



M2K - USA Sales Tax Series

Determining Nexus

ALERT #4

Foreword

Sales and Use tax compliance is a major challenge for businesses operating in the United States. Unlike many countries with a single national sales tax, US sales tax being a local levy, there are **thousands of taxing jurisdictions**. This means businesses must navigate a maze of different tax rates, taxability rules, filing schedules, and exemption requirements just to sell the same product in different states.

The complexity doesn't stop there. The **2018 Supreme Court Wayfair decision** changed the game by requiring businesses to collect and remit sales tax even if they have no physical presence in the state. Now, simply exceeding a certain number of sales or revenue in a state can trigger a tax obligation, making it even harder for remote sellers and online businesses to keep up. States have moved quickly to enforce these "economic nexus" rules, and the risk of audits and penalties for non-compliance is higher than ever. Further, certain states levy sales tax on enumerated services, which is unknown to many businesses operating in the United States.

M2K's US Sales Tax Series is designed to educate the readers/ businesses & simplify the complexities. In the series, we will explain how sales and use taxes work, when should you get registration, what are the compliances that would apply, etc.



What is nexus?



Nexus is the connection between a business and a state that gives the state the legal authority to require the business to collect and remit sales tax.



In June 2018, the U.S. Supreme Court issued a game-changing ruling in **South Dakota v. Wayfair, Inc.**, overturning decades of precedent and allowing states to require out-of-state sellers to collect and remit sales tax—even if the seller has no physical presence in the state.



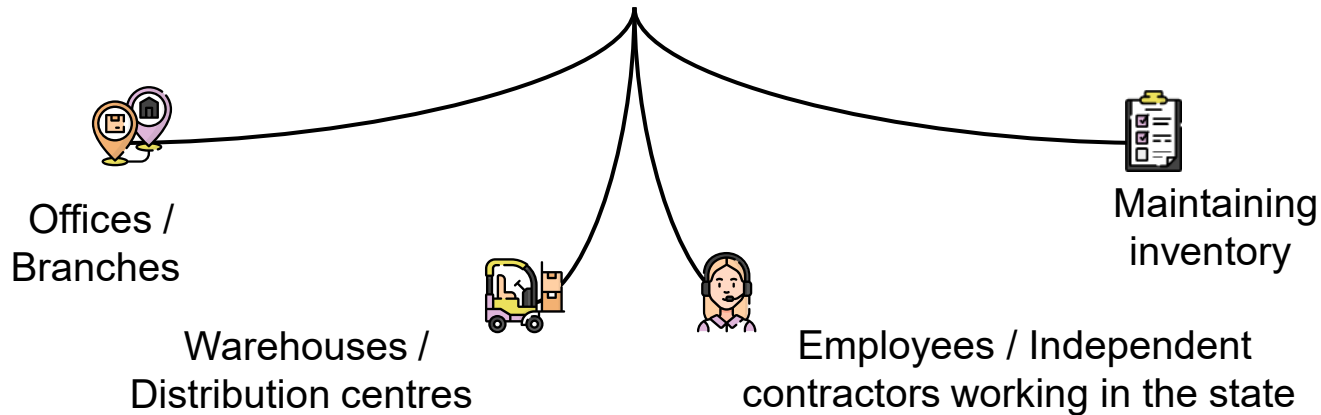
This decision redefined the concept of nexus, shifting from a strictly physical model to one that includes economic activity also. The result was the creation of economic nexus laws across the country.



The various types of nexus that could trigger registration in a particular state are physical presence, economic presence, affiliate presence, click through arrangements, etc.

Physical nexus

Physical nexus is the most traditional and straightforward type of nexus. A business has physical nexus in a state if it maintains a tangible presence there. This includes:



Example: If your business has an office in Colorado, you are required to register, collect, and remit sales tax in Colorado, regardless of how many sales you make.

Economic nexus

- ❖ Economic nexus rules allow states to require sales tax collection based solely on sales volume or transaction count into the state - even without physical presence.
- ❖ Most states have adopted thresholds similar to South Dakota's: \$100,000 in annual sales or 200 transactions. If a business exceeds the thresholds mentioned in the state law, it must register for sales tax.
- ❖ For determining the threshold, certain states require inclusion of even sales that are not taxable i.e., sale for resale, exempt sales, etc. Therefore, even if there may not be a requirement to collect sales tax, the business might still have to register and file sales tax returns.
- ❖ The period for determining the economic threshold is generally on a yearly basis. However, the determination could be based on current year or previous year, depending on the state rules.
- ❖ **Example:** If a company located in Illinois makes \$150,000 in online sales to customers in California with no physical presence there, it still must register in California due to economic nexus.



Other key triggers for nexus

- **Affiliate nexus:** Affiliate nexus occurs when a business has a relationship with another business that has a physical presence in a state (related parties like associates, subsidiaries, holding companies, etc.).
- **Click-through nexus:** This can occur when a business pays a commission or referral fee to a third party for sales made through their website or marketing efforts. It creates a presumption of nexus for out-of-state sellers who compensate an in-state person for business solicitation.
- **Participating in trade shows:** Participating in trade shows or professional events in a state may trigger nexus, especially if the event involves soliciting sales.
- **Employees / agents:** Having employees or agents working remotely from another state can create nexus in that state.



Stay tuned for more updates on Sales & Use Tax

Please find below the list of alerts proposed to be released in the series (every Tuesday & Thursday). In case you have missed the previous alerts, click on the [hyperlink](#).

General overview

1. **Introduction to sales & use tax**
2. **Situs of sale**
3. **Sales tax exemptions**
4. Determining nexus
5. Registration & compliances
6. Voluntary disclosure agreement
7. Sales tax on software & SAAS

State wise overview

- | | | |
|----------------|--------------------|--------------------|
| 1. Delaware | 18. Kansas | 35. North Dakota |
| 2. New Jersey | 19. Kentucky | 36. Ohio |
| 3. California | 20. Louisiana | 37. Oklahoma |
| 4. Alabama | 21. Maine | 38. Oregon |
| 5. Alaska | 22. Maryland | 39. Pennsylvania |
| 6. Arizona | 23. Massachusetts | 40. Rhode Island |
| 7. Arkansas | 24. Michigan | 41. South Carolina |
| 8. Colorado | 25. Minnesota | 42. South Dakota |
| 9. Connecticut | 26. Mississippi | 43. Tennessee |
| 10. Columbia | 27. Missouri | 44. Texas |
| 11. Florida | 28. Montana | 45. Utah |
| 12. Georgia | 29. Nebraska | 46. Vermont |
| 13. Hawaii | 30. Nevada | 47. Virginia |
| 14. Idaho | 31. New Hampshire | 48. Washington |
| 15. Illinois | 32. New Mexico | 49. West Virginia |
| 16. Indiana | 33. New York | 50. Wisconsin |
| 17. Iowa | 34. North Carolina | 51. Wyoming |

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Thank You



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