

Operating across state lines presents tax risks — or possibly rewards



It's a smaller business world after all. With the ease and popularity of e-commerce, as well as the incredible efficiency of many supply chains, companies of all sorts are finding it easier than ever to widen their markets. Doing so has become so much more feasible that many businesses quickly find themselves crossing state lines.

But therein lies a risk: Operating in another state means possibly being subject to taxation in that state. The resulting liability can, in some cases, inhibit profitability. But sometimes it can produce tax savings.

Do you have “nexus”?

Essentially, “nexus” means a business presence in a given state that's substantial enough to trigger that state's tax rules and obligations.

Precisely what activates nexus in a given state depends on that state's chosen criteria. Triggers can vary but common criteria include:

- Employing workers in the state,
- Owning (or, in some cases even leasing) property there,
- Marketing your products or services in the state,
- Maintaining a substantial amount of inventory there, and
- Using a local telephone number.

Then again, one generally can't say that nexus has a “hair trigger.” A minimal amount of business activity in a given state probably won't create tax liability there. For example, an HVAC company that makes a few tech calls a year across state lines probably wouldn't be taxed in that state. Or let's say you ask a salesperson to travel to another state to establish relationships or gauge interest. As long as he or she doesn't close any sales, and you have no other activity in the state, you likely won't have nexus.

Strategic moves

If your company already operates in another state and you're unsure of your tax liabilities there — or if you're thinking about starting up operations in another state — consider conducting a nexus study. This is a systematic approach to identifying the out-of-state taxes to which your business activities may expose you.

Keep in mind that the results of a nexus study may not be negative. You might find that your company's overall tax liability is *lower* in a neighboring state. In such cases, it may be advantageous to create nexus in that state (if you don't already have it) by, say, setting up a small office there. If all goes well, you may be able to allocate some income to that state and lower your tax bill.

The complexity of state tax laws offers both risk and opportunity.

Please contact Ceschini, CPAs at (631) 474-9400 for more information about this topic and other tax and business developments – such as new IRS regulations and court decisions.

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