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Hidden Exposure: Origination or Destination Sales Tax Rate?

By J. Pablo Garciga

Even before dealing with the more complex sales tax issues, upon determining that one has nexus in a US state, vendors must determine the proper sales tax rate to charge - a determination fraught with ambiguities.

If a vendor has sales tax nexus (i.e., the responsibility to collect and remit sales taxes) in only one State, the determination is a bit easier. However, even in this simple scenario: does one charge the origination or destination rate? In the US about 45 states and many local jurisdictions impose sales and use taxes. There are thousands of possible sales tax rates. The 'correct' rate to charge depends on a given State's rules. The sheer quantity of rules often leads to confusion.

Assume a vendor is headquartered in Virginia ('VA') and therefore has VA sales tax nexus. VA follows an origin based sourcing for intrastate sales. If an order for merchandise is placed at the vendor's store in Pennington Gap, VA, and the merchandise is shipped to the buyer in Herndon, VA, which sales tax rate should be charged? Keep in mind that Pennington Gap (origination) imposes a 5.3% sales tax and Herndon (destination) imposes a 6.0% sales tax. Since VA follows the origination rate for in-state vendors, the proper sales tax rate under these circumstances would be 5.3%.

But, is that the whole story?

What happens if the vendor making the sale described above is an out-of-state vendor making an interstate sale to a customer in VA? Assume the vendor is located in the adjacent State of Maryland and has no physical connection to VA other than sporadic visits throughout the year by a traveling salesperson who creates VA use tax nexus for the Maryland vendor. Since VA follows the destination rule for interstate sales, the proper sales tax rate to charge under this scenario would be 6.0%. Sales tax compliance in the US is a risky venture.

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Funaro & Co. PC provide a wide range of services, including accounting and auditing, tax reporting and compliance, tax advisory, management consulting, and transaction advisory.

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