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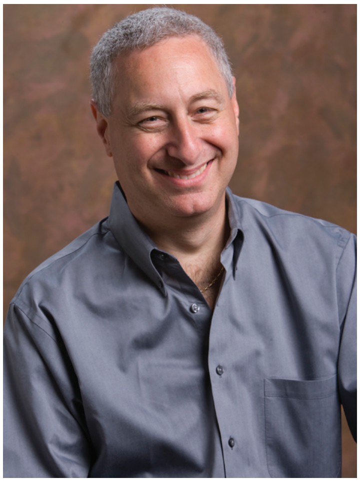
Sales Tax Anxiety, Part 2

As if music retailing wasn't challenging enough, most store owners across the U.S. are now frantically addressing new and ever-evolving sales tax laws stemming from the 2018 Supreme Court "Wayfair Act" decision regarding a state's right to collect sales tax from out-of-state retailers. In case you missed it, go back and read Part 1 (which can also be found on our firm's website fkco.com) for a full explanation of what lead up to this monumental tax law change, as well as what retailers are now facing with regard to sales tax compliance.



Minimize your audit risk and maximize your sales tax collection

As promised in the February/March issue, this Part 2 is comprised of the steps and suggestions to help assure your store remains in compliance with ever-evolving new sales tax laws. Suffice it to say, any retailer who generates a sizable amount of revenue from online sales should pay particularly close attention to this topic to make sure you remain in compliance with new sales tax laws that will arise from the recent Supreme Court decision.

Accordingly, here are eight easy things you can do to help you survive an unwelcomed, intrusive and probably inevitable sales tax audit from any state:

Step 1. Determine if you created "nexus" in any new state over the year. Have you sent a road rep into a neighboring state to service a particular school? Did you spend time delivering and installing a customer's new sound system in a church, synagogue or nightclub in a neighboring state? Did you hire new employees that work from an out-of-state remote location? Are you using a third-party reseller (like Amazon) to fulfill orders with your inventory sitting in an out-of-state warehouse? Answering "yes" to any of these questions may mean you have nexus, the obligation to collect sales tax, in a new state.

Nexus laws are often complex, vary by state and need to be carefully reviewed for each state where you conduct business. Also, keep in mind that a sales tax rate is really the sum of state, county, city, local and special district taxes. If you have indeed established sales tax nexus, be prepared to accurately determine the applicable sales tax rate to calculate, file and remit your sales tax liability.

Step 2. Determine when you are required to pay sales tax and file sales tax returns. The beginning of the year is a great time to make sure you know how often you'll be required to file your sales tax returns and when payments are due. Some states require you to file sales tax returns monthly. Other states will determine the frequency (monthly, quarterly, annually) of filing sales tax returns and remitting the tax based on an estimate of the dollar volume of sales you typically generate and your resulting sales tax liability. And some sales tax authorities will send forms and notices in advance of their filing due to date, and others don't bother.

If you don't receive a sales tax form, it doesn't mean one isn't due. Determine the frequency and timing of these returns and liabilities, and mark your calendar to make sure you file and pay on time to avoid late filing or payment penalties.

Step 3. Determine if you are required to file and pay sales tax electronically. Some tax jurisdictions now require sales tax liabilities be paid electronically, while others do not. Knowing a state's payment options will ensure you pay the correct way and avoid penalties for paying the wrong way; yes, some states will actually penalize you if they don't get their money electronically. Also, check to see if sales tax prepayments are due. A number of jurisdictions require prepayment for large tax amounts with different filing schedules.

Step 4. Reconcile your "sales tax payable" general ledger account often. Make time to reconcile your sales tax liability account against your source documents. Here's an easy way to do it: 1) start with the balance of your "sales tax payable" account at the beginning of the accounting period; 2) add the total monthly amount billed to customers; 3) subtract the total monthly amount of sales and use tax paid; and 4) reconcile this calculated amount with the current balance in your sales tax payable account at the end of the accounting period. This is a great way to assure you're remitting the correct amount of sales tax.

Also, verify all payments have cleared the bank. While this may seem unnecessary, a lost check could result in an unexpected sales tax liability. Review your process for receiving and handling incoming tax notices, especially if you employ part-time bookkeepers.

Step 5. Know the taxability of new product sold and services rendered. Do you offer services like instrument repairs, product delivery and installation, piano storage or audio consulting? What is the taxability of these services and their related material and labor components?

Here's a common blunder that'll get you into the proverbial hot water in most states if ever you undergo a sales tax audit. Your state deems only the "parts" component of an instrument repair is subject to sales tax, but your repair invoices don't separately break-out the charge for parts and the charge for labor; you have now inadvertently rendered the entire repair invoice subject to sales tax. Also, what's exempt from sales tax in one state may be taxable in another.

Step 6. Confirm a customer's tax-exempt status. Always make sure to verify a customer's tax-exempt status is updated and agrees with their exemption certificate on file. Have any of your customers' resale certificates expired? If so, they must be replaced to continue not charging sales tax to your customers.

Step 7. Timely address any tax notice. Always deal with any tax notice in an expeditious manner. Even though you've filed and paid on time, tax authorities can make mistakes when processing your return or payment. If they misread a postmark or misapply your payment to an incorrect account, you will wrongly receive a tax due notice. Unfortunately, failing to respond to a notice may result in a levy to your bank account, a lien on your corporate officers or suspension of your business license until the issue is resolved. Don't ignore tax notices; deal with them the minute they arrive.

Step 8. Maintain proper recordkeeping in the event of an audit. Sales tax audits strike terror into the hearts of many business owners. Not only are they a drain on time, money and personnel but they are the proctological exam of all audits because a sales tax audit can (a) expand beyond the initial audit time periods, (b) encompass the examination of thousands or tens of thousands of transactions, and (c) often be used as "feeders" to audits of other businesses. Given all states are desperate for new revenue to balance their budgets, sales tax audits are the proverbial low-hanging fruit.

Assuring you retain supporting sales documentation and make it easily accessible will go a long way toward minimizing the cost of an unexpected audit. Your documentation should include (a) a reconciled general ledger system, (b) copies of federal and state income and sales tax returns, (c) customer invoices, (d) contracts, (e) sales tax exemption certificates, and (f) any other documentation supporting the components of any taxable sale.

SOME FINAL THOUGHTS

To state the obvious, sales tax compliance is not a money-making activity. It is a necessary evil for all retail businesses. But if it's done right, diligent compliance can help preserve business resources in the event of an audit. And you don't have to bear this burden alone, given the plethora of resources available to you to keep you sales tax compliant. Consider using sales tax collection software (like Avalara or TaxJar) that directly integrates with your accounting software platform.

Also, now's the time to check in with your professional team. Talk to your CPA to help determine where you may have sales tax nexus. Meet with your attorney to make sure your sales contracts and other business practices are compliant with all applicable laws. The goal is to minimize your audit risk and maximize your sales tax collection and reporting efficiency. This will, in turn, save you time and resources to devote toward activities that actually increase your revenue. **MI**

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