

IT ONLY TAKES ONE...AUDIT, THAT IS

Why ALL Businesses (Foreign and Domestic) Should Be Filing Sales Tax Returns

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A Wisconsin Sales Tax Auditor walks into a bar and says to the Owner, "Please provide a listing of all your purchases of goods and services by vendor for the past year".

The Owner, thinking that it's a simple request, gets the list together. As he is handing it to the Auditor, he says, "Here it is, but if you don't mind my asking, why do you want it?"

The Auditor replies with a smile, "I needed a list of who to audit next."

Sound like a joke? Well, it isn't. That is how easy it will be for state auditors to come up with their list of targets.

Think you are exempt from filing because you are a foreign business covered under a treaty?

Incorrect! The treaties are for Federal taxes only, not states.

Think you are exempt from filing because you don't have a physical presence in the state?

Not anymore! The Supreme Court ruling in Wayfair did away with that exemption and created an Economic nexus test.

Think you are exempt because you don't sell a product?

Think again! Services in many states are subject to sales tax and whether it's called a Sale, a Fee, or Revenue doesn't matter. (WARNING: Service businesses have other nexus issues as well.)

Think you are exempt from filing because your product is exempt from tax?

Nope! The exemption from assessing tax is just that, from assessing, not from filing. After all, how is the state to know it's exempt unless you tell them it's exempt via filing a return.

Think you can hide because you don't have any clients who are over the threshold?

Don't be surprised if you still get audited because tracking your activity is as simple as creating a spreadsheet from your customers.

Now that almost all of the states have instituted some sort of Economic Nexus standard for sales tax, pretty much any business selling across state lines will have multiple sales tax filings. Since sales tax is a tax on the local purchaser and not the selling business, and advances in technology has made it much easier to track, file, and remit, the highest court has ruled states have the right to require businesses to comply if they wish to do business within the states' borders.

Still thinking about not filing? Here are 6 reasons why you should:

1. The statute of limitations isn't running until you file. This means a state's right to audit and assess taxes doesn't begin until after the return is filed. So.... if you don't file.... the states can go back to day 1 of when their law went into effect.... 10 years from now, 20 years from now, 100 years from now (okay, unlikely but still possible). Some states like California are highly aggressive and it is not uncommon for them to go back 10 years.
2. One word....penalties. Even if you don't owe any tax, many states have a minimum late/non-filing penalty for the sales tax returns which can add up quickly. For example, New York State has a \$100 per return minimum penalty. Each year you can potentially rack up \$1,200 in unnecessary late filing penalties for a zero due tax return just because you didn't file it. Now multiply that times a few states and you can see how that can add up quickly.
3. It's a customer service and cash flow nightmare. Remember that this is normally a customer paid tax. But if you owe tax under audit, you are responsible for paying it. Good luck on going back to your customer to get that money back. Even if you have a good relationship, it's highly unlikely that they will be willing to pay a past tax now and take a hit to their bottom line that they can't pass on to their customers. So now you are stuck picking up that tab.
4. An audit fight is expensive. In addition to the potential hit from the taxes, the time it will take in personnel hours and possibly professional fees to go through an audit and fight the determination will be costly. Remember, the states have unlimited man hours and time is on their side. You do not have the unlimited hours and every hour or dollar spent dealing with the audit is less time and money spent on developing your business.
5. Not filing could affect your financial statements. Any uncertain tax positions that become material enough may have to be accrued for and/or disclosed in your financial reports. What is material depends on the size of your business and the amount of potential taxes that could be assessed. But remember, this is cumulative. Since there is no statute of limitations running until you do file, the amount of potential assessments will just get higher and higher each year.
6. Sales tax audits can lead to other things. The various departments at the states do talk to each other. It's not unusual for a sales tax audit to be followed by a letter from the state's Secretary of State asking why you aren't registered to do business there or the tax department asking why you haven't filed income tax returns or their unemployment department asking if your "independent contractors" really are ICs or if they are actually employees. It may be as innocuous as a letter asking questions or as invasive as a tax audit. Either way you are now on their radar for not being compliant.

All is not doom and gloom though.

The states have "informally" agreed to not apply the Economic Nexus standard retroactively. But there is no "One Size Fits All" application. The determination period and the minimum filing requirements vary widely state by state.

That said, if you should have been filing before, this new standard will not erase that liability. It will, however, make it much easier for the states to catch those who are not in compliance. Coming forward before a state's "Invitation" to an audit by using a voluntary disclosure program may still be possible and is highly recommended.

Regardless, the time to start filing sales tax returns is now. Now about that bar.....

Want to know more about Nexus and Wayfair? Visit our blogs on the subject here:

- <https://www.dopkins.com/blog/should-you-be-collecting-sales-tax-probably-remote-seller-sales-tax-hits-more-than-just-e-commerce/>
- <https://www.dopkins.com/blog/kill-quill-the-supreme-court-gets-salty/>

Dopkins can assist you in determining your state filing requirements. For more information, please contact your Client Service Coordinator or Victoria S. Carlin at vcarlin@dopkins.com.



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