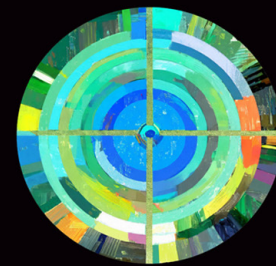


M&A Tax Talk

Indirect tax considerations in M&A transactions in a post-*Wayfair* world

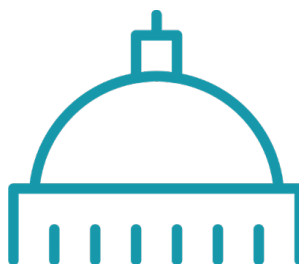


The 2018 *Wayfair* ruling significantly changed how states impose sales tax. For taxpayers contemplating a M&A transaction, staying apprised of the changing landscape will be increasingly important to avoid unexpected indirect tax liabilities.

Changing rules under *Wayfair* may not make it “easier” to determine filing obligations

In June 2018, the US Supreme Court ruled in *South Dakota v. Wayfair, Inc.* that states may require a sales tax collection by out-of-state sellers, even when the seller does not have a physical presence in the state. This is a significant departure from the previous standard established in *Quill Corp. v. North Dakota* in 1992, which generally held that a physical presence was required to collect sales or use taxes on sales made by out-of-state retailers to in-state residents.

As a result of *Wayfair*, all states have imposed nexus standards based on economic thresholds. For example, Connecticut requires a business with at least \$100,000 in CT gross receipts and which has 200 or more retail transactions from outside CT to destinations into CT for the preceding 12 months to register and collect sales tax, but Pennsylvania requires at least \$100,000 of sales. Although the *Wayfair* decision may make it easier to initiate the “sales tax” discussion in the context of a transaction, the due diligence process still must be performed to understand a company’s historical sales tax position and potential exposures. Further, the process



may be more complex due to the changing state sales tax rules and requirements. A buyer should analyze and understand a target company’s activities across the United States to determine if a physical nexus (a taxable presence in the state) was created and, for more recent periods, evaluate any areas of economic nexus.

Deloitte’s M&A practitioners can assist clients in performing a thorough analysis of a company’s activities. Through this process, a buyer may learn that the company created a physical nexus based on one of the various pre-*Wayfair* nexus triggers, including physical locations, inventory, traveling salespersons, marketing, or service employees in a state. Other activities may fall under additional nexus rules, such as the “affiliate,”ⁱ “clickthrough,”ⁱⁱ and “marketplace provider/ facilitator”ⁱⁱⁱ rules.

For periods post-*Wayfair*, a buyer still needs to consider all the physical nexus rules first, and then consider the target company’s presence in any states that have economic nexus standards. States have implemented additional nexus standards based on the *Wayfair* ruling where a physical nexus has not been created. Nexus analyses should also be performed for businesses that have determined there is no registration or sales tax collection requirement for states that impose indirect tax. Further, a business with growing interstate activity may have triggered economic nexus at any time.



ⁱ “Affiliate nexus” refers to a connection between a vendor and another entity that may be related in some way or that performs certain work that can be attributed to the vendor to cause, or presume to cause, the vendor to have nexus in the taxing jurisdiction.

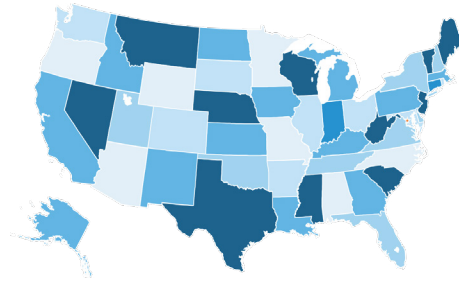
ⁱⁱ “Click-through” An out-of-state business establishes “click-through nexus” in a state when an in-state business receives a commission for referring a certain amount of sales to the out-of-state seller, as through a website link (“clicking through”). New York was the first state to create a click-through nexus law in 2008.

ⁱⁱⁱ “Marketplace facilitator” A marketplace facilitator is a business or organization that contracts with third parties to sell goods and services on its platform and facilitates retail sales. Marketplace facilitators enable these sales by listing the products, taking the payments, collecting receipts, and in some cases assisting in shipment. When we refer to “marketplace facilitator laws,” we’re talking about legislation surrounding the sales tax responsibilities of these facilitators that a number of states have been implanting or enacting.

Transaction considerations

Evaluating sales tax registrations and filings, particularly a previously unidentified obligation, creates challenges for both buyers and sellers. The look-back period for which a jurisdiction can conduct an examination related to a physical nexus can be quite long if a taxpayer fails to file sales tax returns. In this case, the jurisdiction may deem that the assessment statute of limitation has not yet begun to run; thus, a company may have years of potential tax exposure if it was not timely filing or remitting sales tax. It is in both the buyer's and the seller's interest to quantify and resolve exposures in a timely manner, which may also potentially limit the applicable period open to assessment (look-back period).

In addition, once a potential issue has been identified, remediation of this obligation can be complicated and time-consuming. A business interested in addressing prior exposures needs to evaluate applicable state nexus rules and facts, which may include physical nexus start dates, potential collection dates, *Wayfair* legislation changes, threshold analysis, and product and customer taxability. Depending on the industry, a business may be able to identify ways to reduce the potential exposure amount for prior periods if customers paid the tax or there are applicable sales tax exemptions. Additionally, certain states may offer voluntary disclosure programs that allow a taxpayer to voluntarily disclose prior year sales tax and filings with limited or no penalties or limited look-back periods if the taxpayer meets the state-specific criteria.



Conclusion

Being prepared to collect and remit the appropriate tax(es) when nexus triggers are met takes time, money, and effort. Even a business with a limited physical nexus footprint may face taxation from new economic nexus rules and will need to actively understand and monitor any state responses to *Wayfair*, as well as how those states apply new policies to business activities.

Buyers will want to understand a target company's historical sales tax obligations for future obligations and also to determine if any issues relate to prior obligations. If any issues are identified, then the buyer will need to evaluate any potential remediation process, including obtaining appropriate representations in the purchase agreement related to historical sales and use tax obligations. Doing a deep dive of business activities, identifying states with sales tax nexus (including start dates) during the diligence process, and remediating potential exposure shortly after acquisition may help reduce unanticipated sales tax post-transaction.

Want to learn more?

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