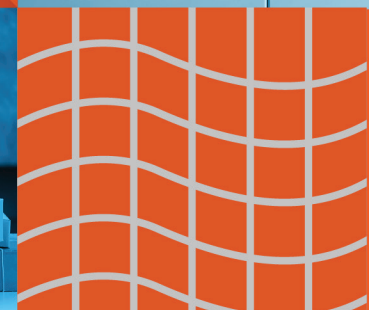


# THE 5 STEPS TO MANAGING SALES TAX COMPLIANCE FOR MARKETPLACES

Choosing the right tax automation solution  
for your business



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## DISCLAIMER

Tax rates, rules, and regulations change frequently. Although we hope you'll find this information helpful, this guide is for informational purposes only and does not provide legal or tax advice.

# Introduction

**In theory, sales tax compliance should be a basic business task – a check box on a long list of must-dos. In reality, it’s tedious, time-consuming, and (often) mind-bogglingly complicated. And as businesses explore more ways to attract customers and increase sales, compliance is only getting more difficult, which is true whether you’re a startup, a household brand, or a legacy company.**

Simply put, there is no feasible way to stay on top of tax compliance without technology. Automating sales tax management with software specifically designed to handle

this work for you is a cost-effective solution; according to an Avalara/Potentiate survey, businesses with 20–499 employees estimate spending an average of \$1,740 per month identifying state sales tax obligations and filing requirements. You can also save your team the time and hassle of manually researching tax changes and updating spreadsheets, not to mention automation can minimize the risk that comes along with human error.

Sales tax can be complicated, but finding the right tax solution fit for your online marketplace doesn’t have to be. It all starts with having a complete picture of compliance.

## THE FIVE STEPS TO MANAGING SALES TAX:

- Step 1.** Understand where you need to register your marketplace to collect and remit sales tax
- Step 2.** Onboard vendors and sellers
- Step 3.** Determine your taxability and identify your buyers
- Step 4.** Calculate the correct taxes for your marketplace
- Step 5.** Remit sales tax, file returns, and deliver 1099 forms

# Step 1: Understand where you need to register your marketplace to collect and remit sales tax

## WHAT IT MEANS FOR YOUR BUSINESS

Sales tax compliance starts with [nexus](#): knowing where you need to collect and remit sales tax based on your business activities within a state or tax jurisdiction. It's key to understand where you have nexus now and where you could trigger it in the future. You should also be clear on whether you have sales tax obligations based on [physical presence nexus](#), [economic nexus](#), or both.

In the U.S. there's no one standard for nexus, every state sets its own rules and thresholds. And these can be vastly different based on where you sell, what you sell, and who you sell to – particularly for marketplaces. Certain states may also include exempt sales in their [economic nexus thresholds](#), which means you could still need to file a \$0 tax return, even if you don't collect tax.

Of course, after you determine where you have tax obligations, the next step is registering to collect and remit tax. Understanding where and how you need to register and which business licenses, forms, and registrations you need to complete before you can begin to collect and remit sales tax is tedious, but key. It's actually illegal to collect sales tax until your business is properly registered; so it's

important to complete this step to avoid fines or risk having to cease operations.

You may have to register for several licenses depending on your business. Because of the variety of products that you sell, you'll have to register for sales and use tax for household goods and certain types of food, excise tax for items like tobacco and fuel, and sometimes even consumer use tax.

## WHY THIS STEP IS IMPORTANT

If you [qualify as a marketplace facilitator](#), you're required to collect and remit sales tax on behalf of the vendors selling on your marketplace. Depending on the size of your marketplace and how you do business, there may be two different paths to take regarding registration.

Your marketplace could register to collect and remit tax everywhere, ensuring that you're prepared when customers across the country place orders. Another option is to selectively register, doing so only when you get orders from customers in new jurisdictions. While the latter option tends to be more cost-effective up front, it can open you up to errors if you

miss a few sales that create tax obligations in new jurisdictions.

Regardless of which route your marketplace takes, knowing where you and your vendors have nexus and getting registered is the first step to maintaining sales tax compliance.

## WHERE PROBLEMS CAN OCCUR

As your business changes, your tax obligations will likely change too. And if you aren't accounting for those changes, you could run into trouble with tax authorities or auditors. Small shifts in your business – an influx of customers, more marketplace sales, new vendors and product types, using drop shippers, selling direct to consumers – could be the tipping point to nexus in more states. It's a lot to manage and changes happen frequently. Keeping up with these changes can inadvertently cause errors and oversights, which could prove costly to your business.

When you go to register your business, you'll find out quickly that the processes, forms, and registration requirements differ from state to state (and sometimes jurisdictions

## Step 1: Continued.

within a state), so there's no simple way to manually register. And getting it wrong or operating without a business license can be a costly mistake.

It's also important to understand marketplace facilitator laws. These laws impose an obligation on the marketplace facilitator to collect and remit sales tax on behalf of the sellers. Marketplace facilitator laws [vary from state to state](#), so be sure you understand the laws as it applies to your business.

### HOW TO AUTOMATE THIS STEP WITH AVALARA

Relying solely on people resources (internal or outsourced) to track and manage nexus simply isn't efficient. You can't expect (or afford) them to be experts on every state's tax rules, regulations, and thresholds, or to constantly monitor when your company's sales could trigger nexus in a new state.

As far as registering goes, there comes a point when your filing cabinets and spreadsheets just won't cut it anymore. Consider a cloud-based license management solution that can

register you to collect and remit sales tax, obtain the licenses you need, and manage your license portfolio in one place.

### WHICH SOLUTIONS ADDRESS THIS STEP

- [Avalara AvaTax](#): Tracks sales activity and sends alerts when you're approaching nexus thresholds
- [Avalara Business Licenses](#): Reduces the complexity of managing license requirements
- [Avalara Sales Tax Registration](#): Register for sales tax in multiple states with one form

### ADDITIONAL SERVICES TO CONSIDER

- [Streamlined Sales Tax](#): Many U.S. states will offset the cost of using a sales tax solution like Avalara – we'll help you get started
- [Avalara marketplace solutions](#): Learn more about our full range of solutions for marketplaces of all types and sizes

### WHAT CAN AFFECT NEXUS:

- Physical location
- Warehouse inventory
- Remote employees
- Affiliate relationships
- Ecommerce and marketplace sales
- Tax-exempt customers and sales

## Step 2: Onboard vendors and sellers

### WHAT IT MEANS FOR YOUR BUSINESS

Your marketplace's success depends on the success of your sellers. You should have a process in place to onboard sellers and collect and remit sales tax for them. [All states with sales tax have marketplace facilitator laws](#) (plus some local municipalities in Alaska) so this is more about making sure your sellers are set up with your system and onboarded with your platform to properly collect sales tax for them.

### WHY THIS STEP IS IMPORTANT

Even if your marketplace is collecting and remitting sales tax for its sellers, they're still required to file their own sales tax returns. Your responsibility as a marketplace is to provide them with the proper documentation to do so, which means matching tax identification numbers (TIN) and providing both W-9s and 1099s to your sellers.

### WHERE PROBLEMS CAN OCCUR

Getting sales tax wrong on behalf of your sellers can be a huge liability for both of you. Under marketplace facilitator laws, you're legally obligated to collect and remit sales tax for your sellers, and you're required to give them the appropriate tax forms ahead of filing season. If you have many sellers, you're responsible for a huge amount of paperwork.

### HOW TO AUTOMATE THIS STEP WITH AVALARA

Managing tax paperwork for multiple sellers can get complicated quickly, especially if you're doing it manually. Investing in an automated solution can save your team time and money while reducing the risk of human error (and paper cuts).

### WHICH SOLUTIONS ADDRESS THIS STEP

- [Avalara 1099 & W-9](#): Collect, manage, and e-file IRS forms for your marketplace sellers

### SOFTWARE INTEGRATIONS

Get real-time tax calculations at the point of sale for your marketplace sellers with tax software integration. Our cloud-based tax compliance automation integrates with [Mirakl](#), [Nautical Commerce](#), and others to deliver more accurate tax rates at the point of sale, saving your marketplace team the tedium and complexity of manually determining taxes across product types and tax jurisdictions.

## Step 3: Determine your taxability and identify your buyers

### WHAT IT MEANS FOR YOUR BUSINESS

It's imperative that you know the taxability of the goods or services that you and your vendors buy, sell, and use. Not all products are taxed the same way across jurisdictions, and even within jurisdictions rates and rules can get complicated.

[Software taxability is also tricky](#); in many states, digital audio files like music and podcasts, digital books, games, and streaming services are taxed differently. Some states, like Alabama, tax digital products, but some states, like Georgia and Missouri, exempt digital goods and services from sales tax. There are also states, like Michigan and Kansas, that tax digital games, but exempt other digital products. Get the download in our latest [state-by-state guide to the taxability of digital products](#).

### WHY THIS STEP IS IMPORTANT

With so many different tax rates and taxability rules to keep track of, it's easy to make mistakes. What's taxed at one rate in one state may be taxed at another rate in a different state or even in another jurisdiction within the same state. In some states, those same products or services could be tax-exempt or partially taxed.

If you or your vendors have tax-exempt customers, you need to consider how you're tracking, managing, and storing exemption certificates. Failure to produce accurate records can result in noncompliance and fines if you're audited.

As a marketplace, it's important to know whether the sellers on your platform are located in [origin-sourced states or destination-sourced states](#). Origin-sourced sales are taxed where the seller is located, while destination-sourced sales are taxed based on where the buyer is located. Most states and Washington, D.C., are destination-sourced, but there are 12 origin-sourced states, including California and Texas, to take note of.

### WHERE PROBLEMS CAN OCCUR

- Suppliers and resellers – You might not need to pay sales tax if you're a supplier. If your marketplace sellers are buying wholesale on your platform to resell, they'll need to provide a resale certificate. Without this certificate, you'll be on the hook for tax for this transaction.
- Retailers with large product portfolios – The more products your business sells, the more tax rates you should be mindful of. Sales tax rates and taxability rules can vary drastically for types of products like clothing, food, software, and home goods.
- B2B – Sellers who primarily sell to other businesses will want to verify that they're getting and maintaining the appropriate tax-exempt documentation. This means obtaining, verifying, and storing exemption certificates from their buyers and suppliers and checking that the information is valid year after year. Each state has its own rules about when exemption certificates expire.
- D2C – If your sellers primarily sell directly to customers, you must stay on top of taxability rules across states and jurisdictions.

## Step 3: Continued.

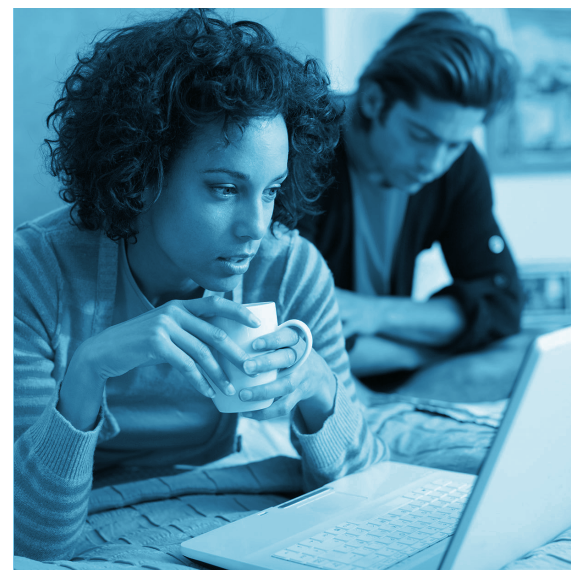
Sales tax holidays can further complicate taxability. A number of states have tax-free weekends for products like school supplies and clothes, energy-smart appliances, and weather disaster supplies. [You should be aware of when these events are happening](#) so you can properly exempt sales tax when necessary.

### HOW TO AUTOMATE THIS STEP WITH AVALARA

Are you keeping track of taxability rules and rates in a spreadsheet, or collecting exemption certificates by email and storing them in a filing cabinet? The inconstant nature of sales tax makes compliance difficult, which is why so many businesses now employ technology to do this work. Avalara software comes with a powerful tax engine and vast tax content library with regularly updated tax rates and taxability rules. Tax automation with Avalara also helps you and sellers monitor changes to taxability, track and store exemption certificates, and keep tidy records in the event of an audit.

### WHICH SOLUTIONS ADDRESS THIS STEP

- [Avalara AvaTax](#): Tracks sales activity and sends alerts when you're approaching nexus thresholds
- [Avalara MatrixMaster](#): Tracks product taxability with the world's largest database of UPCs
- [Avalara Tax Research](#): Access intuitive sales tax research for sales and use tax, VAT, and GST
- [Avalara Tariff Code Classification](#): Classify Harmonized System codes with confidence
- [Avalara Exemption Certificate Management](#): Makes it easier to collect and manage exemption certificates





## Step 4: Calculate the correct taxes for your marketplace

### WHAT IT MEANS FOR YOUR BUSINESS

Get your calculator ready – it's time to calculate sales tax! There are more than 13,000 sales and use tax jurisdictions in the United States, and each one has different rates and taxability rules. Depending on the types of goods and services your business deals with, you could be determining rates and calculating sales tax for a while.

You should understand which variables make up a tax rate, like tax jurisdictions and product taxability, and then put a plan in place to monitor and apply the most up-to-date tax rates on your transactions. Failure to calculate the correct tax can result in overcharging or undercharging your customers, and having to answer for the difference in penalties.

### WHY THIS STEP IS IMPORTANT

It's nearly impossible to calculate marketplace taxes without software that updates frequently and applies tax automatically. This statement is especially true for marketplace facilitators who may have sellers located in different tax jurisdictions. Customers want a seamless checkout experience, which means when they're buying from sellers across jurisdictions, they want all the sales tax to be calculated correctly in their cart. And sellers need to know that if your marketplace is collecting and remitting tax on their behalf you're not mixing up Boise and Baltimore when it comes to tax rates.

### WHERE PROBLEMS CAN OCCUR

As a marketplace your system will be processing transactions from all over the place. That means you need a system that will have the correct tax rates and apply it correctly across every sales and use tax jurisdiction mentioned earlier, and it needs to support multiple "ship-from" origins in a single transaction.

### HOW TO AUTOMATE THIS STEP WITH AVALARA

With automated tax calculation integrated with your ERP, tax rates are instantly applied to every transaction, taking into consideration item taxability rules and exemptions. Get alerts when you're at or about to exceed nexus thresholds. Address validation software pinpoints where the sale originated and applies the applicable tax amounts at checkout. These features help make tax compliance for multistate sellers and cross-border sales much easier to get right, resulting in more accurate calculations and happier customers.

### WHICH SOLUTIONS ADDRESS THIS STEP

- [Avalara AvaTax](#): Tracks sales activity and sends alerts when you're approaching nexus thresholds

## Step 5: Remit sales tax, file returns, and deliver 1099 forms

### WHAT IT MEANS FOR YOUR BUSINESS

So you've determined your nexus obligations and taxability, registered to collect and remit tax in the appropriate jurisdictions, and created a detailed calendar of state sales tax holidays. Now it's time to remit sales tax and file returns (and send out tax forms to your sellers).

### WHY THIS STEP IS IMPORTANT

Your sellers rely on the information you give them to accurately file their sales tax returns, so it's imperative that you [deliver the correct 1099 forms](#) in a timely manner. Forms 1099-K are typically [issued to eligible sellers](#) by the end of January following the previous tax year for which they're filing.

### WHERE PROBLEMS CAN OCCUR

Each tax authority has their own regulations and forms around sales tax remittance, including due dates, format (paper or electronic filing, which is becoming increasingly popular), and frequency. In most states, you should remit taxes to a state agency that then distributes the tax dollars to local agencies. But in some states, like Alabama, Colorado, and Louisiana, you'll have to register and file with those local agencies too.

As we discussed earlier, the more sellers you have on your marketplace, the more complicated the paperwork gets. You'll need to send out accurate 1099 forms to all of your sellers and ensure they receive them on time.

### HOW TO AUTOMATE THIS STEP WITH AVALARA

Collect, manage, and e-file your IRS forms with an automated solution. Avalara 1099 & W-9 can help you streamline vendor information collection, store forms in a secure location, and send information directly to the IRS.

### WHICH SOLUTIONS ADDRESS THIS STEP

- [Avalara Returns](#) and Avalara Managed Returns: Sync your sales data with the marketplace software you already use and remit payments automatically
- [Avalara 1099 & W-9](#): Collect, manage, and e-file IRS forms for your marketplace sellers
- [DAVO by Avalara](#): Automate sales tax for your food service marketplace

# A complete tax compliance solution built for how you do business

At Avalara, we live and breathe tax compliance. That means that we have solutions to help you determine nexus obligations, register, calculate sales tax, manage exempt sales, and file and remit your returns – saving you time and hassle.

Learn about the Avalara suite of products that can help simplify compliance.



## **Avalara AvaTax**

Apply sales and use tax calculations



## **Avalara Business Licenses**

Manage licenses in a secure database



## **Avalara Cross-Border**

Streamline international compliance, classify tariff codes, and register for VAT



## **Avalara Exemption Certificate Management**

Collect, store, and manage documents



## **Avalara Returns**

Prepare, file, and remit sales tax returns



## **Avalara Tax Research**

Get tax research in plain language



Avalara helps businesses of all sizes get tax compliance right. In partnership with leading ERP, accounting, ecommerce, and other financial management system providers, Avalara delivers cloud-based compliance solutions for various transaction taxes, including sales and use, VAT, GST, excise, communications, lodging, and other indirect tax types. Headquartered in Seattle, Avalara has offices across the U.S. and around the world in Brazil, Europe, and India. More information at [avalara.com](https://avalara.com).