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CUSTOMS DUTY AND TAX RESEARCH

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Customs Duty

I- Customs Duty Information

What Is A Customs Duty?

Relevant information for US resident customers*

Customs Duty is a tariff or tax imposed on goods when transported across international borders. The purpose of Customs Duty is to protect each country's economy, residents, jobs, environment, etc., by controlling the flow of goods, especially restrictive and prohibited goods, into and out of the country.

Dutiable refers to articles on which Customs Duty may have to be paid. Each article has a specific duty rate, which is determined by a number of factors, including where you acquired the article, where it was made, and what it is made of. Also, anything you bring back that you did not have when you left the United States must be "declared." For example, you would declare alterations made in a foreign country to a suit you already owned, and any gifts you acquired outside the United States. American Goods Returned (AGR) do not have to be declared, but you must be prepared to prove to U.S. Customs and Border Protection the articles are AGR or pay Customs duty.

The Customs Duty Rate is a percentage. This percentage is determined by the total purchased value of the article(s) paid at a foreign country and not based on factors such as quality, size, or weight. The Harmonized Tariff System (HTS) provides duty rates for virtually every existing item. CBP uses the Harmonized Tariff Schedule of the United States Annotated (HTSUS), which is a reference manual that the provides the applicable tariff rates and statistical categories for all merchandise imported into the U.S.

Duty-Free Shop articles sold in a Customs duty-free shop are free only for the country in which that shop is located. Therefore, if your acquired articles exceed your personal exemption/allowance, the articles you purchased in Customs duty-free shop, whether in the United States or abroad, will be subject to Customs duty upon entering your destination country. Articles purchased in a American Customs duty-free shop are also subject to U.S. Customs duty if you bring them into the United States. For example, if you buy alcoholic beverages in a Customs duty-free shop in New York before entering Canada and then bring them back into the United States, they will be subject to Customs duty and Internal Revenue Service tax (IRT).

Determining Customs Duty

The **flat duty** rate will apply to articles that are dutiable but that cannot be included in your personal exemption, even if you have not exceeded the exemption. For example, alcoholic beverages. If you return from Europe with $200 worth of purchases, including two liters of liquor, one liter will be duty-free under your returning resident personal allowance/exemption. The other will be dutiable at 3 percent, plus any Internal Revenue Tax (IRT) that is due.

A joint declaration is a Customs declaration that can be made by family members who live in the same household and return to the United States together. These travelers can combine their purchases to take advantage of a combined flat duty rate, no matter which family member owns a given item. The combined value of merchandise subject to a flat duty rate for a family of four traveling together would be $4,000. Purchase totals must be rounded to the nearest dollar amount.

Tobacco and Alcohol (example of restricted Merchandise)

For both alcohol and cigarettes, the quantities eligible for duty-free treatment may be included in your $800 or $1,600 returning resident personal exemption, just as any other purchase should be. But unlike other kinds of merchandise, amounts beyond those discussed here as being duty-free are taxed, even if you have not exceeded, or even met, your personal exemption. For example, your exemption is $800 and you bring back three liters of wine and nothing else, two of those liters will be dutiable and IR taxed. Federal law prohibits business-to-private consumer shipping of alcoholic beverages by mail within the United States.

How to Pay Customs Duty

If you owe Customs duty, you must pay it before the conclusion of your CBP processing. You may pay it in any of the following ways:

- U.S. currency only.
- Personal check in the exact amount, drawn on a U.S. bank, made payable to U.S. Customs and Border Protection. You must present identification, such as a passport or U.S. driver's license. CBP does not accept checks bearing second-party endorsement.
- Government check, money order or traveler's check if the amount does not exceed the duty owed by more than $50.

In some locations/POEs, you may pay duty with either MasterCard or VISA credit cards.

Increased Duty Rates

Items from Certain Countries

Under what is known as its "301" authority, the United States may impose a much higher than normal duty rate on products from certain countries. Currently, the United States has imposed a 100 percent rate of duty on certain products of Austria, Belgium, Denmark, Finland, France, The Federal Republic of Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden and the Ukraine. If you should bring more of any of these products back with you than fall within your exemption or flat rate of duty, (see below) you will pay as much in duty as you paid for the product or products.

While most of the products listed are not the type of goods that travelers would purchase in sufficient quantities to exceed their exemption, diamonds from the Ukraine are subject to the 100 percent duty and might easily exceed the exemption amount.

For information on countries that may become subject to a higher than normal duty rate, check the Department of Commerce Web site.

Countries with Free or Reduced Customs Duty Rates

The United States gives Customs duty preferences-that is, conditionally free or subject to reduced rates-to certain designated beneficiary developing countries under a trade program called the Generalized System of Preferences (GSP). Some products that would otherwise be dutiable are not when they are wholly the growth, product, or manufacture of a beneficiary GSP country. Visit the Office of United States Trade Representative website for additional GSP information.

Mailing and Shipping Goods - Customs Duty Guidance

Unaccompanied purchases are goods you bought on a trip that are being mailed or shipped to you in the United States. In other words, you are not carrying the goods with you when you return. If your unaccompanied purchases are from an insular possession (IP) or a Caribbean Basin Initiative (CBI) country and are being imported within 30 days and sent directly from those locations to the United States, you may enter them as follows:

- Up to $1,600 in goods will be duty-free under your personal exemption if the merchandise is from an IP.

- Up to $800 in goods will be duty-free if it is from a CBI or Andean country.
- Any additional amount, up to $1,000, in goods will be dutiable at a flat rate (3%).
  To take advantage of the Customs duty-free exemption for unaccompanied tourist purchases (mailing/shipping) from an IP or CBI country:

- **Step 1.** At place and time of purchase, ask your merchant to hold your item until you send him or her a copy of CBP Form 255 (Declaration of Unaccompanied Articles), which must be affixed to the package when it is shipped.
- **Step 2.** (a) On your declaration form (CBP Form 6059B), list everything you acquired on your trip that is accompanying you. You must also complete a separate Declaration of Unaccompanied Articles form (CBP Form 255) for each package or container that will be sent to you after you arrive in the United States. This form may be available where you make your purchase. If not, you may find the form on the CBP website.
- **Step 3.** When you return to the United States, the CBP officer will: (a) collect Customs duty and any tax due on the dutiable goods you have brought with you; (b) verify your list of unaccompanied articles with your sales receipts; (c) validate your CBP Form 255 to determine if your purchases are duty-free under your personal exemption ($1,600 or $800) or if the purchases are subject to a flat rate of duty.
- **Step 4.** Two copies of the three-part CBP Form 255 will be returned to you. Send the yellow copy of the CBP Form 255 to the foreign shopkeeper or vendor holding your purchase, and keep the other copy for your records.
- **Step 5.** When the merchant gets your CBP Form 255, he or she must place it in an envelope and attach the envelope securely to the outside wrapping of the package or container. The merchant must also mark each package "Unaccompanied Purchase." **Please remember that each package or container must have its own CBP Form 255 attached**, the most important step to follow in order to gain the benefits allowed under this procedure.
- **Step 6.** If your package has been mailed, the U.S. Postal Service will deliver it after it clears Customs. If you owe duty, the Postal Service will collect the duty along with a postal handling fee. If a freight service transports your package, they will notify you of its arrival and you must go to their office holding the shipment and complete the CBP entry procedure. If you owe duty or tax, you will need to pay it at that time in order to secure the release of the goods. You could also hire a customs customhouse broker to do this for you. However, be aware that customhouse brokers are private businesses and are not CBP employees, and they charge fees for their services.
- If freight or express packages from your trip landed in the U.S. before you return and you have not made arrangements to pick them up, CBP will authorize their placement into general order bonded warehouse or public storage after 15 days (days

for perishable, flammable, explosives). This storage and all other related charges (transportation, demurrage, handling) will be at your risk and expense. If the goods are not claimed within six months, they will be sold at auction.

- Per U.S. Postal Service regulations, packages sent by mail and not claimed within 30 days from the date of U.S. arrival will be returned to the sender unless the amount of duty is being protested.

II-Internet Purchases

Relevant information for US resident customers*

Your Responsibility and Liability

Getting a foreign-bought item successfully delivered to the United States is very complicated. There are specific rules and regulations that govern the act of importing - and they can be extremely complex and confusing - and costly.

That artisan cheese from Italy may be a snap to find and buy on the Internet, but U.S. Customs and Border Protection could seize your purchase because certain regulations **prohibit the importation of dairy products from particular countries without a permit.**

Your great auction purchase of gorgeous linen products? Depending upon the country of origin, quota restrictions could hold them up in CBP for a long time. And storage charges in such cases can be expensive.

In other words, "Buyer, Beware." When you buy goods from foreign sources, you become the importer. And it is the importer - in this case, **YOU** - who is responsible for assuring that the goods **comply** with a variety of both **state and federal government import regulations**. Importing goods that are unsafe, that fail to meet health code requirements, or that violate quota restrictions could end up costing you quite a bit of money in fines and **penalties**. At the very least, such goods would be detained, and possibly destroyed, by CBP.

Knowing what is admissible is just part of the story. The other part is knowing how to import. Depending upon what you are importing and its value, the procedures can be very complicated.

It does not matter whether you bought the item from an established business or from an individual selling item in an on-line auction. If merchandise, used or new, is imported into the United States, it must clear CBP and may be subject to the payment of duty as well as to whatever rules and regulations govern the importation of that particular product into the United States.

Hint: To speed a package through CBP examination at a port's International Mail Branch, the seller should affix a completed CN 22 or CN 23 (U.S. Customs and Border Protection Declaration Form) to the outside of the package. This form may be obtained at local post offices worldwide.

Reminder: U.S. Customs and Border Protection holds the importer - YOU - liable for the payment of duty not the seller.

- **Informal Entries:** If the value of your purchase(s) is less than $2500 and your goods are being shipped by mail or freight, they may, in most cases, be imported as an informal entry. However, there are exceptions to this. For instance, if the importation is determined to be for commercial purposes, the value limit for filing an informal entry for many textile items is either $250 or $0 - depending on whether or not the item is subject to Quota (see below). Clearing goods through CBP as an informal entry is less arduous a process than clearing them by filing a formal entry. Essentially, when goods are cleared as an informal entry, CBP will prepare the paperwork, including determining the classification number and duty rate for your merchandise.
  The duty rate for many items typically bought in an on-line auction is zero, however, CBP may charge a small processing fee for mail imports that do require the payment of duty.

  If your goods are sent by a courier or express service, their brokers will usually handle the paperwork, and bill you for their services. If your goods are being shipped by freight, and you want to clear them through CBP yourself, be sure the shipping company has instructions to deliver them to a port near you. Otherwise, you will need to arrange for someone else to clear the goods for you when they arrive. Your alternative is to ask the seller to make arrangements to have your goods forwarded to your door, in which case you should expect to pay for the services of the customs broker who coordinates this when your goods arrive in the U.S.A.

- **Formal Entries:** If your goods are valued at more than $2500, or for commercial textile shipments (clothes/materials) regardless of value, you will be required to file a formal entry, which can require extensive paperwork and the filing of a U.S. Customs and Border Protection bond. As mentioned above and for various reasons, CBP may require a formal entry for any importation. CBP, however, rarely exercises this right unless there is a particular concern about the circumstances surrounding an importation.

Because filing a formal entry can be complicated, the U.S. Customs and Border Protection recommends importers consider hiring a customs broker to complete the transaction. Lists of brokers can be found on the port pages of CBP web site.

One of the most difficult things about filing formal entries is accurately identifying the correct classification number of the item being imported. The Harmonized Tariff Schedule of the United States (HTSUS) lists classification numbers for every conceivable item under the Sun. The HTSUS is the size of an unabridged dictionary, and specialists train for months to learn how to correctly classify goods.

The classification number of an item determines many requirements pertaining to that item's importation such as its duty rate, eligibility for special import programs like the Generalized System of Preferences (GSP) or the North American Free Trade Agreement (NAFTA), and whether or not the item is subject to quota restrictions.

Failure to correctly classify an item can result in fines and/or delays in delivery. You may write to U.S. Customs and Border Protection for a binding ruling, and/or contact an import specialist at your local port for help to identify the proper classification number for your imported item.

- **Quota:** Many kinds of goods imported for commercial use may be subject to a quota limit. It is the classification number of the article as identified in the Harmonized Tariff Schedule of the United States and the country of origin that determine whether or not an item is subject to quota requirements.
  In some cases, the quota is absolute, meaning that once the quota is filled - because the quota has reached its limit for that particular period of time - no additional quantities of that item may be imported until the next open period. Such merchandise must be warehoused or exported. Other quotas are tariff-related, which means that a certain quantity of goods may enter at a low rate of duty, but once that threshold is reached - during a specified period of time - a higher duty rate will be assessed for any additional quantities of that particular imported good. Unlimited quantities of some merchandise subject to tariff-rate quota may, however, enter at over the quota rates.

  If you are importing goods for commercial use or resale, it's a good idea to contact your local port of entry for more specific information.

  Fill levels for quotas are currently posted on the CBP Electronic Bulletin Board in the file called Quota Threshold Status. Fill levels for textile items can be found in the Quota section of Importing/Exporting.

  The Quota program is generally applied only to commercial importations. While the importation of many goods imported under "personal use" quantities are not affected by quota restrictions, there is one exception; made-to-measure suits made in Hong Kong, which are restricted for both personal and commercial use.

- **Electronic Transmission Information**: Materials downloaded from the Internet are not subject to duty. This applies to any goods or merchandise that are electronically transmitted to the purchaser, such as CDs, books, or posters. However, the unauthorized downloading of copyrighted items could subject you to prosecution. Downloading child pornography is also a crime. U.S. Customs and Border Protection has the authority to investigate and prosecute persons involved in this and other illegal activities.

III- Customs duty calculation

Relevant information for foreign businesses*

Customs duty calculation lets you calculate the various values that you need to process imports and exports based on logistics documents. The decisive factor is duty calculation, which you can (or must) perform independently based on country-specific requirements. A lot of sap websites suggest using their systems to calculates custom duties from the customs value as the tax base and from the duty rates applied to the customs value. In fact, to record customs duties, you must first define tax components, tax dependency codes, tax calculation codes, and set up the tax determination. After you have set up your customs duties structure, the system will calculate and record customs duties.
The data you need for the customs value can be transferred from the logistics documents in an integrated feeder system or entered manually in the documents for customs processing. For example, the system takes the invoice price from logistics documents in the feeder system. You can implement Business Add-Ins (BAdIs) to include other values in customs value calculation. To calculate the duties, the system uses the geographical constellation in the business partner relationship and the product classification to determine the relevant customs duty rates and applies them to the customs value as the calculation base.

Methods for Calculating Customs Duties

For each customs duty component, you define the method to use for calculating customs duties. Define the calculation method on the Tax Calculation Code page. Three methods exist for customs duties:

Percentage:

The customs duty is a percentage of the customs duty assessable value of the item.

Customs duty assessable value is the total of:

- CIF value of the item in local currency.

  This is the sum of total FOB item value, freight, insurance, and other charges.

- Landing charges.

  This is 1 percent of the CIF item value. The user can change this amount on the BOE.

- Any previously applied customs duties.

Amount:

The customs duty is a flat amount. A lot of Websites have simplified systems that suggest to enter the flat amount to be applied to the PO schedule in the Tax Amount field on the Tax Calculation Code page.

Quantity:

The customs duty is a unit price multiplied by the number of units. By entering the unit price in the Tax Amount field on the Tax Calculation Code page the systems mentioned above calculate the customs duty, the system multiplies the tax amount by the item quantity on the transaction.

Customs duties rates

All pricing and commercial information are listed on the website https://dataweb.usitc.gov/tariff/database. The products are listed by coded categories. Once the category code of the relevant product is determined, you can access tables detailing the percentages to be applied.

IV- Importing and Exporting Basics

Relevant information for US resident businesses*

Importing and exporting can help your business expand at home or abroad, but it's important to follow all laws and regulations. U.S. Customs and Border Protection (CBP) has basic information on importing and exporting.

Importing

Imports are any resources, goods, or services that producers in one country sell to buyers in another country. CBP offers tips for new importers, including those who have recently started importing or who would like to know more about the process.

Some types of goods and services require a license or permit to import into the U.S. as a part of your business.

Exporting

Exports are any resources, intermediate goods, or final goods or services that a buyer in one country purchases from a seller in another country. Export.gov provides tools, assistance, and expert knowledge to help your company grow in the global marketplace.

Depending on the good or service, you may need a license or permit to export it from the U.S. as a part of your business.

Obtain an Import License or Permit

In most cases, you will not need a license to import goods into the U.S. But, for certain goods being imported, some agencies may require a license, permit, or other certification.

Follow this checklist to avoid problems when importing:

- Check the requirements of federal agencies. Guidelines from U.S. Customs and Border Protection (CBP) describe the types of items that may require a license or permit, with contact information for the related agency.

- Contact the local port of entry you'll use to import your goods for import requirements and other information about the process.
- Even if you do not need an import license, you must fill out CBP entry forms within 15 calendar days of the date that your shipment arrives at a U.S. port of entry. Make sure to provide your importer number on all these forms.
- Your importer number is your IRS business registration number. If you do not have this number or you do not own a business, then your importer number is your Social Security number (SSN).
- You may also request a CBP assigned number by completing CBP Form 5106 and presenting it to the entry branch at a CBP port of entry..

Get an Export License or Permit

Most items exported to a foreign buyer will not require an export license. However, all items are subject to export control laws and regulations.

The best way to find out if an item requires an export license is by checking which agency has jurisdiction over or regulates, the item you are trying to export. Search this list of federal departments and agencies to find out whether you need an export license for your product.

To avoid any problems, follow the U.S. Customs and Border Protection's (CBP's) exporting requirements or contact the local port of entry used to export your goods.

sales taxes

I- How do state and local sales taxes work?

Forty-five states and the District of Columbia levy general sales taxes that apply (with some exemptions) to all goods and certain services. Thirty-seven states (including, Alaska, which has no state tax) also allow general sales taxes at the local level. Most states apply separate sales taxes to particular goods, including tobacco, alcohol, and motor fuels.

How much revenue do State and local governments raise from sales taxes?

States rely on sales taxes more than local governments do. States collected $457 billion from sales taxes in 2017, or 35 percent of their own-source general revenue (table 1). “Own-source” revenue excludes intergovernmental transfers. Nearly two-thirds ($300 billion) of that total came from general sales taxes, while the other third ($157 billion) came from selective sales taxes (or excise taxes) on specific purchases such as motor fuel, tobacco, and alcohol. Local governments collected $124 billion from sales taxes in 2017, or 11 percent of their own-source general revenue. Of that total, $89 billion came from general sales taxes and $34 billion came from selective sales taxes. (Census includes the District of Columbia’s revenue in the local total.)

TABLE 1

State and Local Sales Tax Revenue

2017

	General Sales Tax		Selective Sales Tax		Total Sales Tax	
	Revenue (billions)	Percentage of own source general revenue	Revenue (billions)	Percentage of own source general revenue	Revenue (billions)	Percentage of own source general revenue
State and local	389	16	191	8	581	24
State	300	23	157	12	457	35
Local	89	8	34	3	124	11

Source: Urban-Brookings Tax Policy Center, "State and Local Finance Initiative Data Query System."
Note: Own-source general revenue does not include intergovernmental transfers.

Nevada relied on sales tax revenue more than any other state in 2017, with general sales and selective sales taxes accounting for 47 percent of combined state and local own-source general revenue. General sales and selective sales taxes also represented 30 percent or more of combined state and local revenue in Arizona, Arkansas, Florida, Hawaii, Louisiana, New Mexico, South Dakota, Tennessee, Texas, and Washington. Among the states with a general sales tax, Massachusetts and Wyoming relied least on general sales and selective sales tax revenue as a percentage of combined state and local own-source revenue (15 percent in both states).

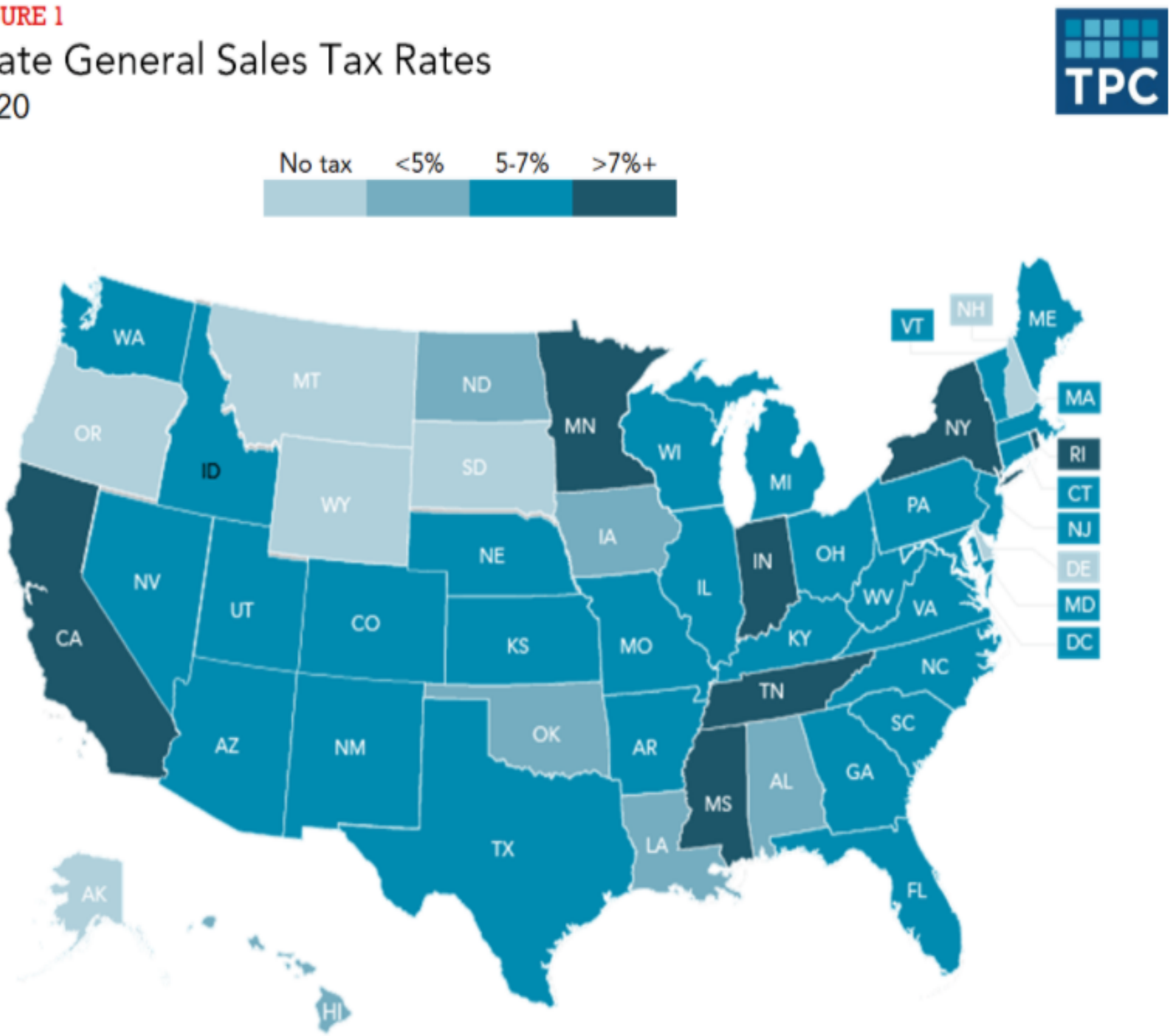
Every state and the District of Columbia collected revenue from selective sales taxes in 2017. The average revenue from these taxes was 8 percent of state and local own-source general revenue, but 15 states collected 10 percent or more from selective sales taxes. Nevada's 17 percent from selective sales taxes was the highest revenue share of any state, while Wyoming's 4 percent was the lowest.

How do general sales tax rates differ across States?

Colorado has the lowest state general sales tax rate (2.9 percent). No other state with a general sales tax has a rate below 4.0 percent, but the state general sales tax rate is below 5.0 percent in 10 other states (figure 1). In addition to California, which has the highest state general sales tax rate (7.25 percent), four states (Indiana, Mississippi, Rhode Island, and Tennessee) have rates at or above 7.0 percent.

Alaska, Delaware, Montana, New Hampshire, and Oregon do not have a state general sales tax.

FIGURE 1
State General Sales Tax Rates
2020



Source: Federation of Tax Administrators (FTA), Tax Rates (as of January 1, 2020).
Note: Tax rates do not include local sales taxes.

Thirty-seven states (including Alaska, which has no statewide tax) allow **local governments to impose their own general sales taxes**. The maximum sales tax rates levied by local governments range from 0.5 percent in Hawaii to 8 percent in Colorado.

What purchase are subject to the general sales tax?

General sales taxes typically apply to most tangible goods. One notable exception is food purchased for use at home: only 13 states tax such purchases, and six of these states tax food at a lower rate than their general sales tax rate. Five of the 13 states that tax food for home consumption provide income tax credits to low-income residents to help offset the tax. In contrast, food bought for immediate consumption at restaurants is taxed in most states, and sometimes at a higher rate than the general sales tax rate.

Many states also exempt prescription and nonprescription drugs, textbooks, and clothing from general sales taxes. Some states have sales tax holidays, periods in which specific purchases—for example, clothes and school supplies right before the start of a new school year—are sold tax-free.

The taxation of services (e.g., dry cleaning, carpentry work, barbershops) is more complicated. All states tax some services, but exemptions are common. Very few states tax professional services, such as doctors and lawyers. Hawaii and New Mexico are exceptions to that rule, taxing nearly all services.

How do sales taxes apply to online purchases?

The evolving treatment of online and other remote sales (e.g., catalog sales) is complex. In 1992, the Supreme Court ruled (*Quill Corp. v. North Dakota*) that under the commerce clause of the US Constitution, a retailer with no physical presence in the online purchaser's state of residence (technically called a "nexus" requirement) is not required to collect a state or local sales tax from the consumer.

However, the Supreme Court revisited this issue in 2018 in *South Dakota v. Wayfair, Inc.*, overturned *Quill*, and gave states broad authority to collect the tax.

The Court indicated that states have a right to require online sellers to charge and collect sales tax from all online buyers, not just those who are physically located in that state

To avoid harming smaller sellers, many states have set a minimum number of transactions or annual amounts of sales below which no sales tax is charged for online transactions.

The Supreme Court upheld a South Dakota law requiring any entity with sales of $100,000 or more or with at least 200 transactions in South Dakota to collect and remit the state's sales tax. Other states quickly enacted similar laws. As of March

2020, Florida and Missouri were the only states with a general sales tax but not a law requiring remote sellers to collect tax.

Many states are now working on legislation that would require **"marketplace facilitators,"** organizations such as Amazon and eBay that allow third-party retailers to also sell items on their platform, to collect state sales taxes on those third-party sales as well. As of January 2020, 38 states and the District of Columbia had marketplace facilitator collection provisions.

Taxing online sales is not completely new, though. Many large retailers had already begun voluntarily collected the tax even before *Quill*. Most notably, **Amazon** has **collected taxes in every state with a general sales tax since April 2017**.

Further, states levy <u>use taxes</u> in addition to <u>sales taxes</u>. Consumers are subject to use taxes on goods purchased outside their state for use in their home state if they did not pay a sales tax and this includes online purchases. The use tax rate is the same as the sales tax rate, but few consumers know it exists and actually pay it. Many states with both a sales tax and an individual income tax (such as California, Kentucky, Virginia, and Utah) give taxpayers a chance to declare liability and pay use taxes on their income tax returns.

<u>Tobacco Taxes</u>

Cigarette taxes are typically levied per pack. In 2020, Missouri had the lowest rate (17 cents per pack) and the District of Columbia had the highest ($4.50). In six states (Alabama, Illinois, Missouri, New York, Tennessee, and Virginia), some local governments levy an additional cigarette tax. Local cigarette tax rates range from 1 cent per pack in Alabama and Tennessee to $4.18 per pack in Chicago (a Cook County tax of $3.00, plus a city tax of $1.18).

All states also levy taxes on other tobacco products, including cigars and loose tobacco. State and local governments also increasingly—21 states and the District of Columbia in 2020—tax e-cigarettes and vaping products.

State and local governments collected $19 billion in revenue from tobacco taxes in 2017, nearly all of it from cigarette taxes.

<u>Alcohol Taxes</u>

Alcohol taxes are generally paid at the wholesale level, so the cost is incorporated into the retail price. The excise taxes are levied per gallon (not as a percentage of the price), and beer, wine, and distilled spirits have different tax rates. In addition to the excise tax, many states also levy a general sales tax on the final purchase price of alcohol, and some states and cities have special sales tax rates for alcohol.

Some states, such as New Hampshire and Pennsylvania, collected most of their revenue from government-run liquor stores instead of traditional alcohol taxes, generating revenue through various fees, price mark-ups, and net profits. In total, 22 states collected revenue from government-owned liquor stores.

State and local governments collected $17 billion in revenue from alcohol in 2017—$7 billion from alcohol taxes and $10 billion from government-owned liquor stores.

Motor Fuels Taxes

Motor fuel taxes are typically per gallon taxes. That is, consumers pay tax based on how much gas they purchase, not as a percentage of the final retail price of gasoline. However, 20 states and the District of Columbia tie at least a portion of their gasoline tax rate to the retail price. The lowest gasoline tax rate is in Alaska (8.95 cents per gallon) and the highest is in Pennsylvania (57.6 cents per gallon).

States earmark much of their motor fuel tax revenue for transportation spending, which has meant funding gaps for transportation as gasoline has recently stagnated. States are considering options like tying the gas tax rates to inflation or population, taxing based on price, and taxing miles traveled instead of gas (as more drivers use hybrid or electric cars). State and local governments collected a combined $47 billion in revenue from motor fuel taxes in 2017.

Local Special Sales Tax

Some cities (e.g., Boston, San Francisco, and Washington, DC) also have special tax rates for specific goods and services (e.g., restaurant meals, hotel accommodations, rental cars, and parking) that are higher than their general sales tax rates. These higher tax rates are often designed to collect a significant share of their revenue from visitors, who use and benefit from city services and presumably have less political clout than local voters.

II- US taxation of foreign corporations with business activities in the Unites States

Foreign corporations may be subject to tax in the United States if they have business activities in the United States or if they receive income from U.S.-sources. Corporations organized under the laws of the United States are subject to tax in the U.S. on their worldwide income. Foreign corporations with business activities in the United States may be required to file a U.S. corporate income tax return, even if the corporation takes the position that its business activities do not constitute a permanent establishment under the terms of the tax treaty between the United States and the country of which the foreign corporation is a tax resident.

Income effectively connected with a US trade or business

When a foreign corporation has sufficient nexus or connection with the United States it may be determined to have a U.S. trade or business for U.S. income tax purposes. A foreign corporation's U.S. trade or business is subject to tax in the United States on a net basis at normal graduated corporate tax rates.

The determination whether a foreign corporation has a U.S. trade or business is made based on the relevant facts and circumstances. For a U.S. trade or business to exist, the activities must be 'considerable, continuous, and regular'. A U.S. trade or business can be found to exist even if the activities are carried out indirectly (i.e. through an agent or representative).

Income earned by a foreign corporation that is not effectively connected with a U.S. trade or business (non-effectively connected U.S.-source income) is subject to tax on a gross basis. This means that no deductions are allowed. This income is taxed at a flat rate of 30%.

Tax treaties

When a foreign corporation is entitled to the benefits or the tax treaty concluded between the United States and the country of which the foreign corporation is a tax resident, the way in which U.S. domestic tax laws apply may change. For example, where a foreign corporation is subject to income tax in the United States under the provisions of the Internal Revenue Code, the terms of the applicable tax treaty may allocate the right to tax the activities that the IRC seeks to tax to another taxing jurisdiction.

FORM 1120-F

Every foreign corporation that is engaged in a trade or business in the United States is required to file a U.S. corporate income tax return (Form 1120-F), even if the foreign corporation has no U.S.-source income or all of its income is exempt from tax under the terms of a tax treaty. Furthermore, even if the foreign corporation takes the position that it has no permanent establishment in the United States, it **may still be required to file a tax return**. Foreign corporation that do not have a permanent establishment in the United States, but do have income from U.S.-sources on which tax was withheld, need to file a tax return when seeking a refund of (part of) the tax that was withheld.

Failing to timely file a true and accurate tax return may result in deductions being disallowed, as well as penalties.

Information returns

In addition to the requirement to file a U.S. corporate income tax return, just like domestic corporations, foreign corporations may be required to file information returns. For example, a foreign corporation may be required to file Form 1099 to report the payment of certain amounts such as interest or dividends. Form 1042 may be required when certain payments are made to foreign persons.

Tax identification number

Foreign corporations may be required to apply for an Employer Identification Number (EIN) for use on tax related documents by filing Form SS-4 with the IRS. An EIN is a tax identification number.

III-What is Nexus?

Sales tax nexus defines the connection between a taxing jurisdiction such as a state and an entity such as your business.
Until this connection is established, the taxing jurisdiction cannot impose its sales taxes on you.

Nexus determination is primarily controlled by the U.S. Constitution, in which the Due Process Clause requires a definite link or minimal connection between a state and the entity it wants to tax, and the Commerce Clause requires substantial presence.

In *South Dakota v. Wayfair*, the Court eliminated the physical presence rule within the Commerce Clause as the standard for creating nexus in a jurisdiction. However, physical presence will still create nexus and is the first consideration in determining nexus. In the lead up to the Court's decision, many states enacted new types of economic nexus legislation to address how sellers conduct business today.

There is no specific shared definition of nexus across the 50 states. Moreover, definitions and rules for determining nexus change constantly, and most states are careful to give themselves room to maneuver in their definitions. This means that a business must look at each state individually when determining sales tax nexus and must stay constantly on top of a slew of changing regulations and interpretations.

Here are a few representative definitions of Nexus that most states would more or less agree with. As you read them, you can almost feel the steel jaws starting to clamp around you:

- "Maintaining, occupying, or using permanently or temporarily, directly or indirectly or through a subsidiary, an office, place of distribution, sales or sample room or place, warehouse or storage place or other place of business."
- "Having a representative, agent, salesman, canvasser, or solicitor operating in this state under the authority of the retailer or its subsidiary on a temporary or permanent basis."
- "Any seller which does not have a physical presence in this state shall remit sales or use tax, if the seller meets either: 1. Gross sales from the sale of taxable items delivered in this state exceed $100,000; or 2. The seller sold taxable items for delivery in this state in 200 or more separate transactions"

Other states may set their own economic nexus threshold, but it must prove to not impede on nor create an undue burden on interstate commerce. South Dakota v. Wayfair established what would be considered acceptable to the Federal courts as being constitutional. Therefore, a majority of states have set the $100,000 in sales or 200 separate transactions as their threshold. These definitions—which focus around having a business presence in a state—are just starting points for determining nexus.

There are innumerable details, timescales, vagaries, and state-by-state idiosyncrasies involved. The point is, if you have knowingly or unknowingly created nexus in a state, then you are subject to some very strict obligations.

Click-Through Nexus legislation typically requires that a remote seller meets a minimum sales threshold in the state in question resulting from activities of an in-state referral agent. The seller must be making commission payments to the in-state resident for any orders that come about as a result of the click-through referral from the resident's website.

Affiliate Nexus legislation typically requires that a remote retailer holds a substantial interest in, or is owned by, an in-state retailer and the retailer sells the same or a substantially similar line of products under the same or a similar business name, or the in-state facility/employee is used to advertise, promote, or facilitate sales to an in-state consumer. The legislation may not always require common ownership. And it may not include activities related to sales, delivery, service and maintaining a place of business in the state on behalf of the out of state business to benefit the out of state business' customers.

Marketplace Nexus legislation typically means that if an online marketplace operates its business in a state and provides e-commerce infrastructure as well as customer service, payment processing services and marketing, the marketplace facilitator is required to register and collect tax as the retailer rather than the individual sellers. This could also impose reporting requirements on the marketplace facilitator.

Notice and Reporting Requirements legislation typically requires that a retailer must notify buyers that they must pay and report state use tax on their purchases. The retailer may be required to send purchasers and the state an annual statement of all of their purchases from the retailer.

Economic Nexus legislation generally requires an out-of-state retailer to collect and remit sales tax once the retailer meets a set level of sales transactions or gross receipts activity (a threshold) within the state. No physical presence is required.

Economic nexus was a central issue in the United States Supreme Court case, *South Dakota v. Wayfair*. On June 21, 2018, the U.S. Supreme Court ruled in favor of South Dakota and overruled the traditional physical presence rule as a necessary requirement to impose sales tax and collection requirements on a remote retailer. This was the first Supreme Court decision on nexus since 1992. States now have the right to require tax collection from online retailers and other remote retailers with no physical presence in their state if they meet certain economic thresholds.

To learn more about the *South Dakota v. Wayfair* decision, read our news item. For a list of resources for remote retailers post-Wayfair decision, visit our Remote Seller Resources page. For information such as effective dates, thresholds, and includable sales for out-of-state sellers making sales into states that have enacted economic nexus legislation, visit our Economic Nexus State Guide.

Types of Nexuses in Online Sales

States have come up with several ways to determine a nexus for online transactions.

- A click-through nexus is a direct connection between the buyer and the seller. This can occur when a business within the state is paid a commission for referring sales to an out-of-state seller, such as via a link on a website.[3]
- An affiliate nexus involves affiliates that are independent businesses that sell through other businesses. The Amazon Affiliates program is a good example. An affiliate isn't an employee or even an independent contractor, but is actively associated with a business, and states have been using this connection to capture sales taxes. This type of nexus often requires that a commission for referrals be paid by the affiliate.[4]
- An economic nexus is the simplest way of determining a sales tax nexus. It's basically just sales. A business might have an economic nexus in a state if it sells over a specific amount or threshold.[5] Idaho has established $100,000 in annual sales as the minimum for establishing a sales tax nexus.[6]

Foreign sales tax liabilities – a question of Nexus

Foreign companies must comply with sales tax in much the same manner US based remote businesses. Sales tax liability is a question of nexus, or simply put "physical presence," and many business actions can contribute to the creation of nexus. While nexus establishing actions differ from state to state common examples are having a storefront, warehouse, or traveling representatives. Businesses, both in the US and outside our borders, are responsible for collecting sales tax in the states in which they have established nexus.