



# LGT SALT SHAKER

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State & Local Tax News brought to you by Lane Gorman Trubitt, PLLC

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MTC Establishing Guidelines  
for Taxing Internet Sales

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**Around the Country**

# The Amazon.com Sales Tax Nexus Battle Comes to Texas

By: Pat McCown

Texas is the latest state to join the sales tax nexus battleground with the online retailing behemoth Amazon. In May 2008 *The Dallas Morning News* published an article describing the Texas Comptroller's Office investigation of why Amazon was not collecting Texas sales tax when it operated a distribution center in Irving since 2006. The company has defended its position of not collecting sales tax by saying Amazon does not actually own the distribution center. It's owned by a Kentucky based subsidiary, Amazon.com KYDC LLC. Undeterred the Texas Comptroller's Office issued an assessment for uncollected sales tax, penalties, and interest of \$269 million. It appears on the surface that Texas is asserting nexus to Amazon based on the physical presence of an affiliated entity, this concept is commonly referred to as affiliate nexus and has not traditionally been applied in Texas.

The current sales tax paradigm in the United States is a result of several high-profile U.S. Supreme Court decisions where it was ultimately determined that a business must have some physical presence in a state before the state can impose a duty to collect and remit sales tax. Amazon and other online retailers have been under increasing pressure in recent years as a number of states have passed legislation specifically aimed at creating a sales tax collection responsibility for online retailers who may lack a physical presence in the state. The first of such legislation was passed by New York in 2008.

The New York legislation expanded the definition of soliciting business in the state to include arrangements where New York residents and businesses that provide links on their website through which a customer is referred to an online retailer in exchange for consideration will create nexus for the online retailer. The presumption only applies if the seller has cumulative gross receipts in excess of \$10,000 from New York customers resulting from such agreements. The New York type legislation is now commonly referred to as "click-through nexus". North Carolina and Rhode Island soon followed New York's lead and passed similar click-through nexus legislation. As of the publication date of this article the Illinois legislature has passed a click-through nexus bill which if signed by the governor will take effect immediately. Both Amazon.com and Overstock.com have filed suit questioning the constitutionality of the New York legislation and in November 2010 a New York Appeals Court reinstated the case, thus the battle goes on.

It's not surprising that the states have begun to challenge the nexus status of online retailers through both new legislation and broader enforcement of existing laws. The Texas Comptroller estimates that in 2006 the state lost over \$541 million in sales tax to online transactions, and that number increases



every year as online sales continue to grow. Among the states that impose a sales tax (45 plus DC) the result is the same as online sales increase sales tax collections decrease. This erosion of the tax base puts great pressure on the states to make up for the loss in tax collections. In addition many "bricks-and-mortar" retailers argue that online retailers have an unfair tax advantage. Some states (CO and OK) have passed legislation that requires the online retailer to disclose through annual filings sales to in-state residents to the state tax officials who in turn can use the information to enforce use tax payment by the in-state purchasers.

The mounting of pressure on all sides of this issue will ultimately result in a new sales tax collection and payment paradigm in the years to come. Whether it be through the passage of federal legislation or grass root efforts among the states the days of buying goods tax free over the internet are likely numbered.

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## Multi-State Employees Can Make Multiple State Withholding A Necessity

In a world which is more connected by technology than ever before, many companies have employees living and working in multiple states. This scenario creates unique challenges for companies to keep track of multiple and inconsistent state tax laws and ensure their compliance.

Different state's rules regarding tax withholding can fluctuate wildly. From the amount to withhold to even the amount of time spent in a specific state before withholding is required, no two are identical and this confusion can lead to a compliance nightmare.

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**Examples of some of these differences include:**

- 20 States (including Pennsylvania, Minnesota and California) require withholding to begin immediately, day and date, with the commencement of work.
- In New York no withholding is required if the employee is there less than 14 days.
- In Arizona no withholding is required if the employee is there less than 60 days.
- Wisconsin and Virginia tie the withholding threshold to levels of income.
- The District of Columbia does not tax non-residents.
- 5 states disallow the employee to allocate days out of the state if they are working in a different state than their employer's main office for reasons other than convenience.

**As you can see, all of these variances in state withholding rules can lead to a lot of confusion and become very costly if handled improperly, but there are steps you can take to insure that you remain in compliance.**

- 1. Examine Accounts Payable and Travel Expense Records** – These records can provide companies with an excellent way to stay on top of where their employees are going as well as service contracts and client locations. Expense reports will also help you establish where employees are located. Stay on them. Make sure they are maintaining records tracking how many days are spent where.
- 2. Establish a Multi-State Withholding Policy** – In today's climate, it is a necessity for multi-state companies to have a multi-state withholding policy.
- 3. Ensure Compliance** – Meet with your employees and make sure they keep you informed when they are performing services on your behalf outside of your primary location.
- 4. Create an Out-of-State Form** – Create a form for employees to complete when they are performing work in another state. Be sure the form tracks the amount of time spent working in that state. The creation of a form will make the process official for your employees, and make it easier for your company to track all the work time spent in multiple states.

With the rules between states being so different and complex it's vital to have an independent State and Local Tax (SALT) Specialist review your records to ensure compliance. If you have any questions or would like your company's records reviewed, do not hesitate to contact Pat McCown, LGT's SALT Partner at (214) 461-1416 or by email at [pmccown@lgt-cpa.com](mailto:pmccown@lgt-cpa.com).

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## MTC Establishing Guidelines for **Taxing Internet Sales**

Colorado recently followed California's lead with the passage of new legislation requiring all out-of-state retailers to report tangible personal property sold into the state and the amount of tax owed.

In response to this increasing state pressure the Sales & Use Tax Uniformity Subcommittee of the Multistate Tax Commission has started work on a "Model Use Tax Notice and Reporting Statute". The Statute is designed to identify the specific information required to be included in any report for compliance with state law.

Factors considered in the proposed guidelines will include:

- Persons and companies required to report and the types of reports that must be produced
- Required notices to consumers
- Whether vendors will be required to send periodic reports to consumers detailing what was purchased, when, and how much tax is due
- Whether a cumulative report sent to the state revenue agency will be required
- Proposed penalties for sellers and purchasers who fail to report taxes due on each transaction
- How proposed reporting should be accomplished

While there is no timetable for when the final version of these guidelines will be established many state and local tax (SALT) experts are already seeing challenges for the states when it comes to enforcing any requirements placed on out-of-state retailers that have no connection with the states in question, other than the sale of property to in-state residents.

As always, LGT's State and Local Tax department will stay on top of developments as they occur. If you have any questions do not hesitate to contact Pat McCown, LGT's SALT Partner at (214) 461-1416 or by email at [pmccown@lgt-cpa.com](mailto:pmccown@lgt-cpa.com).

For any questions as to how these changes may affect you or your business, contact Pat McCown, State and Local Tax Partner at (214) 461-1416 or by email at [pmccown@lgt-cpa.com](mailto:pmccown@lgt-cpa.com).



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For more information about LGT or to speak to a SALT specialist please contact Pat McCown, SALT Partner at 214-461-1416.



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## Around the Country...



### California – 1% Penalty for Payment

**Method** – Taxpayers in California who are required to pay electronically, but instead make payments by another method will be struck with a new 1% penalty unless they are able to justify their chosen payment method. According to California law, electronic payments are required once a taxpayer makes an estimated tax or extension payment exceeding \$20,000 or files an original return or tax liability greater than \$80,000.

### Florida – Virtual Employee Triggered

**Actual Nexus** – In an environment where states seek to expand their definitions of what constitutes nexus, an employee working in Florida performing online administrative duties triggered nexus in Florida despite the fact that the employee did not solicit sales.

### Illinois – No Refund for You!

Further illustrating the dire economic straits many states find themselves in, Illinois, among others, have chosen not to issue refunds to taxpayers who overpay on their reported tax returns. Instead they offer a vague promise to pay the refund at an unspecified future date. In cases such as this, the best option for the tax payer may be to elect that the overpayment be used as an advanced payment on the taxes they owe next year. Even taxpayers not currently eligible for a refund may want to consider taking the election in case future federal changes produce a refund of already paid state tax.

**No Fly Zone** – The Illinois Supreme Court recently declared that a company had use tax nexus in the state due to multiple takeoffs and landings by the company's private plane. The court ruled that Illinois was owed the tax despite the plane being hangered in another state and the company being headquartered outside of Illinois. Examining the aircraft's flight records over a two year period revealed that almost half of the plane's 290 flying days involved at take-off or landing in the state. If the ruling spreads to other states, this precedent could have an impact on many businesses that hanger aircraft in other states than where it's chiefly used.

### Michigan – Granting Amnesty –

The State of Michigan joined other states such as Florida, Illinois, Kansas, Maine, Pennsylvania, New Mexico, Nevada, Massachusetts and New York when it announced that it will be rolling out a new offer of general tax amnesty next year beginning May 15 and carrying through to June 30, 2011. While an offer of Amnesty may sound like a godsend, it's important to consult with a tax professional before taking part. Often, due to their specific circumstances, there are other tax implications that participants may not be aware.

### Massachusetts – No Finished

**Product? No Problem!** – As it turns out, some manufacturers in Massachusetts are still exempt from the state's manufacturer's sales tax even if they have yet to create a finished product. In a ruling from the state's Supreme Judicial Court it was decided that a company which produced a blueprint for a telecom chip was eligible for the tax exemption even if it hadn't produced the finished product since it was an "essential and integral step in production". This decision may prove to be a tremendous advantage for startup companies in the process of manufacturing their first products and prototypes.

### Texas – Moving the Goal Posts –

When Governor Rick Perry rolled out the Texas Enterprise Fund many economists praised it as an effective weapon against a flagging economy. However, a recent report from the not-for-profit organization, Texans for Public Justice/Austin, has indicated that 37 of the 50 companies participating in the program have failed to meet their job-creation targets and deadlines forcing the Governor's office to either restructure the deals, changing their employment goals, or keep those companies in non-compliance.

### Foreign Concepts of the Foreign

**Manufacturer Tax Rate** – The Texas Comptroller's Office recently issued guidance regarding eligibility for the .5% rate for US retailers that are part of an affiliated group. If the affiliated group includes a foreign entity that manufacturers more than 50% of the goods sold by the US retailers, the affiliated group is NOT eligible for the .5% rate. It does not matter that the foreign manufacturer is not part of the combined group. The fact that it is part of the affiliated group is enough to disqualify the entire affiliated group from using the .5% rate.

### Washington – Have a Sweet Tooth?

– Washington State demonstrated it had a sweet tooth when it came to new laws taxing candy, soda and bottled water. All carbonated beverages sold in the state are now subject to a temporary excise of two cents per twelve ounces through June 30, 2013. In addition, Washington extended its sales tax to bottled water as well as candy. The state complicated matters when it defined candy as food product that does not include flour as one of its ingredients. Under this unusual definition of "candy" many traditional sweets such as Kit Kat, Twix and Twizzlers and new products such as Pretzel M&M's are not taxable since all contain flour as an ingredient. This has increased confusion surrounding the new law and the state has since issued a listing of almost 10,000 sweets identifying which are and are not subject to the new tax.