

# Word to the Wise



A Newsletter for Clients and Friends of Wouch, Maloney & Co., LLP



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## Dramatic Sales Tax Change

The U.S. Supreme Court issued a ruling in the South Dakota vs Wayfair case that opens the door for states to impose sales tax on sellers outside their borders. The case highlights a new standard of business presence called "economic nexus" that may have major implications for businesses and consumers alike.

### Economic nexus explained

The exact definition varies, but in general, economic nexus makes a connection between a taxing authority (usually a state) and a seller based on certain sales or transaction levels. The Supreme Court agrees with South Dakota that having economic presence is enough to require an out-of-state retailer to register with the state to collect and remit sales tax. For example, the state of South Dakota mandates that if a retailer has \$100,000 in annual in-state sales or has 200 separate in-state sales transactions over the previous 12 months, they must collect sales tax on all sales in South Dakota.

### What it means for businesses

- **New, lower threshold for tax exposure:** Sales tax nexus was mostly determined by physical presence. If a business has an office or employee located in a state, they likely were required to collect tax on sales in that state. The economic nexus standard removes the physical presence requirement with this ruling. Businesses now may need to compare sales-by-state data to the individual state economic nexus laws to determine whether they have a sales tax obligation in that state.
- **More tax registrations & filings:** Businesses that sell outside their state may need to register in many more states – maybe all 50. With more registrations come more compliance management and more sales tax returns that need to be filed on an ongoing basis. The impact on workload for sales tax staffs could be huge.
- **Increased audit potential:** With each new state registration comes a new potential audit authority. Sales tax audits almost always bring in additional revenue for states, so they will be looking to capitalize on the increased registrations. Sales tax compliance management is more important than ever and could lead to state income tax changes.

### What's next?

As many as 16 states have economic nexus laws in place to try to take advantage of the new ruling, with many more to introduce legislation. By nature, Internet retailers will be hit the hardest and are expected to lobby in states that have not passed economic nexus laws. In addition, it will take states some time to get their systems updated to handle the new laws and increased filings. While there might be some short-term delays during implementation, sales tax changes appear to be on their way.

**Please let us know if you have any questions about the new sales tax change by calling us at 215-675-8364.**

## Beware IRS Scams

Tax scams that involve sending emails appearing to come from the **IRS** and/or **accounting professionals** are becoming increasingly common. Scammers often send emails to victims in the hopes of luring them into giving up their personal and financial information. *Checking the email address of the sender may immediately alert you to a false email.*

If you receive a suspicious email claiming to be from the IRS or Wouch, Maloney & Co., LLP:

- Don't reply to the message or open any attachments.
- Forward the email to [phishing@irs.gov](mailto:phishing@irs.gov). Then delete the email.
- Call us if you're not sure the email is from us.



## Setting up Your Business Accounting System

You've done the hard work. You have a new business idea or you've found an existing business to purchase. Want to help ensure your business success? Pay attention to correctly setting up your business' accounting system. Here's how:

- **Consider business entity.** Choosing the right legal and tax entity for your business is important. Consult experts to discuss your options. On the tax side, sole proprietors use a Form 1040 Schedule C to report their activity, while other business entities such as S-Corporations and Partnerships file informational returns and pass-through profits to your individual tax return. C-Corporations require separate tax returns without pass-through of profits onto your personal tax return.
- **Determine if you'll use cash versus accrual basis.** There are different approved methods of accounting. You will need to determine which is best for you. Sometimes your business dictates a required method, but not always. The basic difference lies in when you can book revenue and expense. One method (cash) is based upon when you actually receive or make payment. While the accrual method allows capturing this same information when there is an established obligation.
- **Separate your books.** If starting a business from scratch, remember to set up separate bank accounts and recordkeeping. IRS auditors are quick to disallow expenses when your business expenses are mingled together with personal expenses. The same is true with credit cards. Use a separate credit card for your business transactions.
- **Use sub-ledgers.** Well-run businesses understand the need to organize elements of their business into accounting categories. These categories often use their own reporting system called sub-ledgers. Common areas are sales, accounts receivable, accounts payable, fixed assets, and inventory.
- **Honor cash flow.** Often success or failure of your business is predicated on whether you have enough cash to pay your bills. Determining your cash needs means understanding the cash situation of your business. To do this requires a good set of records. This includes recording your current situation on a timely basis and establishing a forecast of cash needs throughout the year.
- **Create a fortress balance sheet.** Banks love a strong balance sheet. If you think your business may need money for expansion, you will want to focus on developing a strong balance sheet that is low in debt and high in liquid assets like cash and accounts receivable. The irony here is that it's easy to borrow money when your records show you don't need it and it's hard to borrow money when you do need the funds.
- **Identify financial pressure points.** Every business has a few financial items that drive profitability. Do you know yours? It might be payroll in a labor-intensive business. It might be rent in a retail establishment. Perhaps your margins are low because of heavy promotional costs. A strong accounting system will help you stay focused on the more important financial elements of your business.
- **Understand seasonality.** By setting up a good accounting system AND forecasting performance over a twelve-month period, you will understand the true needs of your business. This is especially important if your business is seasonal in nature.

Remember, by spending time setting up the accounting system that is right for you, you are increasing your business' chance for success.

