Nexus Requires Compliance and Begins by Filing Tax Returns

"Nexus" may sound like the name of a new smart phone, but it actually refers to the relationship of a taxing jurisdiction that enables it to subject your business to taxation. In addition to your business' home state and city, other states and local jurisdictions where you conduct business can have nexus.

In the past, nexus was determined by a physical presence such as a branch office or manufacturing facility, but e-commerce has extended the definition of nexus. Nexus requires a business to file returns for sales tax and for income or franchise taxes. If you don't file, your business may be liable for past due taxes, penalties and interest.

Sales Tax Nexus

A landmark case for sales tax nexus was the U.S. Supreme Court decision in 2018 in favor of the state of South Dakota in the case of *South Dakota v. Wayfair, Inc.* Since that decision, retailers with annual in-state sales in excess of $100,000 or 200 or more separate transactions now must collect sales tax and file sales tax returns in that state. This ruling applies to retailers located both inside and outside the state.

As a business owner, you collect sales tax from your customers at the time of purchase. You hold that money until you file your sales tax return and remit the proper amount to the taxing authority. If taxes are not collected and paid, your business will be liable and could face penalties and interest. Many retail businesses and restaurants go bankrupt due to their failure to collect and remit sales taxes.

Income/Franchise Tax

You already file income/franchise tax returns in the state and jurisdiction where your company is based. However, if you have locations in other states such as a factory or warehouse, or employees traveling into another state or generating meaningful sales there, you may need to file tax returns there as well.

It's critical to stay up-to-date on filing income/franchise tax returns in all appropriate jurisdictions. If your business ever has to bring a lawsuit in that state, your company must be qualified to do business there as a foreign corporation and filing tax returns supports this qualification. Most states require minimal paperwork and often a certificate of good standing from your home state to register to do business in another state. Your attorney can help you with filings and compliance issues.

If your business is in a highly regulated industry such as liquor or entertainment, it's even more important to comply with tax filing requirements in the states where you do business. Each jurisdiction has its own taxes and filing requirements too. For example, New York City has a commercial rent tax and although it has been reduced over the years, it is still on the books and payment is required.

Voluntary Disclosure Programs

If you find that your business has not been paying sales or income/franchise taxes properly, you will likely be liable for back taxes, penalties and interest in each state and/or jurisdiction. A positive note is that the statute of limitations is set at three years after filing, after which the taxing authority can't audit your return.

If you realize after the fact that you should have filed in a tax jurisdiction but did not talk to your tax consultant about filing an amended return, you may also be liable for back taxes, penalties and interest. However, many states and taxing jurisdictions have "voluntary disclosure" programs that encourage businesses to catch up by filing outstanding or amended returns. In many cases, penalties are waived and payment terms can be very favorable. Keep in mind that it is better to voluntarily come forward than to be found out by the taxing authority.

If you have any questions about nexus and what it may mean for your business, please contact Frankel Zacharia, LLC at 402.496.9100.