MarketWatch

Opinion: States will move quickly to capture more sales tax in wake of Wayfair ruling

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Most will lower thresholds for online and catalog sales, tax expert says

The Supreme Court has issued its decision in the pivotal case of South Dakota v. Wayfair, Inc. The decision will have a profound effect upon sales taxation across the country.

The case centered on whether a business is required to collect sales tax in the state of a purchaser, and if sales alone is sufficient to create "nexus" (the ability of a state to subject a business to its taxes). Wayfair **W, -4.47%** challenged the State of South Dakota law requiring any entity with a minimum of $100,000 in sales or 200 individual transactions within the state to collect sales tax.

The Supreme Court sided with the state, overturning the previous nexus standard which established that a company needed to have physical nexus in a state in order to be liable for the collection of that state's sales tax. Physical nexus is defined as having either property or payroll in the state, including a resident employee working from home or inventory stored in that state.

Under the Wayfair ruling, the court determined that sales alone are sufficient to create nexus. Online and other out-of-state retailers are now required to collect sales tax once their sales in South Dakota exceed $100,000 or they have at least 200 individual sales transactions in the state.

Other states are sure to follow suit and enact laws establishing nexus based on low-threshold sales. (A number of states currently have laws with higher thresholds, but they have been on hold pending the outcome of this case).

The end result of the ruling will be an increase in tax revenue for states and higher operating costs for internet sales companies, which will inevitably translate into higher costs for consumers.

Sellers are now obligated to comply with the individual sales tax rules, rates, and processes of states that enforce nexus. Many companies may need to contract with sales-tax preparation firms to cover the filings and upgrade their billing systems to ensure they are charging the correct tax rates based upon the address of the buyer.

It is likely that most states and other jurisdictions that have sales taxes will implement similar laws. States have long argued that the inability to enforce sales-tax collection requirements on internet and other out-of-state sellers results in unfair competition and increasing budget deficits. This case provides a simple and appealing way for state legislatures to increase tax revenues without alienating in-state constituencies.

In addition, failing to enact such legislation may result in a backlash from home-grown companies struggling to compete against the advantage afforded online and other out-of-state sellers who otherwise have no requirement to collect sales taxes on in-state sales.

Finally, the concern centered on whether states, emboldened by this decision, will seek to expand the use of sales thresholds to create income-tax nexus for sellers. Many states have enacted economic nexus rules for income taxes that create a filing responsibility based on the amount of sales in a state. These amounts have generally been set at $500,000 and above.

Now, states may seek to lower those thresholds to impact more sellers, and states that have not sought income tax nexus may move forward with new legislation.

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