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**CRAIN'S**  
CHICAGO BUSINESS

## The sales tax puzzle

How to avoid learning tax laws the hard way

by Mary Kane



Among the lessons Kevin Kelly learned when the state audited his catering business: Keep duplicate invoices, filed in chronological order. Photo: Yvette Dostatni

Small business owners who don't understand sales tax may get a tutorial in the form of a state tax audit.

Caterer Kevin Kelly learned that lesson last year, when the Illinois Department of Revenue informed him that he should've been charging customers the state's 6.25% sales tax — sometimes.

Mr. Kelly now knows he doesn't have to charge sales tax when customer supply their own food and his J&L Catering LLC provides only waiters, bartenders and cleanup.

But if J&L provides the food — an entire meal or just part of it, like hors d'oeuvres or dessert — it must charge sales tax on the service. Prior to the audit, he had never charged sales tax in that situation.

"It's extremely confusing," says Mr. Kelly, 35, whose River North-based company has 33 full-time employees and \$3.2 million in annual sales. "The law isn't very clear. And some of it just doesn't make any sense."

### STATE HEADACHE

Mr. Kelly isn't the only entrepreneur who's puzzled by sales tax, and he won't be the last Illinois business owner to find out what he's missing by getting audited.

In March, state investigators collected \$200,000 in delinquent sales taxes from 15 companies in Cook County after threatening to revoke their business licenses.

Last year, after getting audited, Target Corp., Wal-Mart Stores Inc. and Office Depot Inc. paid the state \$2.4 million in uncollected taxes on Internet sales.

"Sales tax has been historically underreported," says a spokeswoman for the Revenue Department. "Illinois is focusing on compliance."

## **TAX TRIGGERS**

That could be problematic given the peculiar complexities of sales tax laws, which differ not only from state to state but also within the states themselves; some 11,000 separate taxing authorities exist across the country. You may not realize that a few visits from a salesperson for your company could trigger tax liabilities. Or that a trade show exhibit might trigger sales tax liabilities in the state where the show was held.

"You've got a business opportunity, you go and take it, and you don't realize the consequences," says Diane Yetter, president of Yetter Consulting Services Inc., a sales tax consulting firm in Chicago.

But there are some basics that can help you keep the rules straight, she says.

### **Dodging the bullet**

You don't have to memorize the tax code. Just follow these tips:

#### **▶ Know where you're liable.**

Businesses are usually liable for sales taxes in states other than their home state if they maintain a sufficient level of presence in those states, known as a nexus, says sales tax consultant Diane Yetter.

Where do you have people and property placed permanently? If you own a warehouse or inventory in another state or have employees there, you may be subject to state's sales tax.

Be alert for inexplicable quirks. Some states impose sales tax on software updates when they're sent by mail on a disk, but not if they're e-mailed.

If you decide you're liable, get a system in place to collect and report the tax. Then "hope the state doesn't come out and perform an audit" anyway, Ms. Yetter says.

▶ **Decide if it's worth it.**

If you've got just a few sales in a state with complex tax requirements, it might be simpler to give up that business than expose yourself to possible penalties, says Barry Margolin, chief financial officer at Learning Resources Inc. in Vernon Hills. Learning Resources, which makes educational toys, sells in all 50 states through catalogs, stores and the Internet. "It can get complex very fast," Mr. Margolin says.

▶ **Get organized.**

J & L Catering LLC's Kevin Kelly thought he had it together, but during a state audit his company's seven party planners spent days combing through customer records when they could have been out selling. One suggestion: Make extra copies of invoices and file them in chronological order. "The lesson is to be so anally prepared you can say immediately, 'I've got it,' " Mr. Kelly says.

▶ **Get help from the state.**

Martha Olson, co-owner of Tablesapes Party Rentals, which party equipment, sought an opinion letter from the state to explain the sales tax laws after clients became confused about their bills.

If a caterer picks up supplies at Tablesapes' Chicago location for a party in the suburbs, the caterer still has to pay the city's 6% rental tax — plus sales tax on the rental cost of the supplies. Showing clients the state's letter "helped clear things up," Ms. Olson says.