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SUPREME COURT DECISION
CONTINUES TO EVOLVE FOR
NONPROFITS THAT SELL ITEMS
TO BUYERS IN STATES WHERE
THEY (THE NONPROFITS) DO NOT
HAVE A PHYSICAL PRESENCE**

**HELPFUL RESOURCES TO ASSIST WITH
COMPLIANCE NOW AVAILABLE**

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NONPROFIT SPECIAL ALERT™



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Significant Impact of 2018 Supreme Court Decision Continues to Evolve for Nonprofits That Sell Items to Buyers in States Where They (the Nonprofits) Do Not Have a Physical Presence

Helpful Resources to Assist with Compliance Now Available

By Mike Batts, CPA & Kaylyn Varum, CPA

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As we originally reported in our June 21, 2018 Special Alert, in 2018 the US Supreme Court ruled in *South Dakota v. Wayfair, Inc., et al.*, that states can, in some circumstances, require a seller that does not have a physical presence in the state to collect sales tax on sales to buyers in the state and remit the taxes collected to the state.¹

This decision has major implications for nonprofit organizations that sell items across state lines.

Background – The Physical Presence Standard

Historically, physical presence has been the most common standard used by state governments to determine whether an entity is subject to a state's sales tax collection and remittance requirements. The core element of the physical presence standard is that a seller must have some type of physical presence in a state in order for that state to be able to assert jurisdiction over the seller for purposes of requiring the seller to collect sales tax on sales to buyers in the state. Examples of physical presence could include having an office in the state, having employees based in the state, maintaining inventories in the state, or owning property in the

state. As noted below, however, application of the physical presence standard by states has not been uniform.

The physical presence standard was affirmed in a landmark 1992 Supreme Court case, *Quill Corp. v. North Dakota*, and thus has often been referred to as the *Quill* principle. In the 1992 case, the Supreme Court ruled that a business must have some in-state physical presence to be subject to collection responsibility for the state's sales tax. However, this in-state physical presence standard was not clearly defined, and state governments employed a variety of definitions in applying the standard.

The *Wayfair* Decision and the Economic Nexus Standard

With the emergence of web-based commerce and large online retailers such as Amazon and Wayfair, a number of states, including South Dakota, began to challenge the physical presence standard affirmed by the Court in *Quill*. Through legislative or regulatory action, these states asserted that physical presence is **not** required to establish "nexus" (a legal term for being subject to a state's jurisdiction) for sales tax collection purposes. These states asserted that a seller can establish nexus in other ways, such as by engaging in a large number of sales transactions with buyers in the state. This version of nexus is commonly referred to as "economic nexus" to distinguish it from nexus based on some type of physical presence in a state.

South Dakota's sales tax law requires a seller to collect and remit sales tax if the seller's South Dakota sales exceed \$100,000 or if the seller has more than 200 separate sales transactions in South Dakota in a one-year period. Wayfair, a large online retailer that had no physical presence in South Dakota, challenged the law, and the case made its way to the US Supreme Court in 2018.

As we originally reported in our June 21, 2018, Special Alert (the day the decision was released),

¹ Source: <https://nonprofitcpa.com/u-s-supreme-court-rules-states-can-collect-sales-tax-from-web-based-sellers-that-do-not-have-a-physical-presence-in-the-state/>

the US Supreme Court held in a 5-4 decision that the physical presence standard for state tax jurisdiction is not a requirement under the Commerce Clause of the US Constitution.² Additionally, the majority of justices ruled that South Dakota's economic thresholds of \$100,000 of sales or 200 separate sales transactions in a one-year period satisfied the substantial nexus requirement with regard to the Commerce Clause.

States Respond to the *Wayfair* Decision

After the *Wayfair* decision, state taxing authorities evaluated their laws to determine the implications for state sales tax collection and remittance requirements in light of the *Wayfair* decision. Every state with a state sales tax has established an economic nexus standard for sales tax jurisdiction. The most common economic thresholds being used are \$100,000 in sales or 200 transactions in a year. Other states have implemented a threshold of \$100,000 of sales (with no transaction threshold), and a handful of states have adopted different thresholds.

Even those states that are using the \$100,000 in sales or 200 transactions threshold have differing methods for implementing the threshold. For example, some states use gross sales and others use taxable sales as the sales base for evaluating whether an entity meets the economic nexus threshold. The period in which sales are evaluated (e.g., current calendar year sales, prior four quarters, etc.) can vary state-to-state.

Resources and Guidance to Assist with Compliance

Summary – State-Specific Nexus Rules

As an independent member of BDO Alliance USA, we are pleased to share a BDO resource that summarizes the current state sales and use tax economic nexus statutes.³ This resource provides

a high-level overview of the economic nexus thresholds and the effective dates for states that have enacted economic nexus statutes.

This resource will be updated from time to time.

Specific Considerations in Applying a State's Rules

As noted above, every state with a state sales tax has established an economic nexus standard for sales tax nexus, and therefore, nonprofits should be monitoring sales by state (both in sales and transaction volume) to determine whether economic nexus thresholds have been reached. However, if a nonprofit organization meets such a threshold in a state, is it required to begin collecting and remitting sales tax in that state? Not necessarily. A nonprofit organization should evaluate its specific circumstances in order to determine if it is subject to a state's sales tax collection and remittance requirements. Factors that should be considered include the following:

- **Is the transaction a sale?** (We note that some nonprofit organizations provide donors with certain items in exchange for contributions. Whether such transactions constitute sales for purposes of a state's sales tax law would be a matter requiring specific legal analysis.)
- **Does the organization have a physical presence in the state or meet the state's economic nexus thresholds?**
- **Is there a specific exemption from the requirement to collect and remit sales tax that applies?** (State laws vary and can contain exemptions from sales tax on transactions based upon the type of items being sold, the fact that the seller is a nonprofit organization, the fact that the buyer is a nonprofit organization exempt from sales tax in the state, the fact that the buyer is purchasing the items for resale, etc.)

² Source: <https://nonprofitcpa.com/u-s-supreme-court-rules-states-can-collect-sales-tax-from-web-based-sellers-that-do-not-have-a-physical-presence-in-the-state/>

³ Source: <https://nonprofitcpa.com/wp-content/uploads/2024/09/Updated-Sales-Tax-Nexus-Chart-as-of-February-2024.pdf>

Decision Tree Resource

Given the complexity and variability of the factors that can apply, BMWL has developed a decision tree resource designed to assist nonprofit organizations in evaluating potential state sales tax collection and remittance requirements in light of the *Wayfair* decision.⁴

Practical Aspects of Compliance with Requirements of Multiple States

A nonprofit organization that determines it has sales tax collection and remittance requirements in a number of states, or that its sales are spread widely across the United States such that evaluation of potential sales tax collection and remittance requirements is burdensome, may wish to consider seeking technological solutions or professional assistance in evaluating and complying with the organization's sales tax collection and remittance requirements. There are several software vendors that provide tax calculation solutions and include state and local tax rates for the entire US, which are updated on a monthly basis. Some of these vendors also provide tax return preparation software, which allows for the generation of signature-ready tax returns. Organizations could also consider outsourcing the return preparation process.

Additionally, if a nonprofit organization determines that it is subject to a state's sales tax collection and remittance requirements, the nonprofit organization should consider (under the advice of legal and tax counsel) whether it is subject to other potential filing requirements in the state.

Other filing requirements could potentially include the requirement to register to do business in a state, the requirement to apply for income tax exemption recognition in a state, etc.

BMWL Can Help

As always, if you would like assistance addressing the information described in this Alert, we would be glad to help! Please email our team at Info@NonprofitCPA.com.

⁴Source: <https://nonprofitcpa.com/wp-content/uploads/2019/11/Sales-Tax-Nexus-Decision-Tree.pdf>