



Thank you for joining us!

The presentation will begin shortly

Current Sales & Use Tax Compliance Troubles and How to Manage Them

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Additional Information

Learning Objective To provide attendees with a timely update on sales/use tax issues and practical solutions for implementation	Instructional Delivery Methods Group Internet-based
Recommended CPE 1.0 CPE Credit	Recommended Fields of Study Taxes
Prerequisites None required	Advance Preparation None
Program Level Basic	Course Registration Requirements None
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Presenters

Meet the instructors



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State and Local Sales Taxes

Today's Topics

Sales taxes –

- Apply to both nonprofit organizations *and* commercial entities (hint: treatment of purchases versus sales differs) in almost 12,000 taxing jurisdictions
- The growing list across the country of what goods and services are subject to sales tax (think “digital” now taxable)
- The U.S. Supreme Court’s *Wayfair* decision (“nexus” -- which states do you need to be concerned about: where you have physical presence AND where you have “economic nexus”)
- More on a nonprofit entity’s sales as taxable versus exemptions for purchases (states differ)
- Tips for assessing your possible risks and liabilities
- Ideas for first resolving issues with the states, and implementing the right compliance procedures

Sales Tax

Sales Tax

Why do both nonprofit organizations care the same as commercial entities do?

Sales Tax: Why do nonprofits care?

A refresher

- Income tax exemption does not automatically confer sales tax exemption; check the states' rules.
- Some states have few or no exemptions for any nonprofit entities, even for exempt purpose purchases; tax is the same as for businesses.
- Where sales tax exemption is granted, it is generally for exemption from paying tax on purchases used in the entity's exempt function.
- Very rare is the exemption from charging tax on the entity's sales. General rule: the entity that is selling taxable goods or taxable services (more on that later) should be charging sales tax to the customer and remitting the tax to the state/locality.
- Each state differs regarding what goods and services are subject to that state's sales tax – for all sellers.



Recent developments:

What is now sales-taxable in our physical and digital world, and where are the states heading?

Recent developments:

What is sales-taxable

- No longer just goods, tangible personal property (but still sales of goods, e.g. routine sales of books, and even non-routine sales, e.g. silent auctions etc.)
- In some states, also “digital goods:” *electronically delivered* documents, books, music, movies, reports, software; also *electronically delivered* services such as information services.
 - Either via change to definition of tangible property, or via specific statutory lists.
- Initial goal was to collect tax on electronic versions of what was previously taxable tangible items, but there is lot more to it now.
- In some states, also some services: information services, data services, access to software as a service (in a few states, almost all services are taxed: Hawaii, New Mexico, South Dakota, West Virginia)
- Consider what goods and services you sell might fit into these taxable categories, requiring the **charging** of sales tax on your sales even though you are exempt from tax on purchases.

“Digital goods” are taxable:

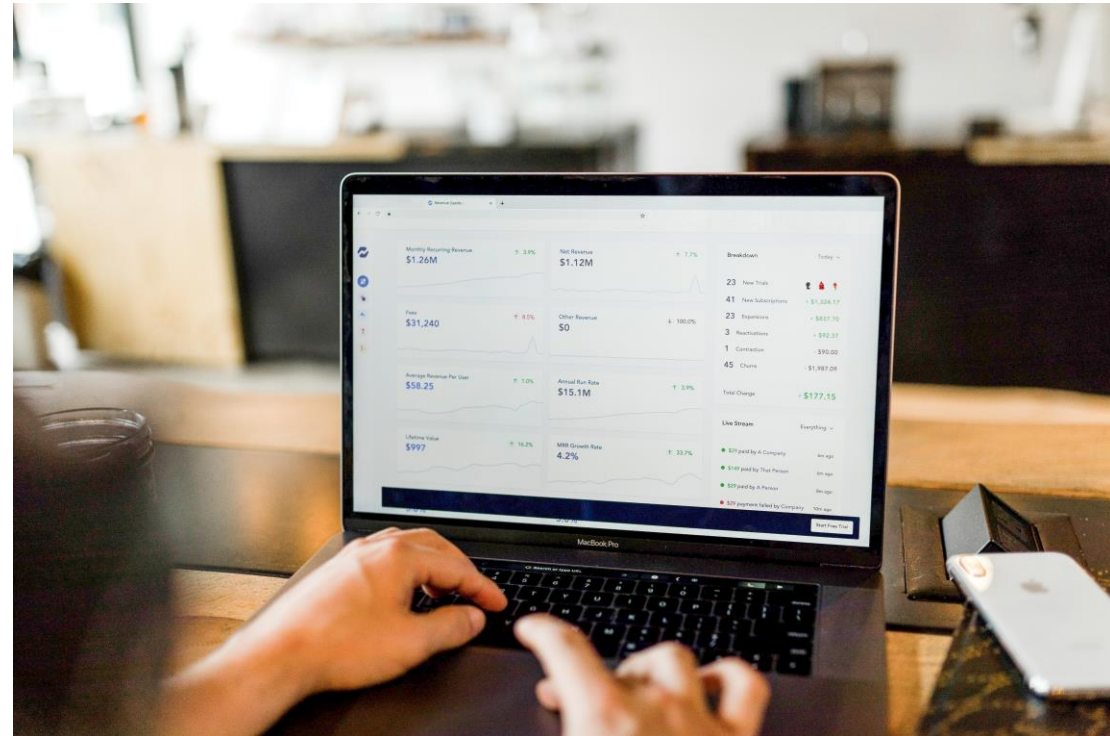
Must check the varied definitions in each state – where the customer is receiving the goods or where is the billing address:

- Alabama
- Arizona
- Arkansas
- Colorado
- Connecticut
- DC
- Georgia
- Hawaii
- Idaho
- Indiana
- Kentucky
- Louisiana
- Maine
- Maryland
- Minnesota
- Mississippi
- Nebraska
- New Jersey
- New Mexico
- North Carolina
- Ohio
- Pennsylvania
- Rhode Island
- South Dakota
- Tennessee
- Utah
- Vermont
- Washington
- Wisconsin
- Wyoming

Examples of “digital goods” sales taxation:

Must check each state for taxability, or not, and for varied definitions.

Examples: Maryland and DC do impose sales tax on digital products, while Virginia currently does not.



Examples of “digital goods” sales taxation: *Maryland*

Maryland taxes digital products and digital codes.

"Digital product" means a product that is obtained electronically by the buyer or delivered by means other than tangible storage media through the use of technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities. Per the statute, "digital product" includes:

- a work that results from the fixation of a series of sounds that are transferred electronically, including: prerecorded or live music or performances, readings of books or other written materials, and speeches, and audio greeting cards sent by email;
- a digitized sound file, such as a ring tone, that is downloaded onto a device and can be used to alert the user of the device with respect to a communication;
- a series of related images that, when shown in succession, impart an impression of motion, together with any accompanying sounds that are transferred electronically, including motion pictures, musical videos, news and entertainment programs, live events, video greeting cards sent by email, and video or electronic games;
- a book, generally known as an "e-book", that is transferred electronically; and
- a newspaper, magazine, periodical, chat room discussion, weblog, or any other similar product that is transferred electronically.

Per the Comptroller's Tax Tip #29, computer software is considered a taxable digital product.

Examples of “digital goods” sales taxation: *Maryland*

The statute also provides that "digital product" does not include:

- prerecorded or live instruction by a public, private, or parochial elementary or secondary school or a public or private institution of higher education;
- instruction in a skill or profession in a buyer's current or prospective business, occupation, or trade if the instruction is not prerecorded and features an interactive element between the buyer and the instructor or other buyers contemporaneous with the instruction;
- a seminar, discussion, or similar event hosted by a nonprofit organization or business association, if the seminar, discussion, or event is not prerecorded and features an interactive element between the buyer and host or other buyers contemporaneous with the seminar, discussion, or event;
- a professional service obtained electronically or delivered through the use of technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities;

Examples of “digital goods” sales taxation: *Maryland*

(Continued) The statute also provides that "digital product" does not include:



- a product having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities where the purchaser holds a copyright or other intellectual property interest in the product, in whole or in part, if the purchaser uses the product solely for commercial purposes, including advertising or other marketing activities; or
- effective July 1, 2022, computer software or software as a service (SaaS) purchased or licensed solely for commercial purposes in an enterprise computer system, including operating programs or application software for the exclusive use of the enterprise software system, that is housed or maintained by the purchaser or on a cloud server, whether hosted by the purchaser, the software vendor, or a third party.

Examples of “digital goods” sales taxation: District of Columbia

DC taxes digital goods.

Per the statute, "digital goods" means digital audiovisual works, digital audio works, digital books, digital codes, digital applications and games, and any other otherwise taxable tangible personal property electronically or digitally delivered, whether electronically or digitally delivered, streamed, or accessed and whether purchased singly, by subscription, or in any other manner, including maintenance, updates, and support. The term "digital goods" does not include cable television service, satellite relay television service, or any other distribution of television, video, or radio service subject to the gross receipts tax on providers of television, video, or radio service.

Examples of “digital goods” sales taxation: District of Columbia



"Digital audiovisual works" means a series of related images that, when shown in succession, impart an impression of motion, together with accompanying sounds. Digital audiovisual works include motion pictures, musical, videos, news and entertainment programs, and live events.

"Digital audio works" means works that result from the fixation of a series of musical, spoken, or other sounds, that are transferred electronically, including prerecorded or live songs, music, readings of books or other written materials, speeches, ringtones, or other sound recording. "Digital books" means works that are generally recognized in the ordinary and usual sense as books that are transferred electronically, including works of fiction, nonfiction, and short stories.

Regulations specify that computer software, both canned and custom, is subject to sales tax in DC.

Access to software as a service (SaaS) is taxable:

SaaS is commonly defined as cloud computing where the software is hosted by the vendor and accessed remotely by the customer. Is it the same as buying/licensing the software? Is there professional service involved?

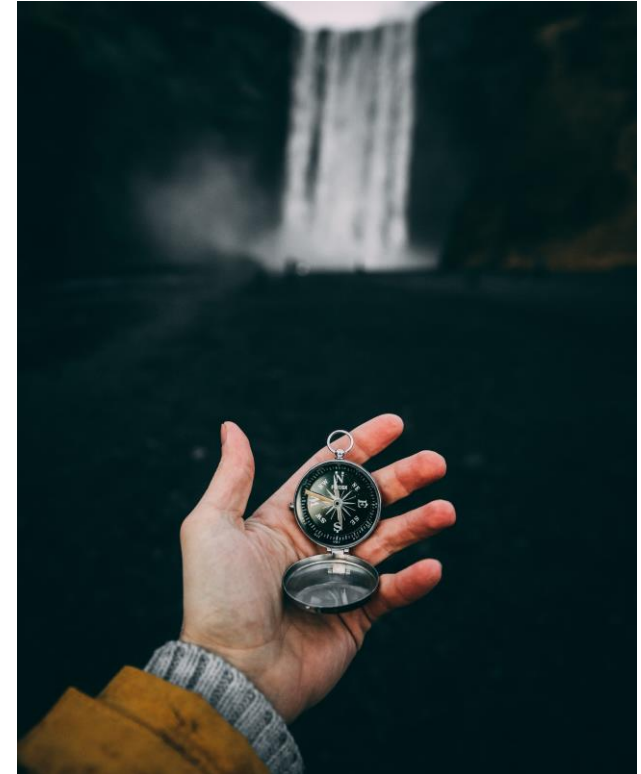
Must check the definitions and inclusions and exclusions in each state:

- Arizona
- Connecticut
- DC
- Hawaii
- Massachusetts
- Maryland (but exemptions for customized and enterprise software)
- New Mexico
- New York
- Ohio
- Pennsylvania
- Rhode Island
- South Carolina
- South Dakota
- Tennessee
- Texas
- Utah
- Washington
- West Virginia

“Information services” and “data processing services” are taxable in several states:

Must check the definitions and exclusions in each state:

- DC
- Florida
- Hawaii
- New Jersey
- New Mexico
- New York
- Ohio
- South Carolina
- South Dakota
- Texas
- Washington
- West Virginia



Examples: Taxable “information services” and “data processing services” -- Texas

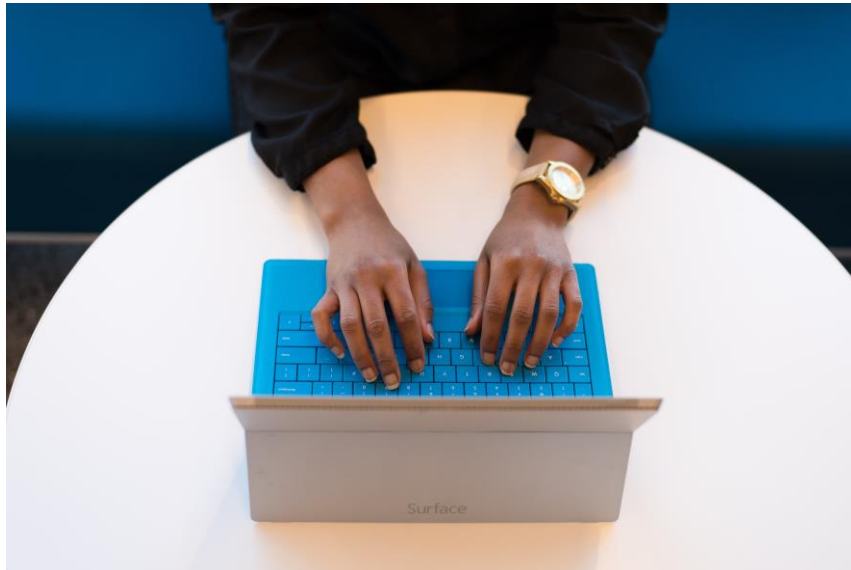
Texas imposes sales tax on both information services and data processing services.

Information services includes such things as newsletter, financial market reports, and data retrieval and/or research for stock quotations, court cases and the like.

Data processing services is the processing of information for the purpose of compiling and producing records of transaction, maintaining information, and entering and retrieving information. Examples include: data conversion services, editing client’s data, data storage, producing reports from client’s data, compiling and producing records.

The Texas Comptroller’s Office has issued many ruling interpreting and applying the law to various fact situations.

Examples: Taxable “information services” and “data processing services” –New York



New York imposes sales tax on information services.

Information services includes collecting compiling or analyzing information of any kind or nature and furnishing reports thereof to other persons, but excluding the furnishing of information which is personal or individual in nature and which is not or may not be substantially incorporated in reports furnished to other persons.

Polling Question #1

Does this discussion make you think that your organization is selling electronically delivered / digital products and services that may be subject to sales tax?

- A. *Yes*
- B. *No*
- C. *Unsure*

Sales Tax “Nexus”

The U.S. Supreme Court Wayfair ruling regarding sales tax collection responsibility

U.S. Supreme Court: *Wayfair, sales tax nexus*

On June 21, 2018, the U.S. Supreme Court issued its decision in *South Dakota v. Wayfair, Inc.* Docket No. 17-494, holding that a physical presence rule for sales tax collection requirements (“nexus”) is “unsound and incorrect” and therefore two prior decisions of the Court are overruled.

[South Dakota v. Wayfair](#)



U.S. Supreme Court:

Wayfair, sales tax nexus

Bottom line: persons and entities that sell sales-taxable goods and services to customers in a state in which the person or entity *has no physical presence*, but meets other thresholds, can be required to charge that state's sales tax to its customers and remit the funds to the state. That is, even if your only contact with the customer is via the internet, phone and mail, you may be subject to sales tax collection requirements.

U.S. Supreme Court:

Wayfair, sales tax nexus

Wayfair applies to all persons and entities, both for-profit businesses and not-for-profit entities, and applies to taxable goods as well as taxable services.

The ruling does not change:

- the fact that physical presence (employees or agents working in the state, an office or property located in the state, etc.) still creates nexus;
- states' laws that impact whether or not a nonprofit's purchases may be exempt from sales tax;
- the general rule that most nonprofits must charge sales tax on their taxable sales even if they are exempt from tax on purchases;
- the list of goods and services that are subject to or exempt from tax in each state.

It does change *who* can be required to charge + collect sales tax.

U.S. Supreme Court:

Wayfair

South Dakota law, S.B. 106, effective April, 2016:

- “An Act to Provide for the Collection of Sales Taxes From Certain Remote Sellers, To Establish Certain Legislative Findings and to Declare an Emergency”
- The Act requires out-of-state sellers to collect and remit sales tax if the seller delivers more than:
 - *\$100,000 of goods or services into the State, or*
 - *Engages in 200 or more separate transactions for delivery of goods or services into the State*
- This Act was purposefully designed to directly challenge the U.S. Supreme Court’s 1992 ruling in *Quill*, which had upheld the physical presence “nexus” requirement for sales tax collection enunciated by the Court in *National Bellas Hess in 1967*.

U.S. Supreme Court:

Wayfair

“Nexus:” the contact or connection a person or entity has with a state that allows the state to impose its laws on the person or entity.

Today we are discussing nexus in the context of state taxation, e.g. the requirements to charge/collect/remit sales tax.

Important note: nexus for taxation can be different from nexus for other legal requirements, e.g.:

- Registration to “do business:” seek advice of legal counsel.
- Registration to solicit contributions: seek advice of legal counsel.
- State taxation requirements: we CPAs can advise.



U.S. Supreme Court:

Wayfair

The prior cases:

- Both *Quill* and *National Bellas Hess* involved mail order sellers who had no physical presence in the state, i.e. no employee, independent agent, office, or warehouse.
- The Court in *National Bellas Hess* relied mostly on a Due Process analysis to hold that the lack of physical presence precluded the state from imposing its sales tax collection responsibility on the company (insufficient *minimal connection*).
- In *Quill*, there was additional consideration of the Commerce Clause, the burdens on interstate commerce (not *substantial nexus*) and the fact that the U.S. Congress has the power to regulate interstate commerce (Congress was invited to act); there was also concern for *stare decisis*, leaving the prior rule in place because it had been relied upon.

U.S. Supreme Court:

Wayfair

Now in *Wayfair*:

- South Dakota's supreme court had ruled in Wayfair's favor, i.e. that SB 106 was impermissible, saying that the *Quill* ruling still controlled, and only the U.S. Supreme Court (or U.S. Congress) could overrule that Supreme Court decision.
- The state appealed.
- Many amicus briefs were filed in support of both the company and the state.
 - *Burdens on interstate commerce, administrative costs, states should better enforce the collection of use tax from the buyers, stare decisis, etc.*
 - *States are losing many millions of dollars in taxes, modern technology makes the collection and remittance easier, etc.*

U.S. Supreme Court:

Wayfair

On June 21, 2018, the U.S. Supreme Court ruled in the state's favor and remanded the case back to the state court to further consider the law's validity *but without physical presence being a requirement*.

- *Quill* was wrongly decided.
- Physical presence is an incorrect interpretation of the Commerce Clause.
- It is an artificial test and does not align with modern e-commerce.
- It creates market distortions instead of resolving them, i.e. the competition between internet sellers and bricks-and-mortar sellers.
- It imposes arbitrary distinctions on economically similar entities.
- *Stare decisis* can no longer support the Court's prohibition of a valid exercise of the states' sovereign power. It is wrong to "ask Congress to address a false constitutional premise of this Court's own creation."

U.S. Supreme Court:

Wayfair

Note: The decision did not just say that e-commerce has changed the business world and therefore there should be a changed rule; the majority's opinion said that *Quill* was wrongly decided:

“

the physical presence rule of *Quill* is unsound and incorrect

U.S. Supreme Court:

Wayfair



Factors that were important to the Court in its voiced approval of the South Dakota law:

- Reasonable exception for small businesses, i.e. the \$100,000 and 200 transactions threshold.
- The law was specifically not retroactive.
- South Dakota is a member state of the Streamlined Sales Tax Project, whose goal is to bring uniformity and simplification to the sales tax compliance process for businesses. (Note that Maryland, DC, and Virginia are not members.)

U.S. Supreme Court:

Wayfair

The dissent, represented by Chief Justice Roberts, would have waited:

“I agree that *Bellas Hess* was wrongly decided, for many of the reasons given by the Court. The Court argues in favor of overturning that decision because the “Internet’s prevalence and power have changed the dynamics of the national economy.” But that is the very reason I oppose discarding the physical-presence rule. E-commerce has grown into a significant and vibrant part of our national economy against the backdrop of established rules, including the physical-presence rule. Any alteration to those rules with the potential to disrupt the development of such a critical segment of the economy should be undertaken by Congress. The Court should not act on this important question of current economic policy, solely to expiate a mistake it made over 50 years ago.” (*emphasis added*)

“Marketplace facilitators” and *Wayfair* nexus

In addition to entities who sell directly to customers, “marketplace facilitators” have also been targets of the states: Marketplace platform that contracts with third party sellers to promote their sales through the marketplace. Includes Standard” or “traditional” marketplaces where multiple sellers sell products, sometimes the same products, on a single platform; and “Referral” marketplaces, where customers may search for products and are then referred to a place to purchase those products. (Think: ETSY, EBAY and others.)

Marketplace collection provisions require online and other marketplaces to collect and remit sales and use tax if a retailer sells products on the marketplace.

All states that impose a sales tax now require tax collection by marketplace facilitators.

Note that in most states the seller must still file a sales tax return even if the tax was collected and remitted by the facilitator.

States' other pre-*Wayfair* attempts at nexus

“Click-through” nexus (the Amazon cases).

Nexus via affiliated / related entities.

Computer cookies create physical presence nexus.

Reporting to states and notices to customers if sales tax not charged ...



Reporting issues outside of *Wayfair*

Notice and Report Laws in many states since 2017, Colorado started it (upheld by U.S. Supreme Court in *Direct Marketing Assoc.* decision).

- Remote sellers who are not registered to collect sales tax must provide notice and reports to the state and to customers; failure to comply can lead to significant fines and penalties.
- Each state's laws are different, in general non-collecting retailers with gross sales of certain thresholds are required to :
 - *Include a notice on your website that use tax may be due on purchases*
 - *Include a transactional notice with each sale informing customers that use tax may be due*
 - *Send annual reminder notice to certain customers that they owe use tax*
 - *Send an annual notice to the state reporting information about the purchasers who owe use tax*
- For the most part, economic nexus and resulting compliance has supplanted these reporting rules.

States economic nexus laws

- Most states apply a threshold of \$100,000 of in-state sales OR 200 transaction to in-state customers
- That is, exceeding these thresholds creates nexus and therefore the requirement to charge sales tax
- A few states use only the dollar threshold, i.e., without the number of transactions
- A few states currently use different dollar thresholds, e.g.,
 - \$250,000 of in-state sales for Alabama, Connecticut, Georgia
 - \$500,000 of in-state sales for California, New York, Texas
- Note also that each state's law contained its own effective date, some in 2018, some 2019 – important for determining the date that compliance should have begun
- **Remember – physical presence still creates nexus, even without exceeding the economic nexus threshold.**

Much activity and interest post *Wayfair*

- **The \$40,000 question: Will Congress consider legislation?**
 - U.S. House Judiciary Committee meeting was held 7/24/2018 to discuss issues.
 - Stop Taxing Our Potential Act (S. 3180) of 2018 and again 2019
 - No Regulation Without Representation Act of 2017 (H.R. 2887) (NRRA)
 - Market Place Fairness Act (S. 698 of 2015)
 - Online Sales Tax Simplification Act (2016)
 - Remote Transactions Parity Act (2017)
- **Multi-state Tax Commission Annual Conference: 7/23/2018**
- **Streamlined Sales Tax Governing Board emergency meeting on *Wayfair*: 7/19/2108**
- **National Counsel of State Legislatures: Principles of State Implementation after Wayfair advisory letter issued 6/29/18**
- **South Dakota Supreme Court to issue ruling on the remand**
- **Protecting Small Business from Burdensome Compliance Costs Act (H.R. 6724; 9/6/2018)**

Polling Question #2

Did Wayfair impact how you look at sales taxes?

- A. *Yes*
- B. *No*
- C. *Unsure*

Post *Wayfair* compliance – how to assess outstanding risk

- Which states' laws may apply to us (“nexus”)?
 - Where do we have physical presence (an employee working in a state either permanently or on a visit basis; a physical location like office, inventory, property)?
 - For “economic nexus”:
 - In which states are our customers?
 - How much is our total annual sales volume in each state? Focus on those with \$100,000 or more.
 - How many transactions do we conduct in each state each year? Focus on those with 200 or more.
 - What is each state's threshold for requiring sales tax to be charged, e.g. sales dollar amount (\$100,000 or different) or number of transactions (200 or different, or is the number of transactions irrelevant)?

Post *Wayfair* compliance – tips for assessing outstanding risk

- Do we sell items or services that are taxable in the states where we have nexus, including “digital” goods and services? Might there be exemptions for some of our sold items, e.g., educational materials sold to schools?
- In the states where we meet the nexus threshold, do we have exempt customers from whom we will need to receive exemption certificates in order to legally avoid charging them the sales tax?
- How long have we had nexus in each state?
- Based on nexus and taxability of our sales, what is the estimated amount of tax owed?
 - Entity risk level? Accounting “materiality”? V. States want it all?
- Should we take advantage of states’ “voluntary disclosure” procedures to remit our liability and limit penalties and amount owed?



Post *Wayfair* compliance procedures

- What accounting and processing mechanisms do we need to have in place to identify taxable transactions, bill the tax on our invoices, collect the tax from our customers, and remit the tax to the states?
 - Do we use a marketplace facilitator who will charge, collect and remit the tax on our product sales?
 - Should we engage an outside servicer to coordinate with our sales process for calculating the proper tax, and for preparing the sales tax returns?
 - **NOTE:** charging the sales tax results in collecting your customers' money that you remit to the states, versus neglecting to charge tax on taxable items usually results in using your own money to pay the states in an audit assessment!
- What processes do we need to have in place to monitor our operations and the state law changes (e.g., additions to goods and services that are taxable under the state's laws), in order to stay compliant and avoid penalties?

Polling Question #3

Did you take away any actionable items from our discussion today?

- A. Yes*
- B. No*
- C. Unsure*

Questions?

Thank you!

(and one more topic, for next time? Next slide...)

For next time: unclaimed property reporting? What is it and why should we care?

Also known as “escheat” -- A liability owed to an individual or entity that has not been paid, and the obligation has been outstanding for a specific period of time outlined in statute (period varies by state and by type of item). Examples are uncashed checks for payroll and vendor payments, and credit balances in accounts receivable.

Laws in all 50 states require the “holder,” the obligor, to make efforts to locate the intended recipient in order to make payment. If the liability remains unpaid after a certain time period, the “dormancy” period, the amount/item must be remitted to the appropriate state – no “taking it back into income.”

There is generally no “statute of limitations” period, the state auditors can audit and assess for many, many years, and no concept similar to “nexus” as in taxes.

Unclaimed property laws are not a “tax” but are usually the responsibility of an organization’s tax or finance or treasury personnel, so we deal with compliance similarly to tax compliance.

Stay tuned for another webinar !