Insights: Publications

6 Key Takeaways | Apportioning and Situsing for Multistate Direct and Indirect Taxes

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Kilpatrick's **Jordan Goodman** recently presented on the topic of **"Apportioning and Situsing for Multistate Direct and Indirect Taxes."**

Jordan provides the following key takeaways:

1. Apportioning for Income Taxes and Situsing for Sales Tax Should Be Easy
Afterall, the transaction generating both income and sales tax is the same transaction. But nothing could be further from the truth. A sale into a state for income tax purposes does not necessarily mean you have a sale for that state's transaction tax.

2. States Use Different Rules to Decide Where Business Income Gets Taxed
When companies do business in several states, each state has its own way to decide how much of a company's income they can tax. For tangible personal property, the general rule of destination still applies. However, over time, for sales other than tangible personal property, most states have switched from older methods (like cost-of-performance) to "market-based sourcing," which means they tax companies based on where their customers are located. But not all states use the same rules, so it can get complicated for businesses operating in many places.

3. For Transaction (Sales) Tax, What You're Selling Changes Where it is Taxed
Whether a company is selling physical goods, services, or digital products (like software or streaming), states have different rules for how to tax each one. For example, software might be taxed based on where the customer uses it, while services could be taxed based on where the benefit is received or performed. This means businesses have to know exactly what they're selling and where their customers are to figure out the right taxes. Even identifying who the customer is has become more difficult.

4. Recent Changes in State Laws Make Things Even More Complicated
Several states have recently changed their tax laws in ways that affect how companies must report and pay taxes. For example, California changed how financial services are taxed. Minnesota now taxes management services based on the end customer. Illinois keeps trying to "level the playing field" for local taxes. These updates mean businesses have to pay close attention to new rules in every state where they do business.

5. Real-Life Examples Show How Tricky These Rules Can Be
Examination of a number of states treatments of certain products reveal the inconsistency from state to state.

Companies selling data from loyalty cards, offering software that handles communications, or selling digital goods like NFTs have to sort through a variety of mazes to approximate situsing the product for sales tax. These examples show that it's not always clear how to classify a sale or which state gets to tax it, especially with new digital products. Sometimes, data like an IP address is the only clue, but it's not always reliable.

6. Companies Need Good Data and Advice to Get Taxes Right
Because the rules are complicated and always changing, companies need to make sure they have the right data in their systems to figure out where to pay taxes. Importantly, complete accuracy may be less important than developing a methodology that can be applied on a nationwide basis with trail that can be audited.

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