



Whitepaper

5 Things to Know before the U.S. Supreme Court Rules on Sales Tax Nexus

1. What's going on?

On April 17, 2018, the Supreme Court of the United States (“SCOTUS”) will hear a landmark sales tax case, *South Dakota v. Wayfair, Inc. et al.*,¹ which could change the entire sales tax nexus landscape for businesses. In this case, SCOTUS will decide whether states can require businesses with no physical presence in the state to collect sales tax from in-state purchasers. The decision is expected to be issued in June of this year. If SCOTUS decides in the state’s favor, this will overturn the physical presence standard that remote sellers have relied upon for nearly half a century and place a significant tax collection burden on businesses.

Currently, a company must have a **physical presence** in a state to collect tax. This Supreme Court case could eliminate that requirement, allowing states to impose a sales tax collection responsibility without a physical presence.

2. How did we get here?

For 50 years, businesses have relied on the physical presence standard established by the landmark case *National Bellas Hess*,² and upheld in the 1992 case *Quill Corporation v. North Dakota*,³ under which

¹ *South Dakota v. Wayfair, Inc., et al.*, 901 N.W.2d 754 (S.D. 2017), cert. granted (U.S. Jan. 12, 2018) (No. 17-494).

² *National Bellas Hess, Inc. v. Department of Revenue of Ill.*, 386 U. S. 753 (1967)

³ *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

sellers are not required to collect a state's sales tax if they have no physical presence in the taxing state.

States are getting what they want through reporting requirements. These laws are so complex that most businesses decide to collect sales tax simply because it's easier.

Colorado tried to poke a hole in this physical-presence wall when it enacted a sales tax notice and reporting law in 2014. This new law doesn't impose a sales tax collection requirement on sellers without Colorado physical presence. However, it does require that they notify purchasers of their sales tax liability and provide Colorado with detail regarding all the taxable purchases of their Colorado customers. This new Colorado law was the subject of SCOTUS's 2015 decision in *Direct Marketing Association v. Brohl* ("DMA").⁴ SCOTUS upheld Colorado's notice and reporting requirement, concluding that it did not violate *Quill* because it did not impose a tax collection requirement on remote sellers but merely a reporting requirement.

3. The current environment has been changing quickly.

The states were quick to respond to the *DMA* decision. As a result, a wave of legislation imposing *DMA*-like sales tax reporting and notice requirements has swept across the US. As of this writing, 11 states now impose this type of reporting requirement.

States have been working hard to expand their reach through:

- Affiliate nexus
- Click-through nexus
- "Kill Quill" legislation
- Economic nexus
- Marketplace legislation
- Reporting requirements

Some states, such as Washington and Pennsylvania, have imposed thresholds as low as \$10,000 requiring remote

sellers to either adhere to onerous notice and reporting requirements, elect to collect tax, or face stiff penalties with mandatory minimum penalties of \$20,000 or more.

In addition to enacting these SCOTUS-sanctioned reporting requirements, states began more aggressively pushing the sales tax nexus envelope with "kill-Quill" economic nexus legislation and regulations designed to force a case up the appeal chain to SCOTUS. So far, 14 states have enacted sales tax economic nexus provisions, most of which are at various stages of appeal in those states' courts.

With *Wayfair*, states now have the SCOTUS case they were seeking.

So, for better or worse, SCOTUS may soon resolve a battle that has been waged between businesses and states for half a century.

4. What's next?

Because several states already have economic nexus statutes in place and more are in the works, the states are expected to move quickly to enforce these rules if SCOTUS overturns the physical presence standard.

Though many hope that Congress will act to create exceptions for small businesses, the reality is that the states likely will move more quickly than Congress in this area, leaving both large and small businesses exposed.

Whom does this affect? Any company that sells products, including software and SaaS.

⁴ *Direct Mktg. Ass'n v. Brohl*, 135 S. Ct. 1124, 1134-35 (2015)

5. How can your business prepare?

These developments impose a daunting burden on businesses, as there are over 7,000 state and local taxing jurisdictions in the U.S., each with a different tax rate. Further, each state (and sometimes each locality) has its own definitions of what is and what isn't taxable.

How is a business supposed to prepare for this onslaught?

Businesses should evaluate their current systems and processes to determine whether they are ready to begin collecting and remitting sales tax across the U.S. and to develop a plan to address any gaps.

- ▶ Have you evaluated which of your products and services may be taxable in each state?
- ▶ Is your billing system equipped to apply taxability determinations and tax rates during the customer invoicing process?
- ▶ Are your accounting systems equipped to account for sales taxes collected and payable, as well as capture transaction-level sales and tax data for tax returns and audits?
- ▶ Have you considered how things like shipping and handling, discounts, coupons, rebates and customer returns will be handled?
- ▶ Do you have sufficient manpower to file the required sales tax returns?
- ▶ What processes are in place to ensure that you're using the current tax rates?

Take an easy first step by attending this complimentary webinar, [Sales & Use Tax Showdown at the Supreme Court: What It Means to Your Business](#), on April 24.

Our sales tax experts will host a live webinar after the oral arguments for *Wayfair* are presented in front of the U.S. Supreme Court. Our National Leader for State and Local Tax Services, Cathie Stanton, CPA, will actually be attending the hearing. From there,

she and her team will share their firsthand knowledge of the key issues, the potential implications on businesses and the proposed reporting requirements.

Don't assume your business will avoid this sales tax tsunami. Get the facts and make sure your business is prepared.



About the Author:

Kathleen M. Holston, CPA, CMI
Senior Manager, Tax Services
Cherry Bekaert LLP

As a Tax Senior Manager based in the Firm's Charlotte practice, Kathleen is a Certified Public Accountant with more than 25 years of experience in all areas of state and local taxation. As a multistate tax expert, Kathleen has worked extensively with clients ranging from small businesses to Fortune 100 companies across a wide variety of industries. Kathleen's experience across all state and local tax types gives her a unique ability to navigate the labyrinth of U.S. state and local tax rules in a coordinated approach to achieve significant tax savings and reductions of risk for her clients.

Kathleen focuses on identifying areas of risk and resolving exposure, entity structuring, complex transactional planning, audit support, tax appeals, legislative monitoring, tax systems and compliance automation, and performance of due diligence engagements. Her work encompasses income and franchise, sales and use, gross receipts, property and transfer taxes.