

Web-Based Businesses and Other 'Remote Sellers' Beware – A Morass of Sales Tax Obligations Are Upon You

Written By **Richard J. Crow** (rjcrow@wardandsmith.com)

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Sales Tax Obligations – Businesses with a Physical Presence in a State

It should come as no surprise that almost all states require businesses with a physical presence in a state and that sell goods or services in the state to collect and pay sales tax on those sales. Most states also have a complimentary tax, referred to as a use tax, which applies to purchasers when the business does not collect the sales tax for one reason or another. The purchaser is obligated to report and pay the use tax directly to the state. In other words,

someone is going to pay the state what it believes it is owed for each sale or purchase.

For a number of reasons, including the habitual failure of purchasers to comply with use tax reporting and payment obligations, and the difficulty of identifying and addressing that noncompliance, states prefer to hold the business responsible for collecting and paying the sales tax. After all, the business is directly engaged in a transaction with the purchaser, has presumably availed itself of the protections, benefits, and market provided by the state, and is, at least theoretically, in a better position to comply with sales and use tax laws. These rules are generally understood by businesses – at least they are understood by businesses that have a physical presence in the state.

Sales Tax Obligations – Remote Sellers

Many businesses today do not have a physical presence in most of the states in which they sell their products or services. The business might be located in North Carolina but sell products to purchasers nationwide through the web, or by catalog, or by some other remote means (we refer to these businesses in this article as "remote sellers"). The North Carolina business is likely aware of its sales and use tax collection and payment obligations for sales in North Carolina – the state where its facilities, employees, and operations are located. But, is the North Carolina business familiar with its sales tax obligations for sales made to purchasers in other states – states where the business has no physical presence or other activities other than perhaps the shipping of products to purchasers in that state?

Many remote sellers have taken, and perhaps still take, the position that they are not required to collect sales tax for sales of products or services to purchasers in a state where the remote seller does not have a physical presence, such as an office or storeroom, warehouse, manufacturing facility, employees, equipment, or stored inventory. States generally disagree and have enacted a variety of statutes over the years, some overly convoluted, in attempts to impose on remote sellers an obligation to collect and pay sales tax for sales made

into the state. Notwithstanding the many attempts by states to enforce compliance by remote sellers with what the states believed to be the legitimate exercise of their taxing powers, many remote sellers simply were unaware that they may arguably have an obligation to collect and pay sales tax in states with which they had little to no substantive contacts.

The Wayfair Case

In its 2018 decision in *South Dakota v. Wayfair*, the U.S. Supreme Court made clear that, notwithstanding the lack of a physical presence by a remote seller in a state, the state does have the power to require remote sellers to collect and pay sales tax on sales to purchasers in that state, as long as the remote seller engages in a significant amount of business in the state. In making its decision, the Court acknowledged that a substantial amount of business today is done remotely and it is no longer justifiable to require that a business have a physical presence in a state before the state can require the business to collect and pay sales tax.

Although good news for states and their budgets, this decision only makes things more difficult for businesses, most of which lack the resources to effectively understand and comply with almost 50 different state sales tax requirements.

The "thresholds" at issue in the Wayfair case that, if exceeded, required the remote seller to collect and pay sales tax in South Dakota, consisting of gross annual sales of more than \$100,000 in the state or engagement in 200 or more separate sales transactions in the state in the preceding or current calendar year. If the business met either of those economic thresholds (referred to as having "economic nexus" with the state), it was required to start collecting and paying sales tax in South Dakota. Promptly after the Wayfair decision, other states enacted similar laws to impose on remote sellers an obligation to collect and pay sales tax when the business sells more than a specified dollar amount of products or services in the state or engages in more than a specified number of sales transactions in the state. As of the date of this article, 45 states now have economic nexus statutes similar to the statute upheld in the Wayfair decision. That means that businesses that sell products or services in states where they do not have a physical presence must now be aware of, and potentially comply with, 45 different state sales tax laws – in addition to the laws of the states where the business has a physical presence.

Economic Nexus Rules Generally

It is impractical to describe in this article every aspect of the 45 different state economic nexus statutes in effect. Although the various laws generally follow the structure upheld by the U.S. Supreme Court in the Wayfair decision, there are nuances and, in some cases, significant differences, among them. Some of those differences concern whether a business counts gross retail sales or only taxable sales in determining whether it meets the sales threshold, or whether the threshold consists of an amount of sales, a number of transactions, or both. Other differences involve the measurement period used to determine whether or when the business exceeds the thresholds, or when the law became effective (which may dictate when the business might have been required to begin collecting and paying sales tax). In addition, the state economic nexus laws might differ regarding the amount of the thresholds. Compounded with the already complex nature of most state sales and use tax statutes – such as discounted rates, a plethora of applicable local sales tax rates, and exemptions for certain industries or products – you end up with an unwieldy and expensive hodgepodge of laws with which remote sellers must comply.

To their credit, 24 states, including North Carolina, adopted the Streamlined Sales and Use Tax Agreement. One of the main purposes of that agreement is to simplify and reduce sales and use tax compliance burdens on businesses. It is a recognition of, and attempt to remedy, the overly complex and disjointed nature of the state sales tax statutes that apply to remote sellers. Member states revised their sales and use tax laws to

conform to the requirements of this agreement, which include simplification of state and local sales tax rates, streamlined sales tax returns, an ability to register to collect and pay sales tax in one or more of the member states by completing one registration through one website (as opposed to separately registering in each state), and other efficiencies. Unfortunately, the remaining states have not adopted this agreement and conformed their sales and use tax laws accordingly, meaning that remote sellers must continue to track and comply with a substantial number of different sales tax requirements.

North Carolina Economic Nexus Rule

North Carolina, which is a member of the Streamlined Sales and Use Tax Agreement, enacted its economic nexus statute effective November 1, 2018. Any remote seller (i.e. a seller that does not have a physical presence in North Carolina but sells products or services to purchasers in North Carolina) that has gross sales in excess of \$100,000 in North Carolina or has 200 or more separate transactions in North Carolina in either the previous or current calendar year, must register and begin collecting and paying sales tax for sales in North Carolina.

Remedying Non-Compliance With Economic Nexus Rules

If your business sells products or services in states other than where it has a physical presence, and the business has not been collecting and paying sales tax in those states, you would be well-advised to review your obligations in those states with your legal counsel. It is possible that your business exceeded the applicable economic nexus thresholds in one or more of those states, or is tracking to exceed the thresholds in the near future. If that is the case, your business might have been required to register in that state and commence collecting and paying sales tax. Your business might be responsible for payment of the due but unpaid sales tax, in addition to penalties and interest. In some situations, the liability is minor. In others, it can be quite significant based on the level of sales in a state and the number of states where you have a sales tax collection and payment obligation.

A significant thorn for most businesses is that the sales tax that was required to be paid to a given state often was not collected by the business, meaning the business must pay the sales tax out of its own revenues because it may be impractical to later collect it from the actual purchasers. However, there are potential options available for addressing past failures to collect and pay sales tax. Occasionally, a state might offer what is referred to as an amnesty program for remote sellers that voluntarily disclose their past non-compliance, file the required sales tax returns, and, depending on the terms of the program, pay some or all of the past due sales taxes. The requirements to qualify for those amnesty plans differ, and you are well-advised to consult with your legal counsel or another professional advisor before taking any action to participate in an amnesty program. Another option includes making a voluntary disclosure of past non-compliance, filing past-due sales tax returns, paying past due sales taxes and interest, and then requesting a penalty waiver. All available options should be reviewed carefully with your legal counsel.

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