Navigating sales tax requirements for marketplace sellers

New sales tax laws create challenges for businesses that sell via an online marketplace

Tax compliance done right

Marketplace Facilitators Overview Guide

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Introduction: Navigating sales tax requirements for marketplace sellers

Many businesses are adopting an omnichannel sales approach to reach new customers, and more and more businesses turn to online marketplaces such as Amazon, Etsy, and Walmart as a channel to grow their business.

While selling via a marketplace can help businesses quickly and easily reach a new customer base, the additional sales tax obligations that go along with selling through these channels can be difficult to understand. To further complicate matters, a number of states have introduced marketplace facilitator laws in the past year, making sales tax compliance even more difficult for marketplace sellers to follow.

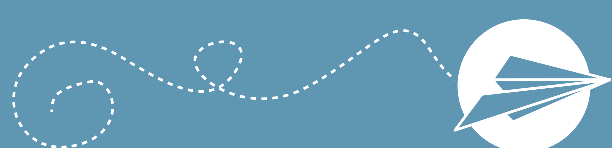
In this guide, we'll look at the five basic steps businesses must take to be sales tax compliant – regardless of sales channel – then we'll dive into marketplace facilitator laws, exploring what they are, where they're enforced, and how they impact the basic steps of sales tax compliance.

Growing marketplace sales

In 2016, half of ecommerce spending took place through online marketplaces and that number continues to grow. Worldwide, marketplace facilitators are expected to more than double their 2017 earnings, from $18.7 billion to **$40.1 billion, by 2022.**

Before we get started, let's quickly review the basic players involved in marketplace sales and sales tax compliance:

- **Marketplace facilitators:** Businesses that provide an infrastructure to facilitate retail sales, collect and process payments, or receive compensation from retail sales. Some of the most well-known marketplace facilitators include Amazon, Etsy, Walmart, and eBay, but there are hundreds.
- **Marketplace sellers:** Businesses or retailers that leverage an online marketplace to sell products to a larger audience. Marketplace sellers benefit from brand awareness, advertising, and a larger customer base through association with a facilitator.
- **Tax authority:** A state or local tax jurisdiction that imposes sales tax collection, remittance, reporting, and marketplace facilitator requirements on businesses selling into the jurisdiction.



Now that we're all on the same page with terminology, let's review the five basic steps to managing sales tax. It's important to understand these steps prior to looking at marketplace facilitator laws so you can fully grasp how these laws impact your business and your associated sales tax obligations.

The five steps for managing sales tax

As your business evolves and changes, your sales tax obligations may also change or expand. And when that happens there are typically five steps you need to take in order to ensure you're compliant at every stage of the sales tax cycle. These steps are applicable regardless of the channel(s) where your business makes sales, but we've highlighted some specific considerations for marketplace sellers throughout these steps.

Step 1.
Determine where your business must collect and remit sales tax

Step 2.
Understand where you need to register to collect and remit sales tax

Step 3.
Calculate the correct sales tax amount

Step 4.
Track and manage exempt sales

Step 5.
Remit sales tax to the tax authority

STEP 1 Determine where your business must collect and remit sales tax

You may not need to collect and remit sales tax everywhere, so determining where your business is required to register, collect, and remit is the first step to sales tax compliance. The connection that establishes a business obligation to collect and remit tax is a concept known as **nexus**. Many business activities create a taxing obligation, including the following:

- Brick-and-mortar locations
- Location of inventory such as fulfillment centers
- Location of company website or data servers
- Employee presence
- Location of company agents or representatives
- Remotely licensed software
- Home office locations
- Trade show, conference, or convention attendance
- Affiliate relationships
- Cookies placed on computers in the state
- Economic activity in the state
- Leads from in-state referrals

While these nexus triggers apply across all sales channels, marketplace sellers should be especially aware of two particular nexus triggering business activities, as they may be more prominent for those that sell via a marketplace: **storing inventory in a warehouse** (even if the warehouse is not owned by you), and **economic activity**. Let's look at these activities in a bit more detail.

Storing inventory in a warehouse

Businesses that participate in the Fulfillment by Amazon (FBA) program may have inventory stored in Amazon warehouses throughout the United States. FBA sellers (and others that sell via a marketplace) may not realize that storing inventory in a state is a nexus-triggering event in all states (except New York), regardless of who owns the storage facility. Since Amazon isn't the only marketplace storing sellers' merchandise in warehouses, and since it's common for businesses to sell through multiple marketplaces, it's crucial that marketplace sellers closely monitor where their inventory is stored or has been stored to determine where they need to collect and remit tax.

Economic activity

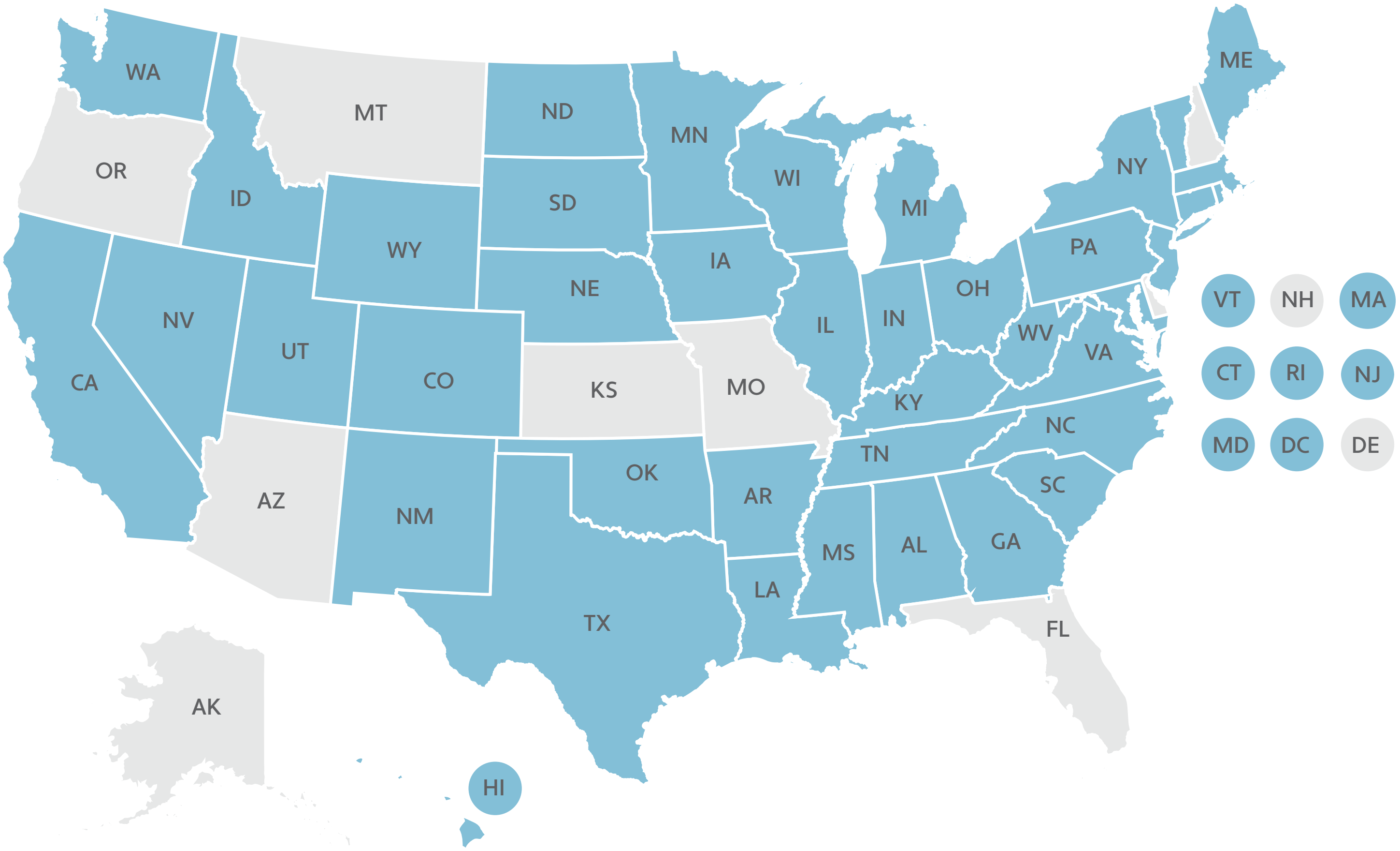
Economic nexus laws are on the rise since the Supreme Court of the United States ruled in favor of the state in South Dakota v. Wayfair, Inc (June 2018). Prior to this ruling, states could only enforce a sales tax obligation on a business that had a physical presence in a state. After this ruling, states can now require remote sellers to collect and remit sales tax based on economic activity alone, even if no physical presence exists in a state.

Prior to the Wayfair ruling, marketplace sellers only needed to monitor where they had some sort of physical connection in a jurisdiction, as that was the de facto standard for establishing nexus. But under new economic nexus laws, sales and/or transaction volume can also establish nexus within jurisdictions. As of July 2019, more than 40 states have economic nexus laws. Each state has different thresholds, effective dates, and applicable sales periods, so it can be challenging to keep the various economic nexus laws straight.

To view details on individual state economic nexus laws, click the map to be taken to our comprehensive economic nexus guide.

STATES WITH ECONOMIC NEXUS LAWS

(As of July 1, 2019)



STEP 2 Understand where you need to register to collect and remit sales tax

After you determine where you have an obligation to collect sales tax, you must register in the appropriate tax jurisdiction before you can begin collecting and remitting. Unfortunately, the process, forms, and requirements to register aren't the same for all state and local tax jurisdictions; however Avalara Licensing can help you navigate the complexity.

It's important to note that if in Step 1 you realize you previously established a tax reporting obligation in a jurisdiction where you're not currently registered and collecting sales tax, you may have a past tax liability that has gone unaddressed. To rectify this situation, you may need to take additional steps to become compliant with the tax jurisdiction, such as remitting unpaid taxes for prior periods or participating in a voluntary disclosure agreement.

The requirement to register in each state used to be fairly cut and dry, but with new legislation, it can be more complicated for marketplace sellers. We'll review other considerations due to marketplace facilitator laws later in this guide.

STEP 3 Calculate the correct sales tax amount

After you've registered, you're ready to start calculating and collecting sales tax. There are more than 12,000 tax jurisdictions in the U.S., and each jurisdiction has different tax rates and product taxability rules, so it can be difficult to know what tax rate to charge. While it's challenging, it's also crucial you get it right so you aren't under collecting for the tax authority, or over collecting causing unhappy customers.

Most marketplace facilitators have built-in sales tax calculation services, but you may need to enable them and set them up properly based on the items you sell and where you need to collect tax. You may also have to pay for this service. The steps for enabling tax calculation are unique for each marketplace, so it's important to consult with the individual marketplace facilitator for set up instructions to enable tax collection.

If you sell via other channels that don't have built-in tax calculations, we encourage you to consider Avalara AvaTax as your automated sales tax calculation solution.

STEP 4 Track and manage exempt sales

Businesses can be exempt from paying sales tax based on the goods or services* they sell, and/or where they sell their products. For example, many states don't charge sales tax for nonprofit or government sales. In addition, products or items intended for resale are typically exempt from sales tax. Regardless of the reason for an exemption, the seller must collect and manage an exemption certificate for each tax-exempt purchaser in order to validate and confirm why sales tax wasn't collected. Failure to produce up-to-date documentation during an audit may leave businesses open to penalties and fines.

Some marketplaces have programs in place to help collect and manage exemption certificates, while others don't allow exempt sales via the marketplace. For example, the Amazon Tax Exemption Program gives marketplace sellers the option to accept exempt sales and have Amazon manage the required documentation.

If you sell through other channels and find it difficult to manage, validate, and store exemption certificates, we encourage you to evaluate Avalara CertCapture as a solution.

STEP 5 Remit sales tax to the tax authority

Now that you've collected the appropriate sales tax amounts, it's time to remit those funds to the tax authorities. Each tax authority has unique regulations around sales tax remittance, including when sales tax returns are due, how they should be remitted (paper or electronic returns), and the frequency returns must be remitted to the taxing jurisdiction

> If you sell via multiple channels or multiple marketplaces, you'll need to gather and compile sales tax data from all sales channels

Sales tax returns must include all sales and revenue, regardless of channel. The key item to remember in Step 5 is if you sell via multiple channels or multiple marketplaces, you'll need to gather and compile sales tax data from all sales channels in order to accurately file your return and avoid double remittance. If you'd like assistance with handling, filing, and remittance, we encourage you to evaluate Avalara TrustFile.

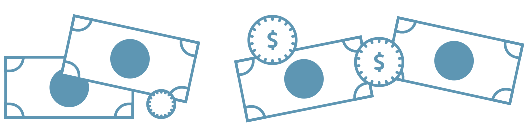
While these steps may seem easy enough to understand and follow, the recent boom of marketplace facilitator laws enacted by states can throw a wrench in their application. Next, we'll review what marketplace facilitator laws are, and how they may or may not impact these five steps.

*Some services such as professional services, consulting, training, etc. are not subject to sales tax and as a result don't require an exemption certificate.

Sales tax and marketplace facilitator laws

Marketplace facilitator laws impose an obligation on the **marketplace facilitator** to collect and remit sales tax on behalf of marketplace sellers. In the previous section, we reviewed the five steps to maintaining compliance that typically fall to the **seller** to track and manage effectively. With the introduction of marketplace facilitator laws, some of the burden of the five steps shifts to the platform that facilitates the sale (the marketplace facilitator, such as Amazon, Etsy, or Walmart). Once we review what marketplace facilitator laws are, we'll review the five steps again to see how they might be impacted by marketplace facilitator laws.

Many marketplace facilitator laws began to appear in 2017, shortly after states realized that while Amazon started taxing sales of its own products, it wasn't charging customers sales tax on third-party, or marketplace, sales. Given that more than half of all Amazon transactions occur through its marketplace, a significant portion of sales were going **untaxed**.



In December 2017, the U.S. Government Accountability Office (GAO) reported that states could substantially increase their sales tax revenue by taxing online marketplace sales. The GAO estimated that while 58–64 percent of non-marketplace online sales were taxed in 2017, only 14–33 percent of online marketplace transactions were subject to sales tax.

> Like many facets of sales tax, marketplace facilitator laws vary by state in their application

Many marketplace facilitators take the position that they're not the actual seller – they merely provide the platform that facilitates sales – and therefore aren't responsible for collecting the sales tax; that obligation has historically fallen on the seller.

States, however, don't want to miss out on tax revenue from marketplace sales. To capture it more effectively, more than 30 states have adopted marketplace facilitator laws in order to shift the collecting (step 3) and remittance (step 5) obligation to the facilitator. Like many facets of sales tax, marketplace facilitator laws vary by state in their application.

Next, we'll highlight the application of marketplace facilitator laws in **three states** to show how they can vary. For a comprehensive list of marketplace facilitator laws, view our State-by-state guide to marketplace facilitator laws resource.

Sales tax and marketplace facilitator laws (cont.)

Alabama

In Alabama, any marketplace facilitator with marketplace sales in excess of $250,000 is required to collect and remit sales tax on sales made by or on behalf of its third-party sellers. While this may seem straightforward, Alabama also has non-collecting seller use tax reporting requirements, meaning a marketplace facilitator that exceeds the threshold of $250,000 in sales may opt out of collecting provided that facilitator complies with the state's non-collecting seller use tax reporting requirements.

New Jersey

In New Jersey, a marketplace facilitator selling into the state is required to collect and remit sales tax on sales made through any physical or electronic marketplace owned, operated, or controlled by a marketplace facilitator, even if the marketplace seller is registered with New Jersey for the collection and remittance of sales tax. However, in New Jersey, a marketplace facilitator and marketplace seller may enter into an agreement with each other regarding the collection and remittance of sales tax. Unlike Alabama, there is no non-collecting seller use tax reporting requirement in New Jersey, so the marketplace facilitator does not have an option to opt out of collection.

Pennsylvania

In Pennsylvania, a marketplace facilitator that maintains a place of business in the commonwealth is required to collect and remit sales tax on the taxable sales made through its forum by any marketplace seller using the forum. A marketplace facilitator that doesn't maintain a place of business in the commonwealth and makes or facilitates $10,000 or more in taxable sales to Pennsylvania customers in the previous calendar year must register to collect and remit Pennsylvania sales tax or comply with non-collecting seller use tax reporting requirements. Starting July 1 ,2019, a remote marketplace facilitator with more than $100,000 in Pennsylvania sales in the previous 12 months is required to collect and remit sales tax on all sales into the commonwealth (i.e., cannot opt out by complying with non-collecting use tax reporting requirements).

As you can see, the application of marketplace facilitator laws varies depending on the state. To add to the mix above, each marketplace facilitator may take different approaches to these laws.

For a full list of states with marketplace facilitator laws, read our State-by-state guide to marketplace facilitator laws.

Now, let's review the five steps to managing sales tax again, with a focus on how things may change if the state has a marketplace facilitator law.

The impact of marketplace facilitator laws on the five steps for managing sales tax

Now that you understand marketplace facilitator laws, let's look at how these laws can impact the five basic steps to managing sales tax. It's crucial for marketplace sellers to remember that marketplace facilitator laws aren't in place across all states, and every marketplace facilitator handles the application of each law differently. So, it's likely that if you sell via a marketplace or multiple marketplaces, you might have different obligations for the various jurisdictions and marketplaces in which you sell.

STEP 1 Determine where your business must collect and remit sales tax

The introduction of marketplace facilitator laws shouldn't impact what constitutes nexus and where your business has a sales tax obligation. Marketplace sellers should continue to monitor their business activities and evaluate where they have an obligation based on the previously-mentioned nexus-triggering activities.

One piece of confusion for many marketplace sellers is the introduction of economic nexus laws and their impact on marketplace facilitator laws.

Most economic nexus laws require sellers to assess their gross revenue or gross sales into a state, **regardless of the sales channel**. That means, if a business surpasses an economic nexus threshold in the state, regardless of how those sales were made, that business has typically established an obligation in the state and must take the appropriate next steps. If you only sell via marketplaces and surpass an economic threshold in a state with an economic nexus law, it may impact your registration requirements - in some cases even if the marketplace collects and remits on your behalf. We'll review this more in step 2. Like most facets of sales tax compliance, each state is unique and laws should be reviewed on a state-by-state basis.

STEP 2 Understand where you need to register to collect and remit sales tax

The introduction of marketplace facilitator laws might impact where your business must register, especially if your nexus obligation is established based on economic activity alone in the state. Typically, if your business has a nexus obligation in a tax jurisdiction, you need to register, regardless of whether the state has a marketplace facilitator law. However, things get tricky when a state has both an economic nexus and marketplace facilitator law. Some states don't require a business to register if they surpass an economic threshold to establish nexus, only sell through a marketplace into the state, and have no physical presence in the state. Most states vary registration requirements based on how the marketplace seller makes sales in each state. For more information on individual state requirements for registration, read the state-by-state registration requirements for marketplace sellers.

Other states updated their registration forms to reflect the introduction of marketplace facilitator laws and allow businesses to indicate if all sales into the state are via a marketplace. Some states are using this information to determine how often sellers need to remit to the taxing jurisdiction.

STEP 3 Calculate the correct sales tax amount

The introduction of marketplace facilitator laws will likely impact sales tax calculations. If you're selling via a marketplace into states with a marketplace facilitator law, you may see that your sales into those jurisdictions have sales tax calculated, or you may be asked by your marketplace to enable sales tax collection in these states.

In any instance, your marketplace facilitator should clearly communicate with you how it handles marketplace facilitator tax collection, including who will be responsible for determining the correct tax rate if the seller is audited. Each marketplace is unique, so always refer to your marketplace for questions.

STEP 4 Track and manage exempt sales

The introduction of marketplaces facilitator laws shouldn't have an impact on exempt sales. An exempt sale still requires a valid exemption certificate in order to verify why tax wasn't collected. Consult your marketplace facilitator if you have further questions and to determine who is ultimately responsible for tracking and managing exemption certificates if the seller is audited.

STEP 5 Remit sales tax to the tax authority

The introduction of marketplaces facilitator laws will likely impact your sales tax remittance. If you're selling via a marketplace into a state with a marketplace facilitator law, your marketplace facilitator will likely begin to remit the sales tax on your items sold through their marketplace. If a marketplace is collecting and remitting on your behalf and you aren't aware or planning to account for this, you risk double filing with the state. Since the marketplace facilitator collected sales tax from the customer, those remittance funds will likely be coming out of your own pocket and profits.

Understanding the requirements that go along with selling through an online marketplace is critical to maintaining sales tax compliance.

But you may save yourself time, effort, headaches, and possibly money by ensuring you have a deep understanding of how marketplace sales can impact your sales tax obligations and compliance. Non-compliance with marketplace laws – or any sales tax legislation – can result in penalties, fines, and other consequences for your business. If you still have questions, review our marketplace sellers' resource hub for additional resources for marketplace sellers.

Because each marketplace is unique, we recommend sellers work directly with the marketplace facilitator to determine how sales tax collection and remittance is handled on their platform. Although we hope you find the information helpful, this guide does not offer a substitute for professional legal or tax advice. If you have questions about your tax liability or concerns about compliance, please consult your qualified legal, tax, or accounting professional. This document was compiled in July 2019. Because states constantly update and amend their sales and use tax laws, see each state's website for the most up-to-date and comprehensive information.

About Avalara

Avalara helps businesses of all sizes get tax compliance right. In partnership with leading ERP, accounting, ecommerce and other financial management system providers, Avalara delivers cloud-based compliance solutions for various transaction taxes, including sales and use, VAT, excise, communications, and other indirect tax types. Headquartered in Seattle, Avalara has offices across the U.S. and around the world in the U.K., Belgium, Brazil, and India. More information at avalara.com.

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