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MOST STATES NOW REQUIRE REMOTE SELLERS TO COLLECT SALES TAX



■ Companies should assume that economic nexus is here to stay following last year's *South Dakota vs. Wayfair* Supreme Court decision and plan accordingly. Nevertheless, for many small- and medium-size companies, there may be no sales tax exposure given current state tax thresholds.

business exemption for retailers with less than \$100,000 or 200 transactions in annual sales.

The court noted that the law provided small-business sellers with a reasonable exemption and prohibited retroactive collection. The court also observed that South Dakota is part of the Streamlined Sales and Use Tax Agreement (SSUTA). The SSUTA is intended to address tax collection burdens by creating a single, state-level tax administration, simplified tax rates and tax returns, uniform definitions, a central electronic registration system for all member states, and the availability of free tax administration software. (There are currently 23 participating SSUTA states in addition to Washington, D.C. For more information, visit www.streamlinedsalestax.org.)

Economic nexus for remote sellers is based on sales revenue or the number of transactions or both. Companies should assume that economic nexus is here to stay following last year's Supreme Court decision and plan accordingly. The court decision has made it less likely that the U.S. Congress will address the issue through federal legislation.

Companies without any physical presence in a state can now be required to collect sales tax based on their sales volume. In June 2018, the U.S. Supreme Court ruled in favor of a South Dakota state law requiring remote sellers to collect sales tax. (The term “remote” applies to internet, catalog and telephone sales, along with other types of transactions.) The court overturned the 1992 *Quill* decision, which required a physical presence to create “substantial nexus,” thereby allowing state sales tax collections.

A company can now have “economic nexus” in a state without otherwise having a physical presence. While granting South Dakota the right to require tax collections based on the volume of sales into the state, the court did not specifically rule on what amount of sales triggers an economic presence. Rather, it sent the *South Dakota vs. Wayfair* case back to a lower court to address the issue of whether the state law

placed an undue burden on interstate commerce. The parties (Wayfair, Overstock and Newegg) then settled out of court in October 2018.

While the question of “undue burden” is technically unsettled, the Supreme Court ruling provided guidance when it deemed the South Dakota law as setting a sensible small-business safe harbor. The South Dakota law established a small-

States have been eager to collect sales tax revenues for years and have been quick to enact laws and update regulations following the court ruling. Since the court indicated that the thresholds set under the South Dakota law seemed reasonable (\$100,000 or 200 transactions), many states have adopted the same thresholds or are setting higher levels.

How Should Companies Respond to the New Developments Governing State Sales Tax?

First, does your company exceed the threshold for remote sales tax nexus? For most states, the threshold is relatively high: \$100,000 or 200 transactions in annual sales. For many small and medium-size companies, there may be no exposure.

If your company does meet a state's economic nexus threshold, should a company immediately register, collect and remit the taxes? Not necessarily.

For all companies, this is a time to step back and review all potential liabilities. For example, is there a chance that your company already had physical nexus and should have been collecting sales taxes due to the presence of a sales representative, a distribution or storage facility, or participation in a trade show? Some states also have economic franchise and other tax obligations. It is important to review the status of a company's presence in a state before registering to collect sales tax.

Returning to the economic nexus threshold issue for remote sales, states may vary in how they are calculated. Revenues may be based on gross sales, retail sales or taxable sales. The number of transactions may encompass one agreement, multiple invoices, or monthly subscriptions. Each state will define when a taxable year has commenced when calculating whether the company is below or above the economic threshold. If a company is close to the exemption threshold for a specific state, it should then review how the state calculates nexus.

All states have a formal or informal voluntary disclosure agreement (VDA) process for addressing tax liabilities. If a company determines that a tax exposure already exists but has not been paid, the company should take advantage of the VDA process

Current Out-Of-State Sales Tax Collection Requirements, as of May 1, 2019

State	Sales Tax Collection Start Date	Exemption for Minimum Sales
Alabama	October 1, 2018	\$250,000
Alaska	No Sales Tax	
Arizona	Proposed	\$100,000 or 200 transactions
Arkansas	July 1, 2019	\$100,000 or 200 transactions
California	April 1, 2019	\$500,000
Colorado	May 31, 2019	\$100,000 or 200 transactions
Connecticut	December 1, 2018	\$250,000 or 200 transactions
Delaware	No Sales Tax	
District of Columbia	January 1, 2019	\$100,000 or 200 transactions
Florida	Proposed	\$100,000 or 200 transactions
Georgia	January 1, 2019	\$250,000 or 200 transactions
Hawaii	July 1, 2018	\$100,000 or 200 transactions
Idaho	June 1, 2019	\$100,000
Illinois	October 1, 2018	\$100,000 or 200 transactions
Indiana	October 1, 2018	\$100,000 or 200 transactions
Iowa	January 1, 2019	\$100,000
Kansas	Proposed	\$100,000
Kentucky	October 1, 2018	\$100,000 or 200 transactions
Louisiana	Enforcement date TBD	\$100,000 or 200 transactions
Maine	July 1, 2018	\$100,000 or 200 transactions
Maryland	October 1, 2018	\$100,000 or 200 transactions
Massachusetts	October 1, 2017	\$500,000 or 100 transactions
Michigan	October 1, 2018	\$100,000 or 200 transactions
Minnesota	October 1, 2018	10 transactions totaling \$100,000 or 100 retail transactions
Mississippi	September 1, 2018	\$250,000
Missouri	Proposed	\$100,000 or 200 transactions
Montana	No Sales Tax	
Nebraska	January 1, 2019	\$100,000 or 200 transactions
Nevada	November 1, 2018	\$100,000 or 200 transactions
New Hampshire	No Sales Tax	
New Jersey	November 1, 2018	\$100,000 or 200 transactions
New Mexico	July 1, 2019	\$100,000
New York	January 15, 2019	\$300,000 or 200 transactions
North Carolina	November 1, 2018	\$100,000 or 200 transactions
North Dakota	October 1, 2018	\$100,000 or 200 transactions
Ohio	January 1, 2018	\$500,000
Oklahoma	July 1, 2018	\$10,000 [\$100,000 under consideration]
Oregon	No Sales Tax	
Pennsylvania	April 1, 2018	\$100,000
Rhode Island	August 17, 2017	\$100,000 or 200 transactions
South Carolina	November 1, 2018	\$100,000
South Dakota	November 1, 2018	\$100,000 or 200 transactions
Tennessee	Proposed	\$500,000
Texas	January 1, 2019	\$500,000
Utah	January 1, 2019	\$100,000 or 200 transactions
Vermont	July 1, 2018	\$100,000 or 200 transactions
Virginia	July 1, 2019	\$100,000 or 200 transactions
Washington	October 1, 2018	\$100,000 or 200 transactions
West Virginia	January 1, 2019	\$100,000 or 200 transactions
Wisconsin	October 1, 2018	\$100,000 or 200 transactions
Wyoming	February 1, 2019	\$100,000 or 200 transactions

since it limits the lookback period of tax liabilities (usually to three years), removes most if not all penalties, and sometimes reduces or eliminates interest. *Caution: The VDA process is not always available once you have registered to collect sales tax, so there is an incentive for conducting a comprehensive tax-risk assessment before registering.*

SEMA recommends that companies consult their accountant or tax professional regarding the issues raised.

The chart on p. 63 shows the current out-of-state sales tax collection requirements, as of May 1, 2019 but please note that these requirements and still changing.

Drop Shipments

A drop shipment is a way for the retailer to deliver a product to the customer via the manufacturer (or wholesaler or another retailer). There are many benefits, such as allowing the retailer to display the goods in a brick-and-mortar store or in a catalog or online without keeping the goods in stock.

There are essentially two transactions occurring in a drop shipment. The first is most likely a “sale for resale” from the manufacturer to the retailer. In that instance, the manufacturer will expect to be issued a resale certificate by the retailer, which is then responsible for collecting any applicable sales tax from the customer. The second transaction is when the retailer bills the customer (the product end-user). The second sale is taxable, as dictated by the laws of the state where the customer resides.

With the two sales transactions come two questions: Do either of the sellers (retailer and manufacturer) have nexus in the destination state? And is the sale from the manufacturer to the retailer a “sale for resale”?

The question of nexus depends on sev-

eral different scenarios. If the manufacturer has nexus in the state where the customer resides, then some type of resale certificate should be provided by the retailer to prevent the manufacturer from charging sales tax on the wholesale cost of the goods sold to the retailer. In turn, if the retailer has nexus in the state where the drop shipment occurs, the retailer will need to charge the customer sales tax on the retail cost of the property (and any delivery charges that are taxable). Below are the most common scenarios encountered with drop shipments but they could vary depending on the parties involved.

If neither the manufacturer or retailer has nexus in the destination state, there is no legal obligation to obtain an exemption certificate or to charge sales tax, assuming sales are below the state’s ‘economic nexus’ threshold for remote sellers but it’s a good practice to collect certificates even if not required.

If the manufacturer has nexus but the retailer does not, the manufacturer will be requesting a resale certificate from the retailer that is valid for the destination

state. While many states will accept a retailer’s “home” state certificate or registration number, some destination states require a certificate from that state. When a state specific certificate is required but the retailer cannot provide one, the manufacturer is required to charge sales tax to the retailer even though the sale is for resale. Some companies choose to voluntarily register in a jurisdiction so they can provide a resale certificate but that means that they will have to start collecting and remitting tax on all taxable sales into the jurisdiction.

If the retailer has nexus but not the manufacturer, then the retailer is obligated to collect the appropriate tax.

If both parties have nexus, the manufacturer will be expecting a resale certificate from the retailer, and the retailer will be collecting the appropriate tax.

Given the various scenarios and state laws, SEMA recommends that companies consult their accountant or tax professional for more information. ■