt based on the specific item and the state
- Food – often have reduced rates or exemptions but very state specific
- Services – often but not always exempt
- Non-profits – Usually don't charge or pay sales tax but must apply for exemption with the state.
- Specific to the product (some states exempt medical products, agricultural products, etc.)
- How do these work in other states?
  - State specific exemption forms that require registration
  - State specific exemption forms that don't
  - Streamlined Sales Tax Agreement Certificate of Exemption (covers multiple states)

Nexus

- Is your connection with another state enough for them to force you to collect tax?
- Historically physical presence was required in order to have nexus for sales and use tax (Quill vs. North Dakota - 1992)
- Examples of physical presence: Delivery trucks, inventory storage, salespeople or technicians in state

What Changed?

- The internet!
- More commerce is done remotely than ever
- Sales are often done online with companies that have no physical presence in the state of the consumer
- States are hurting for sales tax revenue because often consumers don't remit consumer's use tax as they should
- States had been whittling away at the physical presence requirement for years with provisions for "click-through" and affiliate nexus, and even proposals that apps on your phone and "cookies" left on your computer created physical presence

Wayfair

- South Dakota set an "economic" standard for nexus of:
  - The seller's revenue in South Dakota exceeded $100,000 annually
  - The seller had two hundred or more separate transactions with South Dakota customers annually

- In June 2018 the Supreme Court decided physical presence was no longer a requirement by siding with South Dakota in the case of Wayfair vs. South Dakota

State progress since Wayfair

- The Supreme Court's decision in favor of South Dakota allowed other states to follow suit
- Most states with a sales tax now have some sort of dollar threshold and many also have transaction thresholds
- Missouri does not yet have Wayfair thresholds. The legislature hasn't been able to come to agreement on how to use additional funds that would be collected
- Localities without would have to pass local use taxes before state action would help local budgets

https://www.streamlinedsalestax.org/for-businesses/remote-seller-faqs/remote-seller-state-guidance

How to assess whether you have an issue

- What do you sell and is it taxable anywhere?
- Do you have any traditional nexus issues? Some common issues include (but aren't limited to):
  - Delivery in company owned vehicles
  - Salespeople in state (this causes a sales tax issue, but usually not income tax)
  - Inventory storage in state
  - Warranty or installation work done in state
- Determine sales by state (based on delivery) and compare to each state's threshold
- Determine transaction counts by state and compare to each state's threshold

Example

- Company sells tangible goods that are taxable in all jurisdictions. Home office is in MO, they deliver on their own vehicles into IL. Nexus issues in red.

	Sales shipped to state	Transactions in state	Wayfair sales threshold	Wayfair Transaction threshold	Nexus notes
AR	271,320	276	100,000	200	
IA	168,459	243	100,000		
IL	98,157	101	100,000	200	Nexus due to delivery activity
MN	90,045	98	100,000	200	
MO	285,675	298	N/A	N/A	Home state nexus
OK	158,962	220	100,000		
SD	142,058	199	100,000	200	
TX	45,682	51	500,000		
WY	98000	205	100,000	200	

What to do if you have an issue

Silent compliance –start registering and filing without dealing with prior periods

- Significant audit risks, penalties and interest
- No statute for returns that weren't filed
- If you didn't collect tax from the customer, you now bear the burden
- Back taxes owed depend on whether this is a Wayfair issue in which you have a "compliance date" to go back to or if this is a traditional nexus issue in which there may be no limit
- Registration with the Department of Revenue is usually required prior to filing. Secretary of State registration is sometimes also required.

What to do if you have an issue

Voluntary disclosure programs

- The state usually makes you file back returns to either the Wayfair compliance date or a specific number of years if your nexus pre-dated Wayfair
- In exchange you pay reduced penalties (but no reduction in interest)
- Not all states have voluntary disclosure programs, but many do
- Taxpayer can usually start the process anonymously

What to do if you have an issue

Amnesty programs

- Rare, but potential if opportunity to fix prior periods if you don't qualify for voluntary disclosure
- Often only offered for a limited time

Software and Accounting System Considerations

- Can your software calculate the location specific sales tax on each sale? There are over 10,000 sales tax jurisdictions in the US!
- Do you need to get an add-on or subscribe to a service that integrates with your software or will you need special programming? Beware – rates change often so inputting rates just once isn't an option.
- Do you have the capacity to prepare these returns in house or do you need to enlist extra help? Sales tax can be on monthly, quarterly, semiannual, or annual reporting periods and it will vary by state.
- Sales tax audits are common. Do you have the capacity to deal with those and the ability to produce exemption certificates to substantiate your filings?
- There are software programs that do nothing but sales tax and also companies you can outsource tax filing obligations to.

Is this only a sales and use tax issue?

- Income taxes –
  - There was never a requirement for physical presence
  - Sellers of tangible personal property whose only activity in a state is the solicitation of sales of that property are protected from income-based taxes by PL 86-272. They are not protected from minimum fees or non-income-based taxes.
  - Some states have created bright-line factor presence thresholds based on dollar amounts of sales, property and payroll. States with income taxes and these factor presence thresholds include (but more are added each year) - AL, CA, CO, CT, HI, MA, MI, NY, PA, TN
    - Example: CA's 2019 thresholds are $601,967 sales, $60,197 property, $60,197 payroll or 25% of total of each of those. If you exceed those thresholds but are protected by PL 86-272, then you still owe the $800 minimum fee.
  - Prior to Wayfair, some might have wondered whether factor presence standards for income taxes would be supported by the Supreme Court. Now there is little doubt.

Is this only a sales and use tax issue?

- Non income type taxes – This includes franchise tax, commercial activity tax, commerce tax, B & O tax, etc.
  - No protection is offered by PL 86-272 because they are generally gross revenue based instead of net income based. A few deductions might be allowed.
  - States with these types of taxes currently include (but aren't limited to) – AL, NV, OH, OR, TX, WA.
  - Each of the states mentioned has a sales threshold that determines your nexus.

Has Covid-19 changed anything?

- State departments of revenue have been impacted by stay at home orders just like everyone else. This might be slowing current audit activity but will that last?

- Will increased changes in shopping habits and the economic downturn put even more pressure on state budgets?
  - Will audits become more aggressive?
  - Will products such as digital goods and services be taxed more frequently?
  - Will sales tax rates increase?

- What impact does new telecommuting in other states have on nexus (income, sales, withholding tax)? Some states have offered specific guidance which is often taxpayer friendly.

What should you do next?

- Don’t wait
- Work with your tax advisors to confirm your suspicions and walk you through the issues above
- Prioritize the items that need your attention first and get started

Questions?

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- Jessica joined Williams-Keepers LLC in 2008, having graduated from the University of Missouri with a bachelor's degree and master's degree in accountancy.
- Jessica is a member of the American Institute of Certified Public Accountants and the Missouri Society of Certified Public Accountants. She is also a member of the Columbia Metro Rotary and volunteers with the Heart of Missouri United Way.