SALT: What You Should Know About State and Local Tax Payments

Arthur F. Rothberg, Managing Director, CFO Edge, LLC

One of the more confusing things that business leaders sometimes have to deal with is the payment of state and local taxes, or SALT. Companies that conduct business in multiple states may be required to pay SALT, but many often aren't aware of this obligation.

Whether or not a company must pay SALT is determined by a concept called "nexus." This refers to any potential connection between the company and a state that would dictate that the company has a presence in the state and is therefore subject to taxation. A company does not have to have a physical presence in a state (like an office or warehouse, for example) for nexus to apply — nexus is determined based on the level of business activity performed in the state.

Nexus and Income Tax

Different nexus standards apply to different kinds of taxes. A company will generally be subject to paying income tax in a state if it has a physical presence in the state (including employees who live there) or gains income from sources in that state. An exception exists for salespeople located in a state other than the state where the company is located, as long as orders are fulfilled in another state.

There is a long list of business activities that could trigger nexus with regard to income taxes, including whether or not the company:

- Leases or owns real or personal property (including inventory) in the state.
- Leases to customers who are located in the state.
- Performs repairs, installations or training or has meetings in the state.
- Participates in trade shows in the state.

To help simplify matters, a model has been created by the Multi-State Tax Commission that states can use to define income tax nexus. The model states that income tax nexus exists if any one of the following applies:

- The company owns at least $50,000 worth of property that's located in the state.
- The company processes at least $50,000 worth of payroll in the state.
- The company sells at least $500,000 annually in goods and services in the state.
- At least 25 percent of the company's sales are made or payroll is paid in the state, or at least 25 percent of its property is located in the state.

Sales and Payroll Taxes

Determining nexus with regard to sales tax is a little bit simpler: Companies are considered to have nexus in a state and be subject to sales tax if they have a physical presence in that state. This includes having employees who live in the state, making deliveries in the state using company vehicles, and exhibiting at trade shows in the state (with some exceptions, including a 14-day limit in some states before nexus applies).

Of course, sales taxes are actually paid by customers, but the company must collect and remit them to state taxing authorities if nexus applies. Failure to do so could shift liability for payment of sales taxes to the business itself. Businesses that ship goods to other states are also usually required to collect and remit sales tax in these states. This includes sales made over the Internet in most states.

With regard to payroll taxes, companies generally must collect and remit these taxes in each state where its employees are located. This is usually fairly simple except in cases where employees live in one state and work in another — for example, if the company is located near the state line. Here, withholding may be subject to both states' laws, which can get complicated unless the states have reciprocal agreements.

If you determine that you owe back state taxes that you weren't aware of, you may be able to take advantage of your state's Voluntary Disclosure Program. These programs eliminate or reduce penalties and interest and reduce the look-back period if the business makes the state aware of the back tax liability. However, your business must make the first move — if the state discovers underpayment of taxes first, it usually is not going to be as forgiving.

Concluding Thoughts

Given the current economic environment, Los Angeles and Southern California executives should make sure they are aware of their SALT obligations. Many states are sharpening their focus on collecting SALT in order to help shore up their budgets, and they have tools at their disposal to help them identify out-of-state business' SALT obligations and enforce collections. An outsourced CFO services provider can help you determine whether or not you have nexus in any other states and ensure that you meet all of your SALT payment obligations.

About CFO Edge

CFO Edge, LLC is a leading Southern California provider of outsourced CFO services. Based in Los Angeles, we are a group of experienced chief financial officers who engage with CEOs and CFOs on demand to address strategic planning, business management, and day-to-day financial operations challenges. Our seasoned professionals deliver services as interim CFOs, part-time CFOs, project-based CFOs, recruitment-to-permanent CFOs and interim-to-permanent CFOs. At CFO Edge, we're passionate about helping our clients create, grow and sustain value. For more information, visit www.cfoedge.com or call 626.683.8840.