Sales Tax Redefined

South Dakota v. Wayfair

Since June's Supreme Court's ruling on *South Dakota v. Wayfair Inc.*, there have been many discussions, newspaper articles and media coverage. As a Washington based retail/wholesale business, you may think that this ruling doesn't apply to you, but you are probably wrong. If you are making sales to customers who are located in other states, this ruling could put you on the path to having nexus in those states, and not being prepared could have enormous consequences.

Nexus is defined as "sufficient presence" in a state, and once nexus is established in a state, you are required to collect and pay taxes in that state. In the previous major Supreme Court decision on this issue in 1992, *Quill Corp v. North Dakota*, the standard for nexus was physical presence holding that a business needed to have employees, sales people, warehouses, or some other tangible representation in the state to be subject to tax.

The *Wayfair* ruling in June has completely altered the nexus landscape. States are now adopting economic nexus regulations based on either the dollar amount of sales to that state, the number of sales to that state or a combination of both. Many states *already* have similar rules for income tax.

Moving forward, you'll need to devise a game plan to ensure compliance with all states.

For sales tax, many states are adopting a threshold of $100,000 of sales or 200 separate transactions into the state, although some have set different thresholds. For example, Pennsylvania has set their sales threshold at $10,000, while California has not yet set a threshold.

The best approach is to register to collect sales tax in states where you have nexus. This will require a lot of work, but there are some third-party vendors that can assist you with the process, such as Avalara, Vertex and TaxJar. Check out their websites for the latest state-by-state guides to sales tax economic nexus rules.

If you are a wholesaler that ships products to other states, you have likely not been keeping resellers permits for your out-of-state customers. We recommend that you start to collect these resellers permits, as you may now have nexus in these states and will need to provide them if/when you are audited. Trust us – it's much easier to do this now versus when you are under audit.

Another thing to be aware of is that many states do not have clear thresholds for when you must file an income tax return in the state, and with economic nexus, a state could request an income tax return even if you have no employees in the state. These rules can be complex, and there are some important differences from sales tax, especially if you are only selling goods. If you receive a “Nexus Questionnaire” or any broad information request about your business activities from a state, even if you are already registered for sales tax, *please contact us for assistance*. Because the questions are not always clear and sometimes based on specific circumstances, it can be easy to answer them in a way that could cause unnecessary tax.

TIP: If you want to be proactive with your point-of-sale, QuickBooks, Xero data, etc., we recommend tracking all out-of-state sales in a detailed matter. Usually companies post all out-of-state sales to one non-taxable code. You could setup a separate tax rate code set to 0% for each and every state that you sell to. This will provide detailed sales reports to track the gross sales and individual transactions, enabling you to determine when you have nexus in each state.

But wait, there’s more…

Some states, including Washington, now have notice and reporting requirements for use tax. Retailers who do not meet the requirements to collect sales tax may be required to notify their customers of their obligation to report and pay use tax on their purchases. There is also an annual requirement for the retailer to provide information on taxable purchases to both their customers and the state. The penalties for not complying to these requirements are significant.

The states that currently have notice and reporting laws are Alabama, Colorado, Kentucky, Louisiana, Oklahoma, Pennsylvania, Rhode Island, South Dakota, Vermont and Washington. If you have any sales sourced to these states, it would be wise to register and collect sales tax on those sales, avoiding the use tax reporting requirements.

Understanding where economic nexus exists and how policies differ from one state to the next is essential for any business that makes sales in multiple states. Please give us a call if you need any assistance or guidance.