

The taxman cometh

How states are aggressively pursuing sales and use tax collections

INTERVIEWED BY ROGER VOZAR

States looking to add revenue to tight budgets are upping efforts to collect sales and use taxes from businesses that may not know they owe money.

“Sales tax is one of the largest revenue producers for many states, second only to personal income tax. Since there are so many transactions involving the exchange of property and services, the states are getting more creative in their attempts to collect the tax due on these transactions,” says Susan Nunez, J.D., LL.M., a principal in Tax Services at Brown Smith Wallace.

Smart Business spoke with Nunez about who owes the taxes and what to do to ensure you’re complying with state laws.

How are sales and use taxes different?

Sales tax is a transaction tax imposed on sales of tangible property and certain services. Use tax is a compensating tax to sales tax. If a transaction isn’t subject to sales tax, it will be subject to use tax.

Typically the sales or use tax is due when the final consumer purchases and uses the asset. A company that buys components or machinery and equipment to manufacture a product may be able to purchase them exempt from tax, but ultimately someone will pay the tax when the product is made, sold and consumed.

How are states trying to collect these taxes?

One way is by sending out nexus questionnaires to out-of-state sellers. These notices are used to determine whether an out-of-state company has a filing responsibility. For example, if a manufacturing company from another state is selling product to customers in Missouri, the state may send that manufacturer a letter to determine whether it has sufficient presence in the state to require a tax filing.

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The state can also obtain federal records of imported products to determine if they were shipped into a state and, regardless of whether the company paid tax on that asset, send a notice that says tax is owed.

These are fishing expeditions; you may not owe tax. But it can be threatening to get a letter saying you owe \$100,000.

Is not remitting taxes owed common?

Usually we see it in reverse — clients overpay taxes because of the complexity of the tax laws. Taxpayers err on the side of being conservative and pay tax on items that may very well be exempt.

It is difficult to determine what state has the right to the tax and who is responsible for remitting it. For example, drop shipments are particularly problematic. Say a Missouri company has a customer and a supplier in Illinois. An order is shipped directly from that supplier’s Illinois facility. It’s taxable in Illinois, but the question is, who is liable for that tax? It varies on whether the Missouri company is registered in the destination state, whether the supplier has a valid resale certificate from its customer and other factors.

Should companies determine if they owe tax or wait until they receive notification?

It’s best to calculate your liability and make

a decision. If a business has a nexus in a state and its tax liability is \$30, the amount is most likely immaterial to the company. But if the company is making \$10 million in sales in a state, it should want to take action and ensure it’s in compliance.

Many states are conducting amnesty programs to bring in more money. Amnesty periods are attractive to taxpayers not only because they often abate penalties, but they also limit the number of years the state can assess tax.

The most important steps for businesses to take is to get a handle on how tax decisions are made, and to develop efficient processes to manage and streamline their sales and use tax compliance burden. People making tax decisions aren’t usually in operations and don’t understand how purchases will be used, so they can’t apply the laws to see if those items will fall within an exemption.

You can increase tax compliance, and ensure you’re not overpaying, by developing a customized sales tax decision tool. This enables the person who procures items or prepares the invoices to determine what is taxable and what may be exempt. It also provides your company the control needed to make good tax decisions. ●