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OPPORTUNITY IN COMPLEXITY

THE RAPIDLY CHANGING LANDSCAPE OF SALES & USE TAX

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Opportunity in complexity

The changing landscape of sales & use tax

By Antoinette Alexander

Thanks in large part to the Internet and the e-commerce explosion, businesses today are operating in a new world of taxation. While navigating the complex and ever-changing sales and use tax landscape can be extremely challenging for business clients, it is affording many accounting firms new growth opportunities.

"Many accountants have a very strong focus on income tax and a very strong focus on maybe other places in the tax-planning phase, but realize there are a lot of opportunities in the sales and use tax space given the dynamic nature and some of the disruption that is occurring in the marketplace to be able to find new avenues to provide guidance and different services," said Mike Sanders, vice president of product management at Wolters Kluwer Tax & Accounting North America, US Corporate.

Sales and use tax has always been an area subject to changes, but industry sources agree that never before have there been such dynamic changes at play. Facing such hot button issues as nexus and cloud computing — to name just a few — the sales and use tax marketplace is becoming a hotbed of opportunities.

"[Firms] are starting to realize that their clients are having more issues than they can handle on their own and they are coming to their CPA firm for help," said Scott Peterson, director of government affairs at Avalara, a cloud-based provider of sales and other transaction tax compliance. "In the last two years, I've seen more interest from CPAs than I have historically."

David Campbell, CEO and co-founder of TaxCloud, agreed and said, "I think a lot of the more forward-looking firms are absolutely expanding their sales and use tax expertise. … We are seeing a lot more interest both to refer their clients to us but also to basically understand how our system works so they know how to access the reports that we generate." TaxCloud provides a sales tax application programming interface that can be embedded within the commerce platforms and point-of-sale systems used by retailers.

NEXUS: THE NEMESIS?

While it isn't exactly new, nexus no doubt remains at the top of the list when it comes to areas of concern. As accounting professionals have discovered, states are eager to expand the definition of nexus.

"Any federal action to expand nexus will greatly increase the need for accounting firms to manage sales and use tax for their clients," said Robert Dumas, managing partner of TaxConnex in Atlanta, referring to such federal legislation as the Marketplace Fairness Act of 2015 and the Remote Transactions Parity Act of 2015. "As the states wait for the federal action, they are busy finding other ways to expand nexus and the taxability of more products and services." TaxConnex is a sales and use tax outsourcing services.

So, what is nexus? Nexus is the connection between a tax jurisdiction and a business that creates a tax obligation, and it is triggered by any number of changes at the state level, such as business expansion, or expiring exemptions and amended sales tax regulations, as defined by Avalara. In addition, nexus may be created when a business has a remote sales force, attends new trade shows, or expands into new markets.

Understanding nexus and its implications for business clients is essential for firms, especially in light of the rapid rise of e-commerce. The reality is that many businesses don't fully understand nexus and what constitute nexus-creating activities until it's too late and they are perhaps slapped with audits and penalties.

Furthermore, an annual sales tax rate study released earlier this year by corporate tax solutions provider Vertex revealed that there are an average of approximately 600 new and changed sales and use tax rates each year. Keeping up with all of the regulations on a state-by-state basis is a daunting task, to say the least.

Firms that successfully position themselves as a nexus resource no doubt stand to benefit. "If there's one thing you must know, it is nexus. Meaning, where do you even have obligations to worry about sales tax? That's the very first thing, and it may be the only thing you need to know," said Andrew Johnson, managing partner of Dallas-based Peisner Johnson & Co., which focuses exclusively on state and local taxes.

Matthew Walsh, vice president of tax at Sovos, a provider of tax and business-to-government compliance software, said, "Historically, if a seller did not have a physical presence, or a presence, in a jurisdiction, they didn't have an obligation to register and collect tax. What that meant, as e-commerce has exploded, is that more and more sellers aren't collecting taxes on these online sales and the states, and the governments are losing that money and looking for ways to capture that. So, what we've really seen is a push to change those rules. It has been a movement for multiple years, but it is really picking up speed now."

It has been estimated that, including catalog, phone and all other interstate transactions, states have lost roughly $23 billion in sales tax annually — a trend they are determined to reverse.

When it comes to nexus, Peisner Johnson offers a list of six nexus-creating activities for sales and use tax:

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Spotlight on CPA.com

What major issues do you see in the sales & use tax arena?
Online sales channels have grown significantly in recent years. States are looking for sources of revenue and are moving more aggressively to increase regulation and add new resources for collection efforts in this area. There are more than 11,000 taxing jurisdictions in the United States, and keeping up with rate changes in each location is challenging. We see growing complexity for sales and use tax compliance going forward.

Michael Cerami
Vice president of business development and corporate alliances, CPA.com

What are you doing to help accountants and their clients handle those issues?
CPA firms can benefit from education and thought leadership in this area, and we — in partnership with VertexSMB — are looking to provide that piece. We also are offering a two-part program with Vertex SMB — a referral program for firms who want to help their clients navigate this area through a trusted third-party source, and an advisory program for CPAs who want to build a practice in this emerging field.

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Complexity

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1. Ownership of real or personal property in a jurisdiction, such as offices, warehouses, machinery or equipment;

2. Leasing of real property or personal property, like warehouses, offices, machinery, equipment, etc.;

3. Maintaining of an inventory, whether consigned, stored, or carried by sales representatives;

4. Travel of employees into a state to conduct sales, training, deliveries, installations, repairs, etc.;

5. Use of independent sales or manufacturer's reps, even if they are not exclusive; and,

6. Use of sub-contractors for repairs, maintenance, installations, etc.

EXPANDING NEXUS

In their effort to capture lost sales tax in today's digital environment, states have increasingly implemented click-through and affiliate nexus policies.

"What you've seen are states tweaking the rules. So, click-through nexus rules or affiliate nexus rules, meaning if you were selling through a Web site and you were given a commission or a kick-back on referring sales, the state would say that is enough to give you nexus. So, some remote vendors would then be caught and would have to start collecting tax," said Sovos' Walsh. "That has worked for a couple of years, but what you've seen in the past year are a couple of states that have actually pushed that further and have enacted what are called economic nexus laws. So, they've gotten rid of the physical requirement."

"What is happening now is states are trying to get more companies to file through click-through nexus and affiliate nexus, and three states have imposed economic nexus," said Alex Laskowski, a partner with Grant Thornton's state and local tax practice in Chicago. He noted that, as of press time, 21 states had enacted click-through nexus and 22 states had enacted affiliate nexus.

Said Carla Yrjanson, vice president of tax research and content for indirect tax at Thomson Reuters, "The major trend and the major difficulty is really keeping up with this evolving nexus. Each of the states can do their own thing. So, if you are making sales into several states it can be very challenging to keep up with the evolving nexus standard and rules. One day you may not have nexus and, with a rule change, you might have that responsibility."

Adding yet another layer of complexity for nexus determinations, said Christine Boeckel, managing editor of state tax — sales, use and property taxes at Bloomberg BNA, is the recent activity surrounding disaster relief and recovery efforts. "In recent months, many states enacted legislation that provides special treatment for businesses that enter their borders to participate in disaster relief and recovery efforts. The legislation typically creates an exception to the state's nexus and registration requirements for those businesses that enter the state for disaster relief purposes during declared emergencies, or it provides exemptions for such businesses on their purchases while they're in the state during disasters."

"This is significant because it creates an additional level of complication for nexus determinations, but shows an awareness of the tax issues for these businesses and helps break down barriers to welcome help into states where residents are in dire need of assistance," Boeckel said.

CLOUD COMPUTING

Cloud computing services are becoming increasingly prevalent — and taxing jurisdictions are taking note. According to industry experts, a key consideration when analyzing the taxability and sourcing of a cloud service is to determine how the transaction will be characterized by the state. "In some states, they consider cloud computing to be a sale against personal property. … We are seeing more states trying to tax cloud computing," said Laskowski, who cited the city of Chicago as an example, which recently extended its personal property lease transaction tax to cloud computing services.

For firms, the cloud opens up both tax planning and administrative analysis opportunities around determining what is taxable, where it is taxable and how to apply the correct taxes to any particular transaction, according to Jeremiah Lynch, a principal at tax firm Ryan in New York.

"[Sales tax] was created in the 1930s as a tax on products, so tangible personal property, and it has generally been a tax based on destination. … Once you get into situations with the cloud and trying to determine who are the users and where are the users located … as those kinds of businesses enter the cloud and offer their services without wires and without worrying about where people are at, it kind of tilts the traditional sales tax world on its head in terms of attempting to source the service to a particular location," Lynch said.

'YOU NEED A GUY'

As many firms and businesses are discovering, sales and use tax is complex — and the complexity shows no signs of abating. To better serve clients, some firms are adding comprehensive sales and use tax compliance services to their practice or are seeking ways to expand their current service offerings.

One such example is Seattle-based accounting firm Peterson Sullivan. Seeing an influx of clients entering multi-state markets and a rise in state compliance-related questions from clients, the firm hired Rachel Le Mieux about three years ago to serve as the firm's first state and local tax partner. "My goal was to come in and create a practice that would serve not only our existing clients but would then help grow revenues by bringing on more clients into the firm," Le Mieux said. "The practice continues to grow and we will probably be having to go out and hire more people simply because the need for state and local services just continues to grow each and every day."

For those clients in multi-state markets, the firm conducts nexus studies on behalf of the clients to identify their potential exposure and assists them with resolutions to those potential issues.

At Peisner Johnson, the firm is working to stay ahead of the marketplace and, as a result, has evolved its service offering. Today, the firm can essentially take over a client's state tax function. "There are so many pitfalls that you can run into. You really 'need a guy.' That's our message. You've got to have either a full-time employee in-house, a full-time SALT person at your firm, or, barring that, you need somebody like us," Johnson said.

AUTOMATE, AUTOMATE

Meanwhile, vendors are ramping up their software solutions to automate sales and use tax processes and to bring together disparate systems.

"[Automation] is so much better and so much more affordable than it was five years ago, say, that even if you've looked at it in the past you ought to relook at it. If you fit that profile of nexus in several states and selling taxable goods, then you are likely a candidate for automation," Johnson said.

"We saw so many parallels with payroll before you had all of the automation tools you have around it — very complex, need to be compliant, really hard to stay on top of all of the rules and regulations, but yet firms really being pulled in to help answer those questions and provide guidance. It's very similar on the sales and use tax side," noted Michael Cerami, vice president of business development and corporate alliances at CPA.com.

To help firms build or expand a sales and use tax compliance and advisory practice, CPA.com and Vertex SMB introduced a cloud-based program for firms. One of the key features of the program is a single accountant console where firms can monitor client sales and use tax compliance, from tax calculation to returns generation and form filing. CPA.com and Vertex SMB also are collaborating on training and educational resources that include webinars, video tutorials and a firm marketing toolkit to help CPAs build expertise and market around sales and use tax in their practices.

There's also a referral program that allows a CPA firm's clients to get discounts and other benefits when their CPA refers them to Vertex SMB.

A NEVER-ENDING STORY

While the future outcome of federal legislation remains unclear, what is certain is that the sales and use tax saga will further evolve as states continue to look for ways to offset budget shortfalls.

"Sales and use tax is an area of scrutiny in today's environment. Less state funds equal more aggressive tactics to bring in needed revenue. States are hiring more auditors and going after non-filers," said Craig Cookle, partner in charge of the sales and use tax practice at Top 100 Firm Wipfli in Milwaukee.

According to Cookle, it is an extremely important topic to address with clients for the following reasons:

- To minimize the potential exposure from noncompliance — tax, interest and penalties;
- To minimize the costs of compliance after the fact;
- To avoid client conversations centered around the fact that issues were not addressed by you;
- To secure tax savings and cash flow for clients;
- To ensure that the statute of limitations runs on the state's ability to assess additional tax; and,
- To help your client if they are anticipating a sale in the future.

"As accounting firms conduct their year-end planning with clients, they should review the business's nexus footprint to add or remove states, if necessary. Additionally, they should review state revenues for significant growth and identify any new products or lines of business that may have sales tax impacts," advised Dumas of TaxConnex. "To assess potential liabilities and historical risk, nexus and state sales data are both critical factors." AT