Four New York SALES TAX Traps to Avoid

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New York sales tax audits are challenging for businesses because of the complexity of sales tax laws and stringent recordkeeping requirements. The state is also very aggressive in enforcing sales tax laws and the consequences of noncompliance are severe. While businesses need comprehensive sales tax guidance, there are a few areas that merit extra attention as potential sales tax traps.

1. Responsible Person Assessments. Certain "responsible persons" involved in a business may be found personally liable for 100% of the business's unpaid sales tax, regardless of their percentage of ownership. However, there is relief for certain LLC members, if their ownership interest and percentage share of the profits and losses of the LLC are less than 50% and they were not under a duty to act on behalf of the company in complying with the sales tax law. If relief is granted, the individual's liability is limited to the greater of his ownership interest or percentage share of profits and losses in the business.

2. Penalties. Penalties for late filing or late payment are percentage-based and increase monthly, up to a maximum amount (unless no tax is due). In addition, there are extra penalties for fraud and inadequate or non-existent records. Interest, criminal fines, and jail time may also apply. Penalty abatement is available where failure to file or pay was due to a reasonable cause and not willful neglect.

3. Bulk Sales. A bulk sale is the sale, transfer, or assignment of business assets, in whole or in part, by a person required to collect sales tax. Generally, the rules require the parties to an asset transfer to give notice of the pending transfer to the state taxing authority before taking possession or making payment to the seller. If sales tax is owed by the seller, the purchaser must withhold the purchase money to satisfy the seller's pre-existing tax debt. If the parties fail to properly notify the state and/or if the purchaser fails to properly withhold the purchase funds, then the purchaser may become jointly liable for the seller's sales tax debts to the extent of the purchase price or the fair market value of the assets transferred to the purchaser, whichever is greater.

4. Annual Reporting. Some industries have annual reporting requirements, such as insurers of motor vehicles, franchisors, and alcoholic beverage wholesalers. They must report information such as their vendors' names and addresses, total amounts of payments made to vendors, financial information related to franchisees, amount of sales to each vendor, etc. This information is used by the Tax Department to determine the accuracy of income and sales tax returns filed by vendors.

Notably, if the taxpayer failed to file or pay and the state hasn't discovered it yet, the taxpayer may be able to "confess" and qualify for the Voluntary Disclosure Program and thereby avoid criminal prosecution and penalties. Taxpayers who failed to file for more than three years can also request a limited look-back period, which provides that they only have to file and pay taxes for the last three years (or six, in some cases).

If a client has not filed or paid sales tax, it is crucial to consult with a tax attorney as soon as possible. Waiting too long to resolve the problem can result in liens, levies, seizure of the business, criminal prosecution, and other consequences.

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