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State Tax News: Desperate Times Call for Desperate Measures

While the U.S. federal government can print money and issue additional Treasury obligations to fund budget shortfalls, U.S. states have no such latitude. Annual operating budgets must be balanced.

In order to balance the budget, states have few alternatives. There is little political will to increase tax rates or bases, particularly during an economic downturn. The only real alternative is to attempt to track and tax the noncompliers, preferably out-of-state companies whose principals cannot exert influence at the voting booth.

If you ship products or provide services into a particular state, there is a reasonably good chance that you will end up in that state's radar and become subject to tax in that state. The U.S. Customs and Border Protection Service routinely provides individual states with information regarding which companies are shipping goods into their state for a nominal fee.

In a 2004 press release Sprint Corporation (i.e. now Sprint Nextel Corporation) boasted that it had equipped Texas state tax collectors with wireless technology that had helped the state increase the collection of delinquent taxes by \$13 million over the previous 16 months. According to the release, the state's enforcement team mobile access for easy retrieval of information to collect taxes while in the field. Sprint boasted that its "...high-speed wireless technology helps field staff increase their field time and productivity to provide timelier taxpayer service and improve tax compliance."

For examples of this technology, consider the following:

- In New Jersey, home of the fictional Soprano crime family, state agents equipped with wireless technology have been stationed at truck inspection stops. If it is determined that the truck is carrying goods destined to a New Jersey customer

where the vendor has not been filing New Jersey tax returns, the truck and the goods have been seized pending the payment of a \$10,000 bond refundable, in whole or in part, after the taxpayer files the required New Jersey returns.

- In Pennsylvania, state tax auditors examining the annual returns of Pennsylvania-based companies routinely go on a “fishing expedition” to identify out-of-state vendors. If it is determined that the vendor does not file a Pennsylvania return, a questionnaire is sent to the vendor. If a completed questionnaire indicates taxability or a questionnaire is not returned, jeopardy assessments are likely to follow.

The rules governing what types of activities are subject to income or franchise tax differ from state to state. Activities that could create taxable nexus in a state includes but is not limited to the following; licensing software, owning inventory, owning goods on consignment, occasional in-state deliveries by a company-owned truck, sale of services or the solicitation of sales and services, set-up of promotional items, attendance at trade shows, presence in the state of a nonsalesperson employee, having a website accessible in a state, arranging third party installation or maintenance of personal property sold to in-state customers, in-state warranty repair services and unrelated parties collecting on delinquent in-state accounts.

Despite this exhaustive list of ways to tax in-state and out of state businesses, many states are in a panic mode. For example, California has suspended the utilization of net operating loss carryforwards in 2008 and 2009 for taxpayers with business income of at least \$500,000.

Given the facts on the ground, Canadian companies doing business in the U.S. should consult with a competent U.S. tax professional to ascertain that their state tax exposures are mitigated.