2025

A TAX COMPLIANCE GUIDE FOR BUSINESSES

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Introduction

If 2024 brought us stranded astronauts and a troop of escaped monkeys, what 2025 might bring is anyone's guess. One thing is certain: Businesses worldwide will need to navigate new tax obligations.

Some tax policy changes, like many European e-invoicing mandates, have been years in the making. Others have yet to take shape. The 47th president of the United States has promised to levy steep tariffs on many imports, but exactly what those tariffs will look like is unknown.

Numerous U.S. state and local tax compliance changes have already been announced, however. We know remote sellers won't need to count their Alaska transactions starting January 1, 2025. We know Utah plans to increase the tax on beer. And we know plenty more.

New tax policy changes will emerge as 2025 unfolds. We have an inkling of what some of those could be: The District of Columbia may eliminate the preferential tax treatment for electric vehicles, for example, and raise the district's cigarette tax. The Washington State Legislature could enact a retail delivery fee.

There could also be lots of surprises. There usually are.

Though we can't predict the future, our ninth annual tax changes report offers analysis, custom graphics, and insights from the tax experts at Avalara. This year, tax professionals beyond Avalara also bring their unique perspectives to the report. Together, we explore emerging tax and compliance trends in:

- U.S. SALES TAX
- RETAIL
- SOFTWARE
- MANUFACTURING
- LODGING
- BEVERAGE ALCOHOL
- COMMUNICATIONS
- EXCISE
- GLOBAL TAX

Let's do this.

DISCLAIMER

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

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Sales tax

Gone are the years when each new day brought a new economic nexus or marketplace facilitator law (or so it seemed). But there's always some kind of change afoot with sales tax. Here's what's happening with sales tax in 2025.

What's ahead:

The state of the states

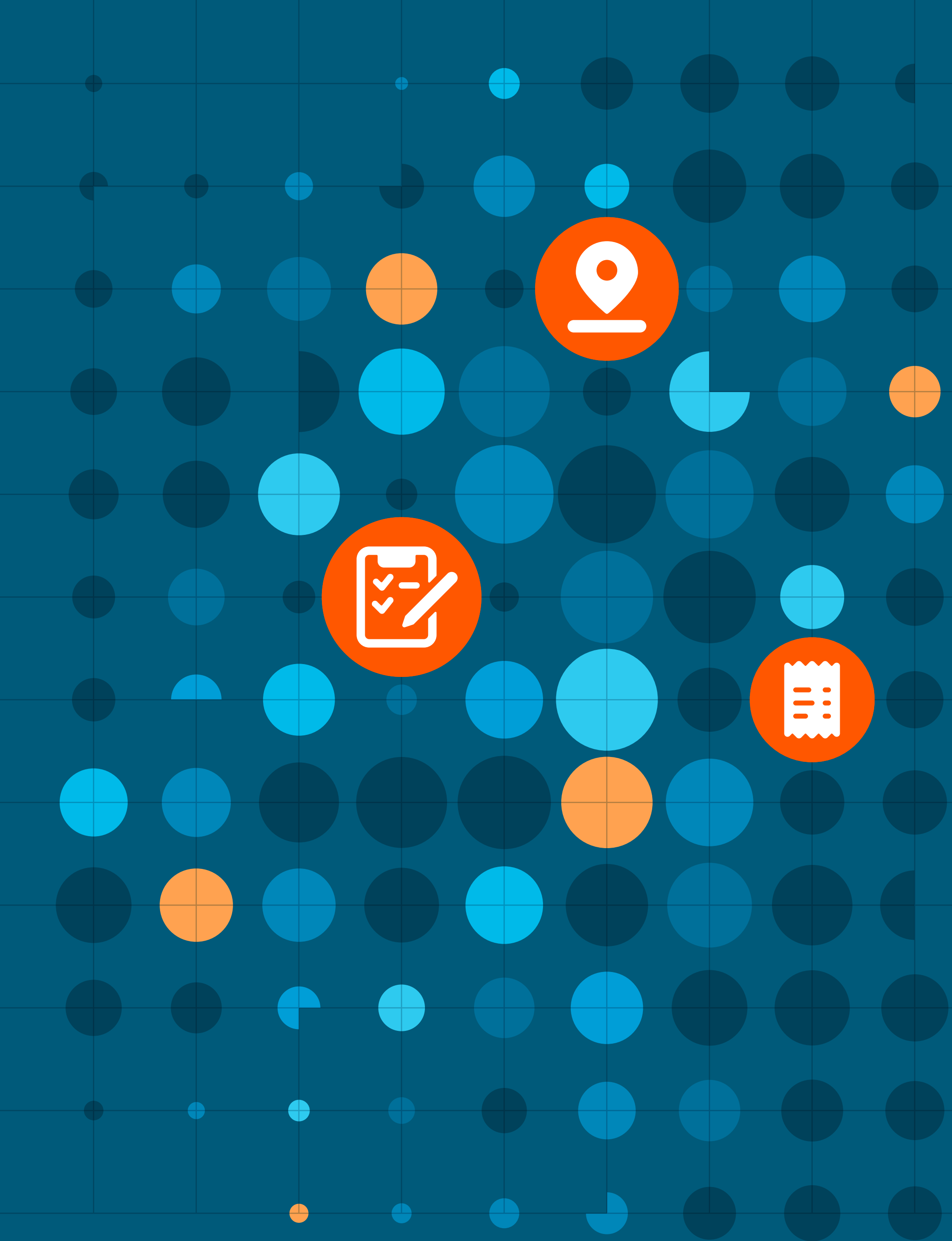
What the numbers tell us about sales tax in 2025

What's new with sales tax nexus in 2025?

Why physical presence nexus still matters

Are any states offering tax relief in 2025?

Other changes affecting sales tax compliance in 2025



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The state of the states

The salad days of stimulus-fueled surpluses and unprecedented growth seem to be wilting. That's one trend likely to impact sales tax in 2025.

State **revenue collections** are once again meeting expectations, after years of uncertainty over how much revenue was coming from federal stimulus, tax relief efforts, or unique pandemic-related conditions. This is a good thing.

And what are those expectations? According to the **National Association of State Budget Officers** (NASBO), states anticipate slow revenue growth in fiscal year 2025. Though most state coffers are fairly full, **Pew predicts** policymakers will probably have "less new money" to fund tax cuts.

That's the situation in Rhode Island. The Ocean State ended the 2023–2024 budget year with a **$292 million surplus**, but most of it's already earmarked to help balance the 2024–25 budget. There's a projected deficit of about $260 million for the 2025–26 budget. Washington state is in a similar **predicament**.

Although **fiscal year 2025 budgets** are for the most part calling for "fewer and more targeted tax reductions," numerous states *are* lowering taxes. "Historically, there's been a lot of talk but little action," says Scott Peterson, VP of Government Relations at Avalara, "but now states are reducing income tax or property tax or both."

How will they fill the resulting revenue gaps? Peterson says many states have budget surpluses and they're hoping for the best. "But states have to balance their budgets. When the surpluses run out, they'll either need to spend less or find another source of revenue."

Kentucky's plan is to reduce income tax only if total revenue exceeds a certain amount (it did in 2023 and 2024 but **won't in 2025**). Nebraska is using savings to fund its property tax reductions, though Peterson thinks it's optimistic to assume they'll generate sufficient tax revenue in the future to maintain their property tax reduction goals. **Arizona** was on course to sensibly phase in income tax cuts but then created a budget gap by accelerating the timeline. The best-laid plans ...

SCOTT PETERSON
VP of Government Relations at Avalara

> **Historically, there's been a lot of talk but little action,**
>
> **but now states are reducing income tax or property tax or both.**

So, what does all this mean for sales tax? How will reducing income tax or property tax affect sales tax collections? We'll explore these topics and more. But first, let's check the numbers.

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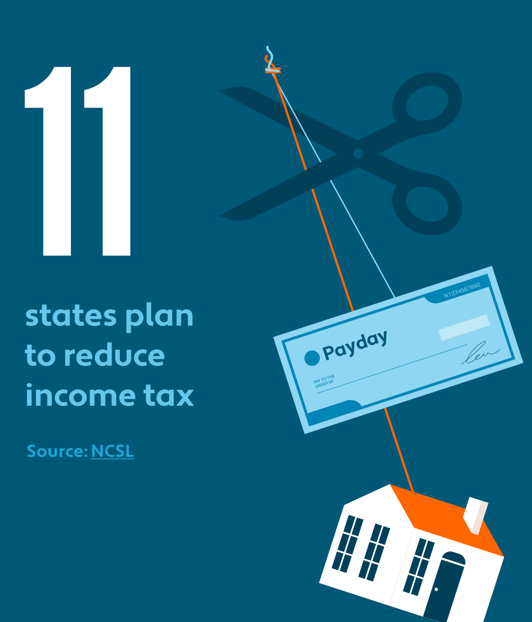
What the numbers tell us about sales tax in 2025

11 states plan to reduce income tax

Source: NCSL



12 states plan to reduce personal property tax

Source: NCSL

6 states have no individual income tax and rely heavily on sales tax revenue

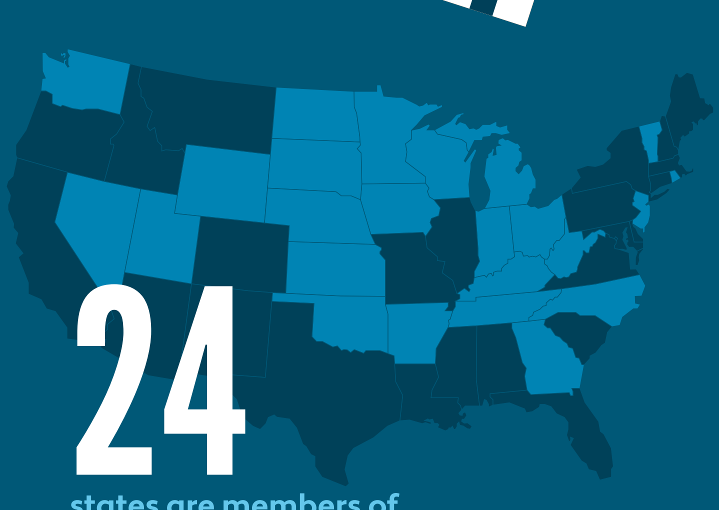
Source: EY

4 states tax services by default

Source: Avalara

41 states tax some but not all services

Source: Avalara



24 states are members of the Streamlined Sales and Use Tax Agreement

Source: SSTGB

30,500+ sellers have registered through the Streamlined Sales Tax Registration System

Source: SSTGB

Services taxability by state

- Services to TPP
- Services to real property
- Amusement/recreation
- Personal services
- Business services
- Professional services

Source: Avalara

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Sales tax revenue in 2025: Broadening the sales tax base?

Sales tax is an essential source of revenue for 45 states, Puerto Rico, and the District of Columbia. It accounts for 30.4% of state tax revenue, second only to personal income tax. Sales tax is also a primary source of revenue for local jurisdictions, though property tax makes up the lion's share.

Despite generating so much state and local tax revenue, in all but a few states, sales tax generally doesn't apply to a majority of services. A surprising number of intangible and tangible goods are also exempt. Perhaps that's why some states planning to reduce income and property taxes see potential in sales tax.

"Some states are leaning toward taxing digital services to make up for reductions in income and property tax," says Brian Smith, Senior Government Relations Director at Avalara.

BRIAN SMITH
Senior Government Relations Director at Avalara

> "Some states are leaning toward taxing digital services to make up for reductions in income and property tax."

That was certainly Virginia Governor Glenn Youngkin's plan for the 2024 budget. He proposed cutting income tax rates 12% "across the board" and modernizing Virginia's sales tax by taxing digital goods and services and raising the state sales tax rate. Alas, for him, the Legislature didn't go for it. Nebraska Governor Jim Pillen proposed a similar plan to raise money for property tax reductions; it too failed to win support.

On the other hand, Louisiana passed a law to tax digital goods and services and increase the sales tax rate effective January 1, 2025.

The Tax Foundation is all for broadening the sales tax base, though it thinks sales tax rates should then be *lowered*. It holds that "the sales tax is, for the most part, a good tax." (Could someone put that on a T-shirt, please?)

More than 170 countries tax consumption, and most nations have a broader tax base than most U.S. states. Sales tax policies have been slow to adapt to the fact that Americans now typically buy far more services than things.

By some estimates, the sales tax base captured about 45% of personal income in the late 1970s. Today, it's closer to 30%, and it was even lower before the pandemic disrupted sales of many services. That means states that exempt most services, which is most states, are leaving a lot of sales tax revenue on the table. Those slow to tax digital goods are in a similar spot.

It's common for at least one state to try to tax new services each year, and some states succeed. Kentucky began taxing services in earnest on July 1, 2018, and broadened sales tax to another 35 services or so on January 1, 2023. Both Maryland and Nebraska tried to tax more services in 2024, though neither were successful.

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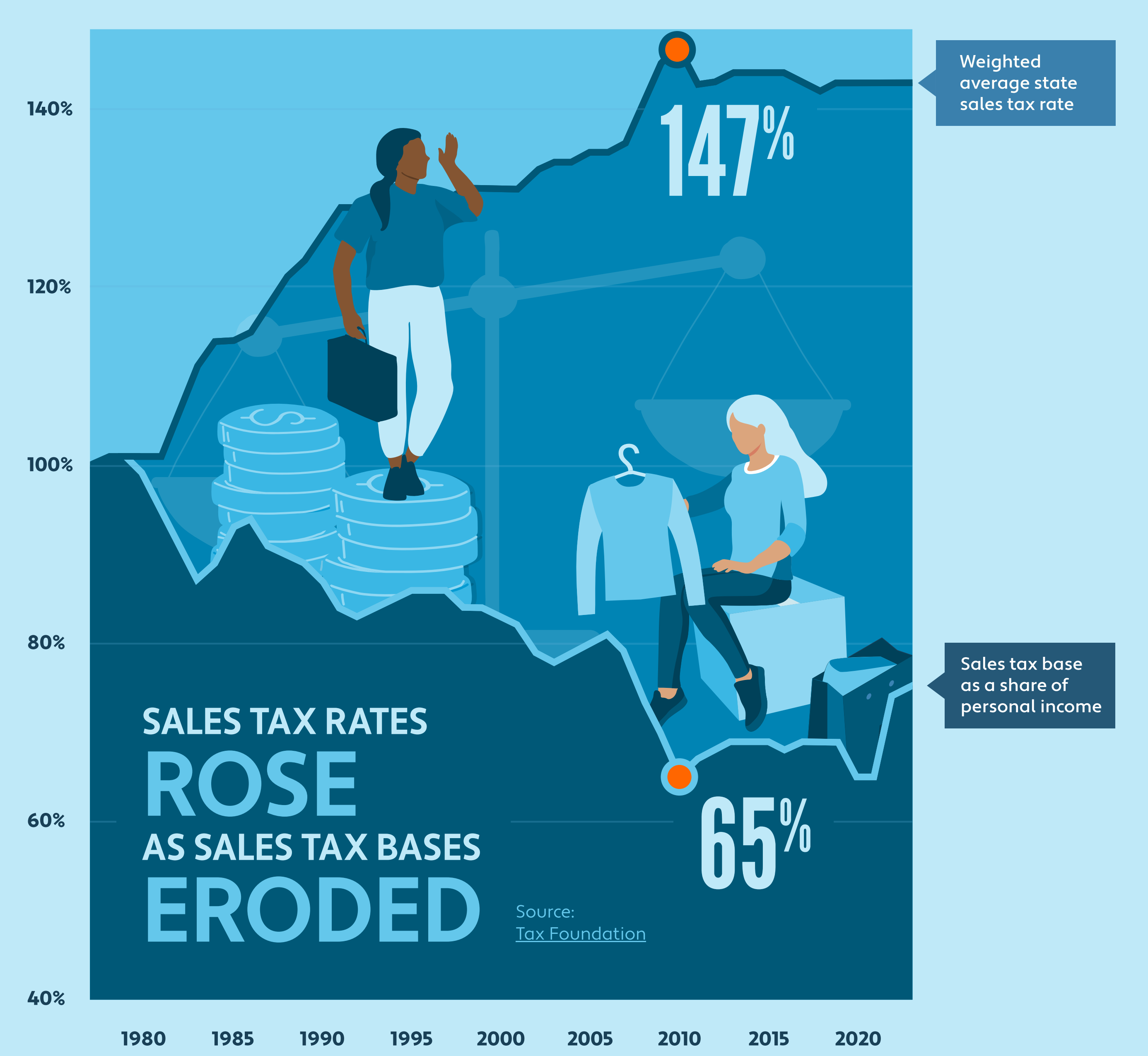

States *are* "slowly and fitfully" modernizing their tax codes, according to the **Tax Foundation**, primarily by taxing digital products with taxable tangible counterparts. But change doesn't come easily. Remember how long it took for states to win the right to tax remote sales?

Of course, once the Supreme Court of the United States overturned the physical presence rule in **South Dakota v. Wayfair, Inc.** (June 2018), economic nexus took off like wildfire. Those were heady days for state legislatures and sales tax aficionados. **Sales tax nexus** updates have made fewer headlines since January 1, 2023, when **Missouri** became the last state to enforce economic nexus rules.

But states are still tweaking nexus laws, and they probably should. Remote sales tax requirements are taxing for businesses, especially small businesses with few resources to devote to compliance.

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What's new with sales tax nexus in 2025?

Collecting and remitting sales tax in multiple states is a burden. Sales tax software can make it easier and less expensive for businesses, as the Supreme Court itself observed in the **Wayfair decision**, but some states sure don't make compliance easy.

Many of the issues raised in Wayfair's **dissenting opinion** remain true today. There are still well over 10,000 U.S. sales and use tax jurisdictions, for instance, and different jurisdictions impose different tax rates and rules. **New Jersey** sales tax still applies to yarn purchased for art projects but not to yarn earmarked for sweaters. **Texas** still taxes plain deodorant but not deodorant with antiperspirant.

Economic nexus rules have added layers of complexity. For starters, businesses that sell into states where they aren't registered must pay close attention to **economic nexus thresholds**. Once they reach a threshold, they'll have to register for sales tax and may need to start collecting sales tax by the **very next transaction**. It's a big and important job, made more complicated by the fact that the thresholds vary from state to state.

The **Tax Foundation** may be onto something when it observes, "states have significant room to reduce compliance costs for remote sales."

Fortunately, for businesses, several states are working to simplify remote sales and use tax compliance. Recent efforts include eliminating the 200-transactions threshold for economic nexus, leveling the playing field for remote sellers in Illinois, and simplifying sales tax compliance in home-rule states.

These changes should help some businesses. Yet they may not be enough to satisfy Congress, which is taking a renewed interest in **providing small business relief from remote sales tax collection**. We expect to hear more on this matter in 2025.

Eliminating the 200-transactions threshold for economic nexus

Following South Dakota's lead, many states initially established an economic nexus threshold of $100,000 in sales *or* 200 transactions in the state in the current or previous calendar year. This was supposed to provide safe harbor for small businesses, but it's not always effective. For some companies with a high volume of low-dollar sales, the cost of compliance may exceed the benefit of selling into these states.

Recognizing this, some states never adopted a transaction threshold and 13 states have **eliminated** theirs. Indiana, North Carolina, and Wyoming did so in 2024, and they won't be the last.

Local jurisdictions that participate in the **Alaska Remote Seller Sales Tax Commission** are **chucking the 200-transactions threshold** effective January 1, 2025. A bill introduced in **New Jersey** also seeks to eliminate the transaction nexus requirement for remote sellers in 2025. **Utah**, which tried and failed to remove the threshold in 2024, will probably try again.

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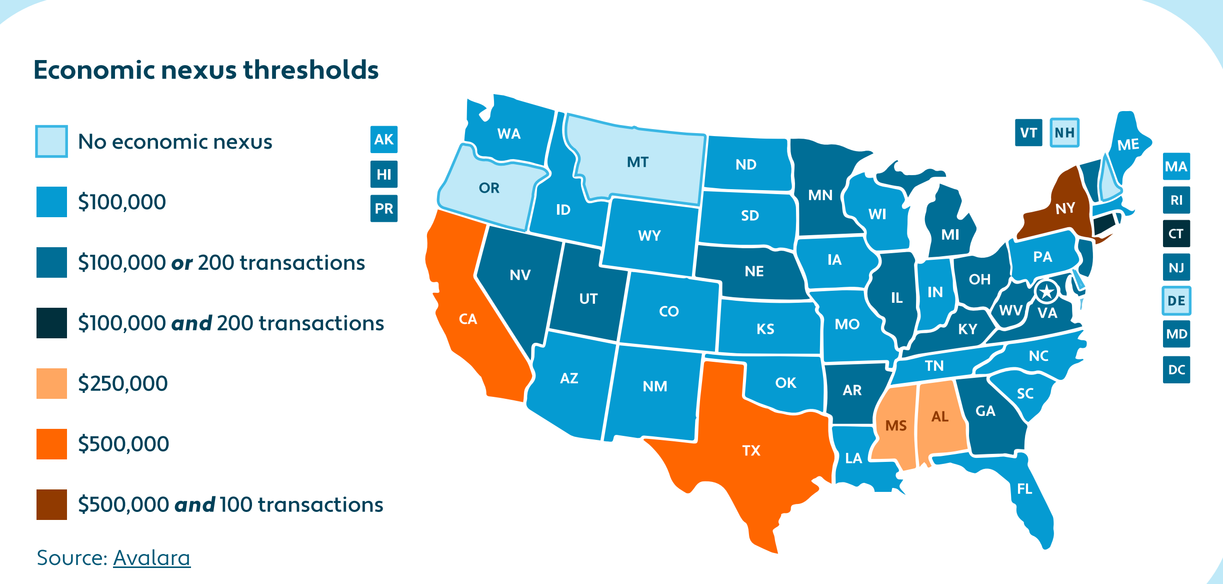

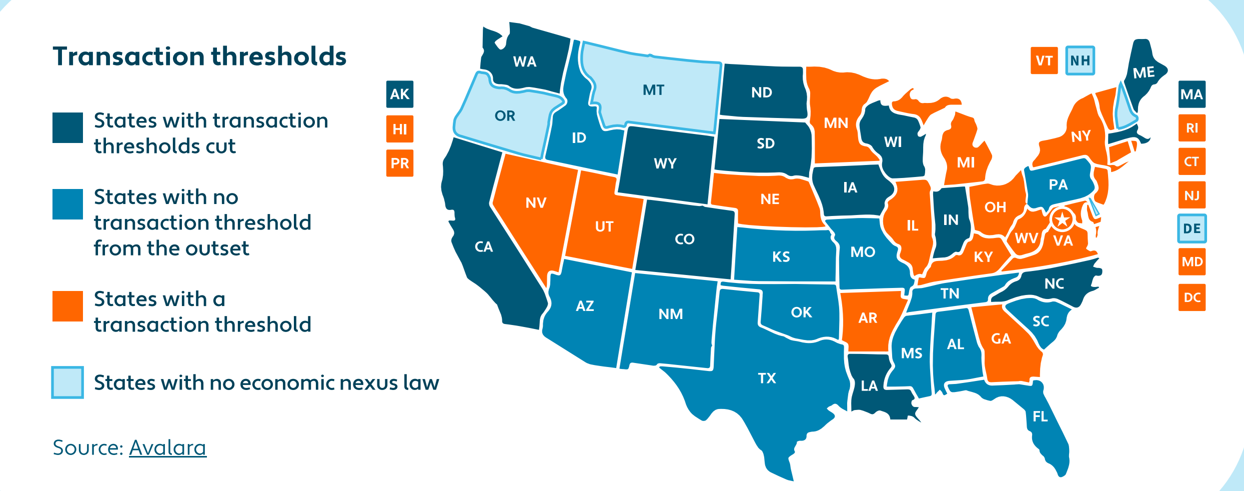

Effective January 1, 2025

The Streamlined Sales Tax (SST) Governing Board is encouraging its 24 member states to cut their transaction thresholds if they haven't already done so – most states that still have them are SST states. "There's a big initiative among the SST states to remove and update the transaction threshold," says Chad Paulson, Manager of SST Government Affairs at Avalara. "It's a burden for small sellers who do very low-dollar transactions to collect and remit in all these states where they don't exceed the dollar threshold."

If you're not sure whether and where you've established economic nexus, taking the **Avalara Sales Tax Risk Assessment** can help.

CHAD PAULSON
Manager of SST Government Affairs at Avalara

There's a big initiative among the SST states to remove and update the transaction threshold.

It's a burden for small sellers who do very low-dollar transactions ...

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Leveling the playing field in Illinois

Several out-of-state businesses are taking issue with **remote sales tax assessments in Illinois**. They maintain the state's requirements place an undue burden on remote sellers and discriminate against interstate commerce. (One company **settled with the state**, but more cases are expected.)

When Illinois first required remote sellers to **collect local taxes**, it established different sourcing rules and collection requirements for *in-state sellers*, *out-of-state sellers* that have a physical presence in the state, and *remote sellers* that don't. Sorting out who was responsible for what taxes where was so nonintuitive the Illinois Department of Revenue created two, yes two, separate **flow charts** for businesses.

Thanks to the enactment of **Senate Bill 3362**, as of January 1, 2025, *remote retailers* and *out-of-state sellers* can use the same flow chart – at least some of the time. Instead of applying the single Illinois use tax rate to transactions shipped from outside Illinois, out-of-state sellers will base sales tax rates for those transactions on the delivery address (aka, destination sourcing), like their remote retailer counterparts.

However, *out-of-state sellers* that have a physical presence in the state will continue to use origin sourcing for *sales fulfilled from inventory located in the state*. Like **in-state retailers** selling from an Illinois brick-and-mortar location, these out-of-state sellers will collect state and local tax at the rate in effect at the ship-from address, not the delivery address on these orders. Yet when selling activities occur within Illinois and the inventory originates from out of state, destination sales tax will be due.

If this will actually reduce compliance complexity is unknown. Sales tax experts have their doubts.

"Under the former Illinois law, remote sellers faced an incredible burden," says Diane Yetter, founder of the Sales Tax Institute. "Under SB 3362, this undue burden will apply to any seller located outside of Illinois or delivering goods from outside of Illinois." Instead of solving a problem, Illinois may have made it harder for more businesses. Yetter adds, "if the state thinks this solves the constitutionality problem, it doesn't. It just means it impacts more businesses and more customers."

"Other states chose to eliminate origin sourcing so every retailer uses destination sourcing (Colorado, Kansas, and Washington), or to create a single statewide rate for remote sellers (Alabama and Texas)," adds Scott Peterson. He's interested to see how the Illinois court cases pan out. Aren't we all?

DIANE YETTER
Founder of the
Sales Tax Institute

... this undue burden will apply to any seller located outside of Illinois or delivering goods from outside of Illinois. If the state thinks this solves the constitutionality problem, it doesn't.

It just means it impacts more businesses and more customers.

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Simplifying sales tax compliance in home-rule states

Illinois isn't the only state in the doghouse over sales tax. Colorado and other **home-rule states** are facing increased pressure to simplify onerous requirements.

"There's a lot of uncertainty around what will happen with economic nexus in home-rule jurisdictions," says David Lingerfelt, Senior Director of Indirect Tax at Avalara. "If a second challenge over remote sales tax ever makes it to the Supreme Court of the United States, it will probably be centered on home rule."

Colorado has already made huge strides; as of April 1, 2024, for example, **Colorado holds taxpayers harmless** if they made errors based on information provided by the Department of Revenue's **Sales Tax Lookup** tool. And more simplification measures are set to take effect in 2025. These include aligning home-rule reporting requirements for lodging marketplaces (January 1); streamlining the process for filing sales and use tax returns (January 1); and harmonizing state and local sales tax administration (July 1).

For 2025, the Colorado Sales and Use Tax Simplification Task Force is calling for the state to improve the functionality of the **Revenue Online search engine** and to establish confidentiality standards to protect taxpayer information obtained by a third-party auditor on behalf of a local jurisdiction. It also wants the Department of Revenue to look for ways to increase municipality and taxpayer use of the **Colorado Sales and Use Tax System** (SUTS).

The Centennial State should get a gold star for its achievements to date, though plenty of complexity remains. Silver, red, green, and blue stars (remember those?) go to the following home-rule states for their simplification measures.

- **Alabama** and **Louisiana** allow certain remote retailers to apply to collect and remit a single sales and use tax rate for all transactions in the state.
- **Arizona** can prevent municipalities from subjecting taxpayers to multiple audits.
- **Louisiana** dropped its economic nexus transaction threshold.
- The **Alaska Remote Seller Sales Tax Commission** (ARSSTC), which serves as the centralized administrator for local governments in the state, is **dropping its economic nexus threshold**.

DAVID LINGERFELT
Senior Director of Indirect Tax at Avalara

"There's a lot of uncertainty around what will happen with economic nexus in home-rule jurisdictions. If a second challenge over remote sales tax ever makes it to the Supreme Court of the United States,

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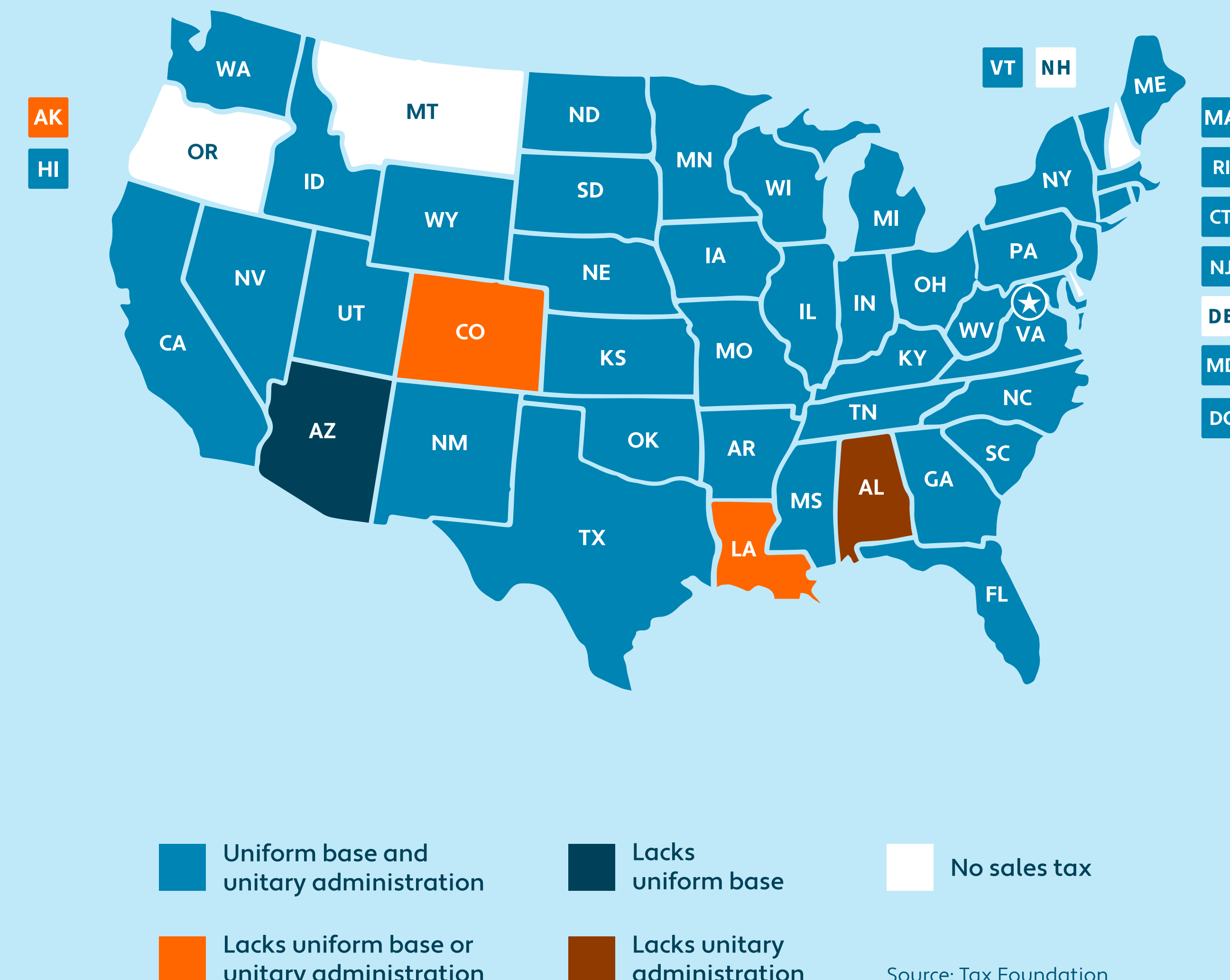
Still, neither Colorado nor Louisiana has a uniform sales tax base or unitary sales tax administration. Alabama also lacks unitary administration, and Arizona lacks a uniform base. There's more work to be done.

The burden of sales tax compliance is real, even for states. That's why the ARSSTC and Missouri have adopted Avalara Tax Research for Government, a self-service tax management system that leverages Geographic Information System (GIS) technology to provide sales and use tax rates and verified tax information.

Economic nexus isn't the only way for a business to create a sales and use tax obligation. Physical presence is still a primary nexus trigger.

Sales tax unity and uniformity



Source: Tax Foundation

Why physical presence nexus still matters

Out-of-state businesses can (and frequently do) establish nexus by having a physical presence in another state. And they often do so without realizing it.

"Many sellers have some sort of physical nexus in a state," Diane Yetter told the **United States Senate Finance Subcommittee on Fiscal Responsibility and Economic Growth** on September 25, 2024. "This might be a significant presence such as a physical location (store, office, manufacturing plant, etc.) or something minimal such as a one-day visit by an independent contractor to solicit a sale. Some of the most common physical presence we see in the companies we work with is inventory or remote employees."

In most states, even a minimal physical connection to a state can trigger nexus and a sales tax obligation. Yetter told the subcommittee "the applicability of physical nexus through these remote activities (inventory and remote workers) has exploded since 2020," resulting in many sellers being required to register even though their sales are below the economic nexus thresholds.

Adding insult to injury, some states are assessing out-of-state sellers for uncollected sales tax going back to the date when they first had inventory or a remote worker in the state. According to Yetter, this has resulted in "significant past liabilities" for several businesses. Some out-of-state retailers incorrectly assume they're not required to register or collect because their sales are below the remote sales threshold; after establishing economic nexus they're surprised to learn they already had physical nexus and therefore owe back taxes.

Unfortunately, exactly how much physical presence is required to trigger nexus varies from state to state and often isn't clear.

The Streamlined Sales Tax State and Local Advisory Council is working to help SST states clarify how much physical presence, if any, a remote seller can have in a state before it establishes physical presence nexus. "A state may allow a seller to have limited physical presence in the state and still treat the seller as a remote seller," it reminds in **Disclosed Practice 8.1** (Remote Sellers).

DIANE YETTER
Founder of the
Sales Tax Institute

Many sellers have some sort of physical nexus in a state. This might be a significant presence such as a physical location or something minimal such as a one-day visit by an independent contractor to solicit a sale.

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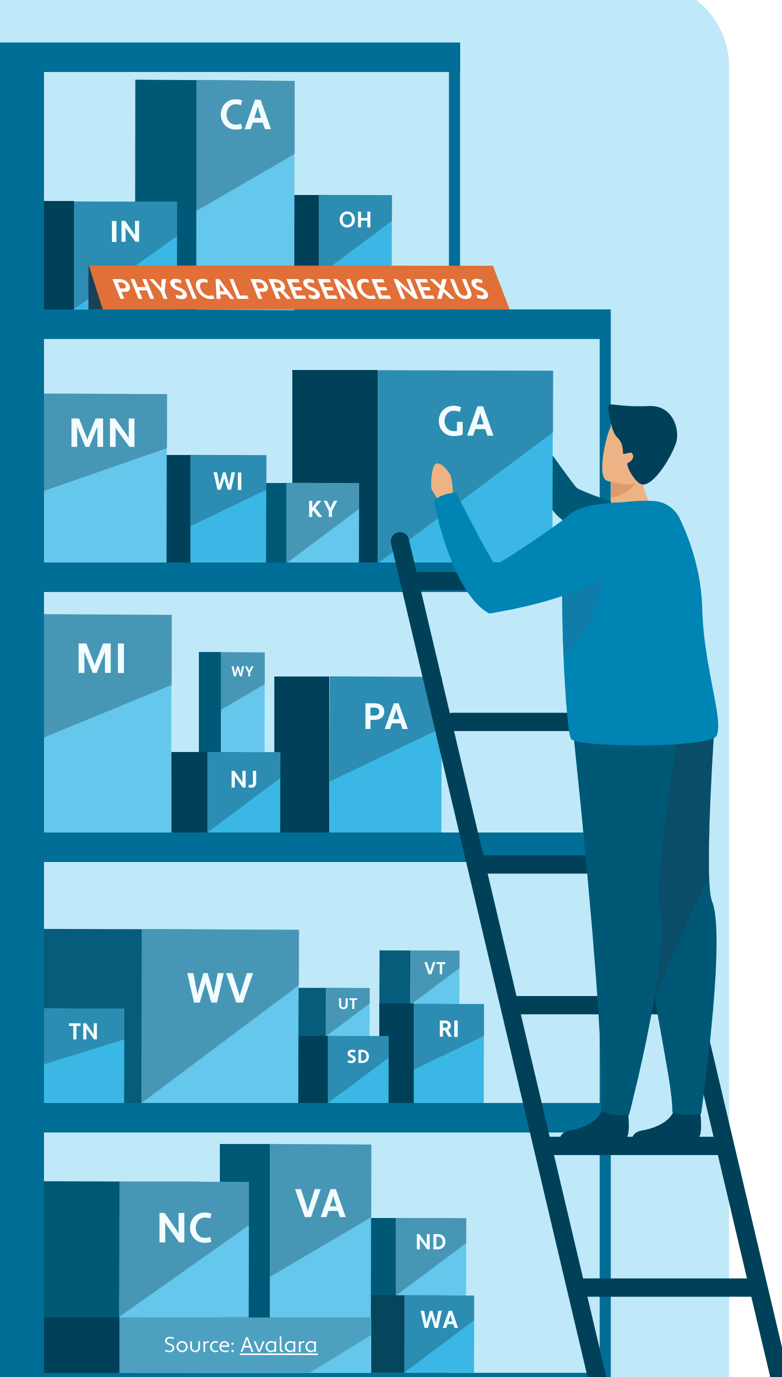

Source: Avalara

Disclosed Practice 8.1 addresses the impact of trade show activities, inventory, and remote employees on physical presence nexus. These are three tricky areas.

- **Trade shows.** To what extent participating in a trade show (or similar event) impacts nexus often isn't clear, though certain states do specify that an out-of-state seller creates nexus if they spend X days or make Y in sales in a set period of time from trade show activity.
- **Inventory.** Holding inventory in a third-party warehouse will give an out-of-state business nexus in more than 20 states, including many SST states. In some states, it won't; and some states haven't said one way or the other.
- **Remote employees.** Having a remote employee in a state can create nexus for an out-of-state business no matter what the employee does. Or, remote employees may create nexus only if they're involved in making sales.

SST states aren't alone in this, especially with respect to the last point. In the Bloomberg Tax 2022 Survey of State Tax Departments, a "high number of states" said "telecommuting employees would create nexus for corporate income *and* sales tax purposes."

"Allowing employees to work remotely at home was meant to be a temporary response to COVID," explains Brian Smith. "But it's become a permanent arrangement with some companies – and a potential nexus-generating activity. States are cracking down on remote workers and their impact on sales tax and income tax nexus. As a result, many companies are now evaluating the tax effect of their remote workers."

Proposed changes to Disclosed Practice 8.1(C) would require SST member states to specify any conditions (e.g., number of days) that will cause a business to lose its remote seller status.

"SST and the business community have been working together ever since the U.S. Supreme Court's South Dakota v. Wayfair decision in 2018 to identify areas where differences exist among state definitions and requirements related to remote sellers," says Craig Johnson, Executive Director of the SST Governing Board. "Many sellers are not aware of these differences."

With help from the business community, SST developed a number of disclosed practices. "These disclosed practices provide information on a whole host of questions including who is a remote seller, what creates nexus in a state, when does a remote seller have to register in a state, when can a remote seller stop collecting in a state, etc.," Johnson explains.

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The SST Governing Board publishes each state's answers on its website as part of each state's Tax Administration Practices section of their Taxability Matrix. Johnson says, "It's extremely important that remote sellers understand there are differences in these areas among the states so they don't inadvertently go down the wrong path – and the disclosed practices make it easy to identify these differences and each state's expectations."

Keep an eye on this issue in 2025, since SST member states may be clarifying their policies, and other states may follow their example.

CRAIG JOHNSON
Executive Director of the SST Governing Board

SST and the business community have been [identifying] areas where differences exist among state definitions and requirements related to remote sellers.

Many sellers are not aware of these differences.

Physical presence is no longer required for nexus in Wyoming resort districts

Interestingly, vendors no longer need to be physically located within a resort district in Wyoming to have a tax obligation, according to the Wyoming Department of Revenue. All retail sales of tangible personal property, admissions, and taxable services made within Wyoming's two resort districts are subject to sales tax as of July 1, 2024.

"Resort districts, often located in areas with significant tourist activity, provide a steady stream of taxable transactions from visitors purchasing goods and services," says Amanda Denniston, Government Relations Manager at Avalara. "By extending this sales tax, Wyoming is trying to ensure that both local and remote vendors contribute to state revenues. High-traffic areas like resorts need all the sales tax dollars they can get to maintain their infrastructure and services."

AMANDA DENNISTON
Government Relations Manager at Avalara

Resort districts, often located in areas with significant tourist activity, provide a steady stream of taxable transactions from visitors purchasing goods and services ...

High-traffic areas like resorts need all the sales tax dollars they can get to maintain their infrastructure and services.

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Physical presence can trigger use tax obligations

Use tax is a complement to sales tax: If a seller doesn't collect sales tax from a buyer at the point of sale, and the transaction is taxable, the buyer is generally required to self-assess and remit the equivalent consumer use tax to the state taxing authority.

But there's more to use tax than that. States also require businesses to pay use tax on tangible personal property purchased in another state then used in the taxing state. Use tax can apply to small items like laptops, intangible goods like software as a service (SaaS), or heavy equipment like steamrollers. And it really shouldn't be overlooked.

Ellingson Drainage, a Minnesota-based company that neglected to pay South Dakota use tax some years back, is now facing a **hefty use tax assessment**. The South Dakota Department of Revenue concluded the company owes more than $75,000 in use tax and interest on equipment used in the state between March 2017 and January 2020.

Ellingson disputed the assessment. It claimed the use tax assessment is unfairly disproportionate to the equipment's usage in the state – some of it was used for just one day.

MIKE DILLON
Founder of Dillon Tax Consulting

What's tricky about treating sales and use taxable events similarly is that a sale is a distinct measurable event that happens one time in one identifiable location, while taxable use or consumption can occur several times in several jurisdictions.

The same product may be subjected to multiple use taxes in multiple states if not fairly apportioned.

This violates the fair apportionment requirement of the Commerce Clause, the company argued, as well as the Due Process Clause of the 14th Amendment. But South Dakota courts sided with the state, and when **Ellingson appealed to the Supreme Court of the United States**, the Court declined to take the case.

The Ellingson case highlights several key use tax compliance challenges.

"Ellingson aptly asserts that use tax must reasonably reflect the in-state component of the activity being taxed, or the economic justification for a state's asserted use tax basis," explains Mike Dillon, founder of Dillon Tax Consulting. "What's tricky about treating sales and use taxable events similarly is that a sale is a distinct measurable event that happens one time in one identifiable location, while taxable use or consumption can occur several times in several jurisdictions. The same product may be subjected to multiple use taxes in multiple states if not fairly apportioned."

It's particularly difficult to apportion the use of digital goods and services, observes Dillon. "Digital goods and services have no measurable 'shelf life' over which to apportion value, are far more mobile than tangible goods, and may be used over and over and over again in multiple states (e.g., taking an online course or streaming a movie while traveling)," he explains.

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"Apportioning use tax among the states where a product is used would require agreement among all the states and the creation of an apportionment tracking system," says Scott Peterson. "The court's decision to deny certiorari could mean that apportionment isn't necessary."

Dillon agrees. "While some states (e.g., Ohio) do apportion value for temporary use, such provisions do not exist in every state. In order to create a uniform, workable multistate apportionment system, states would need to agree on: the classification of goods; a 'first functional use' standard; sourcing rules; the measurable life of both tangible and digital products; and reciprocal credits for both sales and use tax paid to other states." Assuming states could agree on all this, which is a big assumption, he thinks it would prove overly burdensome to individual consumers. "Tracking the use of certain digital products could also call into question privacy concerns."

The Ellingson case is a cautionary tale: Businesses should keep use tax top of mind.

As Ellingson demonstrates, it's distressingly easy for a company to find itself liable for years' worth of back sales or use taxes. Fortunately, states periodically offer tax relief programs to encourage businesses to come into compliance. Such programs don't come along often but can be a lifesaver for delinquent taxpayers when they do.

SCOTT PETERSON
VP of Government Relations at Avalara

Apportioning use tax among the states where a product is used would require agreement among all the states and the creation of an apportionment tracking system.

The court's decision to deny certiorari could mean that apportionment isn't necessary.

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Are any states offering tax relief in 2025?

Yes, though not necessarily tax amnesty.

Massachusetts offered tax amnesty at the end of 2024

The Massachusetts Department of Revenue was tasked with providing a 60-day **tax amnesty** program some time before June 30, 2025. From November 1 through December 30, 2024, it **waived most penalties** for qualifying taxpayers who voluntarily file tax returns for eligible tax types and pay the total amount of delinquent taxes owed.

Funding for the Massachusetts tax amnesty program is brought to taxpayers by the **fiscal year 2025** budget. There may be a lesson here for Kentucky lawmakers.

Kentucky tax amnesty is up in the air

Kentucky Governor Andy Beshear has been going head-to-head with the Legislature over tax amnesty for years. It's still not clear who'll come out on top.

The Legislature passed a law mandating the establishment of a tax amnesty program in 2022. Governor Beshear **vetoed** the amnesty because it didn't provide any funding for the program, and the Legislature overrode the veto. However, due largely to funding issues, the Kentucky Department of Revenue was unable to get the program off the ground.

A similar scenario went down in the spring of 2024: Governor Beshear **vetoed** the sections of House Bill 8 requiring the Kentucky Department of Revenue to launch a tax amnesty program on October 1, 2024.

The Legislature didn't override the veto this time around – but it didn't honor it either. Instead, it determined the governor didn't have the authority to make line-item vetoes to any portion of the bill and filed **House Bill 8** with the Secretary of State without the governor's signature.

So, what happens next?

The **Department of Revenue** says it "shall not implement the tax amnesty program," but this **may not be the end** of this conflict. If you have outstanding Kentucky tax obligations, there may be a chance to come clean with reduced penalties yet. The Department of Revenue may end up providing a 60-day tax amnesty program in 2025.

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SST may offer a voluntary disclosure program for remote sellers

The SST Governing Board is considering a voluntary disclosure program that would limit the lookback period for back sales tax liabilities to two years and waive penalties and late-filing fees for eligible remote sellers.

"This request was brought to the SST Governing Board by accounting and legal practitioners with clients who, for some reason, are not collecting sales tax where they should," explains Scott Peterson, who served as Executive Director of the Streamlined Sales Tax Governing Board for seven years prior to joining Avalara in 2012. "As with all amnesty-like initiatives, it's believed new tax collections will come from this effort." At the very least, it could allow unregistered sellers to pay their tax obligations without going bankrupt.

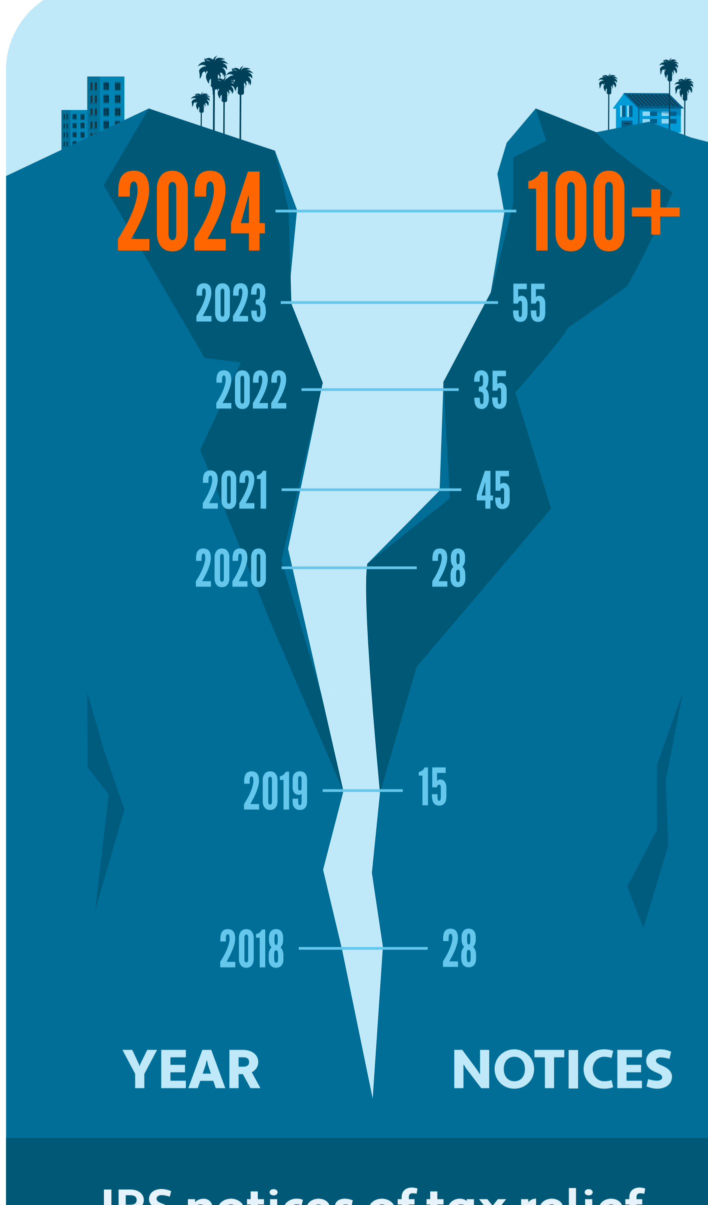
If approved, SST member states would be required to offer the voluntary disclosure program to qualifying businesses that fulfill the terms of the program. More on this to come in 2025.

Natural disasters spark tax relief in multiple states

A different form of tax relief often comes in the wake of extreme weather. Such federal, state, and local tax extensions are becoming more common. In 2018, the IRS posted fewer than 30 notices announcing tax relief for victims of earthquakes, fire, flooding, landslides, severe storms, volcanic eruptions, and the like. For 2024, the IRS already published more than 100 such notices as of December 1, 2024.

California, Kentucky, Minnesota, and South Carolina are among the states that offered extra time to affected taxpayers in 2024. For Hurricane Helene alone, tax extensions were granted to qualifying taxpayers in Alabama, Florida, Georgia, North Carolina, South Carolina, Tennessee, and Virginia. Similar programs will certainly resurface in 2025 whenever and wherever they're needed.

"One would think these programs would be the same across states," says Peterson. "They aren't because they're tied to the power given to governors to suspend laws during times of emergency. Because state legislators create the law, they also limit which laws a governor can suspend."



IRS notices of tax relief in disaster situations

Source: IRS

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SCOTT PETERSON
VP of Government Relations at Avalara

"One would think these programs would be the same across states. They aren't because they're tied to the power given to governors to suspend laws during times of emergency.

Because state legislators create the law, they also limit which laws a governor can suspend."

While tax departments are sometimes granted the authority to be flexible with deadlines during emergencies, they appreciate receiving tax payments and returns when they're due (or earlier!). To that end, many states incentivize businesses to pay sales tax on time. Like all sales and use tax policies, these incentives are subject to change.

New and updated vendor discounts for paying on time

Illinois caps retailers' discount

Illinois has allowed timely filers to retain 1.75% of the retailers' occupation tax collected. Beginning with returns due on or after January 1, 2025, the vendor discount is capped at $1,000 per month.

Louisiana lowers vendor compensation credit

Effective January 1, 2025, Louisiana is lowering the vendor compensation credit for businesses operating one or more locations within Louisiana from $1,500 to $750 per calendar month.

Wyoming amends vendor compensation credit

As of July 1, 2024, vendors that file and remit Wyoming sales and use tax on time may claim a vendor compensation credit of 1.95% of the total tax due. The credit is capped at $500 per reporting period. To qualify for the credit, the vendor's account must be in good standing and the returns and payments must be postmarked by the 15th of the month the tax is due.

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Other changes affecting sales tax compliance in 2025

Much as we'd like to, we can't cover *every* 2025 tax change in this report. There are too many jurisdictions, too many new laws and regulations, too many interesting court cases.

Nevertheless, here's a healthy sample of other tax changes on the horizon.

A direct pay permit change in Illinois

Illinois allows businesses holding a **direct pay permit** (DPP) to make multiple purchases from a supplier throughout the month without paying tax at the time of sale. This is helpful for businesses that make a lot of **purchases through procurement cards**, use electronic data interchanges, or purchase items with taxability that's hard to determine at the time of sale. It enables the buying business to calculate the tax due more accurately.

Senate Bill 3282, enacted August 9, 2024, requires each direct pay permit holder to review its purchase activity annually starting with calendar year 2024. By March 31, 2025 (and March 31 in subsequent years), permit holders must verify purchases made during the preceding calendar year were sourced correctly and the correct tax rate was applied. In the event an error is discovered, the business must file an amended return by April 20.

"To date, Illinois has not put out much guidance on the direct pay permit change," observes Lauren Stinson, Partner at Cherry Bekaert Advisory. "However, in theory it should not substantially impact taxpayers with a direct pay permit. With the luxury of having a DPP comes the obligation to have strong processes in place to ensure that all tax due is accurately calculated and remitted. Having an additional requirement that on an annual basis permit holders need to review their purchases should be no different than what they should be doing in practice."

Illinois will assess a $6,000 penalty on direct pay permit holders who fail to complete this purchase review. However, the Department of Revenue may waive the penalty if it determines that at least 95% of the transactions for the calendar year were correctly sourced and taxed. As discussed earlier, correctly sourcing Illinois sales can be tricky.

Stinson explains the extra compliance requirements could suggest a lot of noncompliance among direct pay permit holders, most of whom are typically subject to regular sales and use tax audits. "While I don't see the audit frequency changing, the $6,000 penalty for noncompliance doesn't seem to be enough of a 'stick' to warrant any extra attention to internal use tax calculation processes. Perhaps better compliance would be had from more of a 'carrot' approach – to reward those taxpayers that have strong systems and procedures in place and are extremely compliant."

LAUREN STINSON
Partner at Cherry Bekaert Advisory

With the luxury of having a DPP comes the obligation to have strong processes in place ...

Having an additional requirement ... should be no different than what they should be doing in practice.

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New de minimis threshold for service providers in Kentucky

Kentucky is changing its **de minimis** sales tax standard for services.

Through 2024, service providers are not required to collect sales tax on services if their gross receipts from enumerated services totaled less than $6,000 during the previous calendar year. This threshold jumps from $6,000 to $12,000 effective January 1, 2025. Businesses that qualify for the exemption are not required to register or maintain an active sales tax permit. Lucky them.

Note: The de minimis exception only applies to businesses that only sell affected services. It does *not* apply to anyone also in the business of selling tangible personal property, digital property, or services that were subject to sales tax prior to July 1, 2018 (e.g., **admissions and lodgings**).

New electronic filing requirements in Maryland

Maryland will soon require businesses to file many returns electronically, including sales and use tax returns – though the Comptroller may allow an exception for certain taxpayers. The electronic filing requirement will take effect for periods beginning after December 31, 2026. Tax return preparers and software companies may not charge a separate fee for electronic filing.

California allows the CDTFA to send electronic sales and use tax assessments

Prior to the enactment of **Senate Bill 1528**, the California Department of Tax and Fee Administration (CDTFA) could only send sales and use tax assessments and determinations to taxpayers via snail mail.

Starting January 1, 2025, the CDTFA may send these types of communications electronically if:

- A taxpayer requests electronic delivery, or
- The CDTFA determines the taxpayer no longer receives mail at their address of record and the taxpayer provided an email address

In addition to authorizing electronic notices, SB 1528 revises the threshold for the unremitted tax collected penalty, which is 40% of any sales tax reimbursement collected but not remitted. The previous penalty was the greater of $1,000 per month or 5% of the tax liability. For determinations made on or after January 1, 2025, the new penalty is the greater of $1,500 per month or 25% of the tax liability amount.

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Sales tax rate changes

There are always plenty of local sales and use tax rate changes to look forward to, far too many to call out here. However, a few recent and upcoming state sales tax rate changes merit callouts.

- The Louisiana **state sales tax rate** will increase from 4.45% to 5% effective January 1, 2025. (A sales tax reduction previously set to take effect on July 1, 2025, has been repealed.)
- The Illinois state sales tax will **no longer apply to food** as of January 1, 2026 (local taxes continue to apply as applicable).
- The Kansas state sales and use **tax on food** drops from 2% to 0% effective January 1, 2025 (local taxes continue to apply as applicable).
- **Oklahoma exempted food** from the state sales tax on August 29, 2024.
- Washington, D.C., will **increase the general sales tax rate** from 6% to 6.5% starting October 1, 2025; the rate will jump again, to 7%, beginning October 1, 2026.

Audits may get a boost from AI

Tax departments may be getting more aggressive and creative with audits – and artificial intelligence (AI) may help.

The trend starts at the top: The **IRS** says it will use AI and advanced analytics to help select partnerships for income tax audits. It will need the assistance. The agency suffers from **staffing problems** that show few signs of abating; and in May, IRS Commissioner Danny Werfel warned it could start **downsizing** as early as 2026 due to funding issues.

Also short-staffed, states are using AI "to multiply the **power of their audit teams**." According to Scott Peterson, "states rarely comment on how they choose someone to audit or how they conduct audits. But it's very safe to say they have long used tools to help in both and AI should be a natural fit."

Even back in 2022, before ChatGPT and similar tools rocked our collective worlds, the New York State Department of Taxation and Finance was able to conduct **56%** more audits than in 2021, despite having 5% fewer auditors. The state is reportedly "sending out hundreds of thousands of AI-generated letters looking for revenue."

SCOTT PETERSON
VP of Government Relations at Avalara

States rarely comment on how they choose someone to audit or how they conduct audits.

But it's very safe to say ... AI should be a natural fit.

To circle back to **an issue addressed earlier in this report**, many of the letters were triggered by remote workers or a change in tax residency. California currently uses AI tools to scan for online credit card sales tax activity or local utility records; it's looking for people who claim residency in another state but may really reside in California.

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Sales and use tax audits are benefitting from AI as well. As **Governing** reports, "sales and use tax enforcement is getting a boost from computerized scanning of online transactions that have been subject to state tax collections since the Supreme Court ruled in favor of the states in 2018." That's a reference to South Dakota v. Wayfair, Inc.

Source: CNBC

Something to keep in mind.

Of course, tax authorities continue to uncover noncompliance through more old-fashioned ways, such as tips from other taxpayers. That's how the Illinois Department of Revenue discovered one retailer was **not correctly taxing the appliances it delivered and installed**: The retailer was remitting use tax on their wholesale cost instead of sales tax on the retail value of the appliance. In September 2024, an Illinois appeals court determined that in addition to the sales tax owed, which will be tripled as allowed under the Illinois False Claims Act, the retailer will be assessed a penalty for each false tax return made from June 2015 to March 2021.

Ouch.

How Avalara can help

Avalara can help you account for tax changes and improve tax compliance for your business. Learn more about our automated solutions for tax research, calculating tax rates, preparing returns, and managing documents.

EXPLORE SOLUTIONS

Up next: Retail

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Retail

Figuring out how to rise above the competition will be a top priority for retailers in 2025. As always, navigating maddeningly complex sales and use tax requirements will be another. The right tools can help retailers succeed in both areas – and help retailers keep customers happy.

What's ahead:

- The retail resurgence
- What the numbers tell us about the retail industry in 2025
- Remote sales tax compliance isn't getting any easier
- Understanding retail delivery fees
- Sales tax holidays aren't relaxing for retailers
- Taxability trends to watch in 2025
- How marketplace facilitator laws are evolving in 2025
- We're finally getting new Form 1099-K reporting thresholds
- Sales and use tax changes affect procure-to-pay too

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The retail resurgence

The year ahead looks promising for retail. Inflation was **close to pre-pandemic levels** in October 2024, and though the tendency to hoard essentials dies hard, the **supply chain has largely stabilized**. For the most part, manufacturers have what they need to make products, and consumers have the resources to buy them.

And consumers *are* buying.

U.S. retail sales in September 2024 exceeded expectations, and retailers are generally optimistic. In the U.K., 85% of senior leaders interviewed by **Retail Week** between May 21 and June 28, 2024, predicted higher year-over-year sales in 2025. Opportunity abounds: For the right price, **67% of global buyers surveyed by NielsenIQ would try a new brand**. That brand could be yours.

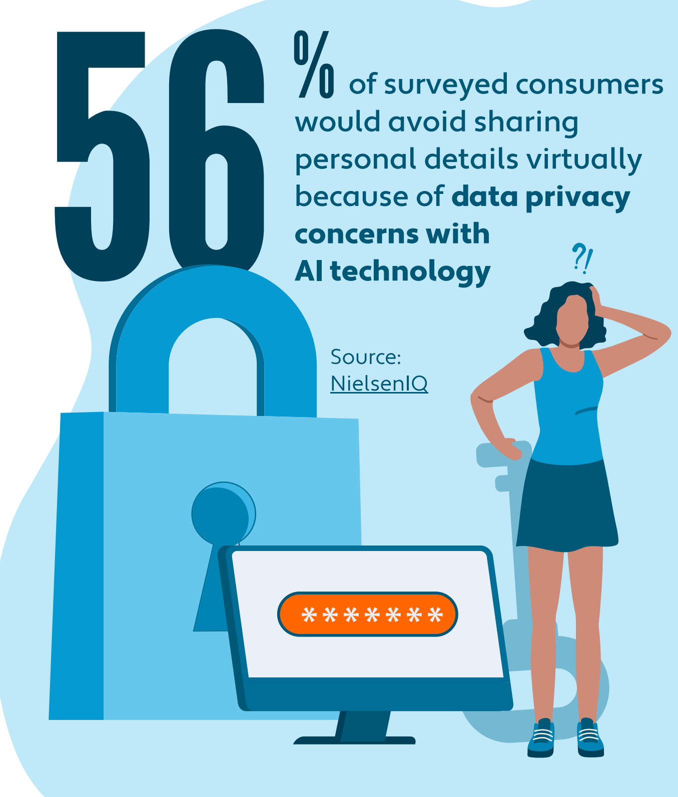
But 2025 won't be without hurdles. For one, consumers aren't buying willy-nilly. They're spending **intentionally**, "focusing primarily on what gives them a sense of prosperity and well-being." That's a tall order, and competition is fierce. Customers will lean toward retailers with user-friendly websites and convenient return policies.

Generative artificial intelligence (AI) and machine learning technologies can help retailers discover and cater to consumer preferences. Many buyers are game: 40% of consumers would accept a product recommendation from an AI assistant, according to the NielsenIQ survey. But new technologies bring new dangers from bad actors. Consumers are certainly wary: 56% of the NielsenIQ survey respondents are concerned about data privacy with AI technology. Having solid governance and security policies is key.

So is getting sales and use tax right.

Sales tax compliance is one of the biggest challenges facing U.S. retailers. It may even be harder for businesses selling *into* the U.S. because the sales tax structure is in a class by itself. There's a general sales and use tax in 45 states, plus Puerto Rico and Washington, D.C. – and no two state sales tax systems are alike. The majority of those states have local sales and use taxes, too, as does Alaska (which has no statewide sales tax).

Keeping up with the multitude of rate, rule, and policy changes is a monumental task. Understanding how all those sales and use tax changes impact your business even more so. This report aims to help by alerting you to some of the most significant retail sales tax changes on the horizon.



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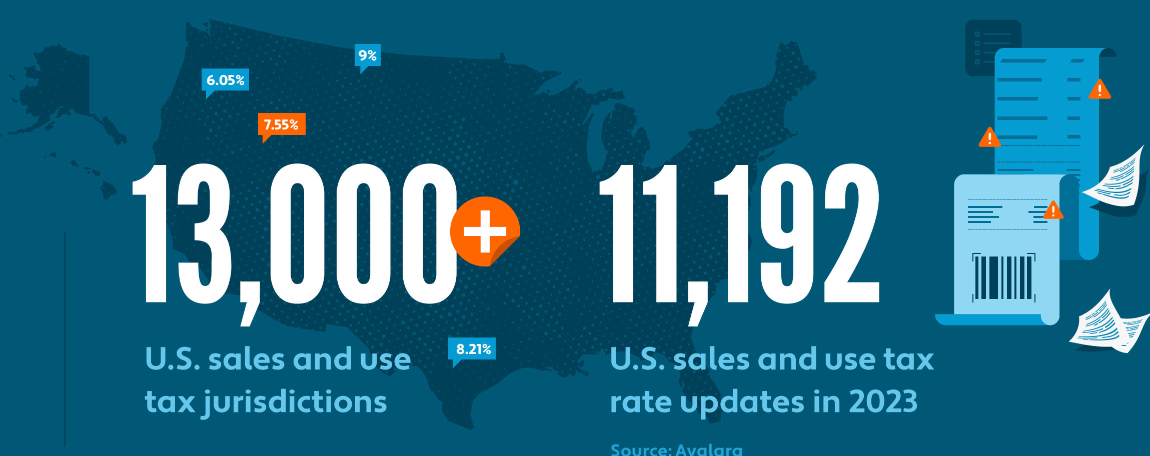
What the numbers tell us about the retail industry in 2025

The retail industry supports 1 in 4 U.S. jobs and contributes more than $5 trillion to U.S. annual GDP

1 in 4

U.S. jobs supported

Source: NRF



13,000+

U.S. sales and use tax jurisdictions

11,192

U.S. sales and use tax rate updates in 2023

Source: Avalara

39 ACROSS **19+**

sales tax holidays | states in 2024

Source: Avalara

98,910

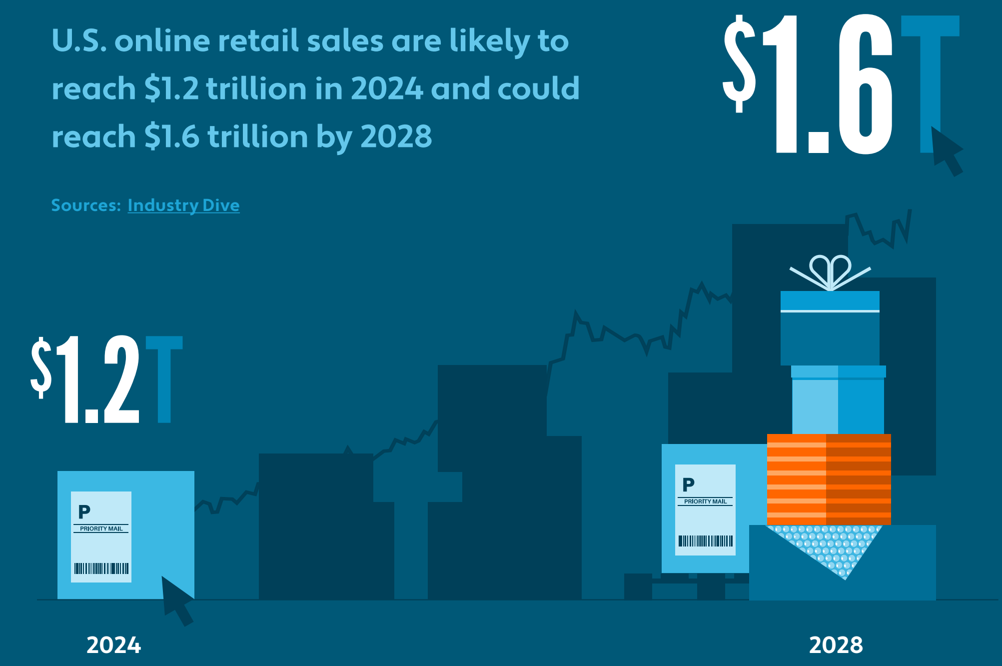
U.S. sales tax holiday rule updates in 2023

Source: Avalara

U.S. online retail sales are likely to reach $1.2 trillion in 2024 and could reach $1.6 trillion by 2028

$1.6T

Sources: Industry Dive



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Remote sales tax compliance isn't getting any easier

Before the Supreme Court of the United States issued its seminal ruling in South Dakota v. Wayfair, Inc. (June 2018), retailers typically only needed to collect and remit sales tax in the states where their business had a physical presence. That excluded a lot of retailers, especially before the emergence of ecommerce.

Economic nexus requirements are changing

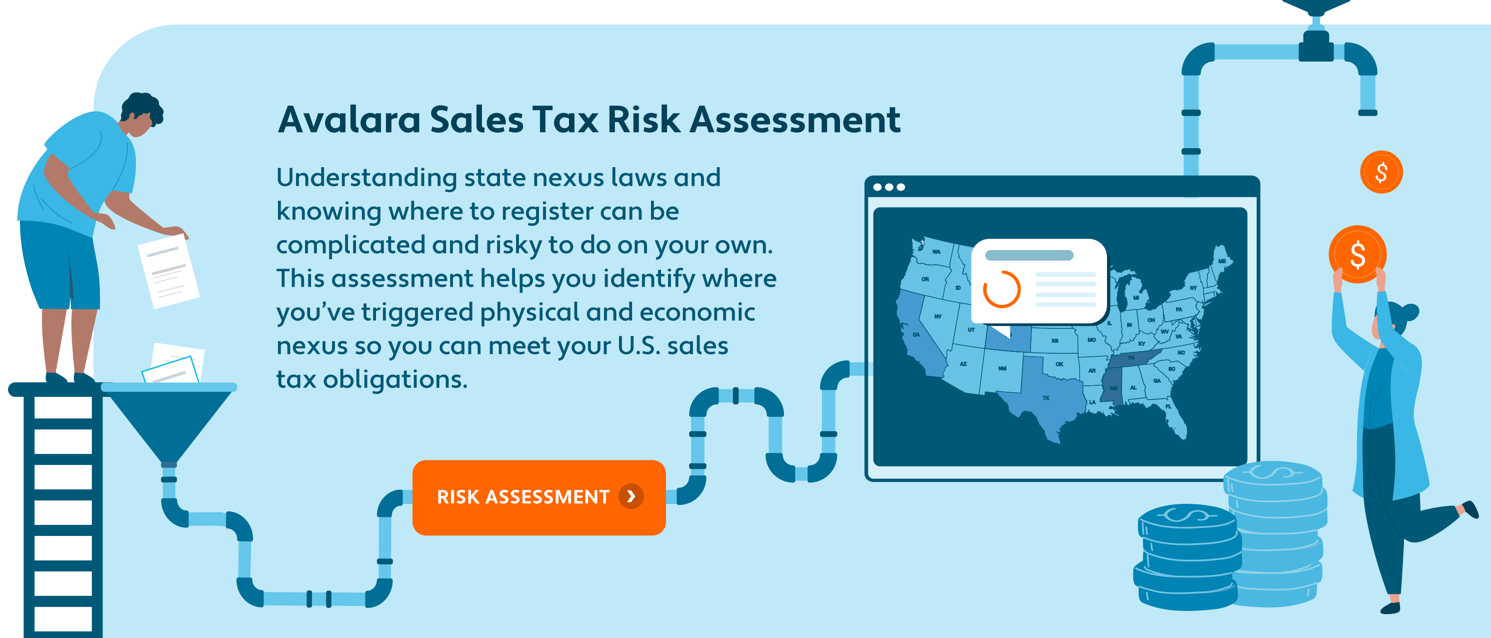
The Wayfair decision didn't eliminate physical presence as a nexus trigger, but it removed the guardrails of physical presence. Today, every state with a sales tax has an economic nexus law that bases sales tax obligations on a remote seller's economic activity in the state. Every state with a sales tax also requires certain marketplace facilitators to collect and remit sales tax on behalf of their third-party sellers, but we'll get into that later.

States do provide safe harbor for small businesses. For instance, remote sellers don't need to register for California or Texas sales tax unless they make at least $500,000 in sales in a 12-month period. In New York, the economic nexus threshold is $500,000 *and* 100 transactions, while Alabama and Mississippi both use a $250,000 sales threshold.

But as of December 2024, in 22 states, having just $100,000 in annual sales is sufficient to give a remote retailer a sales tax obligation. In another 20 states, the economic nexus threshold is $100,000 in sales *or* 200 sales transactions.

The transaction threshold is losing ground: 13 states have already eliminated it; Alaska is ditching it effective January 1, 2025; and New Jersey is moving to drop it in 2025. It's a bugbear for small businesses while it persists, especially for those with a high volume of low-value sales. Taking the **Avalara Sales Tax Risk Assessment** can help you determine whether and where you may have economic nexus.

We cover economic nexus and physical presence nexus more thoroughly in the sales tax section of this report. On to another issue plaguing ecommerce businesses: retail delivery fees.



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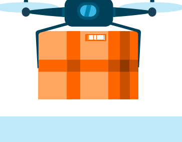
Understanding retail delivery fees



One of the biggest sales tax issues affecting retailers and marketplace facilitators these days is actually a retail delivery "fee," not a sales tax. How about that?

If you haven't yet encountered one – and the emphasis here is on "yet" – a retail delivery fee (RDF) is a fee on retail sales delivered by motor vehicle. Colorado was the first state to conceive of such a thing and is proving to be a trendsetter.

The **Colorado retail delivery fee** (currently 29 cents) caused a kerfuffle when announced in May 2022, mere weeks before taking effect July 1. For starters, nearly all retailers with a sales tax obligation in the state were told they'd have to collect the fee from their customers and state it separately on invoices. Many businesses weren't sure how to do that. The fact that the Colorado Department of Revenue initially couldn't answer some questions, like whether retail deliveries made by the USPS would be subject to the fee, didn't settle retailers' nerves.

Colorado eventually smoothed out most of the fee's kinks. It established an exception for some businesses and waived the requirement for retailers to collect the fee from customers; companies can now pay the fee themselves if that's easier or less costly. It found the answers to retailers' questions (the fee *does* apply to retail deliveries of taxable goods delivered by the USPS). But compliance challenges remain; for example, local sales tax applies to Colorado's RDF in some parts of the state but not in others.

When a **similar-but-different retail delivery fee** took effect in Minnesota on July 1, 2024, retailers and marketplaces were hit with new trials and tribulations.

Minnesota's 50-cent retail fee is less straightforward than its Colorado counterpart. The Colorado fee applies to *all* taxable tangible personal products delivered by motor vehicle (unless delivered to an exempt purchaser) but *doesn't apply* to any goods that are tax exempt. Yet more than 100 different taxable items, including a bunch of baby products, are *not* subject to Minnesota's fee. And clothing, which is generally tax exempt in Minnesota, *is* subject to the RDF – if the transaction equals or exceeds $100.

So that's fun.

Source: Avalara

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Lauren Stinson, Partner at Cherry Bekaert Advisory, explains that while retail delivery fees may have been well-intentioned, execution of fee collection has been problematic for taxpayers. "From an administrative perspective, sellers are finding it difficult to collect on top of the already burdensome and complex sales tax. Often needing internal IT programming to change invoicing and billing systems and/or shopping carts, smaller businesses are disproportionately impacted and are frequently paying the tax out of pocket as opposed to charging their customers."

Stinson adds that RDFs (and other types of fees) often result in higher prices. "In addition to the consumer paying the fees, sellers may need to raise prices to cover the extra cost of compliance – so it can have a double impact. Perhaps the question the states need to ask themselves is not, 'How can we raise revenue?' but, 'How can we do so in a way that is truly reflective of the source of the problem?'" She says fees and taxes that are more aligned with last-mile deliveries could more evenly impact the sellers putting the extra vehicles on the road.

Yet more RDFs are likely in the cards according to David Lingerfelt, Senior Director of Indirect Tax at Avalara. "A retail delivery fee is a great way to raise revenue without raising taxes. It's hard to raise the sales tax rate or expand the sales tax base, but it's relatively easy to implement a retail delivery fee."

LAUREN STINSON
Partner at Cherry Bekaert Advisory

"Smaller businesses are disproportionately impacted and are frequently paying the tax out of pocket as opposed to charging their customers.

In addition to the consumer paying the fees, sellers may need to raise prices to cover the extra cost of compliance – so it can have a double impact."

Which states are adopting retail delivery fees?

And sure enough, at least six states are contemplating retail delivery fees of their own: Maryland, Nebraska (also LB19 and LB48), Nevada, New York, Ohio, and Washington. "They're doing this in other states," Nebraska State Senator Carol Blood told the Revenue Committee when advocating for her retail delivery fee bill. "Right?"

Lingerfelt thinks Washington will be the next state to implement a retail delivery fee, and he's probably correct. A retail delivery fee analysis published in June 2024 by the Washington State Joint Transportation Committee concluded that "a modest fee on the delivery of retail goods in Washington has the potential to generate significant revenue for state and local jurisdictions." Yet it also acknowledged that an online retail delivery fee could negatively impact businesses of all types, so we'll have to wait and see how this plays out.

Retail delivery fees are definitely something to watch for in 2025. One could soon be coming to a state near you, though Stinson is hopeful that other states will tread carefully in this area. If they do pass such legislation, she says "states must learn to give taxpayers more time to get systems in place."

Sales tax holidays are another pain point for retailers, and for now at least, they're much more prevalent than retail delivery fees.

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Sales tax holidays aren't relaxing for retailers

There were at least 39 **sales tax holidays** in 2024 across 19 states, plus Puerto Rico and some localities in Alaska. The exact number is hard to pin down because sales tax holidays can change (like just about everything related to sales tax).

In 2024 alone:

- **Florida** established five new sales tax holidays.
- **Mississippi** moved up its tax-free weekend and extended it by one day.
- **New Jersey** repealed its tax-free weekend.
- **Ohio** extended and expanded its 2024 sales tax holiday.
- **Washington, D.C.**, created a new 4/20 medical cannabis sales tax holiday.

And in a surprise move, **Canada** offered a last-minute sales tax holiday in December.

Such changes make it hard for businesses to stay sales tax compliant. In fact, although sales tax holidays were conceived to boost sales, they may actually have an adverse effect on retailers.

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The impact of sales tax holidays on retailers

32%	of respondents have had sales increase during sales tax holidays
60%	struggled to make a profit due to sales tax holiday complexities
32%	described sales tax holidays as a "logistical nightmare"
58%	spend at least $10,000 annually preparing for sales tax holidays
57%	hire temporary staff to handle the increased demand
24%	found it difficult to understand the rules and restrictions
53%	pay their employees overtime

Source:
Avalara/Censuswide survey

How sales tax holidays impact retailers

To better understand the full impact of sales tax holidays for retailers, Avalara asked Censuswide to survey 500 operations and/or finance professionals at small and midsize U.S. retailers in August 2024.

The responses were fascinating: 26% of retailers surveyed were concerned about complying with varying rules and exclusions; 73% reported difficulties in complying with sudden sales tax holiday changes. See more takeaways from the survey to the left.

In addition to complicating compliance for businesses, sales tax holidays don't come cheap for the states that host them. According to the Institute on Taxation and Economic Policy, 2024 sales tax holidays cost states and localities over $1.3 billion in lost revenue.

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What states can do to simplify sales tax holidays for businesses

To reduce the compliance burden on retailers, survey respondents recommended that states:

- Eliminate sales tax holiday price caps.
- Reduce the number of yearly sales tax holiday changes.
- Issue sales tax holiday guidance at least six months before the event.

Ohio and Canada should take note.

In September 2024, the Streamlined Sales Tax Governing Board found Ohio to be **out of compliance** over its holiday. Why? The 2024 sales tax holiday began on July 30, and the Ohio Department of Taxation notified vendors of the changes on May 31, 2024 – *not* "at least 60 days prior to the first day of the calendar month in which the holiday will begin," as required under the Streamlined Sales and Use Tax Agreement (SSUTA, or simply SST).

Sorry, Ohio.

"SST decided 22 years ago that states should be required to provide notice for tax changes," explains Scott Peterson, VP of Government Relations at Avalara and former Executive Director of the Streamlined Sales Tax Governing Board. "The issue was then as it is today: How much notice is appropriate? Currently, SST requires 60-day notice. Is 59 days too little notice?"

Maybe, maybe not. Ohio's 2024 sales tax holiday exemption applied to almost all tangible personal property priced $500 or less – not just clothing and school supplies subject to price restrictions as in prior years. So, it affected many retailers that haven't had to comply with Ohio sales tax holiday rules in the past.

Perhaps not surprisingly, it seems some retailers **continued to charge Ohio sales tax** on items that should have been exempt. Some businesses reportedly determined it would be "too difficult to change their systems to accommodate the rules … for such a short period of time."

Whatever their reasons, businesses that erroneously collected sales tax on qualifying sales tax holiday items may find themselves having uncomfortable conversations with disgruntled customers and fielding requests for sales tax refunds. The **Ohio Department of Taxation** has encouraged consumers mistakenly charged sales tax to "take their receipt to the retailer for a refund."

SCOTT PETERSON
VP of Government Relations at Avalara

> **Sales tax holidays … present a unique opportunity for retailers to drive sales, but the complexities involved can turn opportunity into a significant challenge,**
>
> **especially for small and medium-sized businesses.**

It's a pickle, and one that could have been avoided with more advanced notice and preparation.

With less than two days to prepare, retailers in Canada may face similar obstacles during the goods and services tax (GST)/harmonized sales tax (HST) holiday.

"Sales tax holidays present, in concept, a unique opportunity for retailers to drive sales, but the complexities involved can turn that opportunity into a significant challenge, especially for small and medium-sized businesses," says Peterson.

So …

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... how can retailers prepare for new sales tax holidays in 2025?

The retailers surveyed in August said they plan to take proactive measures to better prepare for sales tax holidays in 2025 and beyond.

- 40% will start planning for tax-free events earlier.
- 35% will hire people dedicated to tax compliance.
- 35% will switch to more advanced sales tax software.
- 25% will invest in sales tax software for the first time (26% said they currently manually manage sales tax holidays themselves, without software).

Getting in front of sales tax holidays is a good idea: Most states that had tax-free events in 2024 will have similar sales tax holidays for retailers in 2025, and there's sure to be at least one state with one or more new sales tax holidays (we're looking at you, Florida).

California, Colorado, Hawaii, Illinois, Michigan, and North Carolina are among the states that considered new sales tax holidays in 2024. And in September 2024, lawmakers introduced a bill to reinstate New Jersey's annual sales tax holiday.

Whatever else can be said about sales tax holidays, they are by definition temporary. More permanent sales and use tax changes are happening as well: new sales tax exemptions, new tax rates, and new taxes.

Taxability trends to watch in 2025

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States continually refine sales tax requirements for retailers, by enacting new laws or by explaining existing ones. Recent and upcoming changes and clarifications center on credit card swipe fees and taxes on groceries.

Credit card swipe fees

Starting July 1, 2025, **Illinois is prohibiting card networks from charging or receiving interchange fees** (aka, swipe fees) on excise tax, gratuities, or sales and use taxes that are included in a transaction. This represents a significant change: Swipe fees currently apply to the total value of the transaction, including gratuities and taxes. Be on the lookout for guidance from the Illinois Department of Revenue.

Credit card fees are top of mind in Texas too. In July 2024, the Tax Policy Division of the Texas Comptroller confirmed that **credit card processing fees are subject to sales tax** when a retailer passes the fees on to customers, even if separately stated.

The Wyoming Department of Revenue also addressed the taxability of credit card fees recently. Per its **September 2024 Taxing Issues** newsletter, a credit card fee or convenience fee *is* subject to tax when the product or service it's associated with is taxable but *is not* subject to tax when the associated product or service is exempt. "This is a reminder by the state that credit card fees are part of the gross receipts from the sale," says Peterson. "There's a movement by retailers to charge consumers a fee to reimburse themselves for the fee they pay to the credit card company."

Expect more states to weigh in on this issue in the coming months and years.

SCOTT PETERSON
VP of Government Relations at Avalara

This is a reminder by the state [Wyoming] that credit card fees are part of the gross receipts from the sale.

There's a movement by retailers to charge consumers a fee to reimburse themselves for the fee they pay to the credit card company.

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Cutting back on grocery taxes ...

With food prices up a whopping 28% since 2019, grocery tax exemptions have been a hot topic in the states where food for home consumption isn't already exempt from sales tax.

As of December 2024, Alabama, Arkansas, Hawaii, Idaho, Illinois, Kansas, Mississippi, Missouri, Oklahoma, South Dakota, Tennessee, Utah, and Virginia all tax groceries at either the full sales tax rate or a reduced rate. Food is subject to local sales tax but not the state sales tax in several other states, including parts of Colorado and Alaska.

But change is afoot.

- Oklahoma exempted food from the state sales tax effective August 29, 2024.
- Kansas is exempting unprepared food from the state sales tax effective January 1, 2025.
- Illinois will exempt food from the state sales tax starting January 1, 2026.
- Alabama may further cut the state sales tax on food for home consumption; it would have dropped the rate to 2% on September 1, 2024, had the state's Education Trust Fund reached a certain benchmark.

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Local sales and use taxes in Alabama, Illinois, Kansas, and Oklahoma still apply.

Arizona, Arkansas, Louisiana, Missouri, Tennessee, and Virginia are among the states that have tried to further reduce or eliminate grocery taxes in recent years, without success. The legislatures in one or more of these states will likely try again in 2025.

Voters got the final say in South Dakota on November 5, 2024, and rejected a measure seeking to prohibit the state tax on food and groceries. In Utah, a proposed constitutional amendment to repeal the state sales tax on food was voided on October 9, 2024, due to procedural issues, so voters had no chance to weigh in.

"Talking about tax policy can become emotional, especially when talking about the taxation of groceries," notes Scott Peterson. "Recently, Utah enacted a very significant change to its tax structure that had to be repealed because it relied on increasing the sales tax rate on groceries up to the normal state sales tax rate. Likewise, in South Dakota the Legislature and the governor have been in a multiyear battle over taxing groceries."

... and taxes on other essentials

Groceries aren't the only products states are interested in exempting. Several states have established or are considering sales and use tax exemptions that benefit certain populations or businesses, such as families or nonprofits. Recent and upcoming changes include:

- New sales tax exemptions for certain nonprofits in Maine and Washington
- New sales tax exemptions for the health care industry in Georgia and Maine
- New sales tax exemptions for families in Nebraska, Nevada, New York, and South Carolina

Clothing sold for less than $110 per item became exempt from local sales tax in Putnam County, New York, on March 1, 2024. South Carolina established a sales tax exemption for feminine hygiene products on May 13, 2024. Nebraska will exempt diapers starting July 1, 2027, and child and adult diapers will be exempt from Nevada sales tax from January 1, 2025, through December 31, 2050.

Though unsuccessful, Kentucky, Missouri, and several other states introduced legislation in 2024 to end pink taxes (in an attempt to exempt diapers, menstrual care products, and/or a variety of baby care products). Many of these states will likely try again in 2025.

Taxability changes don't merely impact direct sellers. They also affect the marketplace facilitators that account for a growing amount of global retail sales.

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How marketplace facilitator laws are evolving in 2025

More than 150 online marketplaces facilitate sales for millions of sellers – close to 10 million sellers on Amazon alone. By 2025, marketplaces are expected to be the "dominant online distribution channel in retail, travel, and food delivery," as well as for a variety of B2C, C2C, B2B, and C2B services. You can find just about anything through an online marketplace, including attorneys, dog walkers, and tutors.

Given the breadth of marketplace transactions and the differences in state laws, it's not always clear when and where the seller or marketplace is responsible for the applicable taxes and fees. Plus, states are still tinkering with marketplace laws. It's hard to keep up.

What follows are just some of the most interesting recent developments affecting marketplace facilitators.

Source: Helium 10

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South Carolina Supreme Court will review Amazon sales tax case

Amazon and South Carolina have been battling for years over whether Amazon is liable for approximately **$12.5 million in unpaid sales tax on third-party sales** made January 1, 2016, through March 31, 2019. This was before South Carolina's **marketplace facilitator law** took effect on April 26, 2019, but after Amazon had established a physical presence in the state.

South Carolina had agreed to waive Amazon's obligation to collect and remit sales tax for a time on the promise that Amazon would invest at least $125 million and create 2,000 jobs in the state. The agreement called for Amazon to collect South Carolina sales tax starting January 1, 2016, and it did – but only on its own sales, not on those of its third-party sellers.

Agreeing with previous court decisions, on January 24, 2024, the Court of Appeals of South Carolina **found Amazon liable for the tax**. Amazon appealed, and on October 3, 2024, the Supreme Court of South Carolina **agreed to review** the case.

"The fact that the South Carolina Supreme Court agreed to take the case leads me to wonder if it will disagree with the state, at least on some point," says Peterson. "It's a shame the wheels of justice move so slowly. This could have a severe impact on marketplaces and their sellers."

All eyes will be on this case as we wait for the court's decision.

SCOTT PETERSON
VP of Government Relations at Avalara

"The fact that the South Carolina Supreme Court agreed to take the case leads me to wonder if it will disagree with the state, at least on some point. It's a shame the wheels of justice move so slowly.

This could have a severe impact on marketplaces and their sellers."

Texas says marketplace fees are taxable

The Texas Comptroller has published a **proposed rule** clarifying that the fees online marketplaces charge to third-party sellers are **taxable data processing fees**.

Per **Comptroller Glenn Hegar**, marketplace sales involve "two purchasers, two sales contracts and two taxable transactions. The purchaser of goods or services through a marketplace pays sales tax on the goods or services purchased. And the marketplace seller, who is purchasing data processing services from the marketplace provider, pays sales tax on those services."

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California makes marketplaces do more to stop organized retail crime

Organized retail crime (ORC) has become a serious problem for marketplace facilitators because many stolen goods are eventually sold to unsuspecting customers through online marketplaces.

After Congress set **new compliance standards** for online marketplaces to help prevent online ORC in 2023, California and a number of other states passed their own versions of the law. Starting July 1, 2025, California will require more online marketplaces to implement more **stringent anti-fraud policies**. These include:

- Establishing and maintaining a policy prohibiting the sale of stolen goods on the platform (including but not limited to suspending or terminating the seller's account)
- Providing a mechanism for individuals to notify the online marketplace that a seller is or may be selling stolen goods
- Providing a mechanism that allows the marketplace and law enforcement to communicate in a timely and confidential manner
- Maintaining internal written policies, systems, and staff to monitor listings in order to affirmatively prevent and detect organized retail crime

"For decades, marketplace trust and safety teams have been fighting against nefarious actors, fraudsters, and organized retail criminals without government resources or much support," explains Jeremy Gottschalk, Founder and CEO of Marketplace Risk. "While it's good to see various states and the federal government finally addressing the problem with well-intentioned steps in the right direction, I fear the impact on smaller, earlier-stage marketplaces could stifle competition and new entrants. With the exponential increase in internet-based criminal activity globally, there is an urgent, corresponding need to increase law enforcement resources to support marketplaces in their efforts to identify and pursue these criminals."

Whether other states will also adopt stricter requirements remains to be seen. It's certainly something to keep an eye on in 2025.

JEREMY GOTTSCHALK
Founder and CEO of Marketplace Risk

With the exponential increase in internet-based criminal activity globally,

there is an urgent, corresponding need to increase law enforcement resources to support marketplaces in their efforts to identify and pursue these criminals.

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California lets rideshare and delivery apps hire independent contractors

The **California Supreme Court unanimously upheld Proposition 22** on July 25, 2024, freeing rideshare and delivery companies like Amazon, DoorDash, Lyft, and Uber to classify workers as independent contractors rather than employees. Prop 22 also entitles app-based rideshare and delivery gig workers to benefits like guaranteed minimum earnings and a health care subsidy.

Rideshare and delivery companies supported Prop 22. Had it been overturned, they could have had to register with every city and county in the state where their drivers operate – and there are 58 counties and 482 municipalities in California. So, phew, for them.

Though Prop 22 only affects companies operating in California (and California workers), other states may follow California's lead. They often do, and at least one other state – Massachusetts – is examining how rideshare companies classify their drivers. Efforts to put the issue on the November 2024 ballot in Massachusetts failed, but the issue could resurface in Massachusetts or other states in 2025.

States may work to prevent double taxation on third-party deliveries

The risk of double taxing marketplace transactions has been around ever since states first started requiring marketplaces to collect and remit taxes on behalf of third-party sellers. It's particularly high for restaurants and other businesses that contract with third-party marketplace delivery platforms (aka, delivery network companies) like DoorDash, Grubhub, and Uber Eats.

Here's an example of what happens. Food delivery marketplaces are often responsible for collecting and remitting taxes on the sales they facilitate, though specific requirements vary by state. Restaurants are required to collect and remit taxes on food sold directly to consumers. If a restaurant's sales system isn't set up to distinguish between the different types of transactions, both the restaurant and marketplace may end up taxing sales made for third-party delivery.

"When restaurants use a point-of-sale (POS) system that integrates Uber Eats or Grubhub orders with their in-house transactions, they may not realize that marketplace facilitators are responsible for the sales tax on those orders," says Amanda Denniston, Government Relations Manager at Avalara. "Unfortunately, we've encountered many businesses that unknowingly file and pay sales tax on these transactions, unaware that the marketplace facilitator has already remitted the tax. This results in a costly double payment – something especially detrimental for restaurants operating on tight margins."

"Double payment becomes more complex depending on location, the platforms the seller uses in their business (there are often more than one), and how the data comes from each different provider," explains George Trantas, Senior Director of Global Marketplaces at Avalara.

AMANDA DENNISTON
Government Relations Manager at Avalara

Unfortunately, we've encountered many businesses ... unaware that the marketplace facilitator has already remitted the tax.

This results in a costly double payment ...

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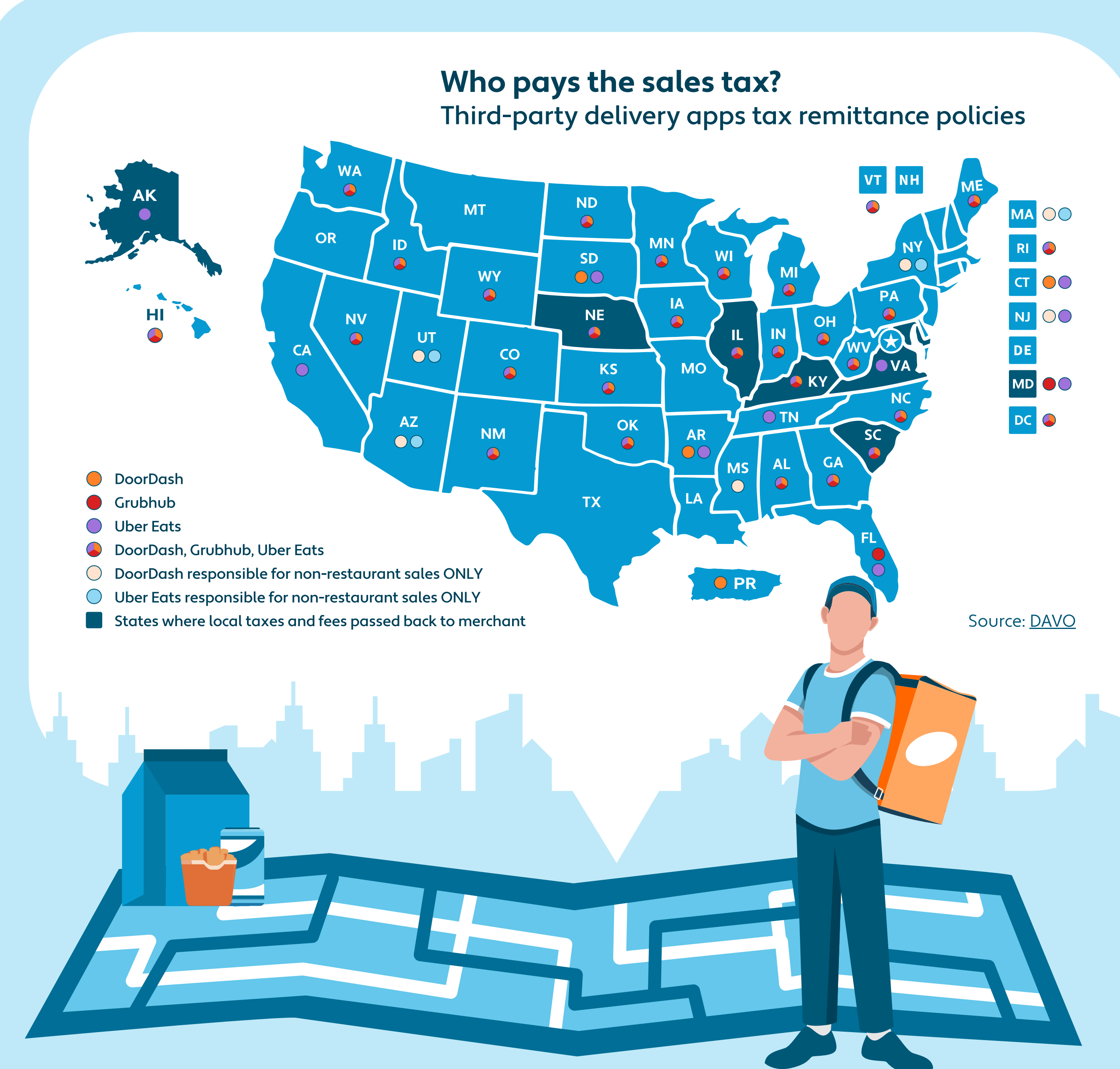
The fact that different states have different laws further complicates the matter. For instance, California *doesn't require* third-party delivery service providers to collect and remit taxes on meals sold through their platforms, but it allows them to elect to do so. The **California Department of Tax and Fee Administration** cautions restaurants that they "may still be responsible to report tax on sales of meals." Restaurants and marketplaces therefore need to do legwork to determine their tax obligations.

NCSL weighs in

The **National Conference of State Legislatures** (NCSL) recognizes that in some instances, marketplace facilitator laws have resulted in "double taxation and unfair tax administration." It knows local tax obligations can further complicate the matter, as marketplaces may collect state taxes but not local taxes, or local taxes but not state taxes. The same goes for meals tax, which is different from sales tax, and for fees like bag fees.

NCSL recommends states exclude certain delivery network companies and similar platforms from the definition of "marketplace facilitator" and the obligation to collect tax, as California has done. Though as California itself admits, that doesn't always solve the problem.



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NCSL also suggests states allow marketplace facilitators to take a "tax paid on purchases resold" deduction on their sales tax returns "for sales tax paid to the marketplace seller due to the marketplace seller's point of sale system not being able to suppress sales tax on facilitated transactions." North Carolina currently allows marketplaces to **recover sales or use tax paid** to a seller in certain instances.

While the most sophisticated delivery app companies usually have the resources to ensure they're collecting and remitting the taxes and fees they're required to collect, tax compliance can be much harder for the businesses they work with. An added complication for businesses is that **third-party delivery apps don't all handle taxes and fees the same way in every state**.

Clear guidance from the states helps, and some states – including **Pennsylvania** and **Texas** – provide it. But it's often distressingly difficult to obtain clear information from tax authorities, and it shouldn't be.

The Streamlined Sales and Use Tax Governing Board (SST) is working on a solution.

SST weighs in

"We are in the early stages of better understanding how these transactions work, what the state's expectations are from the restaurants and the food delivery companies, if double taxation is happening, and what can be done to eliminate it," says Craig Johnson, Executive Director of the SST Governing Board. "At this point, I anticipate that the SST will develop some disclosed practices related to this issue."

That should be a big help for the 24 states that are members of SST and companies doing business in those states. Unfortunately, states that don't participate in SST don't need to adhere to SST best practices, and double taxation can arise in any and all states.

"The determination of the correct tax to collect from customers shouldn't be a guessing game for the seller," Diane Yetter told a **United States Senate Finance Subcommittee** on September 25, 2024, at a hearing on providing small business relief from remote sales tax collection. The president and founder of the Sales Tax Institute and Yetter Tax added that "states need to make the taxability rules, as well as rates and boundaries, clear, accessible, understandable, and fair."

CRAIG JOHNSON
Executive Director of the SST Governing Board

> **We are in the early stages of better understanding how these transactions work,**
>
> **what the state's expectations are from the restaurants and the food delivery companies, if double taxation is happening, and what can be done to eliminate it.**

Some SST states are moving in that direction. In May 2024, the Nevada Tax Commission drafted a proposed regulation to clarify a host of **sales and use tax requirements for marketplace facilitators**, marketplace sellers, and remote sellers. Among other topics, it addresses requirements for delivery network companies. If the **proposed regulation is adopted**, it will have the effect of law once filed with the Secretary of State.

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DIANE YETTER
Founder of the
Sales Tax Institute

The determination of the correct tax to collect from customers shouldn't be a guessing game for the seller.

States need to make the taxability rules, as well as rates and boundaries, clear, accessible, understandable, and fair.

Michigan and Ohio introduced bills to address this issue in 2024. We look forward to seeing which other states, if any, will do the same in 2025. Scott Peterson expects most states to take some action, legislative or regulatory. "No state ever intended to tax transactions twice." he says. "Delivering someone else's food should never have become as complicated as it is in some states."

There's good reason for states to get on top of this: The food delivery market size is projected to grow to $213 billion by 2030.

As food delivery marketplaces strive to sort out their sales and use tax obligations, marketplaces that ship goods from overseas are dealing with an altogether different matter: additional attention at customs.

Customs and Border Protection will scrutinize marketplace shipments

Here's the quick and dirty summary. Under customs Entry Type 86, goods meeting the de minimis threshold of $800 can be imported into the United States duty free. The U.S. Customs and Border Protection (CBP) now processes more than 1 billion de minimis packages a year. With a growing body of evidence that Entry Type 86 is being exploited, CBP is upping efforts to ensure compliance. As of May 31, 2024, CBP had suspended multiple customs brokers from participating in the Entry Type 86 test and was looking to restrict and screen Entry Type 86 imports.

Approximately 50% of marketplace shipments into the United States originate in China and need to pass through CBP. Most of the shipments qualify for Entry Type 86, so most are now facing heightened security. This could be a massive disrupter. If nothing else, it will likely slow cross-border marketplace shipments.

George Trantas says ensuring your data and import documentation are complete, accurate, and timely can help avoid Entry Type 86 delays. He recommends providing detailed information, including the bill of lading or air waybill number, entry number, planned port of entry, shipper and consignee names and addresses, country of origin, quantity, fair retail value, 10-digit HTSUS number (the U.S. tariff code), and IOR (importer of record) number. Implementing automation for your international tax compliance can help.

A change to the 1099-K reporting thresholds is another issue marketplaces will need to monitor in 2025.

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We're finally getting new Form 1099-K reporting thresholds

In 2021, Congress passed a law lowering the 1099-K reporting threshold from $20,000 *and* 200 transactions to simply $600. This will have an enormous impact on gig workers; people who sell goods through Venmo, PayPal, or similar platforms; and the marketplaces themselves.

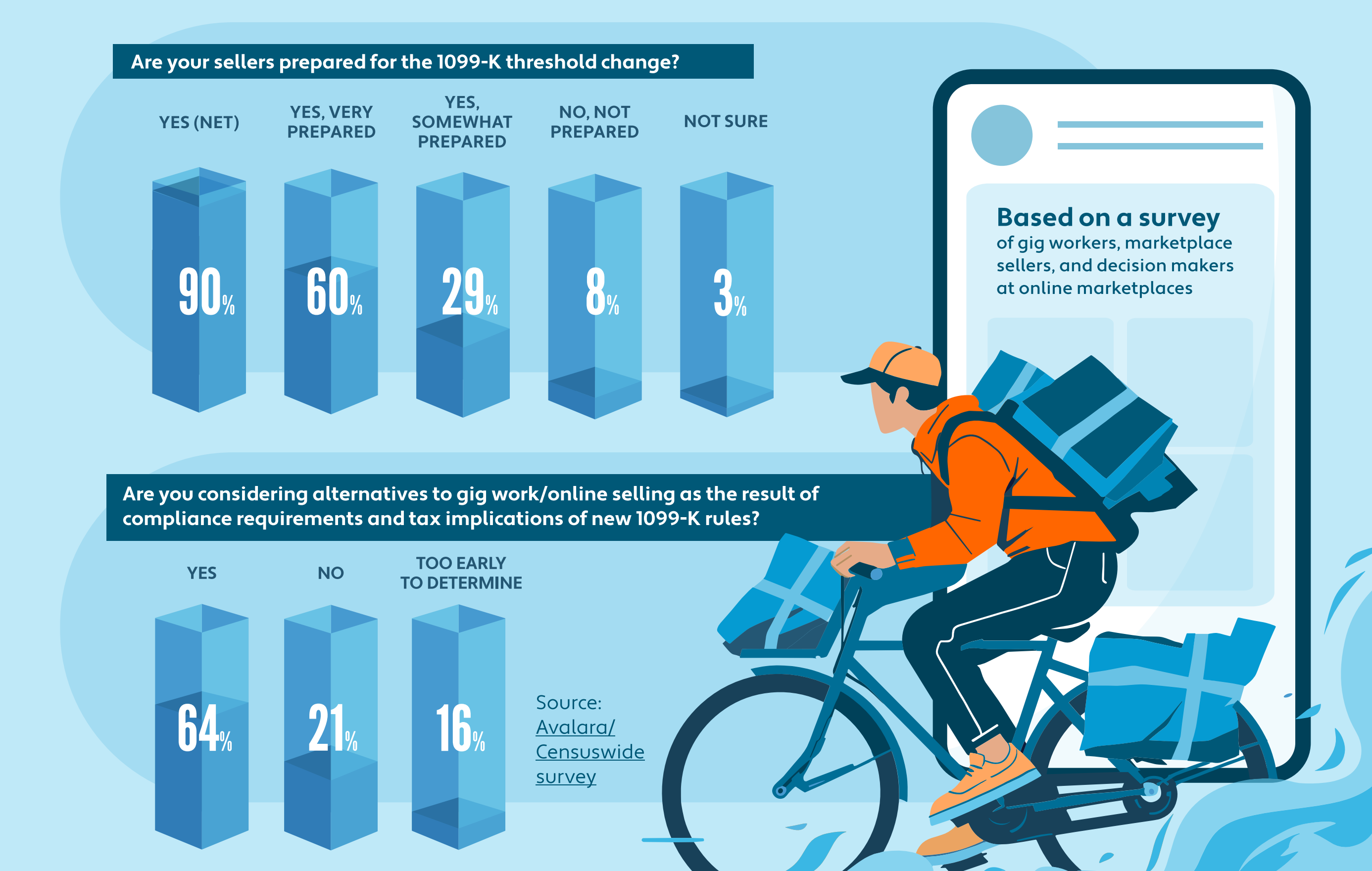
The threshold change was supposed to take effect with the 2022 tax year, but due to the scale of the change and the number of businesses it would affect, the IRS pushed it back a year. In late 2023, the IRS delayed the effective date a second time. It said then that it would phase in the implementation of the $600 reporting threshold, starting with a $5,000 threshold for tax year 2024.

Then, crickets.

On November 26, 2024, the IRS announced it will phase in the lower reporting threshold for third-party settlement organizations (TPSOs), also known as payment apps and online marketplaces (think Airbnb, eBay, Etsy, PayPal, Venmo). TPSOs will be required to report transactions when the amount of total payments for those transactions is:

- More than $5,000 in 2024
- More than $2,500 in 2025
- More than $600 in calendar year 2026 and after

Congress may still push to bring the threshold back to $20,000/200 transactions. But for now, marketplaces, payment apps, and others affected by the Form 1099 threshold change should comply with the $5,000 threshold … and be nimble.



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Sales and use tax changes affect procure-to-pay too

Agility can also help businesses handle procure-to-pay processes, which can challenge any company.

When buying taxable goods and services, retailers either need to pay the vendor the tax due or ensure the vendor has an up-to-date exemption certificate. Vendors are required to collect certificates at the time of sale, and tax authorities can be sticklers on this point. In 2023, a hospital that failed to give its vendors resale certificates when purchasing meals for resale ended up paying roughly $1 million in sales tax on the transactions. Had the hospital furnished the proper documentation at the time of sale, it would not have been liable for the tax.

It's a cautionary tale that can affect businesses in any industry, including retailers and marketplaces.

Retail businesses also need to self-assess and pay any consumer use tax due. Several different scenarios can trigger use tax liability. For example:

- The vendor may lack nexus and not collect sales tax.
- The vendor may undercollect sales tax.
- The buyer may consume inventory purchased tax free.
- The buyer may move inventory to a different jurisdiction.

"Gotcha!" triggers abound with use tax, making it a focal point for auditors and a common source of negative audit findings. Fortunately, tax automation software can help.

Avalara AvaTax for Accounts Payable identifies the overpayment and underpayment of sales tax on purchases and applies tax based on jurisdiction, taxability, and special rules. It also reconciles transactions and applies the use tax owed on returns automatically, reducing the likelihood of costly errors.

This report highlights just some of the sales and use tax changes coming to the retail industry in 2025. There will be more; there always are.

It's difficult for retailers to meet the demands of sales tax compliance without relying on automation and other technology. There are too many nuances, too frequent changes. And frankly, wouldn't you rather be spending your time focusing on something else?

How Avalara can help

Avalara can help you account for sales and use tax changes and improve tax compliance for your business. Learn more about our automated solutions for calculating tax rates, preparing returns, and managing documents.

EXPLORE SOLUTIONS

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In a way, the digital era is contributing to an eroding sales tax base because only about half of states currently tax digital products or streaming services. This is bound to change, eventually. States will need the revenue. But when will it change? What will change look like? And how will it affect software tax compliance?

What's ahead:

Businesses and tax jurisdictions jump aboard the AI train

What the numbers tell us about the software industry in 2025

Will there be new taxes on digital goods and services in 2025?

Should states tax B2B sales of digital goods and services?

The rise of the digital services tax

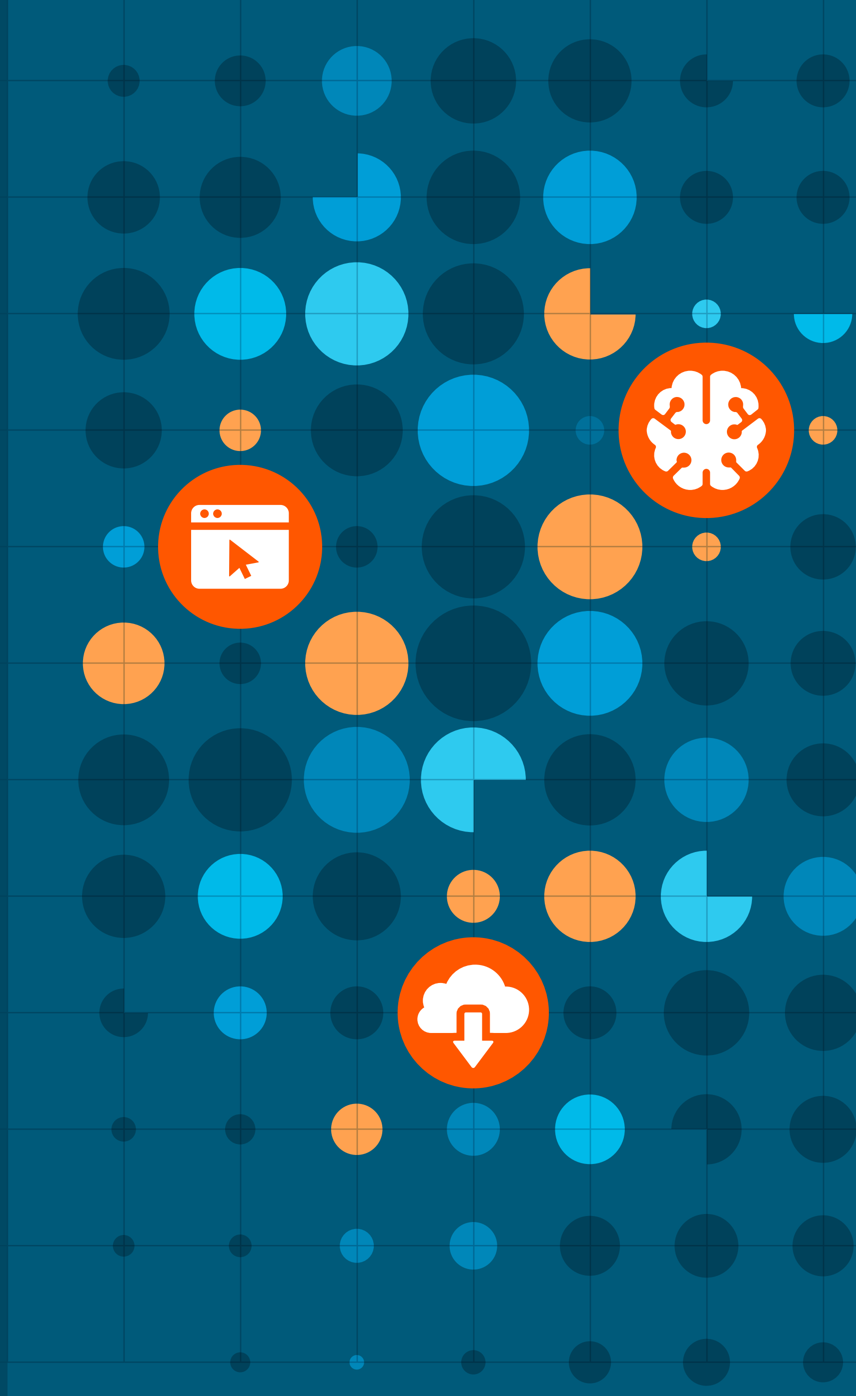
Will digital ad taxes be replaced by link taxes?

The challenge of sourcing digital goods: Multiple taxation and nowhere sales

So, how do you source sales of digital goods?

Tax breaks for software companies: New sales tax exemptions

Property tax considerations for software companies



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Businesses and tax jurisdictions jump aboard the AI train

We can't talk about the software industry today without discussing generative artificial intelligence (AI), so let's just start there. OK?

Like just about every other industry, software businesses are giddy with the promise of generative AI. If the promises prove true, gen AI will help software companies assist customers, **boost developer productivity** (perhaps as much as 45%!), forecast demand, improve marketing, increase profitability, and more.

So, software businesses are investing in machine learning technology. A lot. Global enterprises spent approximately **$15 billion** on gen AI solutions in 2023 alone, representing about 2% of the global enterprise software market. McKinsey expects gen AI to impact almost all software categories. "Gen AI will drive significant growth in the software space," it predicts. "By 2027, spending on the technology could reach between $175 billion and $250 billion."

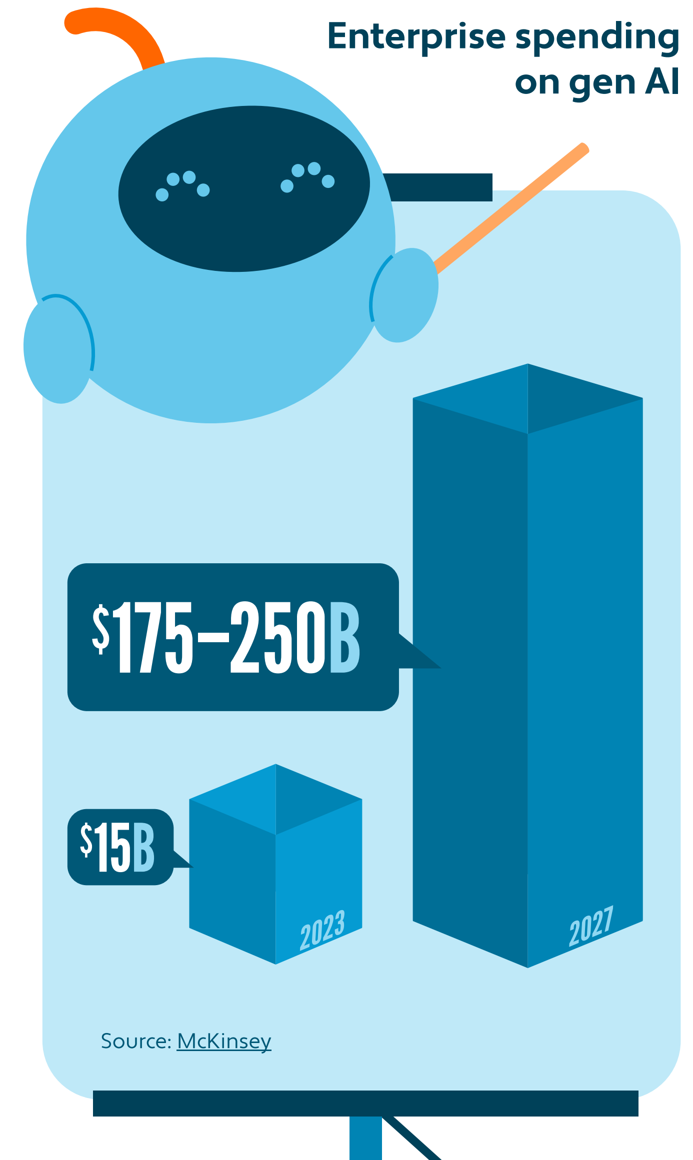
Opportunity abounds for businesses – and tax jurisdictions – prepared to jump on it. The new technology could eventually spark new tax policies too.

David Lingerfelt, Senior Director of Indirect Tax at Avalara, hasn't heard any talk of taxing AI yet. "2024 was a fairly quiet year for states in terms of cutting-edge tax changes." He expects that ultimately, states will treat AI like software, for tax purposes. "States that tax software will likely tax sales of AI."

Tax policies often lag behind developments in technology. Most state tax authorities haven't established metaverse or blockchain tax laws either, and those hogged headlines long before ChatGPT debuted at the end of 2022.

Lingerfelt expects state and tax officials to circle back to metaverse tax laws and blockchain tax compliance once the brouhaha over gen AI recedes. In the meantime, states looking to update sales tax policies affecting the software industry could follow recommendations offered by the **Multistate Tax Commission** (MTC) or **Streamlined Sales Tax** (SST); key areas of focus for these organizations include sales tax sourcing requirements and whether to tax or exempt business-to-business (B2B) transactions.

We'll get into these fun topics and others. But first, let's see what the numbers have to say about the software industry.



What the numbers tell us about the software industry in 2025

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Digital goods and services

31

states + D.C.

Source: Avalara

Software as a service (SaaS)

20

states

Source: Avalara

Digital advertising

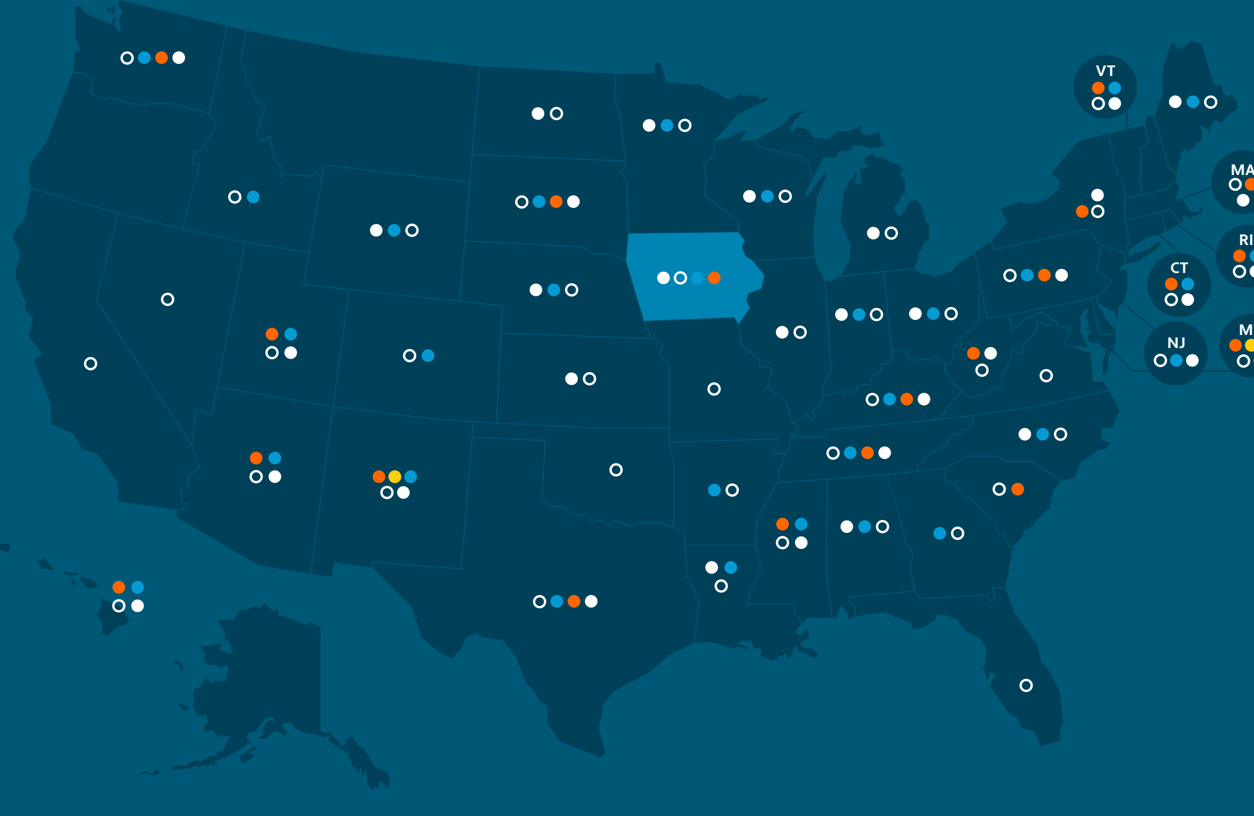
2

states

Source: Avalara

States subject to software sales tax

as of October 2024



- Digital goods and services
- Software as a service (SaaS)
- Digital advertising

CANNED SOFTWARE

- Delivered through physical media
- Delivered electronically

Iowa is the only state that has a broad sales tax exemption

for business purchases of digital products and services

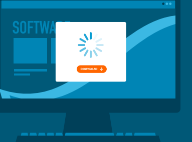
Source: Multistate Tax Commission

CANNED SOFTWARE

Delivered through physical media

states

Delivered electronically



states

Source: Avalara

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Will there be new taxes on digital goods and services in 2025?

Tax experts from the Tax Foundation and the Institute on Taxation and Economic Policy (ITEP) generally favor a broad sales tax base, which includes taxation of digital services and goods (e.g., streamed music and video, ebooks, digital images). Many politicians do too – but expanding the tax base can be a hard sell.

In 2024, it took Louisiana lawmakers three separate legislative sessions to agree to tax select digital products and services. Starting January 1, 2025, Louisiana sales and use tax will apply to digital audiovisual works, digital audio works, digital books, digital codes, digital applications and games, and digital periodicals and discussion forums.

Several states attempted to implement digital products tax changes in 2024.

- Virginia Governor Glenn Youngkin introduced a plan to tax digital goods and services starting January 1, 2025, but the Legislature didn't approve it.
- The Kansas Legislature made a move to tax digital property and subscription services and to allow for a reduced rate in certain circumstances, but the bill died in committee.
- Massachusetts and New York both considered data excise taxes but ultimately chose not to pursue them.
- The DC Tax Revision Commission is exploring a data excise tax and a tax on digital ads and services; progress is slow.

"Most state tax structures have hardly changed from when they were first enacted," explains Scott Peterson, VP of Government Relations at Avalara. "When legislators and governors talk about expanding the sales tax to services and digital goods, it's almost always in conjunction with reducing property or income taxes. The expansion of the sales tax almost always produces less tax revenue than the wanted reductions."

Still, digital goods are being added to the tax base in a growing number of states. Select digital goods and services are subject to sales and use tax in approximately 31 states and Washington, D.C. Georgia started taxing digital products on January 1, 2024; Vermont began taxing software as a service on July 1, 2024; and as noted, Louisiana will tax digital products beginning January 1, 2025.

Moreover, both Texas and Michigan clarified the taxation of digital goods.

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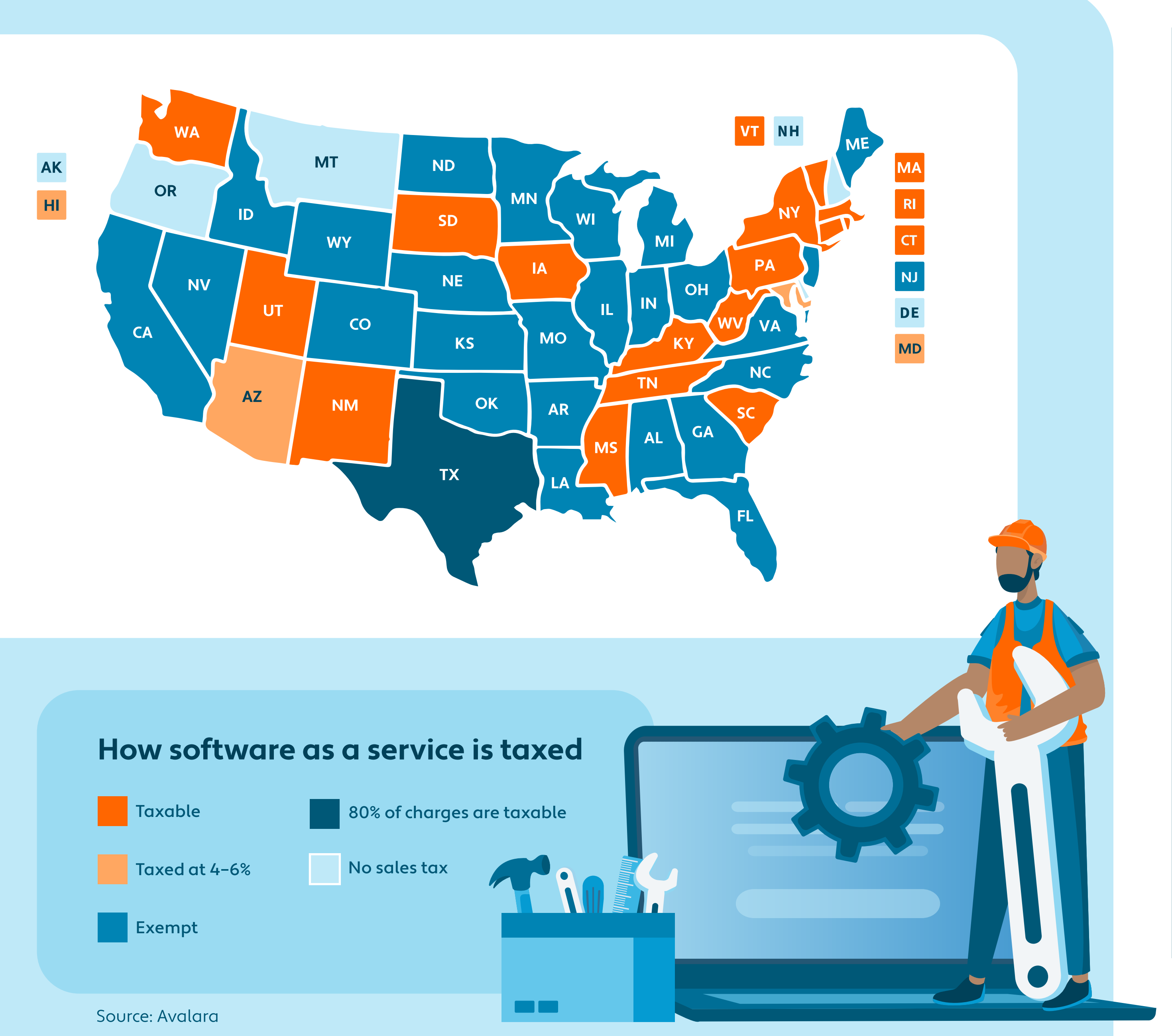

Source: Avalara

A **private letter ruling** published by the Texas Comptroller in July 2024 explains that a company's charges for a license to install code to track user interactions on a customer's website are taxable sales of software. Monthly subscription fees and fees based on the amount of user sessions are also taxable charges in Texas because they're considered to be data processing.

Per **guidance on the taxability of non-fungible tokens** (NFTs) published in August 2024 by the Michigan Department of Treasury, Michigan does *not* tax digital goods or NFTs representing digital goods (e.g., a digital image or sound). However, "if the NFT represents an ownership interest in tangible personal property," the NFT is subject to Michigan sales tax.

Good to know.

There will likely be more clarifications like these in 2025. Whether any states actually extend their sales and use tax to any digital products or services in 2025 remains to be seen. "Each legislative cycle there seems to be momentum around expanding the tax base into digital goods and services," observes David Lingerfelt. "The success of these efforts is largely dependent on the state of a state's budget and general political climate." Learn more about the state of state budgets in the **sales tax section** of this report.

Should states tax B2B sales of digital goods and services?

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One issue that proved a sticking point for Virginia in 2024 was whether to tax or exempt business-to-business (B2B) sales of digital services and goods. The governor and House wanted to tax business-to-consumer (B2C) sales of computer-related services, data storage, software application services, streaming services, and website hosting, but provide an exemption for B2B sales. The Senate supported taxing B2B as well as B2C transactions. In the end, they couldn't get past the stalemate.

Virginia isn't the only state to grapple with this issue, or to take heat for considering a tax on B2B digital goods and services. The Multistate Tax Commission (MTC), which has been studying state sales tax policies on digital products for years and is producing a white paper on the topic, has received similar feedback.

The debate over taxing B2B transactions

Some state tax experts are opposed to any kind of tax pyramiding (which is what happens when business inputs are taxed), while others take a more nuanced approach.

During an MTC panel on business inputs in July 2023, Karl Frieden of the Council on State Taxation (COST) recommended states limit taxes on business inputs "and focus sales tax as broadly as necessary on the final consumer." Panelist Michael Ettlinger of ITEP agreed taxing business inputs isn't ideal but also held that "taxation of business inputs is not as bad in practice as it is in theory; it's an important part of the state revenue picture."

Clearly, there's no one right way to tax digital products. But if there was, Iowa may come close to it.

Iowa taxes specified digital products, software, and related services but provides an exemption for specified digital products sold to a commercial enterprise for use exclusively by the commercial enterprise. Iowa also exempts specified digital products sold to a "non-end user" or to entities exempt from paying sales and use tax.

Yet Iowa is an outlier. Maryland, New Jersey, North Carolina, and Washington provide limited exemptions for business purchases of digital goods or software, and Connecticut has a reduced sales tax rate for certain business purchases of digital products. Louisiana specifies that software, information services, and digital products purchased or licensed exclusively for business use are sales tax exempt when certain conditions are met. However, Iowa is the only state that offers a broad sales tax exemption for business purchases of digital products and services.

There's no one-size-fits-all solution to taxing businesses' digital sales. Nevertheless, the Tax Foundation believes "other states would do well to follow Iowa's example." It strongly supports exempting purchases for business use.

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But providing a B2B sales tax exemption for business inputs wouldn't necessarily eliminate compliance complexity.

"While B2B exemptions offer clear advantages, states contemplating their adoption should also focus on simplifying the administrative processes involved," says Stephen Bradshaw, State and Local Tax Partner at Bennett Thrasher. "For example, New Jersey grants a B2B exemption for downloaded software but requires sellers to obtain an exempt use certificate (Form ST-4) from buyers. Streamlining these procedures – perhaps by adopting a model similar to Maryland's, which only necessitates proof of B2B usage – could improve both accessibility and compliance."

Expect to hear more about taxing digital goods and services – and the pros and cons of exempting business inputs – in 2025. Businesses buy *a lot* of digital goods and services. Globally, **spending on digital transformation** is on track to reach $3.9 trillion by 2027. That could generate an awful lot of sales tax revenue. Or not.

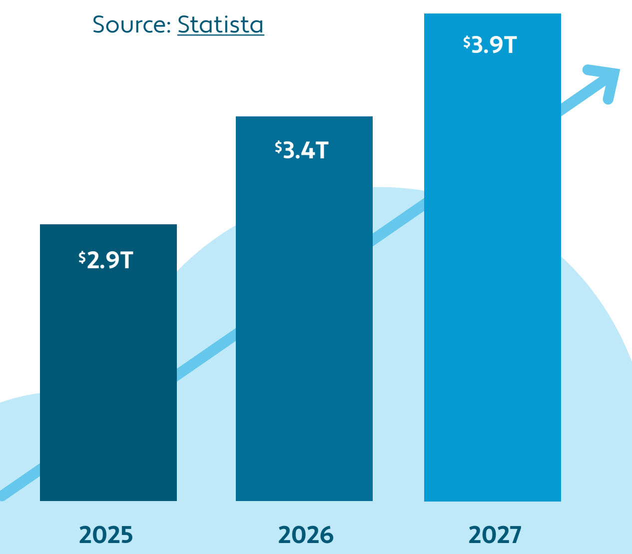
A tax on digital services could also fill governments' pockets.

STEPHEN BRADSHAW
State and Local Tax Partner
at Bennett Thrasher

> **While B2B exemptions offer clear advantages, states contemplating their adoption should also focus on simplifying the administrative processes involved.**
>
> **Streamlining these procedures ... could improve both accessibility and compliance.**

Spending on digital transformation is EXPECTED TO REACH $3.9T by 2027

Source: Statista



By 2030, **the global e-learning market may reach $543B**

Source: Persuasion Nation

By 2027, **the global advertising market may reach $871B**

Source: Sonary

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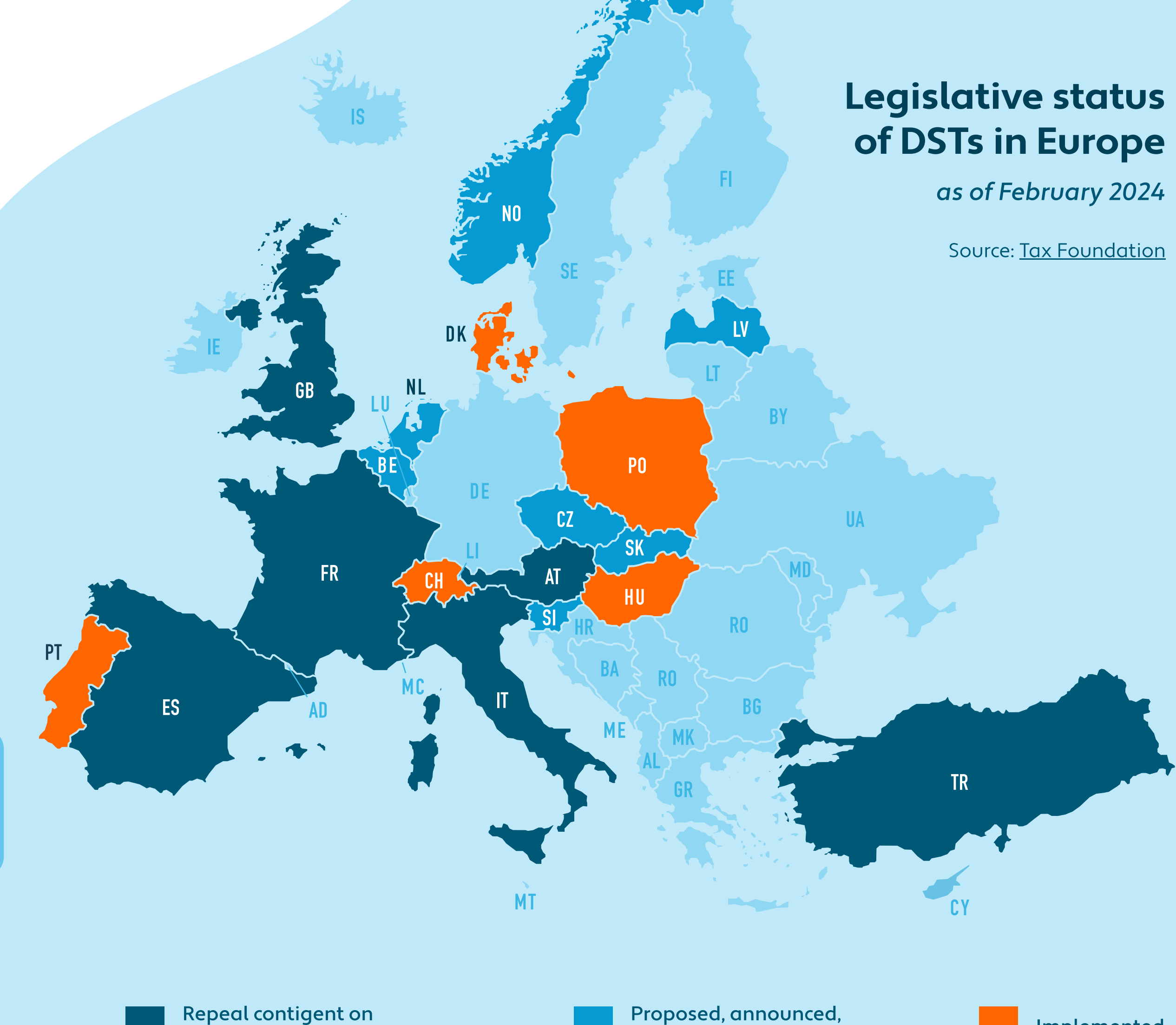
The rise of the digital services tax

Although controversial, a growing number of countries participating in the Organisation for Economic Co-operation and Development (OECD) have implemented, announced, or proposed a digital services tax (DST).

The OECD is working on a two-pillar plan to modernize the international tax system: Pillar One would change where the most profitable multinational digital companies pay taxes; Pillar Two would establish a global minimum tax. DSTs, which were meant to be interim measures, are proliferating as countries haggle over the details of the plan.



Legislative status of DSTs in Europe

as of February 2024

Source: Tax Foundation

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The Canada digital services tax is finally taking effect

The Canadian government put forward a 3% DST in the fall of 2020 and provided more details in its Budget 2021. Then the waiting began.

"Canada temporarily paused implementation of its DST to allow the OECD to build a framework for ensuring large profit global corporations pay their fair share of tax," explains David Lingerfelt. "When Pillar One of the OECD's plan failed to go into effect in 2023, Canada moved forward with its DST. I believe additional countries will implement DSTs because the OECD has been unsuccessful negotiating consensus with member countries on how to shift tax revenues from home countries to where the global corporation has significant consumer interaction."

In 2024, Canada's Digital Services Tax Act "received royal assent." It came into force on June 28, 2024. The 2024 calendar year is the first year of application of the DST, and it applies to taxable Canadian digital services revenue earned since January 1, 2022.

This is a tax on big businesses: It applies to taxpayers with at least €750 million in total revenue from all sources in a particular calendar year and more than $20 million CAD in Canadian in-scope revenue. There are four categories of in-scope revenue:

- Online advertising services revenue
- Online marketplace services revenue
- Social media services revenue
- User data revenue

Domestic and foreign businesses that meet the threshold for the DST must apply to register by January 31, 2025. The Canada Revenue Agency will publish information about how to file a DST return in early 2025.

The U.S. is opposed to digital services taxes in general and Canada's DST in particular. However, at least one state has adopted a tax on digital advertising services.

DAVID LINGERFELT
Senior Director of
Indirect Tax at Avalara

" I believe additional countries will implement DSTs

because the OECD has been unsuccessful negotiating consensus with member countries on how to shift tax revenues from home countries to where the global corporation has significant consumer interaction.

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Will digital ad taxes be replaced by link taxes?

With the exception of New Mexico, where digital advertising is subject to gross receipts tax, Maryland is the only state to tax digital advertising services. It may not do so for long. The Maryland digital advertising services tax has been repeatedly challenged in court and though the state won another victory in July 2024, several more lawsuits are still in play. Attorneys representing the plaintiffs are confident Maryland courts will eventually overturn the law.

If Maryland's digital advertising tax is found to be unconstitutional, the state would have to return the tax it's collected with interest. "That would be an administrative headache for the state," says Lingerfelt. "It would also significantly impact the state's budget. The digital advertising tax was tied to funding the state's public education. The state would be forced to act quickly to increase taxes using less controversial approaches."

Digital advertising taxes have been floated in several other states, including Massachusetts, Nebraska, New York, Tennessee, and Washington, D.C. None have been approved. The states are probably waiting to see what happens in Maryland.

Interestingly, California came quite close to enacting a tax on digital ads (AB 886) and/ or data extraction (SB 1327) in 2024. Both bills were ultimately dropped after Google agreed to pay what's often called a "link tax." It will pay California more than $172.5 million over five years for the right to link to news content. The revenue is to fund journalism in the state.

Link taxes seem to be gaining traction worldwide. The United States Senate started looking into a federal link tax in 2023 "to save local journalism," though nothing's come of it. Efforts in Australia, Canada, and some other countries are seeing more success.

"Taxes have long been used as a public policy tool to incentivize or discourage industries and behaviors," observes Lingerfelt. "In that regard, link taxes are not new. There are serious consequences with link taxes. Online platforms could retaliate by refusing to do business in a given jurisdiction. And in the long run, link taxes could fuel consolidation in the newspaper industry, limiting access to diverse news and information."

Canada's Online News Act

- Creates a bargaining framework to ensure online platforms compensate news businesses fairly
- Encourages platforms to reach voluntary commercial agreements with news businesses
- Establishes a mandatory mediated bargaining process for when a platform and news business cannot reach a fair agreement

Source: Government of Canada

The challenge of sourcing digital goods: Multiple taxation and nowhere sales

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One reason the Maryland digital advertising services tax is under fire is what the Tax Foundation calls its "**suspect sourcing rules**."

"Figuring out the best way to source sales of digital goods is difficult," says David Lingerfelt. "States haven't made much progress on this issue. Businesses still struggle to appropriately source their digital sales."

A lack of uniformity in sourcing rules might result in "nowhere sales" or "sales subject to multiple taxation," observed a **Multistate Tax Commission Subcommittee** in 2021. Let's pull on those threads.

Multiple taxation

Due to the nature of digital goods, multiple jurisdictions could conceivably tax the same transaction. After all, a resident of Illinois can purchase and download a digital book while vacationing in Florida. A resident of Texas may stream a movie from a hotel in New York City. Which jurisdictions should get the tax: Illinois or Florida? Texas or New York?

Figuring out how to source such transactions is even more complicated when the buyer is a business and the digital products or services are used by dozens, hundreds, or thousands of employees nationwide. Is every state where an employee is located entitled to the tax, or at least some of it? If not, who gets first dibs?

"Digital products can be accessed from anywhere in the world," Lingerfelt points out. "Sellers are not going to monitor and store the IP address location of where the digital product or software was first made available. In practice, sellers of software and digital products will maintain an address for their customers in the ordinary course of business. This is where they will source the sale. In some instances, the address may be nothing but the ZIP code the customer entered for billing. ZIP codes are not precise for tax calculation, but they are practical."

DAVID LINGERFELT
Senior Director of Indirect Tax at Avalara

Digital products can be accessed from anywhere in the world.

Sellers are not going to monitor and store the IP address location of where the digital product or software was first made available.

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Nowhere sales

Nowhere sales represent the other side of the equation. If digital goods and services are used everywhere, there's a risk they'll be taxed nowhere. A state could assume a business is paying tax to a different jurisdiction, which may (or may not) actually be the case.

"Nowhere sales tax is possible because the location of the sale might differ from where the product is used," explains Scott Peterson. "The use tax is intended to kick in when that happens."

The fact that sellers often don't obtain a complete address for digital transactions further complicates sourcing. It's difficult to figure out which jurisdiction is entitled to the tax if the buyer doesn't provide a complete address, and they're often not required to when no tangible goods are exchanged.

"This creates rate issues that are often discovered only during an audit," Peterson points out. "Colorado and Nebraska both say that using a five-digit ZIP code in lieu of a street address will result in an audit assessment at the highest local rate applicable in the five-digit ZIP code area."

SCOTT PETERSON
VP of Government Relations at Avalara

"[Not obtaining a buyer's complete address] creates rate issues that are often discovered only during an audit.

Colorado and Nebraska both say that using a five-digit ZIP code in lieu of a street address will result in an audit assessment at the highest local rate applicable in the five-digit ZIP code area.

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So, how do you source sales of digital goods?

The Tax Foundation recommends sourcing sales of digital goods and services to wherever the product or service is first used. "This approach cuts down substantially on complexity for taxpayers and tax collectors alike, and squares with sourcing rules for tangible goods."

The Streamlined Sales and Use Tax Governing Board has been working to craft best practices for sourcing digital transactions when the buyer's complete address isn't obtained. To remain in compliance, SST member states like Washington must adhere to the standard sourcing rule hierarchy set by the Streamlined Sales and Use Tax Agreement (SSUTA).

In July 2024, SST approved final amendments to SSUTA sourcing rules for digital sales. It gives member states that have local sales taxes two options.

- If the *five-digit ZIP code* area includes more than one tax rate, the state *may* assign the highest, lowest, or blended rate in the five-digit ZIP code area.
- If the *nine-digit ZIP code* area includes more than one tax rate, the state *must* assign the lowest combined tax rate imposed in a nine-digit ZIP code area.

Each choice comes with consequences. For example, if 1) a state assigns the highest rate in a five-digit ZIP code area, 2) the seller requested address information from the buyer, and 3) the buyer failed to provide it, then the purchaser is *not* entitled to a refund for the difference between the tax collected and the tax that would have been collected if the requested information had been provided.

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Tennessee adopts destination sourcing for digital products and software

Tennessee, which is an associate member of SST, has **adopted most of the SST sourcing provisions**. As of July 1, 2024, the Volunteer State applies destination sourcing rules for interstate sales of services performed on tangible personal property and computer software, as well as leased property such as licensed computer software or specified digital products.

For the leased property, recurring periodic payments are no longer sourced to Tennessee if the primary property location moves out of Tennessee during the lease period; they become exempt interstate sales. Likewise, if the primary property location is moved into Tennessee from out of state, subsequent payments must be sourced to Tennessee and taxed accordingly. The primary property location is the address the lessee gave the lessor for the property.

British Columbia clarifies sourcing of SaaS and IaaS

British Columbia has clarified how its **provincial sales tax** (PST) applies to software as a service (SaaS) and infrastructure as a service (IaaS). Like tax authorities in the U.S., Canadian tax authorities have been grappling with sourcing issues.

B.C. PST applies whenever software is purchased for use on an electronic device ordinarily situated in B.C. This holds true whether the buyer is a B.C. resident or nonresident, and whether the purchase took place in or outside of B.C. Therefore, anyone who's liable for the tax and isn't charged PST at the time of purchase must self-assess and pay the tax due.

When software is purchased for use in multiple jurisdictions, the buyer is required to pay "a proportional amount of PST" if the software is used in the course of business on both an electronic device ordinarily situated in B.C. *and* a device ordinarily situated outside of B.C. This is true whether the software is purchased in B.C. or outside of B.C.

David Lingerfelt says British Columbia's approach to sourcing software is not new. "Essentially, British Columbia has tweaked 'the first made-for-transmission' approach to sourcing software to take into account where the user or device is 'normally situated.' Both approaches miss the mark. In reality, the seller collects the minimally required information necessary to bill the customer. The billing address may or may not represent where the device or user is normally situated."

Though British Columbia announced this policy in the spring of 2024, it's enforcing it retroactive to April 1, 2023. This is one reason why it pays to be proactive and automate tax collection and remittance. Implementing **tax automation for the software industry** can help software and SaaS businesses calculate rates for domestic and international sales based on regularly updated, complex taxability rules and exemptions.

DAVID LINGERFELT
Senior Director of Indirect Tax at Avalara

In reality, the seller collects the minimally required information necessary to bill the customer.

The billing address may or may not represent where the device or user is normally situated.

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Tax breaks for software companies: New sales tax exemptions

In 2024, several states considered or adopted new sales tax exemptions that may improve the bottom line for businesses in the software industry. There's fresh information out of Illinois, Kentucky, Oklahoma, and Texas.

Bear in mind that sales tax exemptions don't give you a free pass on tax liability. "SaaS is exempt in Wisconsin," says Myles Metzger, a Use Tax Product Solution Consultant at Avalara, "but under audit, if the SaaS software contains a messaging and/or email notification component and the value of this is not separately stated on the contract or invoice, Wisconsin will likely attempt to tax the entire purchase as a taxable telecommunication service."

In his experience, state audits are getting more aggressive in trying to broaden their tax base.

MYLES METZGER
Use Tax Product Solution Consultant at Avalara

> **SaaS is exempt in Wisconsin, but under audit, if the SaaS software contains a messaging and/or email notification component and the value of this is not separately stated on the contract or invoice,**
>
> **Wisconsin will likely attempt to tax the entire purchase as a taxable telecommunication service.**

Illinois codifies exemption for software

The Illinois Department of Revenue has long used a five-part test to determine whether software licenses are subject to tax or exempt. With the enactment of HB 4951 in June 2024, Illinois has codified the department's policies.

The sale of a license for computer software is not taxable provided the conditions outlined in Section 130.1935 are met.

This exemption also applies to the Chicago Lease Transaction Tax and any other local tax adopted prior to January 1, 2023.

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Kentucky exempts data center equipment

A sales and use **tax exemption for data center equipment** took effect in Kentucky on July 15, 2024. Equipment eligible for the exemption includes but isn't limited to computer software, connections, routers, and servers.

To qualify for the exemption, the data center must be located in an area with a population of 500,000 or greater, meet certain criteria, and be approved by the Kentucky Economic Development Finance Authority.

Oklahoma exempts digital asset mining

A temporary **sales tax exemption for digital asset mining** took effect in Oklahoma on November 1, 2024. "Digital assets" are defined as "a type of virtual currency that utilizes blockchain technology and that (1) can be digitally traded between users, or (2) can be converted or exchanged for legal tender."

The exemption applies to oodles of machinery and equipment used to mine digital assets, including but not limited to cabling, computers, servers, and software. It's set to expire on December 31, 2029.

Texas rules online admissions tests are exempt

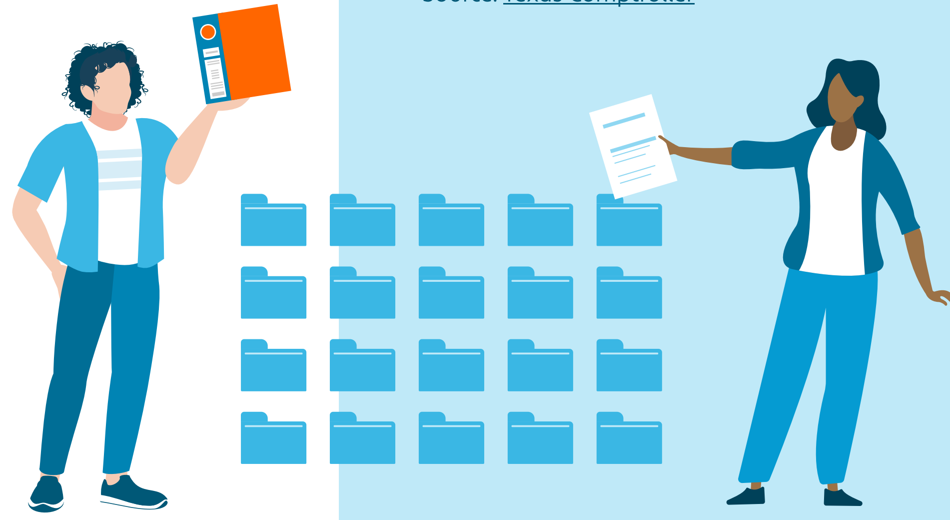
In a private letter ruling, the **Texas Comptroller** said a company's computer-based, secondary education admissions testing services are *not* subject to Texas sales tax. This is a bit surprising because Texas sales tax generally applies to data processing services, and the services in question include some data processing.

According to the Comptroller, "these activities are performed to facilitate the taxpayer's testing service that provides an assessment of a student's readiness for college," and testing a student's readiness for college **isn't a taxable service**. So there you have it.

Examples of data processing services in Texas

- Check preparation
- Accounts payable or receivable preparation
- Web hosting, website creation and maintenance
- Data storage, including offsite backup of electronic files
- Conversion of data from one type of medium to another (e.g., converting paper documents or videotapes to digital files)

Source: Texas Comptroller



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Property tax considerations for software companies

There's a tax on real property in every state, though it may apply only locally. And 37 states (plus Washington, D.C.) assess a tax on business personal property. Like any other industry, software companies with significant business in these states must comply with real and personal property tax requirements.

Software companies may not have as much heavy equipment as manufacturers or other industries, but that doesn't make personal property tax compliance any less complex. The desktop and laptop computers, office equipment, and servers owned by software companies are all considered personal property and may be subject to tax. Fiber backhaul or cellular service businesses may also be liable for property tax for the fiber to a cell tower or even the fiber strands running up a tower or on leased equipment — this is true in some states even where business personal property is not generally taxed.

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Determining the value of equipment like computers and servers can be particularly challenging because they depreciate quickly. Jurisdictions have different "floors" for different properties; after a certain number of years, the property is typically valued at 10% or 15% of its original value forever. "Yet some computer software can be worth literally nothing after a time," explains Carl Hoemke, GM of Property Tax at Avalara. "It's important to review the assessed value of your equipment, and if it exceeds the fair market value, you can contest the assessment. Avalara helps businesses with this."

Determining software's taxability is also complex. For example, Washington state provides an exemption for custom computer software but not embedded software; canned software is subject to personal property tax, but modifications to canned software are exempt.

Keeping up with property tax changes adds to its complexity. "You can't assume that what happened last year will be the same this year," warns Hoemke. "Exemptions change. Definitions change. People misinterpret statutes. The systemic impact of a change may not be what the legislatures intended. For example, Mississippi exempted broadband a few years back, and now the application of the law is being disputed in numerous counties across the state."

CARL HOEMKE
General Manager of
Property Tax at Avalara

> **You can't assume that what happened last year will be the same this year.**
>
> **Exemptions change. Definitions change. People misinterpret statutes. The systemic impact of a change may not be what the legislatures intended.**

These are just some of the main issues affecting tax compliance for software industry facility owners; we wish we had the space to cover them all, but there are just too many.

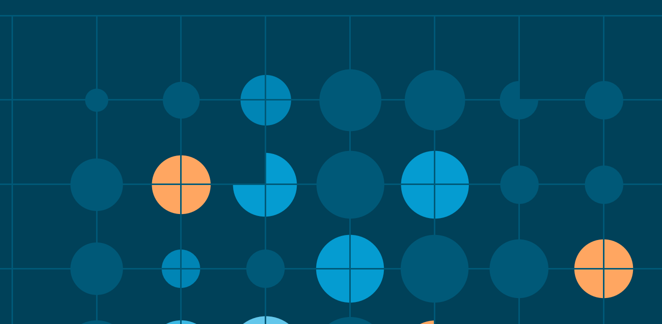
Staying compliant with these and other digital product tax changes and software-as-a-service tax rules requires a lot of resources. Tax automation for the software industry can help.

How Avalara can help

Avalara can help you account for tax changes and improve tax compliance for your business. Learn more about Avalara's cloud-native tax compliance solution for software and SaaS businesses, including tax rate calculation, returns preparation, and exemption certificate management.

EXPLORE SOLUTIONS

Up next: Manufacturing >



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Manufacturing

Following the high-tech revolution of the last few years, 2025 will likely see tax changes, exemptions, and incentives fuel different types of industry growth. Manufacturers are facing new developments (and challenges) in electric vehicle manufacturing, experiencing stricter scrutiny concerning exemption certificate management, and struggling with personal property tax compliance. Let's dive deeper into what we can expect over the next year.

What's ahead:

A new tax road map for the manufacturing industry

What the numbers tell us about the manufacturing industry in 2025

New exemptions for the manufacturing industry

Tax credits and electric vehicles

Business personal property tax challenges

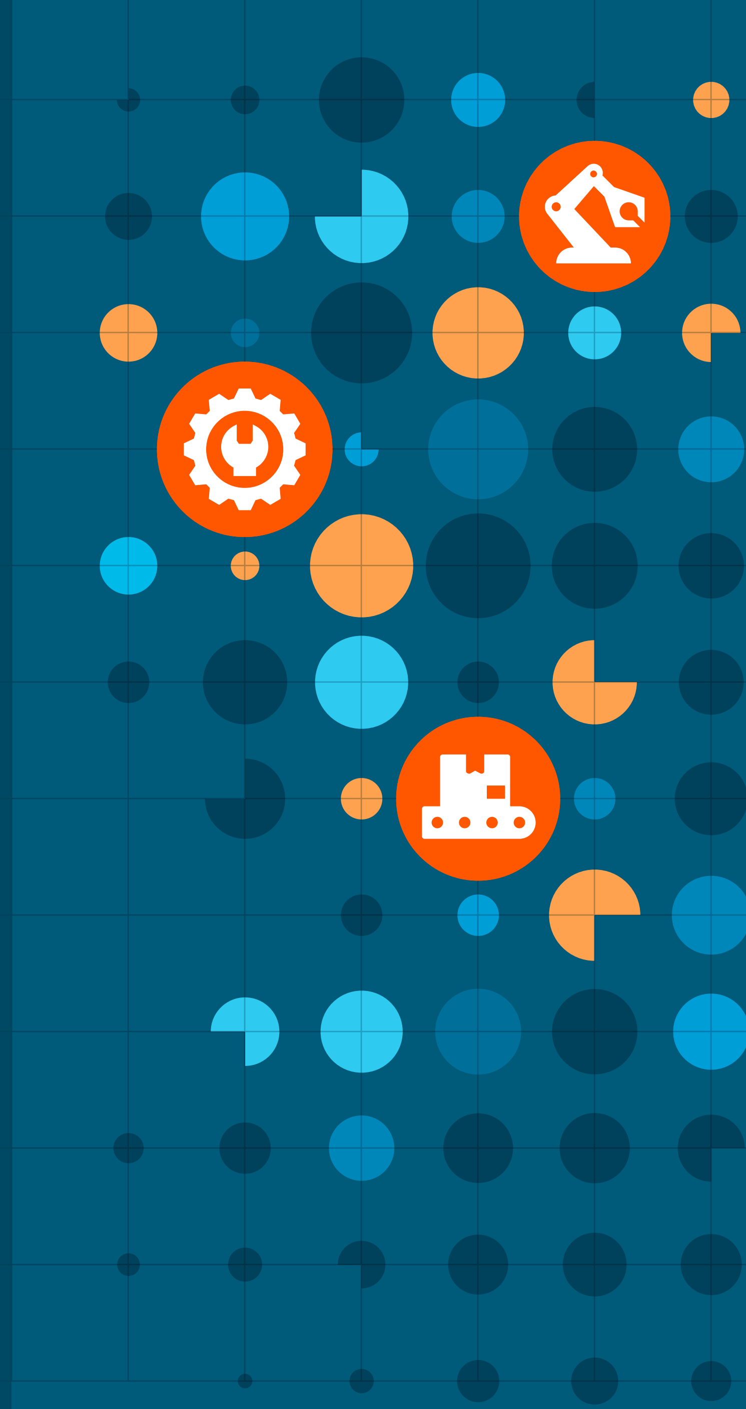
Tech trends and taxability trouble

Retail delivery fees and you

Economic nexus for manufacturers in 2025

Procure-to-pay and compliance

Consumer use tax



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A new tax road map for the manufacturing industry

Like other industries, manufacturing has been shaken by supply chain disruptions, staffing shortages, a changing workforce, and a scramble to integrate technology into day-to-day operations. These and other conditions can affect tax compliance.

Businesses are settling into Industry 4.0: the digital transformation of the manufacturing industry. As 2025 unfolds, they'll likely face tax compliance challenges, including how new tax incentives influence where they build operations, what states' evolving policies on personal property taxability mean for their finance teams, and how to avoid penalties and fees when state auditors show up.

As manufacturers make their way through 2025, it's increasingly important to stay abreast of legislative changes. States are considering incentivizing data mining centers and offering electric vehicle credits. They're redefining what falls under the umbrella of "manufacturing" when it comes to tax exemptions and adopting retail delivery fees. All while intensifying audit scrutiny and paying closer attention to manufacturers' exemption certificate management.

Keeping up with sales and use tax trends and policies, plus knowing what they mean for your business can be a full-time job. It certainly is for us – and luckily for you, we love it. To help you navigate the year ahead, we've rounded up some of the key tax trends and changes affecting the manufacturing industry in 2025. Let's start by looking at some stats.

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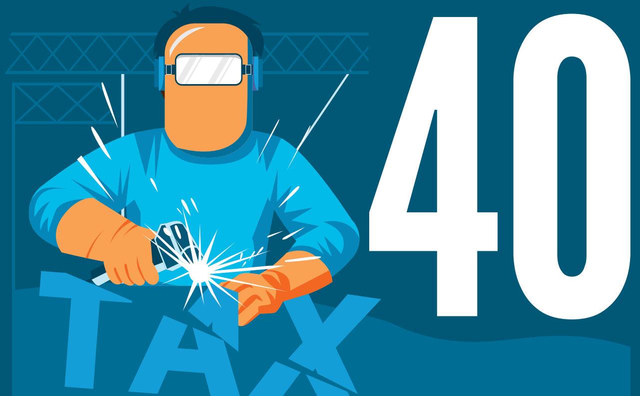
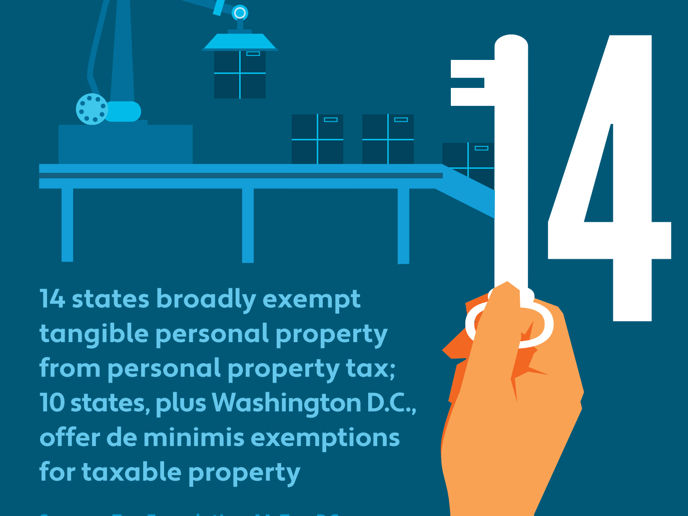
What the numbers tell us about the manufacturing industry in 2025

40 states, plus Puerto Rico and Washington, D.C., include exempt sales in their economic nexus threshold

Source: Avalara



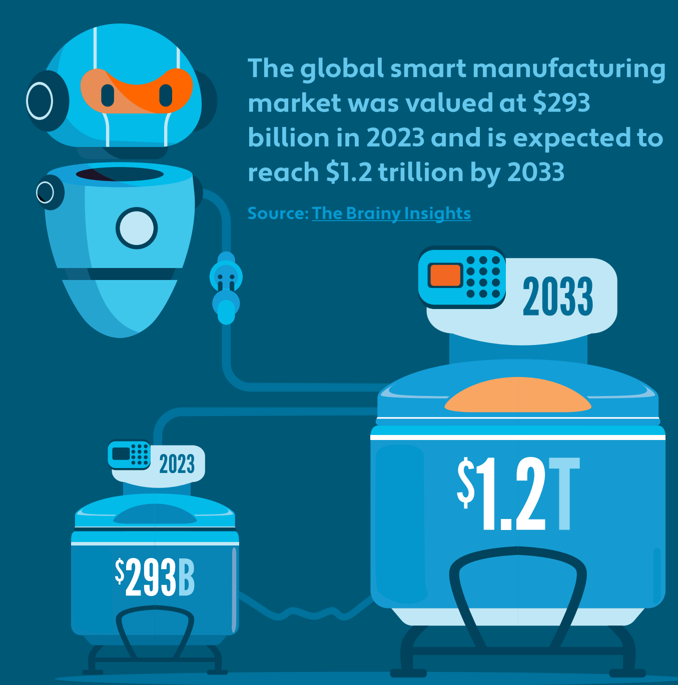


14 states broadly exempt tangible personal property from personal property tax; 10 states, plus Washington D.C., offer de minimis exemptions for taxable property

Sources: Tax Foundation, MyTax.DC.gov

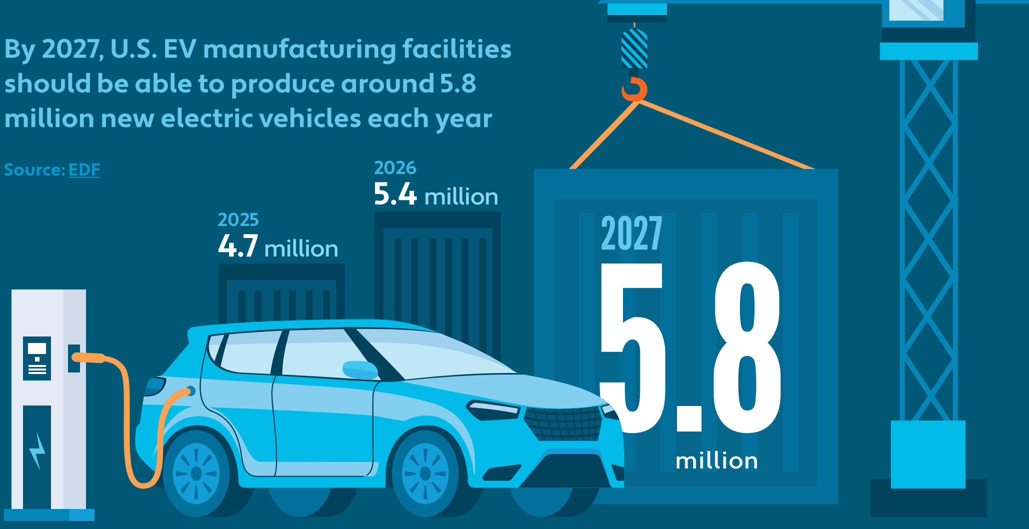
The global smart manufacturing market was valued at $293 billion in 2023 and is expected to reach $1.2 trillion by 2033

Source: The Brainy Insights



By 2027, U.S. EV manufacturing facilities should be able to produce around 5.8 million new electric vehicles each year

Source: EDF



32 states are offering tax incentives for data centers

Source: Tax Notes

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New exemptions for the manufacturing industry

It's not only new *taxes* that complicate compliance for the industry; new *exemptions* can also throw a wrench into the works.

Whether your business buys or sells tax-exempt products, you'll need the appropriate paperwork to back up the exemptions. If you make tax-exempt sales, you need to collect exemption certificates from your customers; if you make tax-exempt purchases, you need to ensure your suppliers have up-to-date certificates from you. Manufacturers often have to manage hundreds or even thousands of exemption certificates, and if your team is collecting, verifying, and storing them manually, there's a lot of room for error.

Per Maria Tringali, Senior Solutions Consultant and Exemption Certificate Specialist at Avalara, "Most businesses I speak with are good at collecting something when the customer is set up initially. But thorough validation of all data and forms is more difficult than one would think. Businesses with the best of intentions to proactively request updated exemption certificates often find follow-through difficult without a dedicated resource. So what we see are PDFs saved to shared drives, with no idea of how compliant they might be."

Exemption certificate challenges can also become a cause of negative audit findings; missing or incorrect documentation can result in out-of-pocket fines and penalties. For example, let's say your total revenue is $10 million, and 90% of your sales is to tax-exempt buyers. If an auditor finds a 30% error rate in the exemption certificates they review, they'll multiply that error rate across your annual revenue. At a state sales tax rate of 8.25%, your business could owe $222,750 in sales tax not collected, plus fines and penalties. That's a big price to pay for just a few missing or invalid documents.

While all manufacturers have to deal with exemption certificates, sales tax exemptions and incentives are often industry specific. States tend to offer exemptions to encourage the industries they want, such as data mining, aircraft manufacturing, or the production of affordable housing.

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Data mining and data center exemptions

Data mining and digital assets procurement is a growing industry, and its growth is fueled in part by state tax incentives. This includes the creation of new virtual currency using blockchain technology that requires the use of servers, computers, transformers, software, and lots of energy.

From November 1, 2024, to December 31, 2029, **Oklahoma is providing a sales tax exemption** for the sales of machinery, equipment, and electricity used in commercial digital asset mining.

In May 2024, the Michigan Senate passed a bill that **extends exemptions to data centers and data center equipment**. As of March 2024, Nevada offers tax **abatements for data centers, but not exemptions**. Lawmakers are split on **whether data centers are a good investment**, and they tend to vote with their tax exemptions.

Exemptions on certain aircraft and aircraft parts

Some states have more high-flying exemption goals. Mississippi's **House Bill 1855**, enacted in April 2024, exempts sales, leases, and other retail transfers of certain fixed-wing aircraft to certified common carriers.

And back in May 2023, in an effort to keep airports and maintenance jobs competitive, Maryland Governor Wes Moore signed two bills into law that extend a sales tax exemption on aircraft parts through June 30, 2030 (**HB 557** and **SB 574**).

Washington state exemptions for affordable housing and semiconductors

Washington state is **keeping tax exemptions closer to the ground**, to the benefit of numerous industries.

- HB 2003 allows an exemption for **leases of public lands used for affordable housing**, effective June 6, 2024.
- HB 1757 provides a partial sales and use tax exemption for goods and services purchased by an eligible farmer starting July 1, 2024 (good news for Washington apple and Rainier cherry farmers).
- HB 2454 exempts farmers from the hazardous substance tax as of June 6, 2024.
- HB 2484 extended tax incentives for **semiconductor manufacturers** in the state effective April 1, 2024.

Washington also offers a **Manufacturers' Sales and Use Tax Exemption** for machinery and equipment used directly in manufacturing or research and development.

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Surprising sales tax exemptions in Texas

"A person processing food for sale is a manufacturer and may claim a sales or use tax exemption on purchases of equipment and other taxable items that qualify for exemption under Tax Code, § 151.318. For example, a restaurant may claim an exemption on the purchase of an oven or a mixer directly used in baking or mixing."

However, "the exemption in Tax Code, §151.317 for natural gas and electricity used in manufacturing is **not** applicable when the gas or electricity is used to prepare or store prepared food."

Source: 34 Tex. Admin. Code § 3.293(6)

What counts as "manufacturing," anyway?

The definition of **"manufacturing" varies between states** where tax is concerned, so if your business has warehouses, factories, or remote staff across states, it's important to know how the tax laws shake out across jurisdictions. Even in a single state, what qualifies as manufacturing for tax purposes can be hazy.

For example, North Carolina provides a sales and use tax **exemption for qualifying mill machinery** for specific industries and circumstances, and the North Carolina Department of Revenue checks that the exemption is properly applied. In one case, the department denied the mill machinery tax exemption claim for a business that used the exempt equipment to produce hot mix asphalt, on the grounds that the machinery was used internally for the company's own construction processes, not for customers.

The case was disputed **all the way up to the state Supreme Court**, which found the taxpayer to be entitled to the exemption. That's good news for the company, but it shows how costly and time-consuming managing manufacturing exemptions can be.

Navigating tax credits can be equally complex.

Research and development tax credits

Definitions of manufacturing are inconsistent from state to state, much like tax credits. Illinois **postponed the sunset of its research and development tax credit** (HB 5005) and included provisions related to aircraft. Meanwhile, California is offering an R&D tax credit beginning January 1, 2025.

Tax credits typically lower the tax that businesses owe, and companies see the savings on their annual bills. Tax incentives can include credits and deductions, and they're put in place to encourage businesses or investments. Exemptions exclude some assets, like income, property, and transactions from being taxed. Several states are using all of these in different ways to boost their economy and entice companies to do business in those states.

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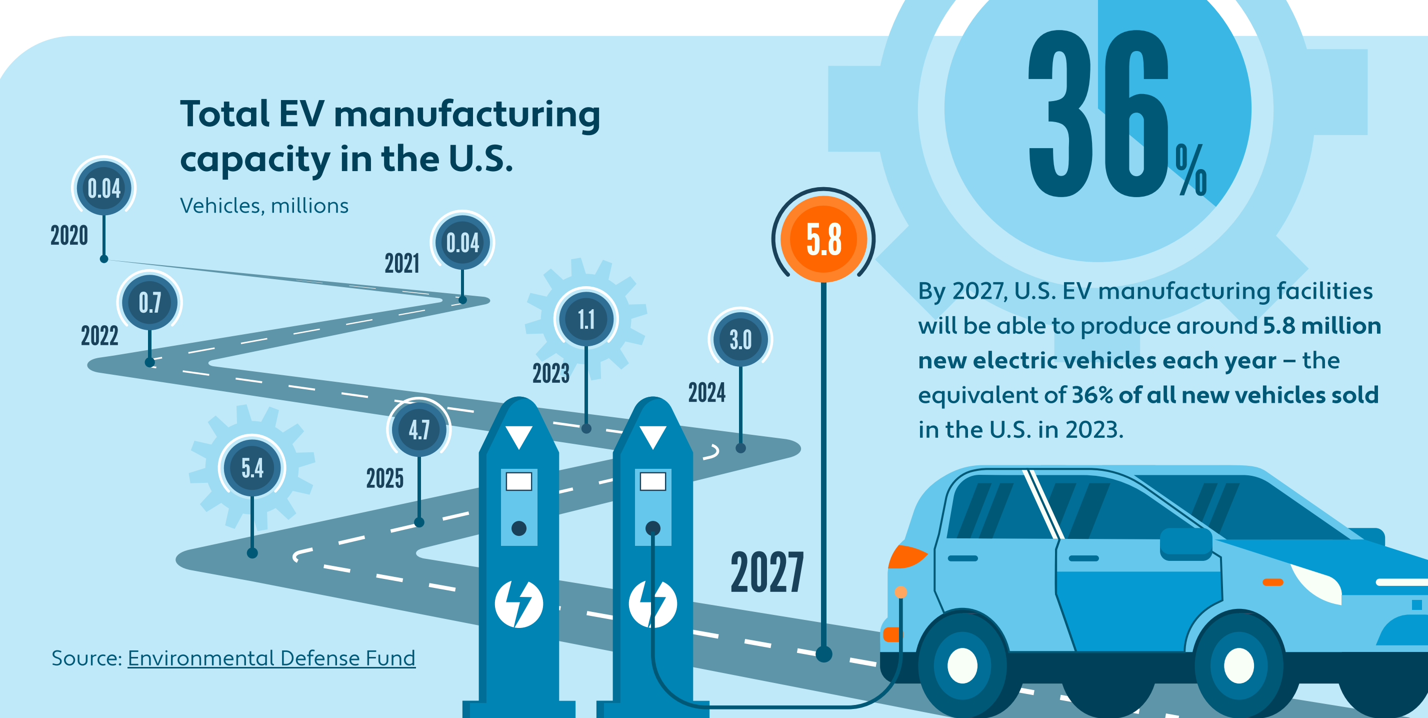
Tax credits and electric vehicles

The electric vehicle (EV) tax credit has been sparking debate among legislators. The tax credit contributed to the popularity of EVs among consumers in the last few years. And thanks to the Inflation Reduction Act, EV manufacturing is a booming industry in the U.S.; a 2024 report from the Environmental Defense Fund predicts that by 2027, U.S. EV manufacturing facilities will be able to produce around 5.8 million new electric vehicles each year – the equivalent of 36% of all new vehicles sold in the U.S. in 2023.

To qualify for the Clean Vehicle Credit, vehicles purchased after December 31, 2022, must undergo final assembly in North America. Battery sourcing rules changed effective 2024; an eligible clean vehicle may not contain battery components manufactured or assembled by a "foreign entity of concern" (FEOC) – any country that proves an economic or security threat to the United States. Beginning in 2025, eligible vehicles may not contain critical minerals that were extracted, processed, or recycled by an FEOC. These changes were proposed in an effort to boost U.S. manufacturing and prevent jobs and factories from going overseas.

But some members of Congress want to end electric vehicle tax incentives. In September 2023, an Ohio senator introduced legislation that would eliminate federal tax credits for electric vehicles and instead replace them with a credit for gas-powered vehicles. And in May 2024, a Wyoming senator introduced legislation to end the federal electric vehicle and charging stations tax credit. Creatively named the Eliminating Lavish Incentives to Electric (ELITE) Vehicles Act, S. 4237 would repeal the tax credit for the purchase of new and used EVs.

Sales and use tax challenges aren't the only tax hurdle manufacturing businesses are up against in 2025. Personal property taxes – especially on equipment like machinery and office furniture – are still a huge pain for manufacturers.



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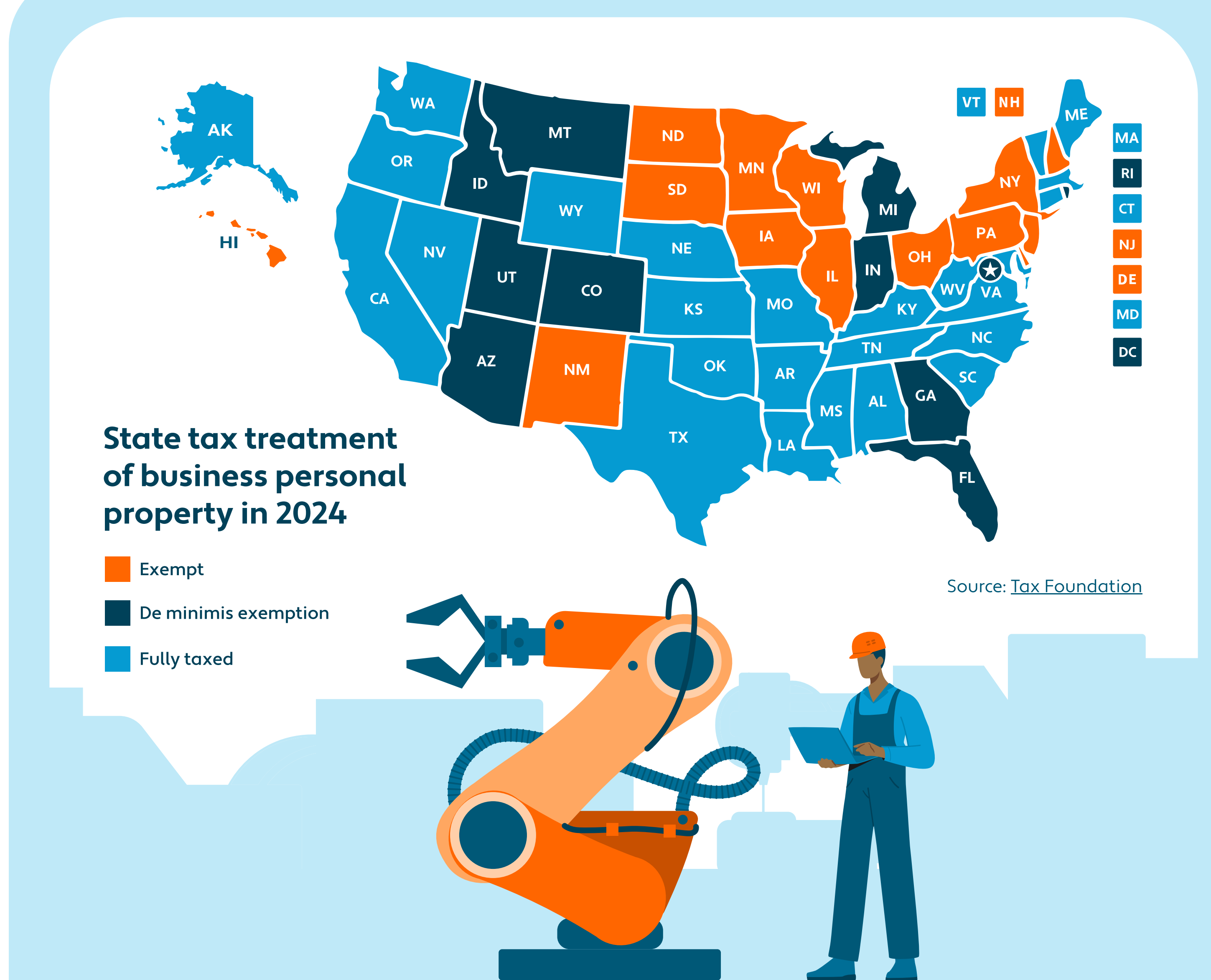
Business personal property tax challenges

Property tax is a headache for manufacturers with a lot of equipment. While real property tax (applicable to land and structures affixed to the land) is relatively straightforward, personal property tax, which includes machinery, equipment, fixtures, and supplies used in the manufacturing process, can get complicated quickly.

Property tax is administered at a local (usually a county or township) level. Consequently, local authorities are often challenged by functions typically afforded by large state organizations – this includes access to labor with domain expertise, expensive software and technology, and infrastructure with the ability to scale the assessment and collection of taxes. As such, many taxing authorities depend on paper and manual processes to manage the property tax process.



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This results in a heavy, paper-driven field relying on older means of processing data, whether it's still sending notices and tax bills to taxpayers via snail mail or manually reading through handwritten returns or returns corporations have filed using automation tools. All of this data then requires manual extraction and data entry into the property tax systems the jurisdiction uses. These challenges leave the taxing authorities with limited time to process valuations, much less the administration of appeals.

States realize personal property tax compliance can be a huge burden for businesses. Even for local governments, it can be more trouble than it's worth. Thus, a number of states have considered making changes to their property tax policies recently:

- **Michigan** passed a bill back in December 2021 that **allows qualified manufacturers to claim a late exemption** of eligible manufacturing personal property beginning in 2024.
- **Arizona, Colorado, Texas,** and 20 other states **sought to reduce or eliminate personal property tax in 2023**.
- **Wisconsin** repealed **local personal property taxes and state taxes** on manufacturing and rail personal property as of January 2024. However, the Badger State failed to pass two other bills to amend property tax (**Senate Bill 2** and **Assembly Bill 2**).
- As of March 2024, many states, including **Arizona, Colorado, Idaho, Indiana, Michigan, Montana**, and **Rhode Island**, have **exempted personal property or allowed a de minimis exemption** for businesses with smaller amounts of property, but inconsistent rules across states can prove to be a problem for manufacturers with warehouses, equipment, and staff across state lines.
- **Georgia** will **increase its personal property tax exemption** from $7,500 to $20,000 as of January 1, 2025.
- **Missouri** looked to **decrease personal property valuations** beginning in 2025, but the bill didn't pass.

The year ahead may see more exemptions for personal property. In 2025, Maryland may try to pass a bill that **exempts all personal property for small and midsize manufacturers** (although small businesses have been **exempt since 2022**).

So what makes personal property tax compliance so onerous? To start, **how personal property is assessed** can be complicated. Each year, business owners file a tax return with a property appraiser, who takes into account the fair market value of everything from office furniture to machinery to vehicles and other equipment. Fair market value is determined by the current cost to replace an item, the item's depreciation, and functional or economic obsolescence. And if your business grows or expands, or downsizes, your tangible personal property obligations will change.

It's also a ton of work, time, and hassle to keep up with personal property tax compliance. Last September, the city of Portland, Maine, began the City of Portland's Personal Property Revaluation, which included **an inspection of every business in the city by an appraiser**. The idyllic coastal city has at least 151,212 small businesses alone, and the appraisal process will likely take a full year. This audit is the first of its kind in at least 50 years, so it wouldn't be surprising for businesses to find that they've been paying the wrong tax amounts for a while.

Whether the assets are tangible or intangible, states are finding ways to tax them. And even though businesses have been grappling with personal property tax for centuries, new technological developments are causing new tax headaches.

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Tech trends and taxability trouble

Digital transformation is still the name of the game for the manufacturing industry (this shift to high-tech processes and products is also referred to as Industry 4.0). To streamline production and reduce costs, businesses are leaning into automation, IoT, digital twins, and smart factories. Using these technologies can have unexpected consequences for tax compliance.

The more technology you integrate into a product, process, or business, the more likely you'll come up against communications taxes. Many manufacturers who have never had to worry about communications taxes are now realizing that the smart technology they integrated into their new product, the software they distribute to remote workers, and the AI they're using to put predictive maintenance systems in place all come with tax obligations.

Other tax changes affecting manufacturers stem from more traditional activities, like deliveries.

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Retail delivery fees and you

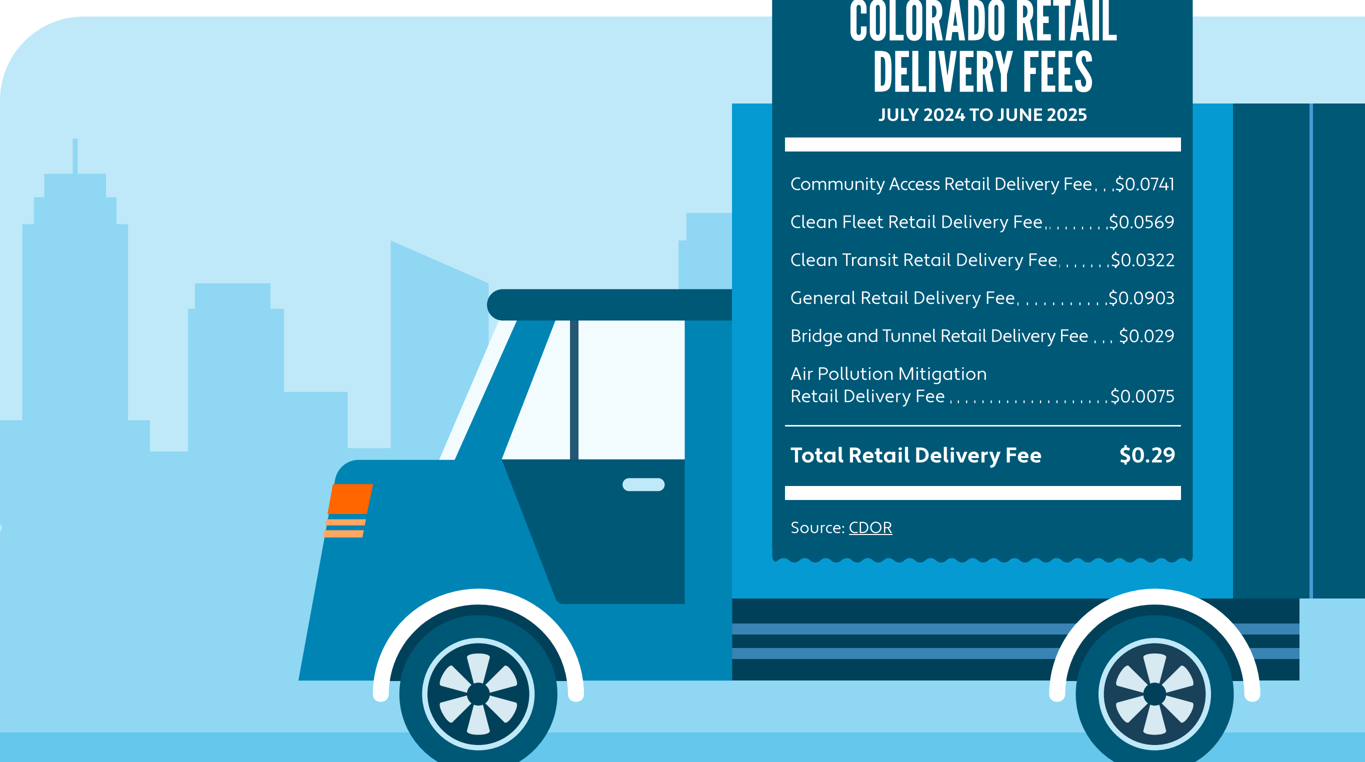
Colorado led the charge in 2022 with the retail delivery fee (RDF) and Minnesota soon followed suit. RDFs can impact manufacturers too. A manufacturer of refrigeration systems, for example, that sells to a grocery store in Minnesota or Colorado would need to remit the fee on those sales.

Business-to-business (B2B) retail sales are subject to the Colorado fee, and after some deliberation, it was determined that USPS deliveries are subject to the fee. The fee increased to 29 cents on July 1, 2024, and although it's a negligible amount per sale, it can add up. Businesses can pay the fee themselves. However, if you collect the fee from the customer in Colorado or Minnesota, you must show the fee on the receipt or invoice.

While only two states have retail delivery fees now, the trend is catching on as states, including Maryland, Nebraska, Nevada, New York, Ohio, and Washington, look for new ways to get revenue.

An automated tax solution like Avalara AvaTax can help you collect and remit delivery fees automatically. Businesses will want to put systems in place sooner rather than later; the implementation of the Colorado fee was fast and furious, taking effect just a few weeks after it was announced. Learn about the impact of retail delivery fees on other industries in the retail section of this report.

While RDFs are only a concern in a couple of states, every state with a sales tax has an economic nexus law.



COLORADO RETAIL DELIVERY FEES

JULY 2024 TO JUNE 2025

Fee	Amount
Community Access Retail Delivery Fee	$0.0741
Clean Fleet Retail Delivery Fee	$0.0569
Clean Transit Retail Delivery Fee	$0.0322
General Retail Delivery Fee	$0.0903
Bridge and Tunnel Retail Delivery Fee	$0.029
Air Pollution Mitigation Retail Delivery Fee	$0.0075
Total Retail Delivery Fee	**$0.29**

Source: CDOR

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Economic nexus for manufacturers in 2025

We could write our annual tax changes report every year for the next decade and there will always be a section for **economic nexus**. Since the 2018 United States Supreme Court decision in South Dakota v. Wayfair, Inc., manufacturers have puzzled over the different business activities that give them an obligation to register for sales tax in different states.

Thirteen states, including Indiana, Wyoming, and North Carolina, have **eliminated the transaction threshold**. **Alaska** is cutting its threshold effective January 1, 2025, and **New Jersey** is also looking to cut the threshold in 2025.

This means that to reach the nexus threshold and have sales tax obligations in the state, sellers only have to meet a sales threshold. But even in those states, calculating economic nexus is still pretty complex, and of course, the laws, threshold amounts, and rules vary between states.

Even if you only make exempt sales, you're still required to **register and comply with sales tax laws in many states**. If you can't get enough of economic nexus updates, check out the **sales tax section** of this report, where we cover it more in depth.

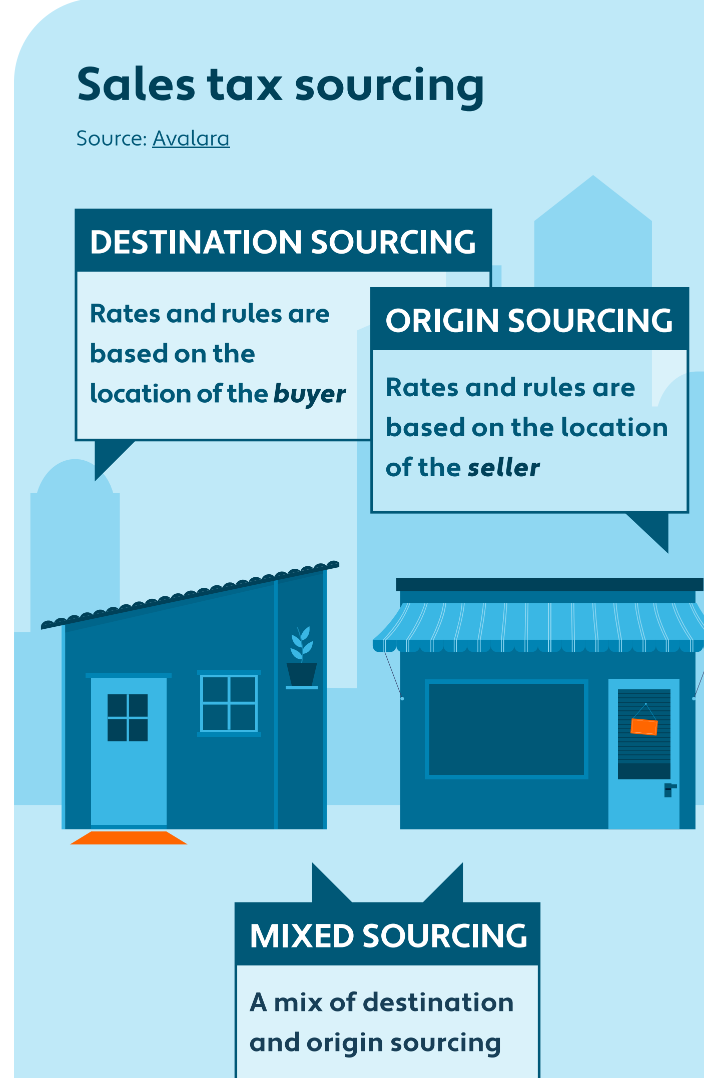
Sourcing rules struggles

It's important to know the **sales rules that are in effect** when you sell into another state or jurisdiction. Is the applicable tax rate based on where the order is shipped from, where it's shipped to, or a combination of both. It becomes particularly challenging when a state switches sourcing rules, or changes requirements for in-state or out-of-state sellers.

Illinois is changing its sourcing rules effective January 1, 2025, at least for some retailers and transactions. Under SB 3362, out-of-state retailers that have a physical presence in Illinois must collect the tax rate in effect at the delivery address (aka, destination sourcing) when shipping goods from outside of Illinois. Previously, these businesses could apply a single use tax rate for orders shipped from out of state. Learn more about the state's new sourcing rules in the **sales tax section**.

Sales tax sourcing

Source: Avalara



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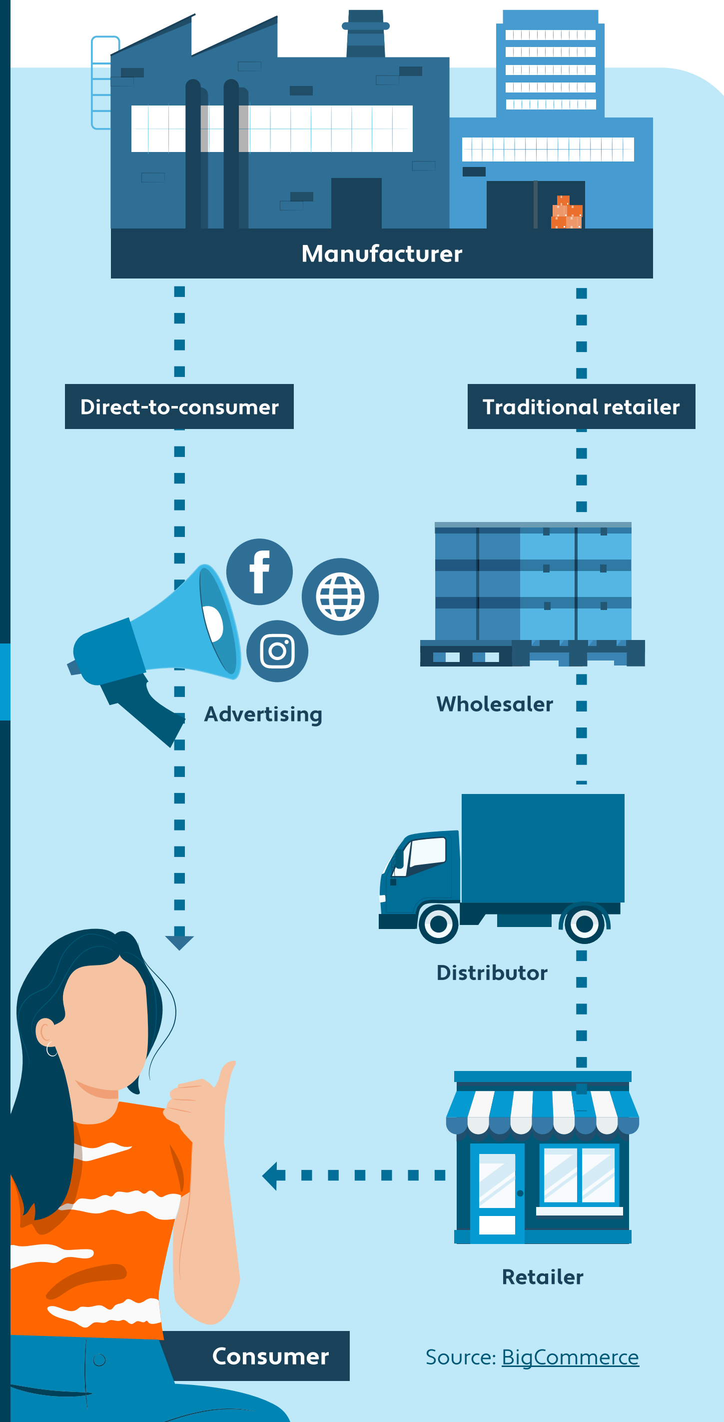

Source: BigCommerce

Manufacturers and omnichannel sales

Direct-to-consumer (D2C) manufacturing is still trending, but what does that mean for manufacturers?

By **selling directly to the consumer**, you have more control over your relationships with customers; you determine pricing and messaging, you can be more agile with your customer service, and your customers get to interact directly with you. And while D2C shipping allows you to have customers all over the world, it could potentially expand your tax obligations thanks to nexus laws.

If you sell into other countries (B2B or B2C), you may also need to contend with the growing number of e-invoicing mandates. Learn more about e-invoicing mandates and other factors that may affect your cross-border business in the **global section** of this report.

Marketplace sales further complicate tax compliance for manufacturers

With the rise in popularity of marketplaces like Amazon and Etsy, it's no surprise manufacturers are getting in on the retail trend. But marketplace facilitator laws can complicate sales tax compliance.

Under these laws, online marketplaces are responsible for collecting and remitting applicable sales tax in states where they have sales tax nexus. Many states don't require individual sellers to register and file returns if they only sell through a marketplace as a remote seller, but some states do. This is one area where manufacturers are getting tripped up. Another is the challenges posed by direct-to-consumer sales.

Maria Tringali puts it this way: "Many manufacturers are turning to marketplaces to increase direct-to-consumer sales. While laws require the marketplace to collect and remit the sales tax, businesses often are unaware that these sales are part of their overall income and, added to direct sales, may require them to register, charge sales tax on non-marketplace sales, and file sales tax returns that include reporting the marketplace sales."

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[Where you store your marketplace inventory]() can also trigger physical presence nexus. If you use marketplaces like Fulfillment by Amazon (FBA), eWorldTrade, or Alibaba and they store your products in fulfillment centers, you may have tax obligations you weren't previously aware of.

Ecommerce and marketplace sales give businesses the agility to compare prices, vendors, and shipping times, but can also present a tax compliance problem. It's important for manufacturers to have a way to collect and verify exemption certificates from buyers at the point of sale. And manufacturers that make exempt sales through marketplaces need to know [whether they're responsible for collecting and storing exemption certificates](), or if the marketplace handles it (most do). Otherwise, you're left emailing back and forth, refunding tax, and managing a lot of paperwork manually.

Another reason to make sure your exemption certificate documentation is in order? Exemption certificates are a point of interest for audits.

MARIA TRINGALI
Senior Solutions Consultant and Exemption Certificate Specialist at Avalara

Many manufacturers are turning to marketplaces to increase direct-to-consumer sales. While laws require the marketplace to collect and remit the sales tax,

businesses often are unaware that these sales are part of their overall income

and, added to direct sales, may require them to register, charge sales tax on non-marketplace sales, and file sales tax returns that include reporting the marketplace sales.

The A-word … *audits*

Between the high-tech trends that opened the industry to a remote workforce and the upsurge of work-from-home during 2020, many manufacturers were able to hire staff all over the country. Having employees in other states can trigger physical presence nexus, which can result in tax obligations.

And the more people you hire from a state, the more likely you are to be exposed to audit risk, according to Myles Metzger, Use Tax Solution Consultant for Avalara. "The remote work boom post-COVID created physical presence sales tax nexus for a number of companies. Since many businesses needed to register for payroll withholding tax in states, it increased their detection risk for sales and use tax. Items employers ship to remote employees, such as laptops and monitors, are subject to sales or use tax, as is software they're accessing in the state."

Just because a product, buyer, or seller is exempt from sales tax doesn't mean they're exempt from sales and use tax audits. There are 40 states, plus Puerto Rico and Washington, D.C., that include some type of exempt sales in their nexus threshold, so you may have more tax obligations than you think.

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More auditors are focusing on exemption certificates too, according to David Knuff, Use Tax Product Solution Consultant at Avalara. "While the number of audits we're seeing hasn't really changed, more states are focusing on exemption certificates. Sales and use tax is the second biggest contributor to state budgets, so states are trying to maximize revenue any way they can. Exemption certificate management and compliance is low-hanging fruit for them, since spreadsheets, filing cabinets, and poor recordkeeping can get messy fast."

DAVID KNUFF
Use Tax Product Solution Consultant at Avalara

> **While the number of audits we're seeing hasn't really changed, more states are focusing on exemption certificates.**
>
> **... states are trying to maximize revenue any way they can. Exemption certificate management and compliance is low-hanging fruit for them ...**

Taxable transactions and exempt sales

- No economic nexus
- States that generally include exempt sales in the threshold
- States that generally *don't* include exempt sales in the threshold

Source: Avalara

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Procure-to-pay and compliance

Getting the procure-to-pay process right is important. Otherwise, you could be looking at missed deadlines, increased costs due to a rushed order or new vendor, unhappy customers, and even a penalty or a fine if an audit goes wrong.

When purchasing goods and services for your company, it's best practice to track and verify invoices to confirm sales tax and exemptions were correctly applied, make sure vendors have valid exemption certificates, and self-assess and pay consumer use tax. Many manufacturers are **turning to technology to help maintain compliance** during these processes; automation software can track and verify invoices at receipt and ensure the exemption certificates in your system are valid and updated regularly.

Economic nexus can also impact the purchases your business makes; if you buy supplies from a vendor with nexus in a state, you'll need to pay sales tax or provide the vendor with a valid exemption certificate. If the vendor doesn't have nexus, you may be responsible for remitting consumer use tax directly to your state tax authority.

Avalara Vendor Exemption Management

SEND CERTIFICATES TO VENDORS TO PREVENT DELAYS AND UNNECESSARY TAXES

Streamline vendor exemption management as your business grows. Increase accuracy while you improve compliance, save time, and reduce risk.

LEARN MORE

Avalara AvaTax for Accounts Payable

CATCH VENDOR SALES TAX ERRORS AND REDUCE LIABILITY

Identify over- and underpaid sales tax on your purchases and apply the correct use tax based on jurisdiction, taxability, and special rules.

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Consumer use tax

Consumer use tax continues to be a particular challenge for manufacturers. This tax is required when sales tax isn't collected on a purchase. For example, when a manufacturer buys machinery in a state where equipment is exempt, then uses it in a state where it's taxable. A Minnesota-based construction company learned this the hard way in the case of Ellingson Drainage, Inc. v. South Dakota Department of Revenue. Ellingson Drainage, Inc. neglected to pay South Dakota use tax, and now has to pay a large use tax assessment; learn more about the case in the sales tax section.

In some states, machinery or equipment is exempt from tax only if it's used in manufacturing. The degree to which a product has to be used and what counts as manufacturing varies from state to state. So if your business didn't pay sales tax at the outset then doesn't meet the use threshold or uses the item for any purposes other than manufacturing, use tax will apply.

Take forklifts, for example. According to Metzger, "In Wisconsin, a forklift has to be used exclusively and directly (95% or more) in the manufacturing process to be exempt from sales or use tax. If you're under that threshold, the forklift is not used exclusively and directly in manufacturing and is taxable. Texas has a much lower threshold; 50%. The taxability rules for your equipment vary widely for taxpayers with factories across multiple states."

As manufacturing becomes increasingly high tech, companies are buying software for employees around the world. If your team in the Seattle office purchases new laptops and drafting software for employees in San Diego, Boston, and Atlanta, your business could owe use tax in California, Massachusetts, and Georgia.

With all these changes and trends, it sure looks like businesses in the manufacturing industry are in for an interesting year. But not to worry – Avalara will be right there with you, keeping track of tax changes and helping you understand how they might affect your business.

How Avalara can help

Avalara Exemption Certificate Management and Avalara Vendor Exemption Management allow manufacturers to collect, store, and manage exemption certificates, making it easier to stay tax-compliant and audit-ready. Coupled with Avalara AvaTax and Avalara AvaTax for Accounts Payable, they can also monitor for potential sales tax obligations, collect the certificates you need from customers, and streamline consumer use tax calculation and vendor invoice management.

EXPLORE SOLUTIONS

Up next: Lodging

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Lodging

The urge to travel remains strong, as does the need for tax revenue among state and local governments. Because they're paid by visitors rather than voters of a particular jurisdiction, lodging taxes can often be easier to implement than other taxes. That's why lodging tax compliance is more critical than ever for businesses in the industry.

What's ahead:

Prepare for a lodging boom in 2025

What the numbers tell us about the lodging industry in 2025

Understanding tax obligations for lodging marketplaces

New tax compliance rules for lodging marketplaces in 2025

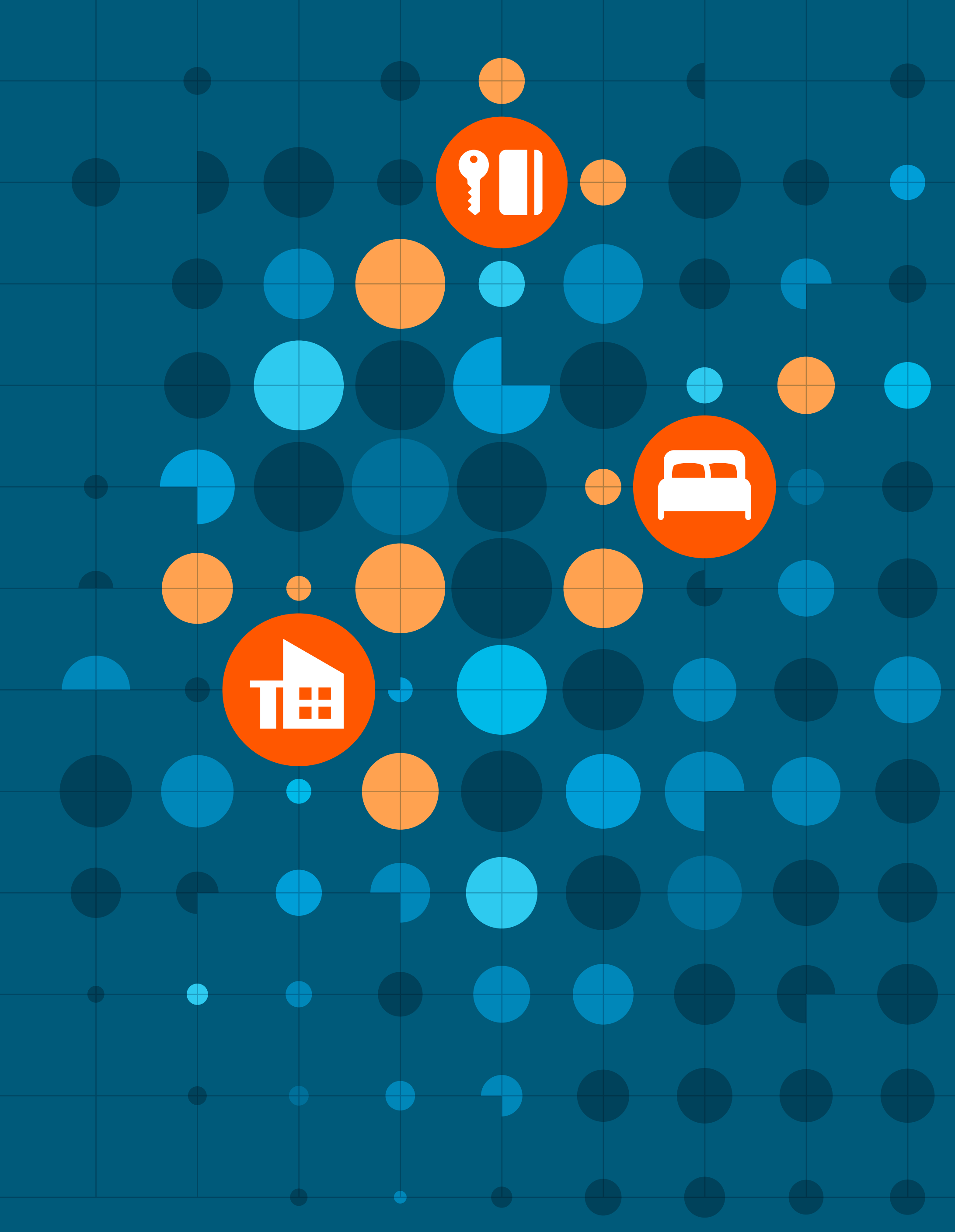
STR tax regulations and compliance challenges

How hotels are competing in the short-term rental market

How extended stays impact hotel and lodging tax compliance

More new lodging tax compliance developments

You can't hide, so you may as well comply



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Prepare for a lodging boom in 2025

Many of us will travel with a vengeance in 2025. Of 5,000 people from five countries **surveyed by McKinsey** in February and March 2024, 66% said they're more interested in travel now than before COVID tethered us to our homes. And while international trips remain a priority for revenge travelers, domestic travel should account for 70% of travel spending – the **prepandemic norm** – by 2030.

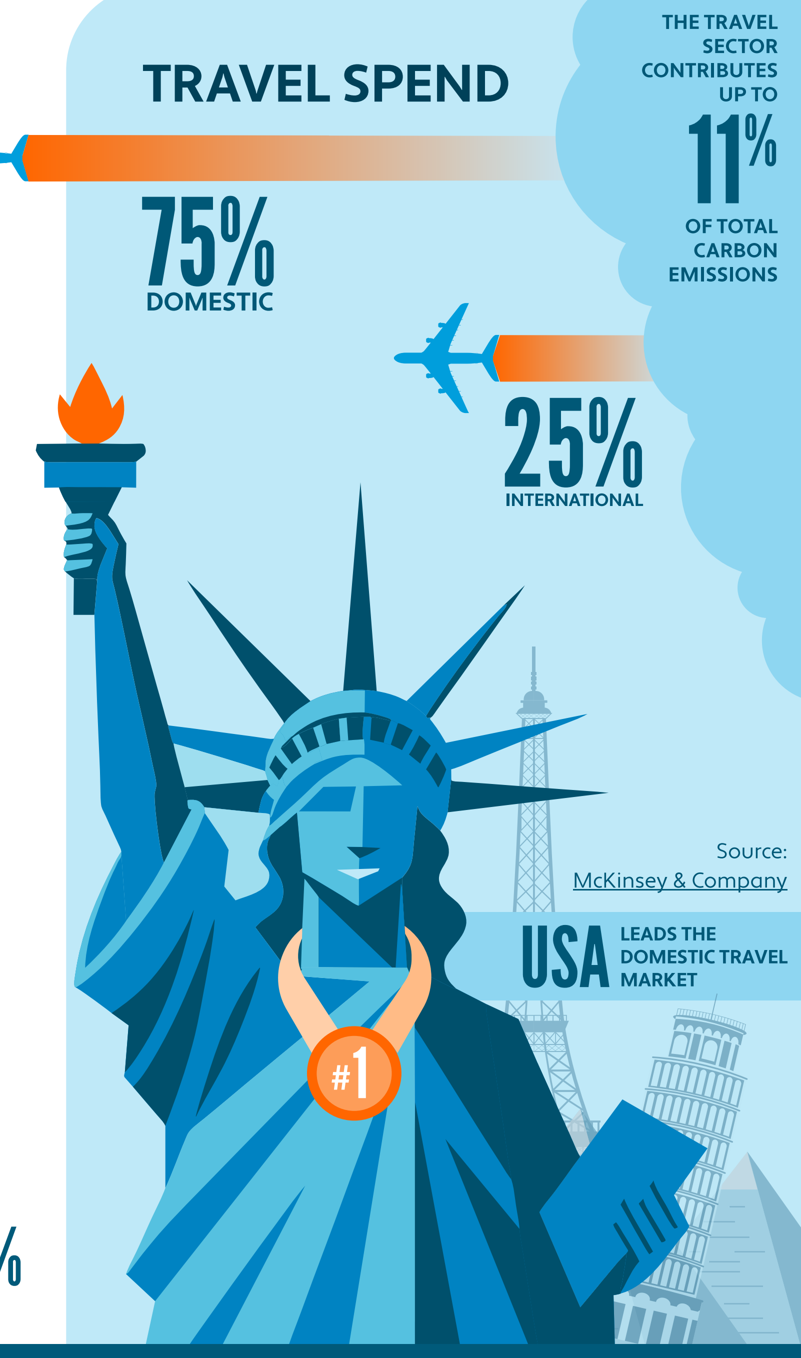
That's good news for lodging providers and the businesses that support them, like lodging marketplaces, online travel agencies (OTAs), and property managers.

Lots of people will travel alone: **69% of travelers** surveyed by American Express said they're planning to take at least one solo trip in 2025. Many will blend business and leisure to experience *bleisure*; there are an estimated **17 million digital nomads** in just the United States.

Whether traveling alone or with others, for business or fun, all travelers need a place to stay. **Demand for short-term rentals** (STRs) is expected to grow by 5.9% in 2024 and 6.8% in 2025. Hotel occupancy, average daily rates, and revenue per available room should see **a slight uptick** as well.

Where there's revenue, taxes tend to follow. That's especially true when there's a need for tax revenue, and the **Tax Policy Center** expects states to experience only modest revenue growth across all major tax categories in 2025. We're certainly seeing heightened interest in lodging taxes at the local level, with jurisdictions using data mining services to uncover noncompliant short-term rentals.

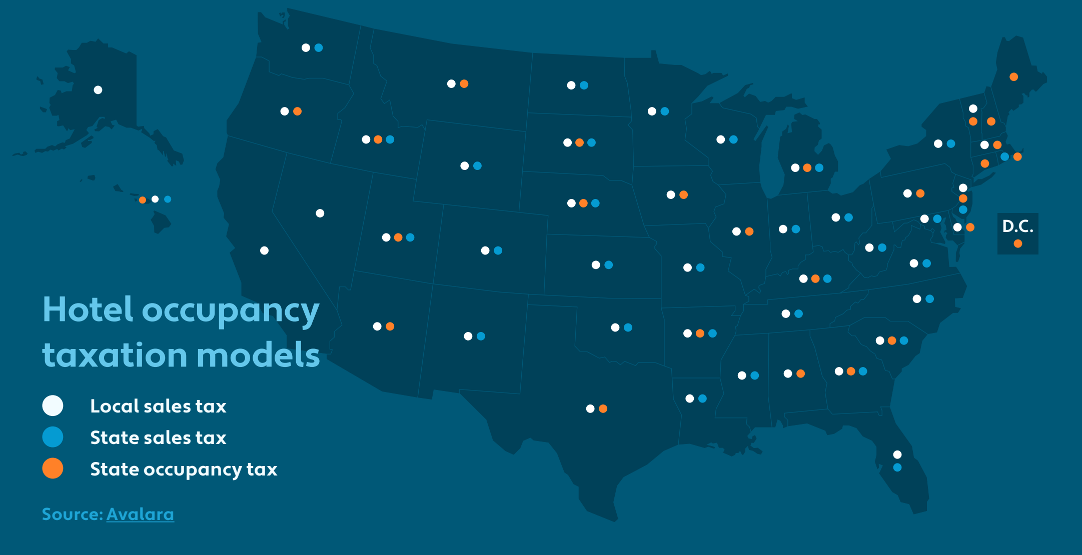
This means businesses in the hospitality and lodging sector need to be aware of tax trends and prepare to become compliant. But first, let's look at some lodging industry numbers.



80% OF TRAVELERS VISIT 10% OF THE WORLD'S TOURIST DESTINATIONS

What the numbers tell us about the lodging industry in 2025

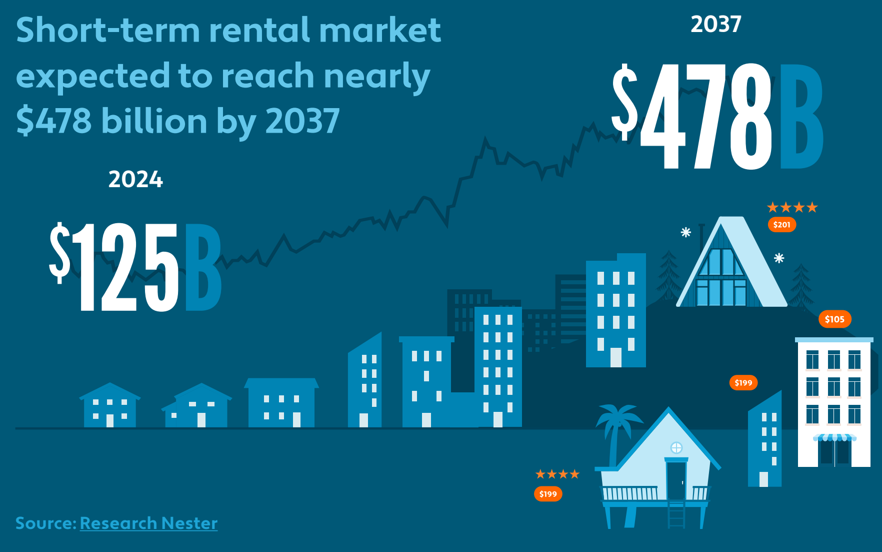
Hotel occupancy taxation models



- Local sales tax
- State sales tax
- State occupancy tax

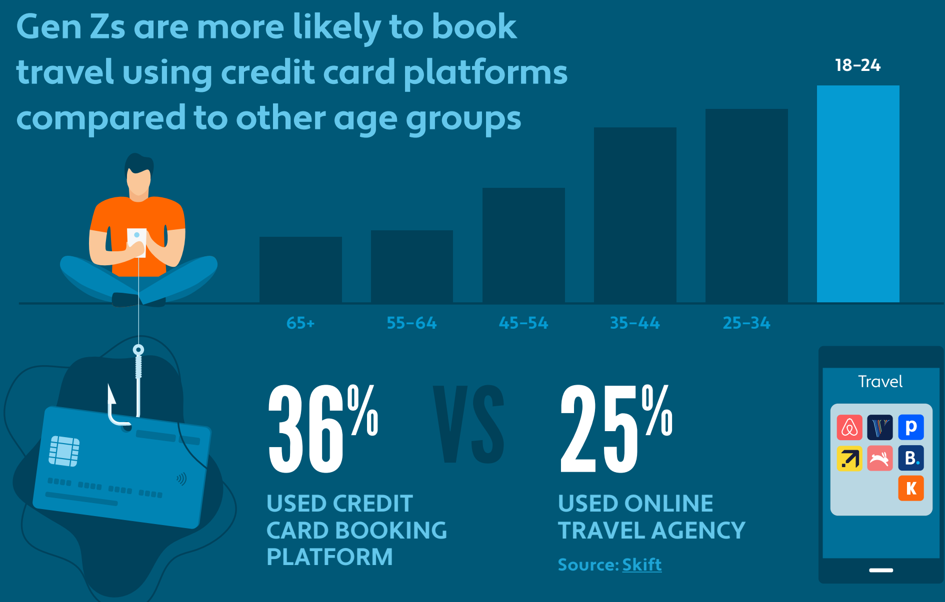
Source: Avalara

Short-term rental market expected to reach nearly $478 billion by 2037



Source: Research Nester

Gen Zs are more likely to book travel using credit card platforms compared to other age groups



36% USED CREDIT CARD BOOKING PLATFORM

VS

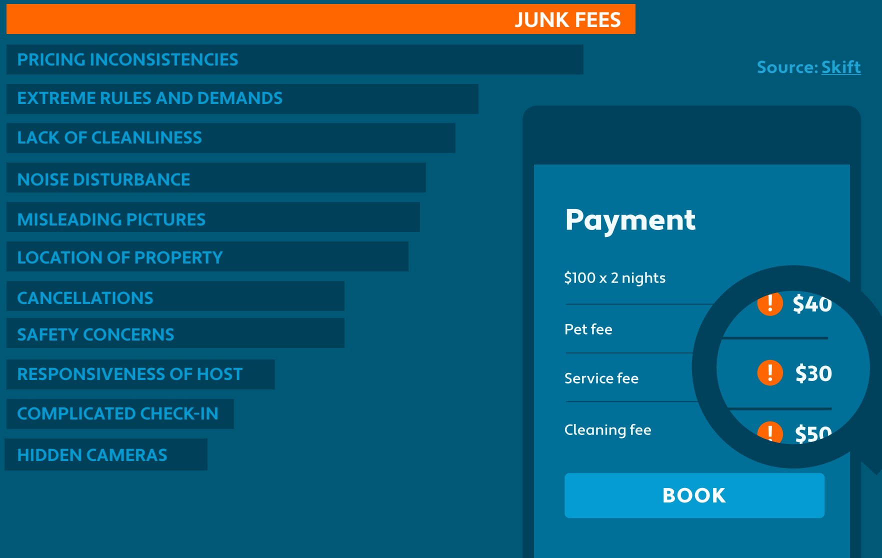
25% USED ONLINE TRAVEL AGENCY

Source: Skift

Unexpected junk fees top the list of issues and challenges with STRs

- JUNK FEES
- PRICING INCONSISTENCIES
- EXTREME RULES AND DEMANDS
- LACK OF CLEANLINESS
- NOISE DISTURBANCE
- MISLEADING PICTURES
- LOCATION OF PROPERTY
- CANCELLATIONS
- SAFETY CONCERNS
- RESPONSIVENESS OF HOST
- COMPLICATED CHECK-IN
- HIDDEN CAMERAS

Source: Skift



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Understanding tax obligations for lodging marketplaces

Defining a lodging marketplace: What you need to know

As lodging marketplaces continue to evolve, so does the tango to determine how each state defines them. Are you an *accommodations intermediary*? A *lodging platform*? An *online travel agency*? Any or all of the above? What even is a *lodging marketplace*?

This isn't just semantics. Though the platforms that facilitate sales of accommodations are fundamentally all quite similar, different states refer to them differently – and if you don't know exactly *what* you are under a state's law, it's hard to decipher your tax obligations. You may be considered an accommodations intermediary in one state but a lodging marketplace in another. You might be subject to one state's marketplace facilitator law and another state's accommodations intermediaries law.

Consider the different laws and requirements in California, New Mexico, and Virginia.

- **California's marketplace facilitator law** doesn't apply to lodging platforms. However, local jurisdictions may **require lodging platforms to collect** local taxes on behalf of hosts.
- Businesses that list and book lodgings or **accommodations in New Mexico** on behalf of third parties are considered marketplace providers and may owe gross receipts tax on the sales they facilitate.
- **Virginia has a marketplace facilitator law** *and* a law specific to accommodations intermediaries, and both impose obligations to **collect and remit applicable taxes**.

"The marketplace facilitator landscape lacks conformity," says Kelly R. Smith, Director of Indirect Tax at Evolve Vacation Rental. "At the state level, there are at least 10 or more different naming conventions for 'marketplace facilitators' in the lodging industry. Simplification and consistency in terminology would help ease some of the confusion."

KELLY R. SMITH
Director of Indirect Tax at Evolve Vacation Rental

The marketplace facilitator landscape lacks conformity. At the state level, there are at least 10 or more different naming conventions for 'marketplace facilitators' in the lodging industry.

Simplification and consistency in terminology would help ease some of the confusion.

The different names might not seem like a big deal – it's just words, after all – but whether your business is subject to a marketplace facilitator law or an accommodations intermediary law can impact your tax compliance obligations.

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And, get this: Although many platforms now list both hotels and short-term rentals, states may have different requirements for facilitators of hotel rooms versus facilitators of short-term rentals. Under Tennessee's marketplace facilitator law, lodging marketplaces can seek a waiver of their tax obligation if "substantially all" of the **sellers on their platform are registered** with the Tennessee Department of Revenue. Yet the state's **short-term rental marketplace law** *doesn't* permit STR marketplaces to seek a waiver from their state and local tax obligations.

So yeah, words matter. And when they change, so can lodging tax compliance requirements for the platforms.

Which taxes do marketplaces need to collect and remit?

This isn't meant to be a trick question, but the answer certainly isn't simple because some fees and taxes may need to be paid by the marketplace, while other fees and taxes may need to be paid by the property owner or manager. Specific requirements depend on the jurisdiction where the property is located.

While marketplaces are generally responsible for applicable sales and use taxes on tangible goods, tax requirements for lodging marketplaces tend to be more nuanced. Some state marketplace facilitator laws are broad and cover all taxes and fees; others are more narrow.

A marketplace's use of the merchant model or the agency model also impacts tax liability.

The merchant model vs the agency model

Online travel companies used to pick a lane and stay in it. "In the past, Expedia played exclusively in the merchant model and Booking.com used the agency model," says Nicole Rogers, General Manager of Lodging at Avalara.

"Under the merchant model," she explains, "an intermediary purchases the inventory directly from a supplier or wholesaler, marks it up, and the OTA is generally responsible for the applicable lodging taxes. Under the agency model, the intermediary facilitates the sale of accommodations and requires the customer to pay the hotel/property directly." The hotel is the merchant of record responsible for the taxes, so intermediaries that collect tax on their markup fees typically remit it to the hotel to remit to the tax authorities.

"Now the lines have blurred," says Rogers. Today, Booking.com, Expedia, and many other OTAs offer both the merchant model and the agency model. The booking platform *and* the lodging provider must be able to properly account for tax in either instance.

Businesses that switch from one model to the other need to keep tax top of mind. Once a business becomes the merchant of record, it becomes responsible for collecting and remitting the tax due.

NICOLE ROGERS
General Manager of Lodging at Avalara

In the past, Expedia played exclusively in the merchant model and Booking.com used the agency model.

Now the lines have blurred.

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The double taxation conundrum with lodging marketplaces

If a marketplace doesn't strictly adhere to a law's requirements, or if both parties aren't clear on their obligations, there's a risk of double taxation: The facilitator and the lodging provider could both collect the same tax.

"In some cases," observes the **National Conference of State Legislatures** (NCSL), "marketplace facilitator tax collection requirements have complicated the determination of the party responsible for collecting and remitting sales and use tax."

An NCSL report on marketplace tax collection identified instances in which in-state businesses refused to stop collecting and remitting transactional taxes after the implementation of a marketplace facilitator law "due to POS or other system limitations." Elsewhere, "facilitators have been assessed for sales tax that was already collected and remitted by sellers."

As the NCSL points out, this has resulted in "double taxation and unfair tax administration which is not the goal of marketplace facilitator laws." Moreover, "the confusion can be exacerbated by transactions that involve multiple taxes, particularly local taxes that are not state administered."

NATIONAL CONFERENCE OF STATE LEGISLATURES

In some cases, marketplace facilitator tax collection requirements have complicated the determination of the party responsible for collecting and remitting sales and use tax.

The confusion can be exacerbated by transactions that involve multiple taxes, particularly local taxes that are not state administered.

Local lodging tax and the risk of noncompliance

"If state-level compliance was the only concern for lodging marketplaces, it would be easier to manage," explains Kelly R. Smith. "Local tax compliance is by far the largest headache in the short-term rental sector."

Local jurisdictions levy and administer *a lot* of lodging and occupancy taxes. Depending on the location of the property, lodging platforms may collect and remit state taxes *or* local taxes, but *not* state taxes *and* local taxes. Or, they may collect all the taxes due but only remit some of them to the appropriate taxing authority; the rest are given to the lodging provider to remit.

Given the widespread lack of conformity between jurisdictions, it's distressingly easy for lodging marketplaces and lodging providers to make mistakes.

Many emerging businesses in this space, including companies specializing in corporate housing, may not realize they're marketplaces (or accommodations intermediaries) and therefore could be liable for taxes. Others may not be up to managing the complexity of compliance. Both scenarios put them at risk.

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"Jurisdictions continue to recognize the opportunities related to lodging tax – both realized and missed – and to refine their definitions and requirements in order to maximize collections," says Pam Knudsen, Senior Director of Compliance Services at Avalara. "This is causing policy and compliance changes across multiple fronts on a regular basis. Staying on top of these changes is critical and can distract an organization from its primary focus."

The fact that local lodging tax requirements frequently change makes compliance even more difficult for marketplaces and lodging providers that operate nationwide. And lodging tax obligations aren't limited to U.S. businesses; they can apply to foreign entities doing business in the U.S. as well.

PAM KNUDSEN
Senior Director of Compliance Services at Avalara

> **[Jurisdictions continue] to refine their definitions and requirements.**
>
> **Staying on top of these changes is critical and can distract an organization from its primary focus.**

Revenue by marketplace

Hybrid remittance scenario

Scenario: Room booked on a **lodging marketplace** for a hotel in **New Jersey**

RECEPTION

Tax collected for the booking
$100

New Jersey has a rule that the **marketplace must pay all state taxes**

Tax on margin
Tax on base

TAX
$25 STATE
$25 LOCAL
TAX
$25 STATE
$25 LOCAL

Lodging marketplace remits
$50 State tax
$25 Local tax

Property remits
$25 Local tax

The lodging marketplace collects state *and* local tax on both the **base** rate (what it paid for the accommodation) and its **margin** (markup fees). It remits all the tax to the state EXCEPT the local tax on the base rate, which it gives to the property to remit.

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New tax compliance rules for lodging marketplaces in 2025

The United States is a big country with lots of tax jurisdictions and rules. We can't cover every change, but here are some of the most interesting.

Accommodations intermediaries must collect and remit in Alabama

Effective January 1, 2025, accommodations intermediaries must collect and remit state and local transient occupancy taxes in Alabama. The tax is imposed on the full retail price paid by the guest for an accommodation, including any fees or charges.

In addition to collecting and remitting the tax, lodging accommodations intermediaries and certain accommodations providers must submit an annual report to the Alabama Department of Revenue listing the physical address of each accommodation that was rented for more than 14 days during the previous year. However, hotels and certain professional property managers are not required to file this annual report.

Online travel companies must collect and remit in Illinois

"Re-renters of hotel rooms" are subject to Illinois hotel operators' occupation tax as of July 1, 2024. A re-renter of hotel rooms is someone not employed by a hotel operator who directly or indirectly, through agreements or arrangements with third parties, collects or processes payments for an Illinois hotel room from guests and either:

- Obtains the right or authority to grant access to, control of, or occupancy of a hotel room in Illinois to a guest, or
- Facilitates the booking of a hotel room in the state

The new law affects hotel operators and online travel companies that have nexus with the state and handle hotel bookings. Hosting platforms for short-term rentals of owner-occupied, tenant-occupied, or non-owner-occupied dwellings are *not* considered "re-renters of hotel rooms." Lucky them.

You might think this would free hotel operators from the obligation to collect hotel operators' occupation tax when a room re-renter collects and remits the tax. You'd be wrong.

According to the Illinois Department of Revenue (IDOR), "Hotel operators must continue to collect Hotel Operators' Occupation Tax from rooms rented to re-renters and remit the tax to IDOR, as well as report the tax on Form RHM-1. **Hotel operators should not claim rentals made to re-renters as exempt for resale.** The Hotel Operators' Occupation Tax Act does not authorize this exemption." Instead, hotel re-renters may claim a deduction for the cost of the room and any taxes paid to a hotel operator for the initial rental of the hotel room.

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Court determines OTAs aren't responsible for collecting Louisiana sales tax on hotel bookings

In April 2024, the **Court of Appeals of Louisiana, First Circuit** ruled in Robinson v. Priceline.com that online travel booking companies were not required to collect and remit sales taxes on the retail rate charged to customers, which includes a service fee. The ruling was years in the making and is significant. As the **Sales Tax Institute** notes, "This case establishes both the importance of definitions under the law and the importance of understanding exactly what a potential taxpayer is buying or selling."

According to the ruling, booking companies aren't liable for the tax because they aren't the hotels that furnish the sleeping rooms (i.e., they aren't the merchant of record). Additionally, the court determined the service fee is not subject to sales tax.

The Louisiana Department of Revenue appealed to the Supreme Court of Louisiana and on October 8, 2024, the court **declined to hear the case**. It explained, "Although there are valid arguments as to why facilitation fees should be taxable, the sales tax laws as they are currently written do not provide for such a result."

San Antonio updates STR tax rules

San Antonio, Texas, now requires STR platforms to ensure all listed short-term rentals include a permit number and to remove any listing lacking a permit number within 10 business days.

San Antonio has also updated its short-term rental tax rules. Effective mid September 2024, an STR platform that collects the state hotel occupancy tax (HOT) must also collect and remit applicable city and county HOTs. However, an STR that does *not* collect the state HOT is *not* required to collect and remit applicable city and county HOT.

Rhode Island requires STR platforms to list registration numbers

Like the city of San Antonio, the state of **Rhode Island** is requiring STR marketplaces to ensure all properties on STR platforms are registered with the state. This **STR registration requirement** is scheduled to take effect January 30, 2025.

Colorado simplifies lodging tax requirements for accommodations intermediaries

The Colorado Legislature has realized how burdensome varying local tax requirements are for local lodging operators and accommodations intermediaries. (Hooray for the Colorado General Assembly!) To help make compliance less onerous, as of January 1, 2025, no local jurisdiction that has a local lodging tax can apply **additional reporting requirements** or standards to an intermediary that aren't similarly applied to all marketplace facilitators. This goes for the state's famously independent home-rule jurisdictions as well as other localities.

Kelly R. Smith believes this will relieve quite a bit of burden for her team. "However, similar rulings in other states have been challenged as an 'overstep' of the state's authority," observes Pam Knudsen. "In June 2024, Florida Governor Ron DeSantis vetoed legislation that would have prevented local governments from enforcing existing STR ordinances or passing new STR measures. This will continue to be an ongoing discussion in various states."

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HONEST PRICING LAW BREAKDOWN

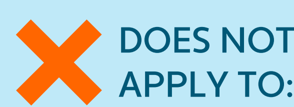
Source: California Office of the Attorney General

APPLIES TO:

- Most goods and services for a **consumer's personal use**

REQUIRES:

- Advertisements for a good or service to **include all mandatory charges**



DOES NOT APPLY TO:

- Goods or services for **commercial use**
- Food or beverages **sold by a restaurant, bar, or grocery store**

EXCLUDES:

- **Government-imposed** taxes or fees
- Reasonable **shipping costs** for physical goods

California prohibits hidden fees

As of July 1, 2024, California prohibits lodging platforms (and hotels and short-term rental businesses themselves) from hiding cleaning fees, pet fees, and assorted other fees. As the California Attorney General explains, the state's **Honest Pricing Law or Hidden Fees Statute** "makes it illegal for most businesses to advertise or list a price for a good or service that does not include all required fees or charges other than certain government taxes and shipping costs."

This should help cut down on customer dissatisfaction over junk fees.

According to Nicole Rogers, most larger OTAs are treating the requirement as global and not just applicable for California-based consumers. They may be wise to do so, since California isn't acting in isolation.

- **Congress** has considered legislation to prohibit unfair and deceptive advertising of hotel room rates and other short-term lodging prices.
- The **Federal Trade Commission** is working on a rule to prohibit "unfair and deceptive fees" and establish "enforcement teeth."
- **Connecticut** considered a bill to require fee disclosures.
- **New York** now prohibits hidden fees on admissions charges.
- **Minnesota** is requiring businesses to include mandatory fees in their advertised price as of January 1, 2025.

California's new law is just one of many compliance requirements affecting OTAs and STR lodging platforms, as well as hotels and STRs that make direct bookings. Compliance with STR tax regulations certainly isn't getting any easier for short-term rental operators.

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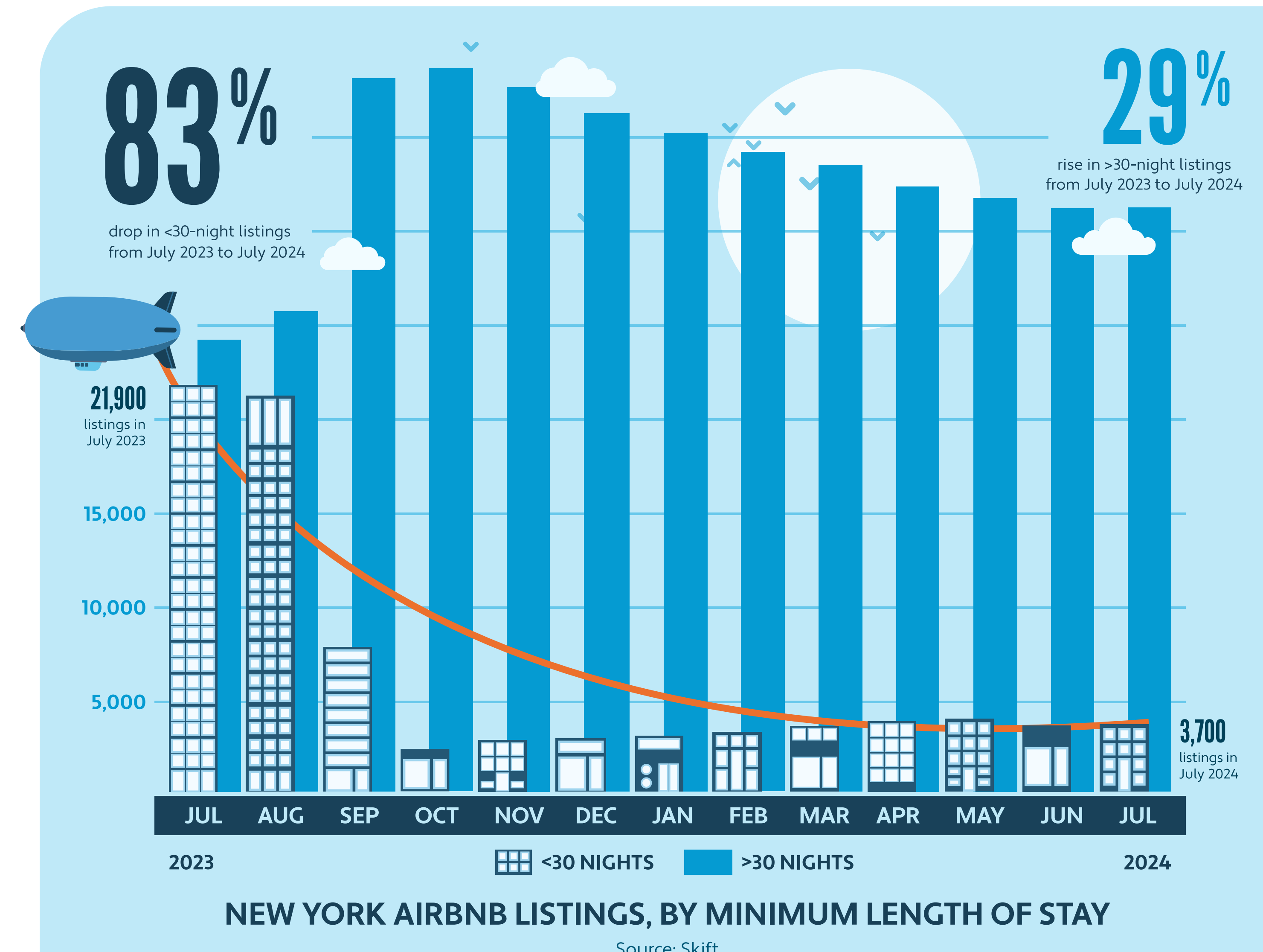
STR tax regulations and compliance challenges

How the rise of STRs is reshaping lodging tax regulations

In addition to updating obligations for lodging marketplaces, many state and local governments are changing tax and compliance requirements for short-term rentals. There's a great deal of opportunity here: In 2023, the [U.S. short-term rental market was valued at $66 billion] and accounted for 20% of the U.S. accommodation sector.

Still, a growing number of communities seem to be reaching the conclusion that less is more when it comes to short-term rentals. New regulations in some jurisdictions allow only owner-occupied STRs, cap the number of STRs, and/or double down on enforcement.

Two of the most extreme examples have emerged in New Orleans and New York City: New Orleans now allows only one owner-occupied STR per city block. New York City has capped the number of STRs at one per host, with no more than two paying guests



NEW YORK AIRBNB LISTINGS, BY MINIMUM LENGTH OF STAY

Source: Skift

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at a time. The property must be the host's permanent residence and hosts must be present while guests are there. Locks on internal doors are not allowed.

Other jurisdictions are following the lead of New Orleans and New York City, in some capacity. These include **Maui County**, Hawaii; **Narragansett**, Rhode Island; **South Burlington**, Vermont; and various communities in California.

"For individuals that travel and previously rented out their apartment or flat while they were gone, this loss of income has caused a hardship in being able to afford their own living quarters. Regulations that are too stringent can potentially have the opposite effect on the problem they are trying to solve," explains Knudsen. "A holistic approach that takes into account all stakeholders is critical."

Moreover, Knudsen wonders how these types of policies will be enforced on an ongoing basis. "How is a jurisdiction going to track the number of days an owner stays in their house? Who's going to stay on top of that? Regulations that don't have a methodology for enforcement end up having limited value."

Property owners and lodging platforms have challenged the more restrictive local ordinances with mixed results. New Orleans and New York City won the right to proceed with their ordinances. But in December 2023, a **judge blocked a more lenient Dallas STR law**. If such lawsuits persist, as they undoubtedly will, the issue may end up before the U.S. Supreme Court.

Many travelers have grown accustomed to the benefits short-term rentals provide: kitchens, privacy, room to spread out. Some won't want to share a host's primary residence. Some may need lodging for more than 90 or 180 days per year.

Enter extended stay hotels.

PAM KNUDSEN
Senior Director of Compliance Services at Avalara

Regulations that are too stringent can potentially have the opposite effect on the problem they are trying to solve.

A holistic approach that takes into account all stakeholders is critical.

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How hotels are competing in the short-term rental market

The global extended stay hotel market is expanding. **Future Market Insights** predicts it will grow at an estimated compound annual growth rate of 11.8% from 2023 to 2033, when it will achieve a value of $166.58 billion. To put that in perspective, the extended stay market was about $49.15 billion in 2022.

Who stays in extended stay accommodations? Construction workers, **corporate executives**, entertainers, interns, journalists, and traveling healthcare professionals, as well as people whose homes have been damaged or destroyed by fire, floods, and other natural disasters – a community that will likely grow in the coming decades.

Some extended stayers prefer the amenities offered by hotels. Others favor corporate housing specialists because they provide a single point of contact and may offer **lower prices** than hotels or short-term rentals.

How do hotel and lodging taxes work with extended stays, since policies were originally intended for short terms and transient occupancy?

Source: Future Market Insights

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How extended stays impact hotel and lodging tax compliance

State and local lodging taxes generally don't apply to extended stays. Unfortunately, what qualifies as an extended stay in one state may be considered a short-term stay in another state.

Navigating the complexities of long-term stay tax rules

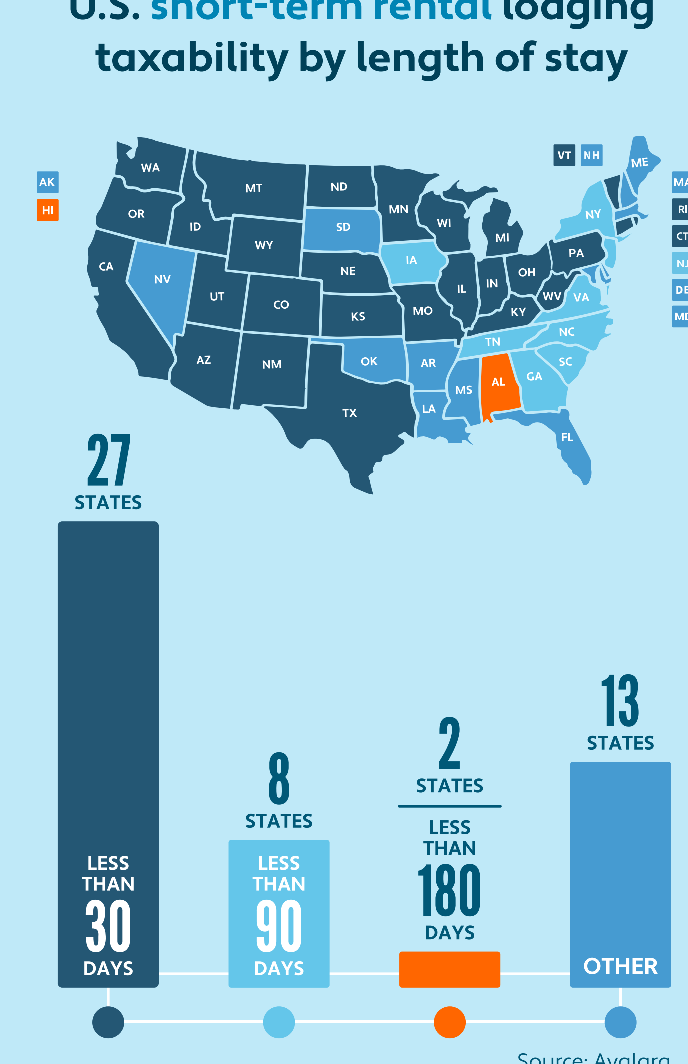
Hotel and lodging taxes apply to stays of less than 30 days in most parts of the country, but length-of-stay thresholds vary by location. For example:

- Stays of less than 90 days are subject to lodging tax in New York and Virginia.
- Stays of less than 180 days are subject to lodging tax in Alabama.
- Stays of six months or less are subject to lodging tax in Florida.

Some jurisdictions have different thresholds for different types of lodging. In Massachusetts, the taxable rental length of stay is 31 consecutive calendar days for STRs but 90 days or less for hotels, motels, bed-and-breakfasts, and lodging houses.

The more hotel brands move into the extended stay space, the more resources they may need to devote to lodging tax compliance issues. Depending on where the lodging is located and how stays are booked and invoiced, it may be necessary to collect tax then refund all or some of it.

Long-term stays booked up front typically present less of an issue because the provider can account for an exemption from the outset. Compliance can be more challenging when a guest extends a stay. In Texas, guests who notify a hotel in writing – beforehand – of their intention to stay 30 or more days are exempt from the day of notification. Yet guests who don't notify the hotel in advance must pay the tax on the first 30 days "and are exempt thereafter."



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Washington state has similar requirements. Sales tax applies to stays of less than 30 continuous days, but for longer stays, whether tax applies to the first 29 nights depends on how the stay is booked.

According to the statute, "A tenant who does not contract in advance to stay at least thirty days is not entitled to a refund of retail sales tax if the rental period later extends beyond thirty days." However, if from the outset a room is booked for 35 days or longer, it would immediately be treated as an extended stay and would therefore be exempt from Washington retail sales tax.

It's a lot to keep straight.

We can't emphasize enough that **different jurisdictions have different rules**. Some, like Washington, only provide a tax exemption for stays that exceed the extended stay threshold. In other states, the entire stay is eligible for a tax refund once the threshold has been met. Keeping track of which rules apply where is a bear. Of the grizzly variety.

And it's best to get tax right from the get-go. Conversations about tax eat up valuable time for staff and can be unpleasant for long-term guests. Who wants to haggle over tax when they could be visiting a museum, or attending a workshop, or writing a book?

Automating lodging and hospitality tax collection and remittance can save time for everyone involved while improving compliance for your brand. "Keeping track of the ever-changing rules and rates is complicated and time-consuming," says Pam Knudsen. "By automating these processes, you can free up your team's time to focus on your core objectives of providing excellent customer service."

PAM KNUDSEN
Senior Director of Compliance Services at Avalara

Keeping track of the ever-changing rules and rates is complicated and time-consuming.

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More new lodging tax compliance developments

There are too many new lodging tax developments to fit into one report, so here are a few standouts.

Maryland taxes rentals of home amenities

Maryland extended its sales tax to rentals of home amenities on July 1, 2024. The tax applies when residential properties in the state offer hourly rentals of specific amenities, such as a pool or tennis court, for up to (but not more than) 15 consecutive hours. Charges for the use of sleeping quarters aren't subject to the tax.

Home amenity rental providers, home amenity rental platforms, and home amenity rental intermediaries are responsible for collecting and remitting the Maryland home amenity rental sales and use tax. If the rental is facilitated by a home amenity rental intermediary or rental platform, the full cost charged to the buyer is subject to the tax. However, the taxable price doesn't include commissions paid by the provider to the facilitator of the sale.

Maryland could be a trendsetter with this. Marketplaces are creative and nimble and are facilitating more, and more specialized, sales (like the use of swimming pools and yards). Marketplace facilitator laws may not cover those transactions now, but once states realize what's happening, they will undoubtedly want the tax revenue.

Delaware taxes tax short-term rentals

Delaware has long had an 8% state accommodations tax on hotel stays, but the state's held out on taxing STRs and bed-and-breakfasts. That will change effective January 1, 2025.

House Bill 168 imposes a 4.5% statewide short-term rental lodging tax and requires "accommodations intermediaries" to collect and remit it. The bill also allows New Castle and Sussex Counties to impose up to a 3% local lodging tax on STRs; both counties are already authorized to levy a 3% local tax on hotel stays.

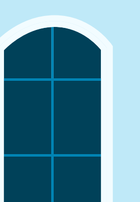
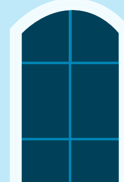
Maryland's definition of "home amenity"

A home amenity is **any portion – indoors or outdoors – of a residential property that is occupied by the hour for not more than 15 consecutive hours**. Examples of home amenity rentals include, but are not limited to, a backyard swimming pool, a backyard pickleball court, or an apartment building's clubroom or rooftop deck.

Maryland's definition of "home amenity rental"

A home amenity rental is the **temporary use**, in exchange for consideration of any kind, of a home amenity.

Source: Comptroller of Maryland

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Other updates to lodging tax laws

Upcoming tax changes include:

- Michigan freed certain cities and counties to increase the **local hotel-motel tax** on accommodations from 5% to 8%, provided voters approve the rate increase.
- Vermont instituted a new statewide **3% surcharge on STRs** effective August 1, 2024.
- Sangamon County, Illinois, was granted the authority to impose a **local hotel tax** of up to 3%.
- Honolulu increased **property taxes** for certain STRs as of July 1, 2024. STR owners who don't live in their STR properties will be charged $9 per $1,000 of value up to $800,000 and $11.50 for anything above that. The previous rate was $4 per $1,000 of assessed value up to $1 million.

Looking ahead, Alaska may implement a **6% statewide bed tax**. The idea was floated in January 2024 but didn't gain traction, even after State Representative Andrew Gray told the committee he might **add a tax cap** and/or provide an exemption for Alaska residents. Still, this is something to watch for in 2025.

If Alaska does eventually establish a state bed tax, will it require lodging platforms to collect and remit it? Marketplace facilitators currently aren't required to collect or remit **local bed taxes in Alaska**.

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You can't hide, so you may as well comply

Varied and changing lodging tax and STR regulations in effect throughout the country make compliance challenging for accommodations platforms, hotels, and short-term rental operators. But complying with registration and tax requirements is essential.

In the current environment, tax authorities are particularly interested in noncompliant STRs. Some jurisdictions are even hiring companies to search and find unregistered properties. AI, data mining, and data scraping tools are also proving to be immensely useful no matter who's doing the looking.

Knudsen says new technologies now enable jurisdictions to search state databases as well as platforms and other rental sites to identify properties in their jurisdiction. "By matching that information against registered STRs, they can identify noncompliant rentals and go after them for back taxes and penalties – which can be significant."

We expect to see even more effective use of these tools in 2025, which will make it even harder for noncompliant STRs to operate under the radar.

The consequences of noncompliance can be severe. If you aren't registered and compliant, you can't have a voice in your community or advocate for your business. If you're found out of compliance, your permit could be revoked for years. If you fail to renew your license/permit in jurisdictions that have capped the number of STRs, you may lose it.

If you neglect to collect and remit taxes, you can end up paying years' worth of back taxes out of pocket. And not just lodging taxes. While lodging tax may be the initial focus of tax authorities, lodging providers may also be liable for a number of other taxes, including personal property tax. STRs that sell drinks to guests may owe beverage alcohol taxes, those that sell other swag may owe sales tax.

"The presence of a short-term rental by default creates an obligation to collect and remit all applicable taxes, not just lodging tax," explains Knudsen. "So, a property that offers other services or fees (e.g., pet fees) may be required to collect and remit additional taxes."

How Avalara can help

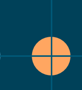
Avalara can help you account for tax changes and improve tax compliance for your business. Learn more about our automated solutions for tax research, calculating tax rates, preparing returns, and managing documents.

Solutions

HOSPITALITY

SHORT-TERM RENTAL

Up next: Beverage alcohol



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Beverage alcohol, communications, and excise

Tax compliance is especially complex for specialized industries like beverage alcohol, communications, energy, tobacco, and vape. For years, manufacturers and retailers that sell these distinct products and services have been subject to countless federal, state, and local jurisdiction rules that constantly change. 2025 will be no exception as businesses seek to adjust to regulatory shifts stemming from recent court decisions and new legislation. Find out what lies ahead to help keep your company ready to ride the ups and downs.

What's ahead:

- **Beverage alcohol**
- **Communications**
- **Excise**

What the numbers tell us

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states and the District of Columbia have enacted laws to permanently allow cocktails to go, and 5 states allow cocktails to go on a temporary basis

Source: Distilled Spirits Council of the United States

70%

Direct sales make up almost 70% of total sales on average for small wineries

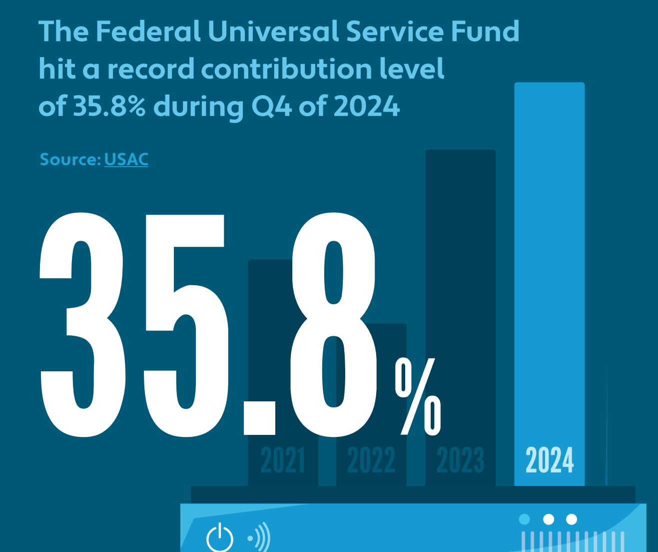
Source: Silicon Valley Bank

COMMUNICATIONS

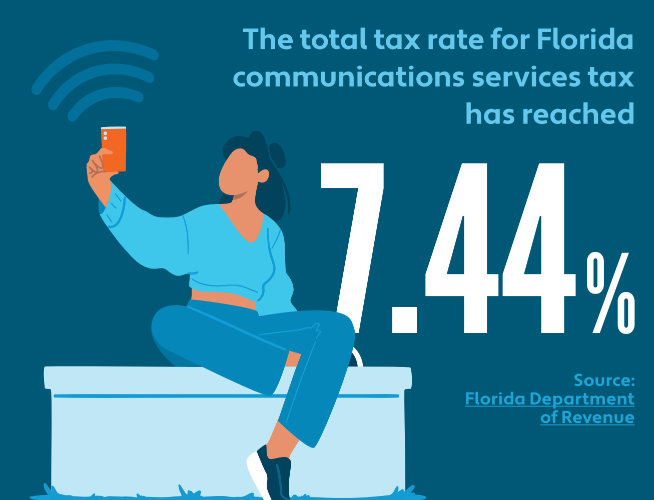
The Federal Universal Service Fund hit a record contribution level of 35.8% during Q4 of 2024

Source: USAC

35.8%



The total tax rate for Florida communications services tax has reached

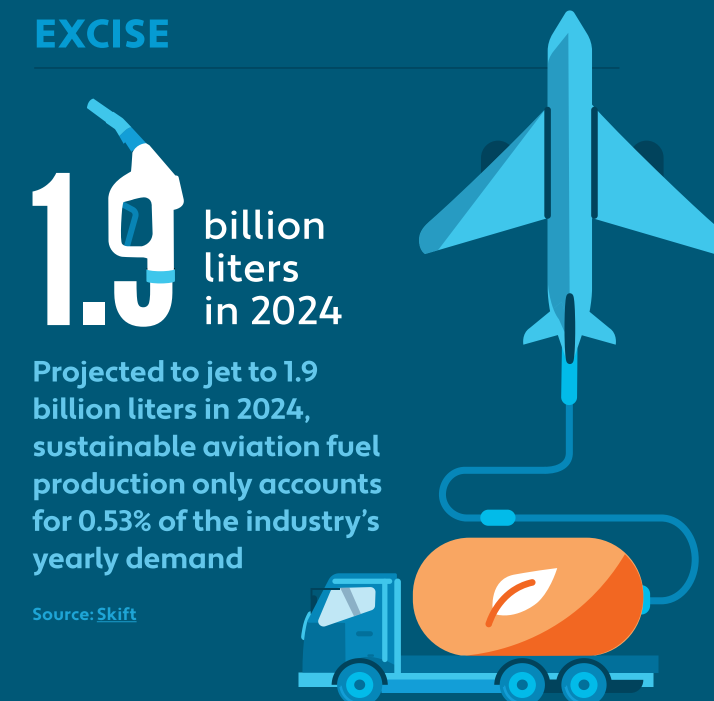


7.44%

Source: Florida Department of Revenue

EXCISE

1.9 billion liters in 2024



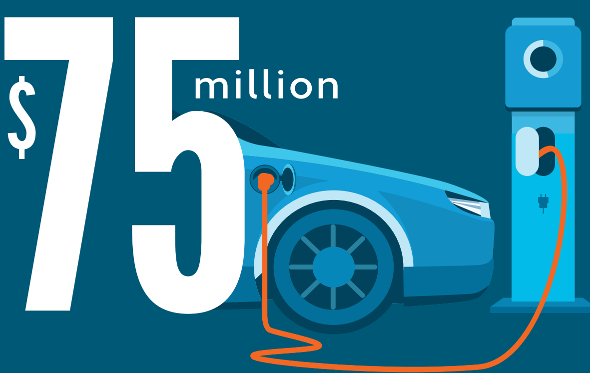
Projected to jet to 1.9 billion liters in 2024, sustainable aviation fuel production only accounts for 0.53% of the industry's yearly demand

Source: Skift

The phaseout of New Jersey's sales and use tax exemption for zero-emissions vehicles is expected to generate $75 million in 2025

Source: NJ Spotlight News

$75 million



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Beverage alcohol

Beverage alcohol businesses have a lot to look forward to in 2025 thanks to changing tax policies that make it easier to sell ready-to-drink products and cocktails to go. But they'll have to continue navigating complex regulations as states take different approaches to direct-to-consumer (DTC) shipping, licensing, and product registration requirements. Blend in a slew of rate changes and the compliance landscape for wineries, distilleries, and breweries remains fluid.

States ease tax burdens as RTD sales expand

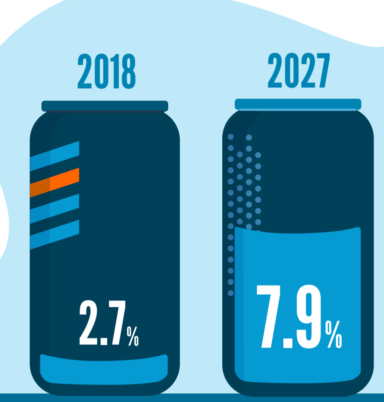
Ready-to-drink (RTD) products remain popular among consumers and the number of brand lines available in the U.S. more than tripled between 2018 and 2022. Despite flat volume growth since 2022, the category is expected to capture 7.9% of the total U.S. beverage alcohol market by 2027.

As more RTD products enter the market, some states are relaxing their tax policies. North Carolina lowered its tax rate for spirit-based RTDs effective June 28, 2024. Senate Bill 527 defines a premixed cocktail as those 24 ounces or less with a maximum alcohol by volume (ABV) of 13%. SB 527 also exempts these drinks from the state's mixed beverage tax of $20 per four liters when sold to an on-premises mixed beverage permit holder such as a bar or restaurant for resale.

More Pennsylvania retailers can now sell RTD cocktails. The Legislature approved SB 688, now known as Act 86 of 2024, allowing convenience and grocery stores, restaurants, and bars to obtain a special permit to sell the canned drinks effective September 16, 2024. Previously, only state-owned wine and liquor stores were allowed to sell the drinks.

Pennsylvania's law defines RTD cocktails as premixed spirit-based beverages up to 16 ounces with a maximum ABV of 12.5%. The Pennsylvania Liquor Control Board began accepting permit applications on August 27, 2024. Businesses that wish to apply for the permit will pay $2,500 per establishment plus an annual renewal fee of 2% of the RTDs sold to be consumed off premises. Legislative analysts project sales will bring in about $35 million a year in state revenue by the 2028–2029 fiscal year.

Maryland considered a bill in 2024 that would have created a new tax category for RTDs. House Bill 663 sought to define an RTD cocktail as "a beverage that contains distilled spirits mixed with nonalcoholic beverages and may contain wine" with an ABV of 12% or less. The bill would have reduced the excise tax rate applied on RTDs to $0.40 per gallon, the same rate currently applied to wine. Maryland introduced a similar bill in 2022. However, neither bill made it out of the Ways and Means Committee before the session ended.



RTDs' share of total beverage alcohol servings in the U.S.

Source: IWSR

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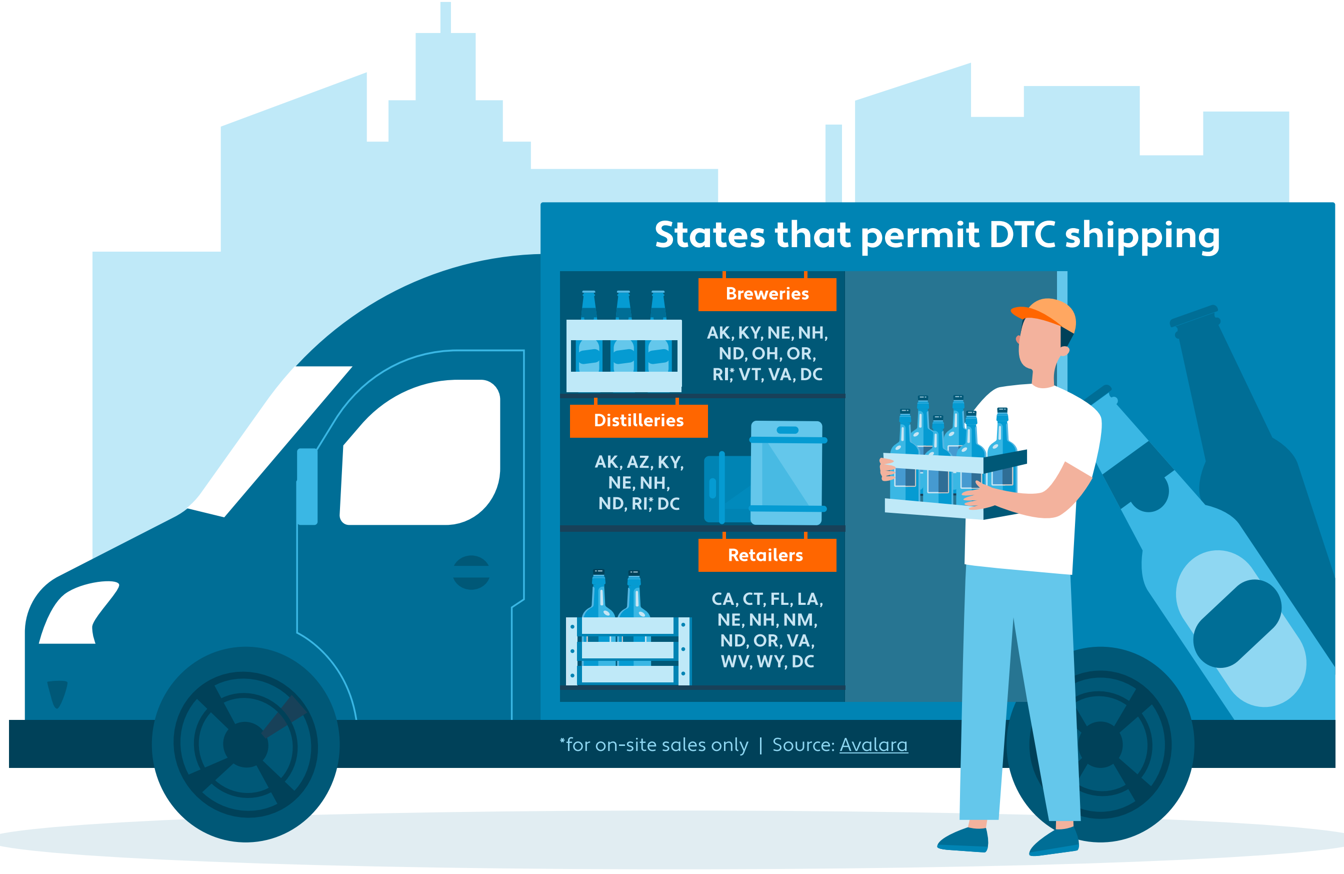
Some states tighten the reins on DTC shipping; others loosen grip

Selling wine directly to consumers (DTC) is a critical business strategy for wineries – and often the most profitable one. Direct sales make up almost 70% of total sales on average for small wineries, according to one survey. As more buyers seek to have their favorite cabernet sent directly to their door, states frequently update their regulations around DTC shipping. It's not just wine that gets the attention. More states are considering DTC legislation for beer and spirits.

"Beverage alcohol businesses that ship directly to consumers are not only faced with obtaining direct shipper licenses in most states, they may also be responsible for reporting and paying excise tax, sales and use tax, and markup tax, depending on the jurisdiction," says Shannon Fahey, Indirect Tax Researcher at Avalara.

"These taxes are often statutory requirements associated with the license itself, or, in the case of some sales and use tax requirements, they may be triggered by economic nexus," she explains. "Rates, forms, filing methods, and other details associated with the required taxes and/or licenses may be subject to change each year, sometimes multiple times in a year. These changes may be triggered by new or updated legislation, regulations, or even simple operating methods of the agencies responsible for these taxes, licenses, etc. The world of beverage alcohol compliance is dynamic, which can pose a challenge for industry members."

Out-of-state wineries can ship DTC in most states and Washington, D.C. Only Delaware, Mississippi, and Utah ban **all** DTC shipping, while Arkansas and Rhode Island allow on-site wine shipments but not off-site shipments. In comparison, out-of-state breweries can ship to consumers in 10 states plus Washington, D.C., and out-of-state distilleries can ship into just seven states and Washington, D.C.



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SHANNON FAHEY
Indirect Tax Researcher
at Avalara

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... The world of beverage alcohol compliance is dynamic, which can pose a challenge for industry members.

Craft distillers can continue to ship DTC within California, a privilege available to them since September 29, 2022. The Legislature enacted the original temporary law, then on September 20, 2024, the governor approved a second one-year extension for the "purpose of providing limited relief to manufacturers recovering from pandemic-related impacts." The bill extends the authorization to ship distilled spirits within California until January 1, 2026.

Wisconsin is putting more stringent conditions in place for third-party shippers. Effective January 1, 2025, all common carriers and fulfillment houses that ship wine DTC in Wisconsin will need to obtain a permit from the state, provide monthly reports on their shipping activity, and make certain their shipments comply with state regulations. Adopted by the Legislature in December 2023, SB 268 also subjects carriers and fulfillment houses to fines of up to $10,000 for shipping without a permit and $2,000 for failing to submit a report. Shipping alcoholic beverages other than wine would result in a $2,000 fine for the first offense and revocation of the permit for a second offense that occurs within a year. The common carrier language in SB 268 was amended in 2024 to ensure that FedEx and UPS could continue to ship wine to consumers under the new law, effective January 1, 2025.

At least two bills (A871 and S1581) introduced in New Jersey aim to remove the state's production cap to allow larger wineries producing more than 250,000 gallons in a year to ship into the state. But, there's been no movement yet. New Jersey is the last state to have a production cap for winery DTC shippers.

Bills recently introduced in Delaware (HB 259) and Mississippi (HB 1561 and HB 430) would have made it possible for businesses to ship DTC but died in committee.

Prior to January 1, 2024, beverage alcohol producers didn't need a license to ship DTC in Alaska. The state's Title 4 Rewrite overhauled, among other things, licensing requirements for direct shippers. However, some direct shippers found it difficult to comply with the initial requirements. Final rules governing DTC shipments to Alaska were adopted to remedy the problem and became effective August 23, 2024. According to Wine Institute, "The new rules replace the interim rules that wineries were unable to comply with and now mirror the SB 9 statutory requirements." DTC wine shipments in Alaska are subject to the state's $2.50 per gallon excise tax. Alaska doesn't have a statewide sales tax but many local jurisdictions levy a sales tax.

Minnesota doesn't require a license to ship DTC but imposes a 50-cent retail delivery fee as of July 1, 2024. The rule applies to DTC wine deliveries in the state if the transaction is $100 or more and the seller had retail sales totaling at least $1 million in Minnesota in the previous year.

These changes highlight both opportunities and challenges that lie ahead for beverage alcohol businesses looking to reach more consumers through direct sales.

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Shifting recycling and registration requirements can lead to confusion

It's been more than two years since California passed legislation extending its bottle bill to containers holding wine and distilled spirits. And more than a year since updated rules went into effect requiring wineries, distilleries, and distributors to register for the bottle redemption program.

Previously, the only alcoholic products covered by the California Beverage Container Recycling and Litter Reduction Act were beer, malt beverages, wine coolers, and distilled spirits coolers with 7% ABV or less. The updated rules took effect January 1, 2024. They require "distributors," which includes wholesalers, wineries, and distilleries that sell directly in California, to pay a container redemption value. Consumers pay a deposit that's refunded when they return their empty container.

Despite a long lead time, some producers say they were caught off guard by the new requirements and at least one compliance specialist expressed frustration with the state's registration system. Three months into the new rules, authorities had processed 2,550 registrations and added staff to address a backlog.

Starting July 1, 2025, the following products will need to be labeled with a California Redemption Value message to be sold or transferred in California:

- Distilled spirits
- Wine, or wine from which alcohol has been removed, in whole or part, whether or not sparkling or carbonated
- Wine and distilled spirit coolers with greater than 7% ABV

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Other states are also making changes to regulations that impact allowed containers and registration requirements.

Florida recently updated its law to allow the sale of wine in larger bottles. HB 583 took effect July 1, 2024, and added five glass container sizes: 4.5 liters, 6 liters, 9 liters, 12 liters, and 15 liters. Distributors and manufacturers can sell wine to other distributors and manufacturers in any size container.

SHANNON FAHEY
Indirect Tax Researcher at Avalara

> **We're seeing more states evaluating how they can include beverage alcohol products in their recycling requirements.**
>
> **... The ever-changing nature of beverage alcohol compliance requirements highlights the need for beverage alcohol companies to stay ahead of regulatory changes ...**

"We're seeing more states evaluating how they can include beverage alcohol products in their recycling requirements," says Fahey. "These policies can vary widely, from alcohol container registrations to container and material reporting requirements, and from updated bottle bills to extended producer responsibility (EPR) programs."

Fahey adds, "The ever-changing nature of beverage alcohol compliance requirements highlights the need for beverage alcohol companies to stay ahead of regulatory changes to ensure they remain compliant."

More states make cocktails to go permanent and redefine delivery laws

Getting a cocktail delivered to your home with your Thai curry order is a convenient perk for consumers in states that allow restaurants and bars to sell boozy beverages for delivery and takeout.

Colorado, Indiana, Maryland, Massachusetts, North Carolina, and Virginia enacted laws in 2024 that make to-go cocktails permanent. New York's budget extended cocktails to go for another five years to 2030. That makes 29 states and the District of Columbia that have enacted laws to permanently allow cocktails to go, and five others that enacted laws that allow to-go cocktails on a temporary basis as of July 2024.

Fewer states allow cocktails to be delivered and without further action, laws are set to sunset in some states.

- The law in Massachusetts includes a caveat: Licensed establishments can no longer sell wine or beer for off-premises consumption unless it's part of a mixed drink effective April 30, 2024.
- Vermont's law that allows licensed establishments to sell alcohol for off-premises consumption is set to end July 1, 2025.
- Washington made the sale of to-go alcoholic beverages permanent in 2023 but the ability to deliver alcoholic drinks in Washington is scheduled to be repealed July 1, 2025.

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States that signed legislation to make cocktails to go permanent into law

States are also taking action on alcohol delivery beyond cocktails.

- **Delaware** allows restaurants, pubs, taprooms, taverns, and other licensed establishments to deliver liquor as of September 6, 2024.
- **Maryland** allows distilleries, breweries, and wineries to deliver their own products directly to Maryland consumers effective July 1, 2024. The law replaces temporary delivery and shipping privileges put in place during the pandemic.
- **Kentucky** allows craft distilleries to sell and deliver directly to retailers effective April 5, 2024. SB 50 permits a craft distiller to self-distribute up to 5,000 gallons of distilled spirits per year directly to a licensed retailer.
- **Virginia** will repeal **third-party delivery licenses** effective July 1, 2026. The passage of SB 635 requires the Virginia Alcoholic Beverage Control Authority to study the issue.

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States continue to implement rate changes

Beverage alcohol businesses also need to be ready to comply with rate changes, which can occur at any time. Recently enacted changes include:

- **Utah's annual omnibus liquor bill** increases the tax on beer incrementally to $13.60 per barrel effective July 1, 2025, and eventually to $14.10 per barrel in 2027. The bill increased the markup for spirits, wine, and malt liquor from 88% to 88.5% and heavy beer from 66.5% to 67% effective May 1, 2024.
- Effective July 1, 2024, **Mississippi increased its bailment fee** charged to manufacturers of spirits and wine from $1 per case to $1.50 per case stored in the state's Alcohol Beverage Control warehouse.
- **Alabama SB 309** changed the additional state sales tax rate on the sale of alcoholic beverages at Alcoholic Beverage Control stores from 2% to the combined county and municipal general sales tax rates levied or assessed in the county or municipality where the transaction occurs. The combined average of the county and municipality tax rates is 5.3% effective October 1, 2024.

Some proposed changes didn't make it into law.

Rhode Island lawmakers tried, not for the first time, to establish a sales tax exemption for beer and malt beverages sold at liquor stores. **H7277** died in committee. Wine and spirits are already exempt from sales tax in Rhode Island. Beer and malt sales accounted for approximately **$135.49 million**, or 31.19%, of gross sales of alcoholic beverages by liquor stores in the state in 2023.

There's still more brewing in the beverage alcohol industry but this is just a snapshot of the top issues affecting the industry. If these updates have your head spinning, software can help make compliance easier by automating tax calculation, shipping verification, licensing, returns, product registrations, and tax research.

How Avalara can help

Avalara tax automation solutions for wineries, breweries, distilleries, and other businesses in the industry can mitigate compliance risk. Learn more about our complete solution for licensing, product registrations, tax calculation, and filing for beverage alcohol businesses.

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Communications

Nothing jolted the communications industry more than the recent court ruling that declared the Federal Universal Service Fund a tax and found it unconstitutional. In 2025, courts will continue to weigh in on matters important to telecom providers as states amend definitions, rules, and rates to keep up with the pace of changing technology. Businesses will need to stay on top of continuously changing regulations to maintain compliance going forward.

Court rules FUSF is unconstitutional

For years, the Federal Universal Service Fund (FUSF) wasn't considered a tax. But on July 24, 2024, a decision by the **United States Court of Appeals for the Fifth Circuit** shook up the telecommunications world. The court not only ruled the FUSF assessment is a tax but declared it unconstitutional.

The case could have significant ramifications for both the communications industry and the programs that depend on FUSF contributions.

"The Fifth Circuit ruled that Congress and the Federal Communications Commission are deferring their tax-imposing authority to a third party and that violates Article 1, Section 1 of the U.S. Constitution. The decision is the biggest news in the communications tax world in 20 years. The U.S. Supreme Court is almost certain to consider the case," says Toby Bargar, Senior Tax Strategist for Avalara for Communications.

The FUSF was created to provide phone service to rural areas, low-income households, schools, libraries, and health care providers. The Federal Communications Commission (FCC) established the fund in 1997 in compliance with the Telecommunications Act of 1966. In 2011, the agency approved using the fund to extend broadband.

The fund is administered by a quasi-public agency called the **Universal Service Administrative Company** (USAC) under the direction of the FCC. The USAC sets the annual budget and the FCC collects the money from telecom companies based on their revenues. The telecom providers, in turn, add those costs to their customers' bills.

TOBY BARGAR
Senior Tax Strategist for Avalara for Communications

The Fifth Circuit ruled that Congress and the [FCC] are deferring their tax-imposing authority to a third party and that violates Article 1, Section 1 of the U.S. Constitution.

The decision is the biggest news in the communications tax world in 20 years.

"The Fifth Circuit determined that the FUSF isn't a surcharge or a fee – it's a tax. The **Sixth** and **Eleventh** Circuits previously upheld the constitutionality of the FUSF. It's long been considered a regulatory imposition, which explains why this latest ruling is highly controversial," says Bargar.

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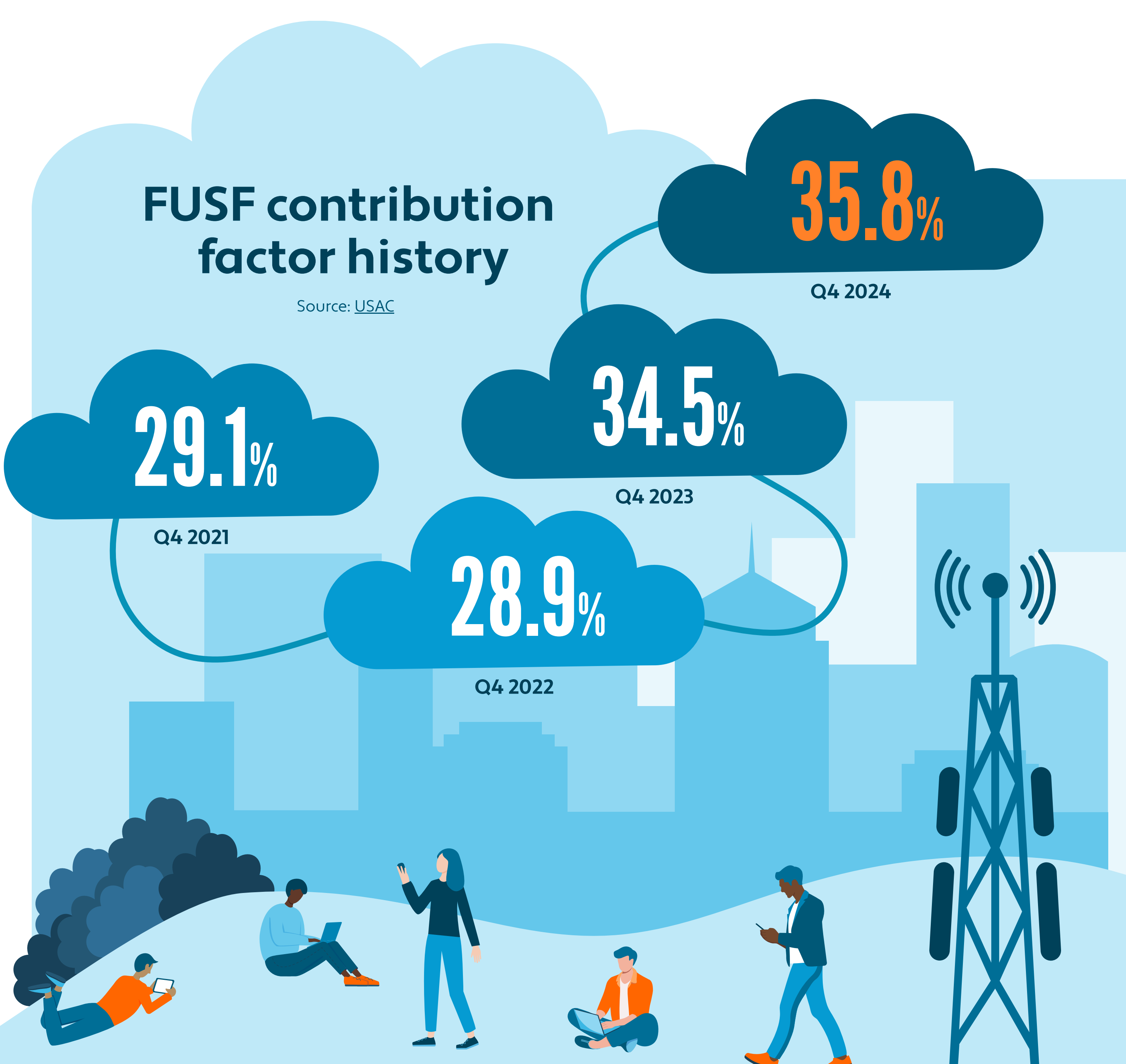
According to Bargar, the Fifth Circuit's ruling is similar to the recent U.S. Supreme Court decision that overturned Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc. The Chevron doctrine was established in 1984 and required courts to defer to federal agencies' interpretations of ambiguous legislation.

"A lot of phone companies depend on the money that comes from the FUSF to build their networks and infrastructure. Many in the communications industry might have wanted some modifications to how the fund works but I don't think anyone wants to see it abolished. That could potentially happen unless Congress is able to come up with a bipartisan solution," Bargar says.

"Federal Universal Service Fund reform has moved at a glacial pace. Now, all of a sudden, it could change in one fell swoop. Especially with the results of the 2024 presidential election, everyone is holding their breath waiting to see what will happen," says Steve Lacoff, General Manager of Avalara for Communications.

The FUSF hit a record contribution level of 35.8% during Q4 of 2024. Internet service providers aren't required to pay into the FUSF, but they might be in the future if internet service is reclassified as a necessary utility and a funding mechanism remains in place.



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Defining a telephone business in Washington state

Under Washington law, a "telephone business" is **"the business of providing network telephone service"** and "network telephone service" is in part **"the providing by any person of access to a telephone network."** In other words, a telephone business provides **access** to a telephone network.

Source: Washington Court of Appeals

Washington's broad definition of "telephone business" could have further implications

Can a company be considered a "telephone business" if it has no physical telecommunications infrastructure of its own? The question was addressed as part of a recent ruling by the **Washington Court of Appeals** that found TracFone Wireless subject to the City of Renton's municipal utility tax.

TracFone buys prepaid airtime from third-party cellular networks, which it resells to individual customers and retailers. The company argued it shouldn't be considered a "telephone business" under state law and its wholesale sales should be exempt from the city's tax.

The court found that TracFone meets the statutory definition of a telephone business because it provides access to numerous telephone networks. The court also found that because customers rely on TracFone to activate and maintain their access to the network, the resale exemption doesn't apply.

"This ruling has significant implications for other companies operating under similar business models, as it affirms the broad taxing authority of municipalities over utility services," noted the **Sales Tax Institute**.

California court addresses tax on cell phones bundled with service

It's common for mobile phone companies to entice consumers with deals on the newest smartphones on the condition that those customers agree to a service contract. The **California Court of Appeal for the Third Appellate District** recently held that the purchase of a discounted cell phone bundled with wireless services is subject to sales tax based on the phone's full price, not the reduced cost.

The court relied on California Code of Regulations, Title 18, **Regulation 1585** while ruling in favor of the California Department of Tax and Fee Administration. The regulation defines a "bundled transaction" as "the retail sale of a wireless telecommunications device which contractually requires the retailer's customer to activate or contract with a wireless telecommunications service provider for utility service for a period greater than one month as a condition of that sale."

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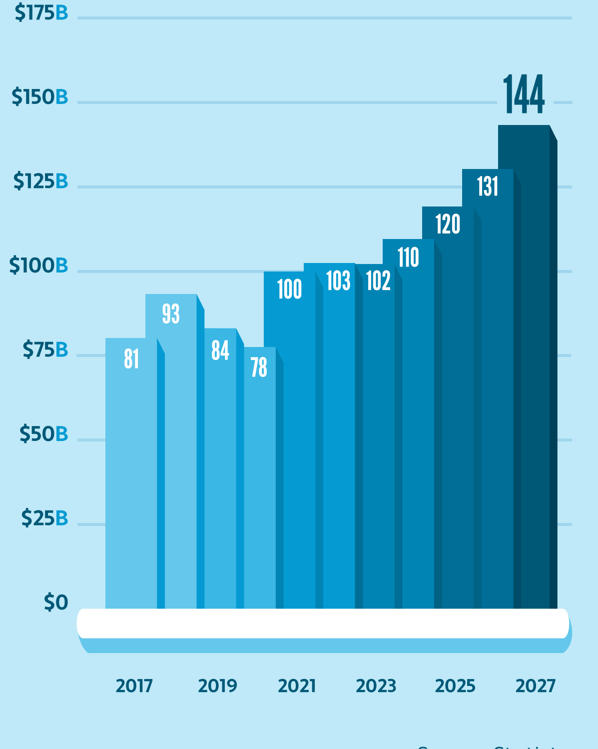

Source: Statista

The court found, "The carrier-retailers do not offer a true discount on the cell phones because they are compensated by the monthly payments in a bundled transaction." Therefore, sales tax should be applied to the full price of the phone.

The court also considered Regulation 1585's history, noting the regulation became operative in 1999 and hasn't been amended since. "An agency's interpretation is likely to be correct if it 'has consistently maintained the interpretation in question, especially if [it] is long-standing,'" the court wrote.

"The impact of this ruling could trickle down to other jurisdictions beyond California," says Bargar. "Telecommunications companies need to have a solution in place to calculate and collect any new taxes on their products."

"Consumers also need to be prepared to pay more," Bargar added, especially as revenues from smartphone sales in the U.S. are projected to grow to nearly $143.7 billion by 2027.

Vermont revamps communications taxes while industry struggles with property tax challenges

Upgraded smartphones come out every year. But states overhaul their communications tax laws far less frequently. Vermont decided the time to modernize its communications taxes and fees is now. The passage of H 657 includes several significant changes that take effect July 1, 2025.

The new law has three major components:

- It expands and increases Vermont's Universal Service Charge. The rate changes from 2.4% of retail telecommunications service to 72 cents for each retail access line in service.
- It repeals the state's telephone personal property tax (telephone tax). However, the state's alternative telephone gross revenues tax will remain in effect until January 1, 2026.
- It redefines communications property as real property. The law applies to personal property taxed at the local level, known as grand lists, that are lodged on or after April 1, 2025.

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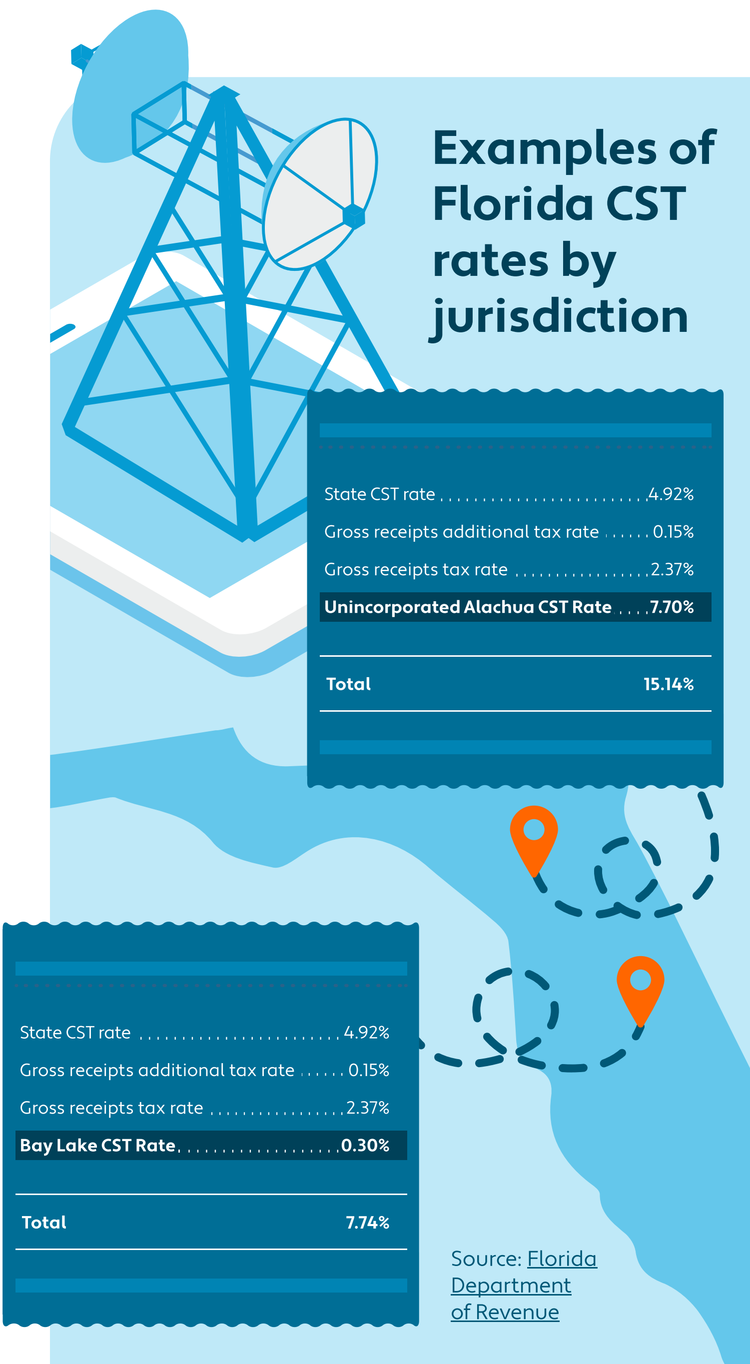
Vermont isn't the only state where communications taxes and property taxes intersect. Telecommunications companies throughout the country deal with property tax compliance hurdles as well.

"Telecom providers have property tax challenges that other businesses don't. They own cables and electronic infrastructure that cross jurisdictional boundaries. They have additional liabilities," says Carl Hoemke, General Manager of Avalara Property Tax. "Wisconsin recently eliminated taxes on personal property for most businesses but deferred the exemption for telecommunications companies 'beginning with the assessments as of January 1, 2027.' Trying to manage personal property tax returns manually drains their teams, which is why more companies like Comcast are switching to an automated property tax compliance solution."

Other communications industry tax changes

There's a flurry of other recent changes and more to come in communications tax compliance. Here are a few that stand out:

- Florida extended its communications services tax (CST) to include streaming services providers back in 2012. Netflix started charging customers the tax on February 15, 2024. Streaming customers in Florida now pay an additional 5.07% as well as any local communications taxes on top of their usual bill. The total tax rate for Florida communications services tax has reached 7.44%. When adopted in 2001, the tax was hailed as a means to simplify Florida's telephone tax laws.
- Massachusetts and New York both introduced bills in 2024 to tax streaming providers but they haven't received much traction. Similar bills were under consideration in Vermont and Virginia but died in committee.



Examples of Florida CST rates by jurisdiction

Rate	%
State CST rate	4.92%
Gross receipts additional tax rate	0.15%
Gross receipts tax rate	2.37%
Unincorporated Alachua CST Rate	**7.70%**
Total	**15.14%**

Rate	%
State CST rate	4.92%
Gross receipts additional tax rate	0.15%
Gross receipts tax rate	2.37%
Bay Lake CST Rate	**0.30%**
Total	**7.74%**

Source: Florida Department of Revenue

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- Illinois amended several provisions in its telecommunications law. HB 3144 changed the definition of "prepaid telephone calling arrangements" subject to the retailers' occupation tax. The legislation clarifies that the definition applies to telephone or telecommunications services obtained through the purchase of a preloaded phone, calling card, or other item of tangible personal property made on or after January 1, 2025.

  The bill also allows a home-rule municipality with a population exceeding 500,000 the ability to impose a prepaid wireless 911 surcharge not to exceed 9% per retail transaction. Chicago's 9% rate took effect November 1, 2024. HB 3144 allows home-rule surcharges to remain in place until July 1, 2029.

- Louisiana passed legislation creating state and local sales and use tax rebates on the sale of certain communications and data center equipment, including fiber-optic cable. Rebates provided under HB 827 apply to purchases made on or after July 1, 2024.

What we've shared represents a small speck of what's happening in the communications industry world but we'll leave you here for now.

How Avalara can help

Staying on top of changing legislation and complying with communications tax requirements is easier with Avalara for Communications. Avalara provides a complete suite of solutions to handle calculations, file returns, and reduce risk for businesses in the communications industry.

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Excise

Excise tax compliance presents numerous challenges for energy, fuel, tobacco, and vape companies and for convenience stores that sell products that span all these industries. Amid new taxes and duties, fewer tax breaks for electric vehicles, and the emergence of new renewable energy products, something is always changing. Companies responsible for collecting and remitting excise taxes will need to evaluate their business practices to remain competitive and stay in good standing with authorities.

Renewable fuels complicate taxation

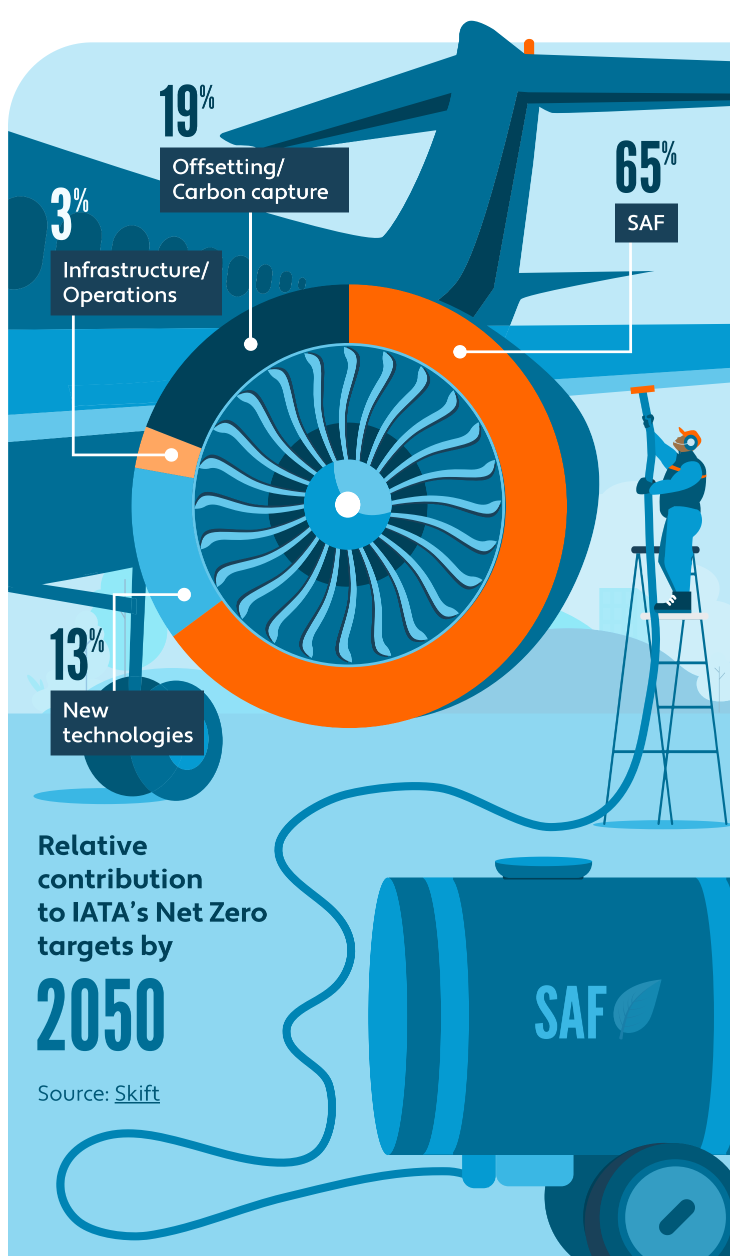
Climate change and renewable energy policies like the Green New Deal have companies searching for ways to reduce their dependence on traditional oil and gas. One result is an uptick in renewable fuels, like sustainable aviation fuel and renewable diesel, entering the market. The trend is creating excise tax challenges for the energy industry.

"Many tax breaks are available for selling renewable fuels but meticulous recordkeeping is required to get them. Regulations around tax refunds change quickly," says Bubba Lange, Senior Director of Product Solution Engineers at Avalara.

Renewable crude comes from bio feedstocks like used cooking oil. This is then distilled to create products like renewable diesel, renewable gasoline, and sustainable aviation fuel. Renewable fuels can also be created by melting plastic bottles and burning trash.

"Renewable diesel and biodiesel are not the same thing. Renewable diesel has the same chemical footprint as regular diesel and is taxed just as if it were a regular diesel product. You need to know which product codes to use to classify renewable diesel products correctly on your excise tax returns," Lange says.

Global aviation companies have set a goal of net-zero carbon emissions by 2050. Sustainable aviation fuel, more commonly referred to as SAF, is helping airlines reduce their carbon footprint. Airbus and Boeing have pledged to make their airplanes 100% SAF compatible by 2030.



Relative contribution to IATA's Net Zero targets by 2050

Source: Skift

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But there's still a long way to go. United Airlines became the first U.S. airline to test SAF in 2009, but today SAF accounts for a meager 0.1% of the company's overall fuel. Air France leads in adoption with SAF comprising just 0.6% of its overall fuel mix in 2022–23.

SAF is only available at certain airports in the U.S. and internationally, although the list is expanding. SAF has been available for departures from Los Angeles International Airport since 2016 and San Francisco International Airport since late 2020. Finnish fuel producer Neste began supplying SAF to United Airlines for departures from Chicago O'Hare International Airport in August 2024. United said the deal was made possible because Illinois enacted a tax credit in 2023 for SAF purchases.

The International Air Transport Association (IATA) projected that SAF production would triple in 2024 to 1.9 billion liters (1.5 million tons). However, this accounts for only 0.53% of the aviation industry's fuel needs for the year.

"As sustainable aviation fuel becomes more common, taxability becomes more complicated and questions arise. What if you buy SAF from another country and it's flown to the U.S.? You didn't pay tax on it. How does that impact your tax credit? It's hard to keep up with the rules, and the rules will change, guaranteed," Lange says.

BUBBA LANGE
Senior Director of Product Solution Engineers at Avalara

"Regulations around tax refunds change quickly ...

Many tax breaks are available for selling renewable fuels but meticulous recordkeeping is required to get them ... you need to know which product codes to use to classify renewable diesel products correctly on your excise tax returns."

Maine amends property tax exemptions for solar energy equipment

Maine amended its legislation to include new limits on property tax exemptions for renewable energy equipment.

Beginning April 1, 2025, solar energy equipment is exempt from property tax only if: "1) the energy it produces is used on-site; 2) the equipment is collocated with a customer or customers that are subscribed to at least 50% of the facility's output; or 3) the energy the equipment produces is transmitted through an electric utility and accounted for using a bill credit mechanism and the generator had a fully executed interconnection agreement prior to April 1, 2024."

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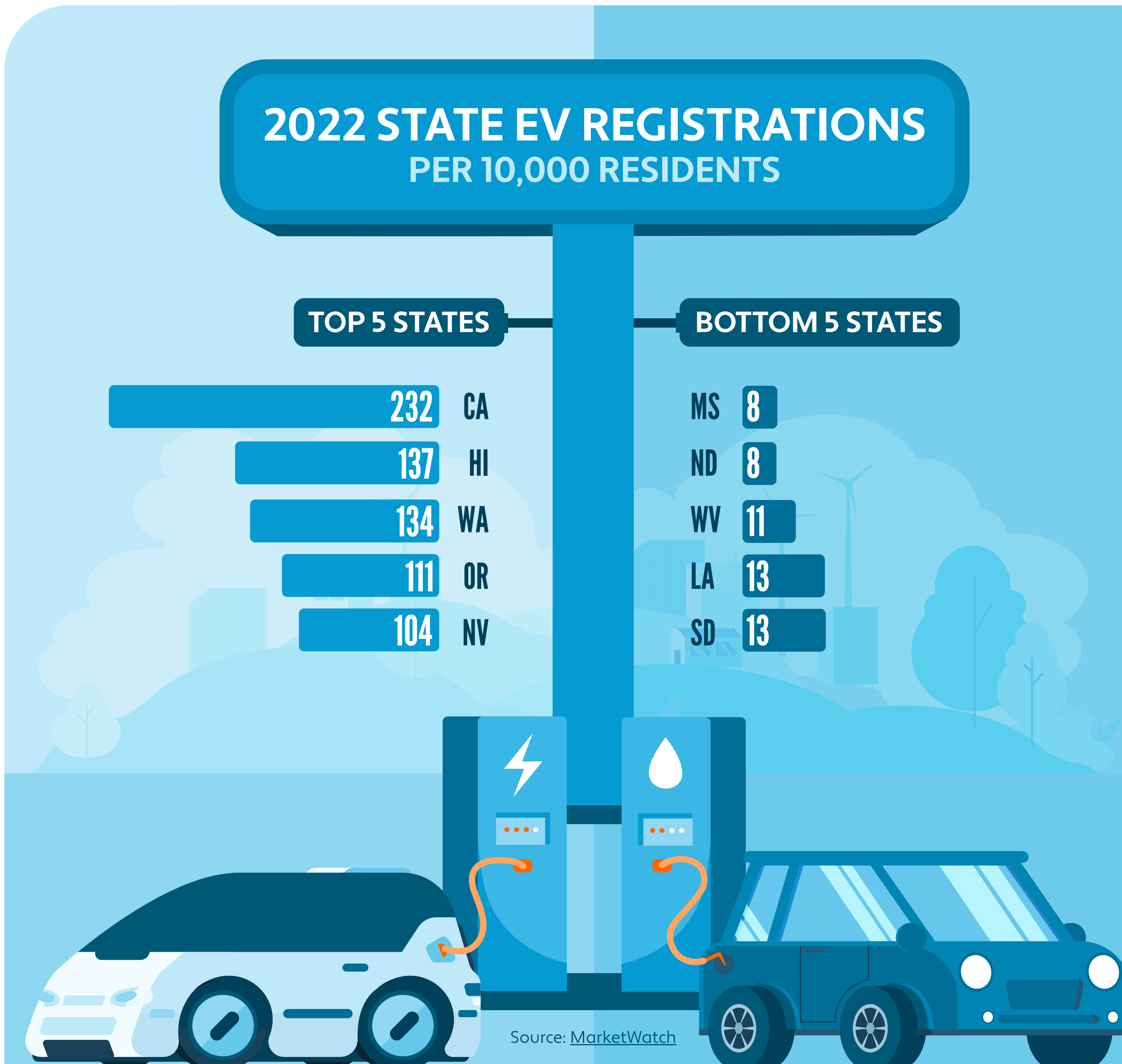
States cut tax breaks for zero-emissions vehicles

Electric cars were predicted to account for more than one in five cars sold globally in 2024 and to help avoid the need for almost 6 million barrels of oil a day by 2030. About 1.6 million electric vehicles (EVs) were sold in the U.S. in 2023, a 60% year-over-year increase from 2022. California, Florida, Texas, and Washington lead the nation with the highest numbers of EV registrations.

Historically, states have incentivized drivers of zero-emissions cars. But as more electric vehicles take to the roads, some states are scaling back on their tax breaks as they seek to recoup their loss of fuel tax revenue from vehicles that don't use gas.

A proposal by the District of Columbia Tax Revision Commission would eliminate the preferential tax rate for electric vehicles and other high-mileage vehicles in D.C. If approved, they'd instead be taxed at the standard 6% rate and provide an estimated $13 million in additional revenue.



Source: MarketWatch

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Pennsylvania eliminated its alternative fuel tax on electric vehicles and replaced it with an **electric vehicle road user charge**. Under the new rule, EV owners will pay a $200 fee upon registration or renewal in 2025. The fee goes up to $250 in 2026 and starting in 2027, the fee will be based on inflation factors.

New Jersey decided to gradually end its sales and use tax exemption for zero-emissions vehicles. Per **A4702**, a tax of 3.3125% applies to receipts from sales of zero-emissions vehicles sold October 1, 2024, through June 30, 2025. Starting July 1, 2025, the full sales and use tax rate (currently 6.625%) will apply.

The phaseout of the sales tax exemption is expected to generate **$75 million** in new revenue for New Jersey's general fund during the 2025 fiscal year.

"Personal vehicles have long represented a significant portion of the sales tax base, and with new registrations of EVs approaching 10% of new vehicle registrations, it is responsible to acknowledge these vehicles as a regular part of the market," according to **The State of New Jersey Budget in Brief** for fiscal year 2025.

Are states increasing excise tax enforcement for online cigar sellers?

Cutting tax breaks for EV drivers isn't the only way states are driving up revenues. Jurisdictions continue to look for other ways to fill the coffers, and collecting more taxes on cigar sales may be next.

Cigars sold online and shipped to consumers in the U.S. are subject to state excise tax laws. That doesn't mean all ecommerce retailers are compliant. Those that aren't might need to reevaluate their business practices.

"Manufacturers and merchants that sell cigars online may have flown under the radar of state tax authorities but that could be changing. We've seen an uptick in cigar companies coming to Avalara because they want to get their compliance under control," says Bubba Lange.

States already enforce sales and use tax laws against ecommerce retailers. The 2018 United States Supreme Court decision, South Dakota v. Wayfair, Inc., led to **economic nexus laws** in every state with sales tax. Previously, businesses only had an obligation to collect and remit sales tax if they had a physical presence in a state.

It's possible, Lange explains, that more states are turning their attention to **excise tax nexus**. Certain activities can trigger excise tax nexus, including when tobacco products are brought into a state.

"Cigar companies need to evaluate their compliance now so they aren't caught off guard by penalties later," says Lange.

BUBBA LANGE
Senior Director of Product Solution Engineers at Avalara

Manufacturers and merchants that sell cigars online may have flown under the radar ... but that could be changing. We've seen an uptick in cigar companies coming to Avalara because they want to get their compliance under control.

Cigar companies need to evaluate their compliance now so they aren't caught off guard by penalties later.

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Canada makes vaping excise duties more complex

While more states may deem taxing cigars lucrative, many jurisdictions continue to focus on vape products.

Calculating excise duty on vaping products became more complicated for retailers in Canada as a result of rate increases that went into effect on July 1, 2024.

Excise duty rates for vaping liquids are now:

- $1.12 CAD per 2 milliliters (mL), or fraction thereof, for the first 10 mL of vaping substance in the vaping device or immediate container
- $1.12 CAD per 10 mL, or fraction thereof, for amounts over the first 10 mL

An additional vaping duty applies for products intended for consumption, sale, or use by consumers in a specified vaping province:

- $1.12 CAD per 2 milliliters (mL), or fraction thereof, for the first 10 mL of vaping substance in the vaping device or immediate container
- $1.12 CAD per 10 mL, or fraction thereof, for amounts over the first 10 mL

BUBBA LANGE
Senior Director of Product Solution Engineers at Avalara

“The average ERP system won’t be able to calculate the excise duties correctly without a lot of work by your IT department.

Avalara for Tobacco is capable of calculating the new excise duties accurately to help sellers remain compliant.”

Duty is calculated on the quantity of vaping liquid contained in each individual pod, not on the total volume contained in the package.

The Canada Revenue Agency provides this example: “A 30mL bottle of vaping liquid, which is intended for sale in a specified vaping province, attracts $7 of vaping duty ($5 for the first 10 mL plus $2 for the next 20 mL) **plus** $7 of additional vaping duty ($5 for the first 10 mL plus $2 for the next 20 mL), for a total of $14 of duty.”

The same rates apply to vaping solids on a per gram basis.

“The new duty rates are likely to cause a headache for Canadian retailers. The average ERP system won’t be able to calculate the excise duties correctly without a lot of work by your IT department. Avalara for Tobacco is capable of calculating the new excise duties accurately to help sellers remain compliant,” says Lange.

Colorado increases taxes on tobacco and nicotine products

Colorado residents will also pay more to vape. Taxes on tobacco and nicotine products including e-cigarettes are higher in Colorado after provisions from Proposition EE went into effect on July 1, 2024. The scheduled changes raise the minimum price for a pack of cigarettes from $7 to $7.50 and increase the per-cigarette tax, the moist snuff tax, and other taxes. The tax increases will provide $20 million to tobacco education programs with remaining revenues funding preschool programs.

Colorado taxpayers approved Proposition EE on November 3, 2020. Previously, nicotine products such as e-cigarettes weren’t taxed in Colorado.

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Other tobacco industry tax changes

- Maine extended its definition of tobacco products that are subject to its Tobacco Products Tax. Effective August 9, 2024, the new definition includes “any products that are made from or derived from tobacco, or that contain nicotine, whether natural or artificial.”
- Mississippi began taxing heated tobacco products effective July 1, 2024. Heated tobacco products are defined under the law as “a product containing tobacco that produces an inhalable aerosol by (i) heating the tobacco without combustion of the tobacco or (ii) heat generated from a combustion source that only or primarily heats rather than burns the tobacco.”

  Heated tobacco products are taxed at the rate of 1.25 cents on each disposable heated tobacco unit or stick sold. The tax must be paid on the regular Tobacco Excise Tax return due the 15th day of the succeeding month for manufacturers and wholesalers or due within 48 hours of receipt for retailers.

  Heated tobacco products are also subject to the fee for non-settling manufacturers at the same rate as cigarettes. Effective July 1, 2024, Mississippi increased the Non-Settling Manufacturer (NSM) fee to 2.14 cents for each NSM cigarette sold. This equates to an increase of $0.14 per carton.
- A proposal by the District of Columbia Tax Revision Commission would raise the district’s cigarette tax to $5.50. If approved, it would create $100,000 in new revenue.
- Effective July 1, 2024, the Maryland state budget increased tax rates for tobacco products, including an increase to the tax on cigarettes from $3.75 to $5 per pack, or $0.25 per cigarette in packages of more than 20. The tobacco tax rate for other tobacco products, like chewing tobacco, increased from 53% to 60% of the wholesale price. The rate levied on electronic smoking devices (other than vaping liquid in containers of 5 mL or less) increased from 12% to 20% of the taxable price.
- Effective July 1, 2024, the tax levied on moist snuff in Oregon increased from $1.80 per ounce to $1.86 per ounce, and the minimum tax increased from $2.17 per retail container to $2.24 per retail container.

No matter how the energy, fuel, tobacco, and vape industries shift over the next year, you can count on Avalara to track tax changes and help you gauge what they mean for your business.

How Avalara can help

Excise tax compliance is challenging for businesses in the energy, fuel, tobacco, and vape sectors because excise taxes vary by state and can change quickly. Avalara solutions designed to meet specific challenges for these industries can help you create efficiencies and reduce audit risk.

Solutions

ENERGY AND FUEL

TOBACCO AND VAPE

Up next: Global tax

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Global tax

Legislation originally designed for physical businesses, tangible goods, and manual processes runs the risk of becoming obsolete. So tax authorities around the globe continue to digitalize tax compliance in an effort to keep pace with digital economies. This section provides updates on significant global compliance changes and digitalization that impact how businesses everywhere operate and stay compliant.

What's ahead:

The cycle of legislative updates

What the numbers tell us about global tax compliance in 2025

VAT in the Digital Age aims to modernize VAT

VAT changes in 2025

Global e-invoicing mandates in 2025: Delays and rollouts

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The cycle of legislative updates

As governments review and replace outdated tax legislation, and businesses adjust to changing compliance requirements, we can see a cycle emerge: Markets evolve, authorities react by implementing new rules, and businesses must then adapt to maintain compliance. As part of this cycle, a level of necessary compromise emerges. Businesses need time to adapt to compliance changes, update their systems, train staff, and expand their knowledge.

Governments, not wanting to sink their own economy or appear unsupportive of industry, are (in most cases) granting businesses this extra time – time that governments themselves can also use to adapt to and train staff for their own legislation and its implications. As a result, it's becoming increasingly common for the rollout of various rules, mandates, and directives to be amended, extended, or delayed. In particular, e-invoicing mandates that have stuck to their original scope and government timelines are few in number.

Speaking of numbers, let's take a look at some.

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What the numbers tell us about global tax compliance in 2025

$16 to $22 per invoice

is the average cost range of manually processing invoices; **automation** can reduce that to

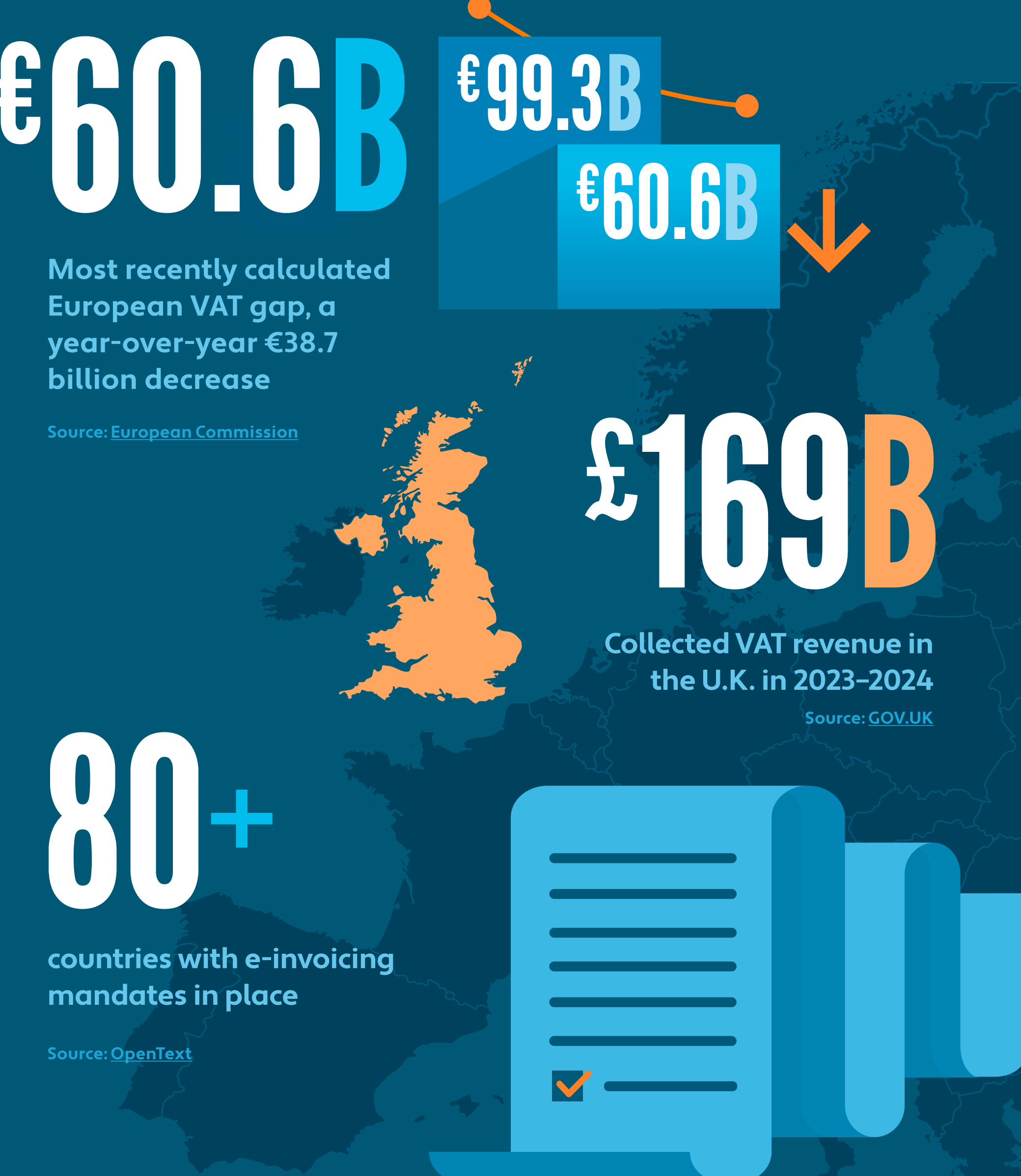
$5 per invoice

Source: Forbes

€60.6B

Most recently calculated European VAT gap, a year-over-year €38.7 billion decrease

Source: European Commission



£169B

Collected VAT revenue in the U.K. in 2023–2024

Source: GOV.UK

AU $82B

collected in net goods and services tax revenue in Australia in 2022–2023

Source: Commonwealth of Australia

80+

countries with e-invoicing mandates in place

Source: OpenText

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VAT in the Digital Age aims to modernize VAT

VAT in the Digital Age (ViDA) is a package of proposed reforms designed by the EU to improve and digitalize tax authorities' administration of value-added tax (VAT) in response to Europe's growing digital economy. Among ViDA plans for the platform economy was the proposal to extend VAT obligations to marketplaces and ecommerce platforms by making them "deemed suppliers."

This means marketplaces will become liable for charging and remitting VAT when making sales within the EU (both domestic and cross-border sales). Short-term rental providers such as Airbnb and passenger transport service companies like Uber would also become deemed suppliers, and they too would be responsible for collecting and paying VAT for their third-party sellers or customers.

The goal of the EU is to bring VAT obligations for these types of businesses in line with those of more traditional service providers. The EU believes the **platform economy has raised significant difficulties** for the application of VAT rules. This includes establishing the taxable status of the provider of the service, and leveling the playing field between small

ViDA

The ViDA initiative seeks to **modernize the EU's VAT system**. Its measures aim to **simplify cross-border trade, curb VAT fraud, and alleviate administrative complexities** for businesses operating within the EU.

THREE PILLARS OF ViDA

Digital reporting requirements

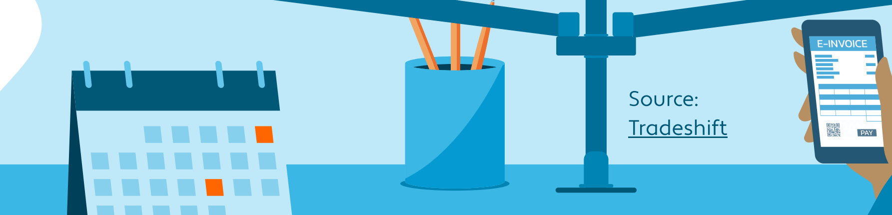
This pillar introduces a real-time digital reporting framework to enable smoother data exchange between businesses and tax authorities. It encourages broader adoption of e-invoicing and standardization of transaction data required for tax authorities.

Platform economy rules

These rules tackle the unique VAT challenges of the platform economy, particularly for short-term rentals and passenger transport. This pillar strives to clarify VAT obligations for these platforms and potentially expand their role in VAT collection.

Single EU VAT registration

This pillar is designed to simplify VAT compliance for businesses operating across multiple EU nations by replacing the need for separate VAT registrations in each country with a single EU VAT registration, thereby streamlining processes and significantly reducing administrative complexities.



Source: Tradeshift

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and medium-sized enterprises (SMEs) and other businesses. The EU aims to address what it perceives as a distortion of competition between online platforms that escape taxation and traditional traders that are subject to VAT. Two of the biggest drivers of this distortion, the EU believes, are the short-term rental sector and ride-sharing companies.

There's widespread support for correcting the distortion between marketplaces and other businesses (to a greater or lesser degree). However, one country was opposed to the proposed changes.

Opposition from Estonia postponed ViDA

Believing the proposed deemed supplier rules for the platform economy would unfairly burden small businesses, the **Estonian government vetoed the ViDA proposal** at the May 14, 2024, meeting of the Economic and Financial Affairs Council (ECOFIN).

Estonia balked at requiring platforms to collect VAT, preferring an opt-in model. It put forward a compromise proposal that would allow platforms to leave it to sellers to collect VAT. It would also allow for other rules applicable to certain entities, such as travel agents and small businesses.

On November 5, 2024, after further negotiations, **Estonia lifted its blocking veto**, and the European Council **adopted the updated ViDA package**. EU finance ministers are expected to adopt the proposal after consulting with the European Parliament.

New ViDA rules on the horizon

"The new rules will update our VAT systems to reflect the digitalization of our economies, help combat VAT fraud, and ease administrative obligations for small companies and individual service providers," said Mihály Varga, Minister of Finance of Hungary.

Under the new ViDA rules:

- VAT reporting obligations for cross-border transactions will be fully digital by 2030.
- Online platforms will be required to pay VAT on short-term accommodation and passenger transport services "in most cases where individual service providers do not charge VAT."
- Online VAT one-stop shops will be improved and expanded so businesses don't need to register for VAT in every applicable member state.

According to the ECOFIN, the new rules should be in place by 2030. The national systems currently in effect "should become interoperable with the EU system by 2035."

MIHÁLY VARGA
Minister of Finance of Hungary

> **The new rules will update our VAT systems to reflect**
>
> **the digitalisation of our economies, help combat VAT fraud, and ease administrative obligations for small companies and individual service providers.**

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DAC 7 and EU tax reporting obligations for digital platforms

Introduced in 2011, the Directive on Administrative Cooperation (DAC) enables EU member states to cooperate on matters of information sharing and tax evasion. The seventh amendment to this directive – DAC 7 – requires digital platforms operating in the EU to report information on sellers to tax authorities, including income (platforms must also show sellers what information is being provided to tax authorities on their behalf).

DAC 7 therefore extends the EU goal for tax transparency to digital platforms, which now have an obligation to collect and report requested information to tax authorities. These platforms include operators of software, websites, or mobile apps that connect sellers with buyers. Operators must be tax residents within the EU, have a permanent establishment in the EU, and facilitate sales by sellers who are residents in EU member states.

As part of DAC 7 reporting requirements, platforms must identify "reportable sellers" using their platform, then inform these sellers of what information will be shared with tax authorities and when. Platforms are required to report the requested information to tax authorities by January 31 of the year following the calendar year in which a seller is identified as a reportable seller.

In other words, platforms had to file the first report by January 31, 2024, to cover 2023 commercial activity. Tax administrations receiving the information then exchanged it between member states by the end of the following month.

The U.K. – no longer an EU member state – has its own version of reporting rules called U.K. Digital Reporting Requirements (DRR), which came into effect at the beginning of 2024. The first reports must be provided to His Majesty's Revenue & Customs (HMRC) by January 31, 2025.

DAC 7 is an example of how the EU increasingly wants platforms and marketplaces (as well as other types of business) within the EU to take greater responsibility in tackling noncompliance and tax fraud. In addition to expanding how and when member states can share transactional information, DAC 7 also includes a legal framework to enable joint audits. Multiple member states can thus form a single audit team to conduct taxpayer audits on cross-border sales, which can serve to expedite issue resolution.

Let's look at more upcoming changes to EU VAT legislation that are intended to provide either clarity, simplification, or an alleviation of administrative burdens.

VAT changes in 2025

The EU will extend the same **VAT registration thresholds** for each member state's domestic businesses to EU businesses from other member states in 2025. The EU hopes to reduce costs and administrative burdens associated with VAT for small enterprises (SMEs) and encourage trade within the single market – a free trade area that allows the movement of goods, services, and people across the borders of EU member states. This SME Special Scheme will consist of two thresholds:

- Domestic threshold of €85,000 – same as the current regime
- Cross-border threshold of €100,000 – businesses can opt to make exempt sales in other EU member states; this is up to €100,000 total sales and may be used in conjunction with the domestic threshold

Sales made in a member state that fall into the cross-border threshold must not exceed the domestic threshold where the commercial activity is taking place. This new scheme is also not available to non-EU businesses.

Virtual events and VAT

Starting January 1, 2025, **new rules regarding VAT on virtual events** will apply. From this date, they'll be taxed at the rate where the consumer is based, bringing livestreams and virtual events in line with rules on electronically or digitally supplied services.

The EU classifies events of any kind as *services*. As VAT laws predate virtual events and the technology required to host them, it hasn't been entirely clear which member state should charge VAT – for example, if the virtual event is happening in one country, but being "attended" in another. There may be future exemptions for educational content.

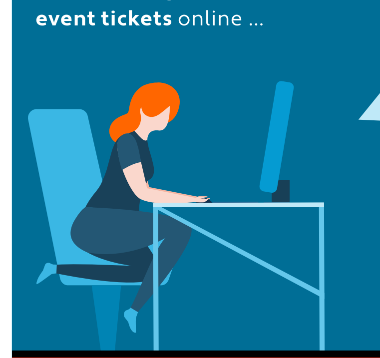
Prerecorded, downloadable, or on-demand content will still count as an "electronically supplied service" and is therefore a telecommunications, broadcasting, and electronic (TBE) service. Both business-to-business (B2B) and business-to-consumer (B2C) supplies of TBE services will continue to be taxed based on the location of the consumer, though B2C transactions are subject to a €10,000 threshold.

Starting **January 1, 2025**, VAT on virtual events, online classes, and digital coaching will be **taxed at the rate where the consumer is based**

Source: SimplyVAT

FOR EXAMPLE:

A company based in the U.K. is **selling virtual event tickets** online ...



... and an individual **buys a virtual event ticket** in Austria

THE BUSINESS MUST:

Register in Austria

Collect VAT on the sale

Report it to Austria on return

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SELL ACROSS THE EU
WITHOUT HAVING TO COMPLETE MULTIPLE REGISTRATIONS AND VAT RETURNS

EU SCHEMES

(OSS)
One-Stop Shop
Designed for businesses selling goods from one **EU member state** to **customers in other EU countries**

(IOSS)
Import One-Stop Shop
Designed for businesses selling goods to **customers in the EU** from **outside the EU**

Register for VAT in any single EU member state and declare all VAT in a single EU VAT return

Source: Avalara

Single VAT registration and changes to OSS and IOSS

Since the EU's goal is to alleviate administrative compliance burdens on EU businesses, **updated text within ViDA proposals** regarding single VAT registration reinforces this. These updates include:

- Planned extensions to the One-Stop Shop (OSS) and Import One-Stop Shop (IOSS)
- Additional steps to reduce VAT fraud
- An extension to the reverse charge rule
- The introduction of a special scheme for the transfer of own goods

These changes are scheduled to take effect **July 2028**, but may change subject to further ViDA delays, as discussed earlier.

Before the introduction of OSS and IOSS in 2021, businesses had to register for VAT in every member state they sold to. OSS and IOSS allow businesses to register in a single member state and declare all VAT from operations across the EU in a single EU VAT return.

While the ViDA proposal currently covers EU remote sales and B2C services within the EU, the revised ViDA text provides clarification. OSS will extend to cover other domestic supplies of goods, supplies with installation or assembly, supplies made onboard EU passenger transport, and supplies of electricity, gas, heat, and cooling. According to the proposal, to reduce the need for multiple registrations, Mini OSS – applicable to the supply of digital services – will become a broader OSS to cover all cross-border transactions within the EU.

As another step toward tax fraud prevention and closing the VAT gap, measures will be introduced to "better secure the correct use and the verification process of IOSS VAT identification numbers." The EU hopes this will prevent certain forms of tax evasion or avoidance by linking the unique consignment and IOSS VAT identification numbers.

Currently, EU member states are required to implement the *reverse charge rule* – which reduces or removes the obligation for sellers to register for VAT in the country where the supply is made – for certain transactions. However, this remains optional for other transactions.

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Once ViDA updates take effect, the mandatory reverse charge will apply to all B2B supplies of goods and services. The provision is the supplier is not located in the EU member state where VAT is due, but the recipient is registered for VAT purposes:

"Rules should be laid down for the mandatory application of the reverse charge mechanism in situations where suppliers are not established and not identified for VAT purposes in the Member State in which VAT is due. When supplying goods or services to a person who is identified for VAT in the Member State where the supply is taxable, these suppliers should apply the reverse charge."

Businesses may be required to complete multiple VAT registrations if they transfer their own goods from one EU member state to another, as when moving inventory between warehouses. They'll be required to report an intra-community supply and an intra-community acquisition in the member state of departure. ViDA proposal updates include a new scheme to simplify compliance requirements for such transfers of own goods for both EU and non-EU businesses.

Transfers made as part of the scheme won't have to be reported in the **recapitulative statement**. "The transfer of a taxable person's own goods to another Member State … triggers a need to register in the Member States from and to where the goods are transferred." To align with the EU's objective of creating single VAT registrations, "the instances in which multiple VAT registrations are required should be further reduced by providing for the application of a new scheme in the framework of the OSS schemes, which is specifically designed to simplify the VAT compliance obligations associated with certain transfers of own goods."

These updates to ViDA could prove to be good news for businesses operating within the EU that wish to avoid having to complete multiple VAT registrations and thus contend with any and all related costs and compliance administrative processes.

COUNCIL OF THE EUROPEAN UNION

"The transfer of a taxable person's own goods to another Member State …

triggers a need to register in the Member States from and to where the goods are transferred."

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Global e-invoicing mandates in 2025: Delays and rollouts

E-invoicing can reduce the costs of invoicing for both businesses and authorities by automating paper-based and manual processes. It also furthers governments' ambitions of automating their tax systems and closing tax gaps by providing insight into transactional data and adding more immediacy.

Other commercial benefits include decreasing the time required to process invoices, boosting efficiency, and significantly reducing errors from manually keying in data (that can prove to be costly). By sharing encrypted data, e-invoicing is also a more secure transmission method than mail or email.

E-invoicing continues to become an exceptionally important aspect of the global tax compliance landscape, despite a number of countries amending or delaying mandates and implementation. The overall picture is that countries – including their governments, tax administrations, and businesses – require more time to get the right systems and technology in place. Previously implemented nonuniform systems and software also take time to replace.

The rollout of e-invoicing mandates will continue, making the importance of awareness and preparedness high on any business's agenda – even if it's located within a country where mandates are not yet in place.

"Despite various delays to the rollout of mandates around the world, it remains a matter of time before e-invoicing is not only implemented, but mandated, worldwide," said Alex Baulf, VP of E-Invoicing and Live Reporting at Avalara. "The benefits of e-invoicing for governments in all world regions are too numerous and valuable for any kind of U-turn to happen. Delays to mandates and amendments to requirements are only a sign that governments want to get things right, and allow businesses the time they need to adapt. It remains imperative for businesses to follow developments in the compliance landscape, and equip themselves with e-invoicing and real-time reporting solutions as soon as possible."

The following pages contain developments to mandates and schedules detailed by country.

ALEX BAULF
VP of E-Invoicing and Live Reporting at Avalara

Despite various delays to the rollout of mandates around the world, it remains a matter of time before e-invoicing is not only implemented, but mandated, worldwide.

It remains imperative for businesses to follow developments ... and equip themselves with e-invoicing and real-time reporting solutions as soon as possible.

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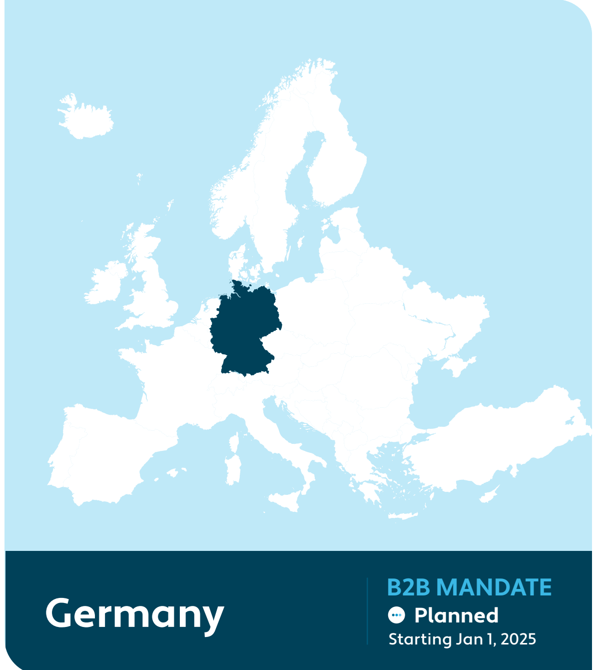
E-invoicing isn't currently mandatory in the U.K. for B2B supplies, though it's being used by businesses on a voluntary basis. In a recent development, U.K. Chancellor Rachel Reeves used the September 2024 Labour Party Conference to announce that HMRC will launch a **consultation on e-invoicing in Britain**.

The government's goal is to promote the wider use of e-invoicing across U.K. businesses and government departments. It believes e-invoicing can reduce manual administrative tasks, improve cash flow, boost productivity, reduce errors in tax returns, and help close the U.K. tax gap. The consultation will gather feedback from U.K. businesses to better understand how HMRC can support the e-invoicing adoption process across multiple sectors.



E-invoicing has been obligatory in Germany for business-to-government (B2G) transactions since November 2020. The country is now set to **introduce mandatory e-invoicing** for business-to-business (B2B) transactions starting January 1, 2025.

Germany will take a soft approach to its B2B mandate by rolling it out in stages over a transitional period lasting until 2027. This is designed to help businesses – particularly smaller ones – manage the costs of implementation and provide a degree of flexibility for the necessary period of adaptation.

Stages of Germany's B2B mandate rollout will be defined by the obligation to receive e-invoices and the obligation to issue them:

- **JANUARY 1, 2025** – All businesses must be ready and able to receive e-invoices. Recipients will not have the option to refuse an e-invoice or request another format.
- **JANUARY 1, 2027** – Businesses with a turnover of €800,000 or more (in 2026) must be ready to issue e-invoices. Businesses with a turnover below €800,000 for the same year can still issue invoices as PDF, paper, JPEG, etc.
- **JANUARY 1, 2028** – All businesses must be ready to issue e-invoices. Only e-invoices as structured data will be compliant.

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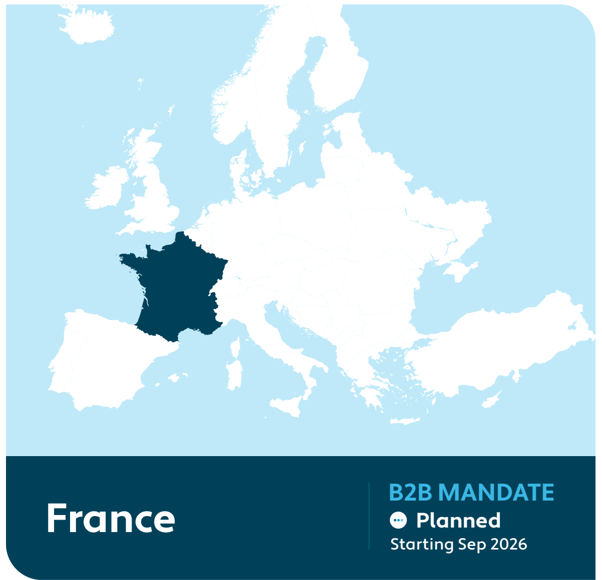
Poland

B2B MANDATE
Planned
Starting Feb 1, 2026

Poland's plan to launch its e-invoicing mandate in July 2024 **was postponed**. Polish authorities believe – following a technical audit – that an architecture rebuild is necessary to include better documentation and maintenance planning as well as training and support for Polish taxpayers.

B2B e-invoicing will become mandatory as of February 1, 2026, for businesses and taxpayers with annual revenues exceeding PLN 200 million. On April 1, 2026, the mandate will extend to all taxpayers.



France

B2B MANDATE
Planned
Starting Sep 2026

France postponed its original e-invoicing mandate launch date of July 1, 2024. The **new mandate schedule** is now set to begin September 2026 and will be rolled out in phases according to business size:

- **SEPTEMBER 2026** – Large businesses must be able to issue and receive e-invoices. All businesses must be able to receive e-invoices.
- **SEPTEMBER 2027**– Small and medium-sized businesses must be able to issue e-invoices.

The obligation to transmit transaction, payment, and life cycle data (e-reporting) will adhere to the same timeline as that for e-invoicing.

The French authorities' decision to extend the timeline is based on giving businesses more opportunity to adapt their resources, processes, and software to changing requirements.

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Spain will not implement a B2B e-invoicing mandate before 2027, a significant delay from earlier plans for July 2025 or early 2026. Spanish authorities have expressed doubts about technical specifications being ready in time. It appears that Spain's e-invoicing plans are more complex than anticipated, and the Spanish government wants to finalize such details before approving legislation.

A two-phase launch period has been proposed, which may be subject to public consultation:

- **2027** – Mandate will apply to large businesses with a turnover exceeding €8 million.
- **2028** – Mandate will apply to all other businesses and taxpayers.

Saudi Arabia has been implementing its B2B e-invoicing mandate in "waves" since 2023, according to annual turnover. From January 2024 to December 2024, the mandate has taken effect for businesses with income between SAR 10 million and SAR 100 million.

The phases are set to continue from the beginning of 2025 as follows:

- **JANUARY 2025** – Businesses and taxpayers with an annual income between SAR 7 million and SAR 10 million
- **FEBRUARY 2025** – Businesses and taxpayers with an annual income between SAR 5 million and SAR 7 million
- **MARCH 2025** – Businesses and taxpayers with an annual income between SAR 4 million and SAR 5 million
- **APRIL 2025** – Businesses and taxpayers with an annual income between SAR 3 million and SAR 4 million

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Malaysia

B2B MANDATE Yes

In July 2024, the Malaysian government announced a six-month transition period for its B2G, B2B, and B2C e-invoicing mandates, to commence August 1, 2024 – another example of a soft launch to give businesses time to fully prepare themselves for e-invoicing. During this period, businesses have the option of using consolidated e-invoices for transactions instead of a single e-invoice for each individual transaction.

The Inland Revenue Board of Malaysia (IRBM) will not impose penalties for noncompliance, provided businesses follow the requirements regarding consolidated e-invoices. The IRBM will, however, reward businesses and taxpayers that implement e-invoicing with "a reduction in the capital allowance claim period from three years to two for the purchase of information and communication technology (ICT)."

The timetable for the preclearance e-invoicing regime is:

- **AUGUST 1, 2024** – Businesses and taxpayers exceeding a turnover of MYR 100 million
- **JANUARY 1, 2025** – Businesses and taxpayers exceeding a turnover of MYR 25 million
- **JULY 1, 2025** – All other businesses and taxpayers

Businesses with annual sales below MYR 150,000 are exempt from the mandate.

Other notable e-invoicing mandate updates

BELGIUM

B2B e-invoicing via the Peppol network: January 2026

CROATIA

B2B e-invoicing: January 2026

ESTONIA

B2B e-invoicing: Businesses will be required to file B2B invoices electronically in 2027 (delayed from 2025)

LATVIA

B2G e-invoicing: January 2025

B2B e-invoicing: January 2026

OMAN

B2B e-invoicing (for large businesses): 2025

PORTUGAL

Digital signature will be required within e-invoicing from January 2025

ROMANIA

B2C live reporting via e-Factura will become a requirement from January 2025

SLOVAKIA

B2B and B2C e-invoicing: January 2025

SLOVENIA

B2B e-invoicing: January 2026

UNITED ARAB EMIRATES

B2B e-invoicing via the Peppol network: July 2026

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Australia, New Zealand, and Peppol

The governments of Australia and New Zealand entered into an agreement on a common approach to e-invoicing in 2018. Having recognized the benefits of a global framework, both governments announced the adoption of Peppol in 2019.

The Peppol e-invoicing network (formally known as Pan-European Public Procurement Online) was originally developed to streamline business with customers within the public sector of the EU, and has since been adopted by more and more global regions. It's now the most common delivery network and standard for trading partners (including governments) to send and exchange compliant e-invoices.

Since adopting Peppol, Australia and New Zealand have established their own Peppol authorities, but work closely to oversee and unify the two nations' adoption of e-invoicing. These authorities define the two countries' requirements for the use of Peppol standards such as invoice specifications, and work with service providers and businesses to ensure the Peppol framework is implemented consistently across the region.

In October 2023, the Australian government committed to mandating the right of the customer to request Peppol-based e-invoicing on B2B transactions. The existing Peppol format in Australia – ANZ Peppol BIS 3.0 – was replaced by the PINT A-NZ specification of OpenPeppol. The format is obligatory for B2G e-invoicing and when e-invoicing is agreed between B2B counterparties.

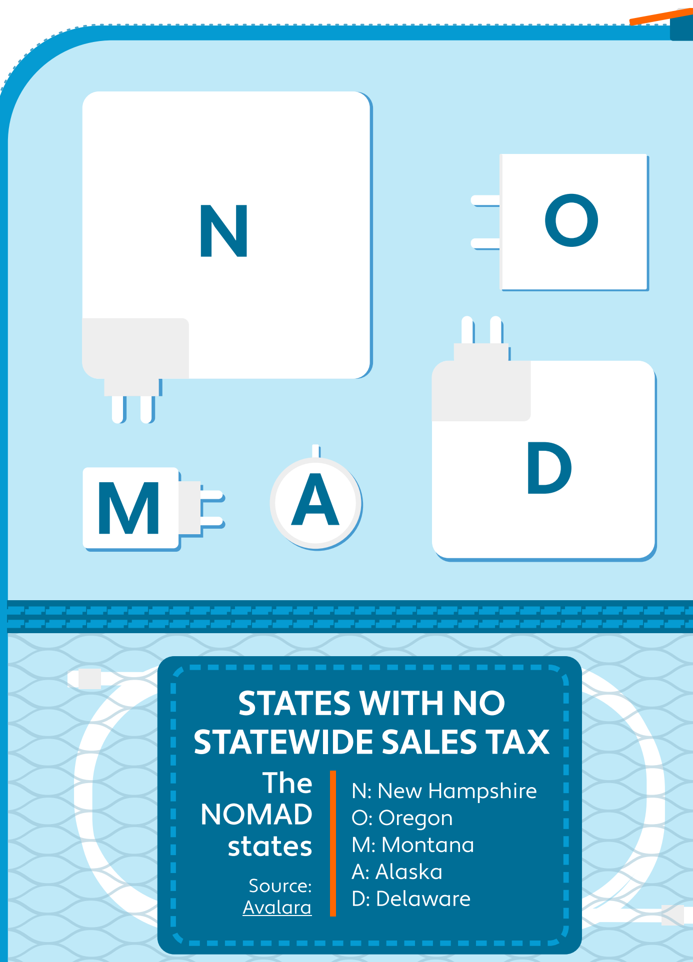
Mandatory use of e-invoicing on the Peppol network came into effect November 2024.

The U.S. perspective: Will e-invoicing be adopted in the U.S.?

The U.S. has so far remained somewhat of a spectator as e-invoicing and live reporting is adopted around the world. This has left many to speculate as to when – or if – the U.S. will follow suit by adopting some form of e-invoicing initiative, and whether U.S. sales tax will be subject to it.

In regions where e-invoicing is being rolled out, such as Europe, tax authorities realized a more harmonized approach to e-invoicing was required to replace the disparate systems and approaches that typified earlier years of e-invoicing.

On the other hand, U.S. states are nonuniform when it comes to sales tax laws, with differing requirements and varying rates across them – including variations within a state or even at the county level. Some U.S. states don't have a state sales tax. This would make the type of harmonization – that has proven to be essential in other parts of the world – difficult to implement across the U.S.



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A cross-state, coordinated approach would be required, which in itself could prove problematic, inefficient, and costly. Furthermore, the U.S. doesn't face as big a problem with tax fraud or an equivalent "VAT gap" – the difference between the amount of tax revenue owed and paid to authorities. Tax compliance rates in the U.S. are generally higher than that of the EU – and other global regions. This makes potential revenue gains for authorities a less significant incentive for e-invoicing implementation.

Though U.S. tax authorities and businesses alike continue to invest in the digitalization of tax compliance and administration, the case for implementing e-invoicing as part of everyday sales and use tax compliance appears weaker than in countries and regions with VAT systems.

While mandatory e-invoicing may never come to the U.S., it's important to note that U.S. businesses operating in countries with e-invoicing requirements must comply with those mandates. And some U.S. businesses are voluntarily taking advantage of e-invoicing to reap the rewards.

The Digital Business Networks Alliance (DBNAlliance) – a nonprofit that oversees the e-invoicing exchange network in North America – **announced** in March 2024 that the first invoice had been exchanged over the network. Avalara issued the e-invoice to the recipient, Storecove, using **Avalara E-Invoicing and Live Reporting**. Chris Welsh, Chair of the DBNAlliance, said, "We look forward to enabling businesses from any industry to electronically exchange their invoices and other supply chain documents moving forward. Our goal is to have over a thousand companies using the exchange framework before the end of the year."

The DBNAlliance currently has over 35 member companies, and is actively recruiting new members.

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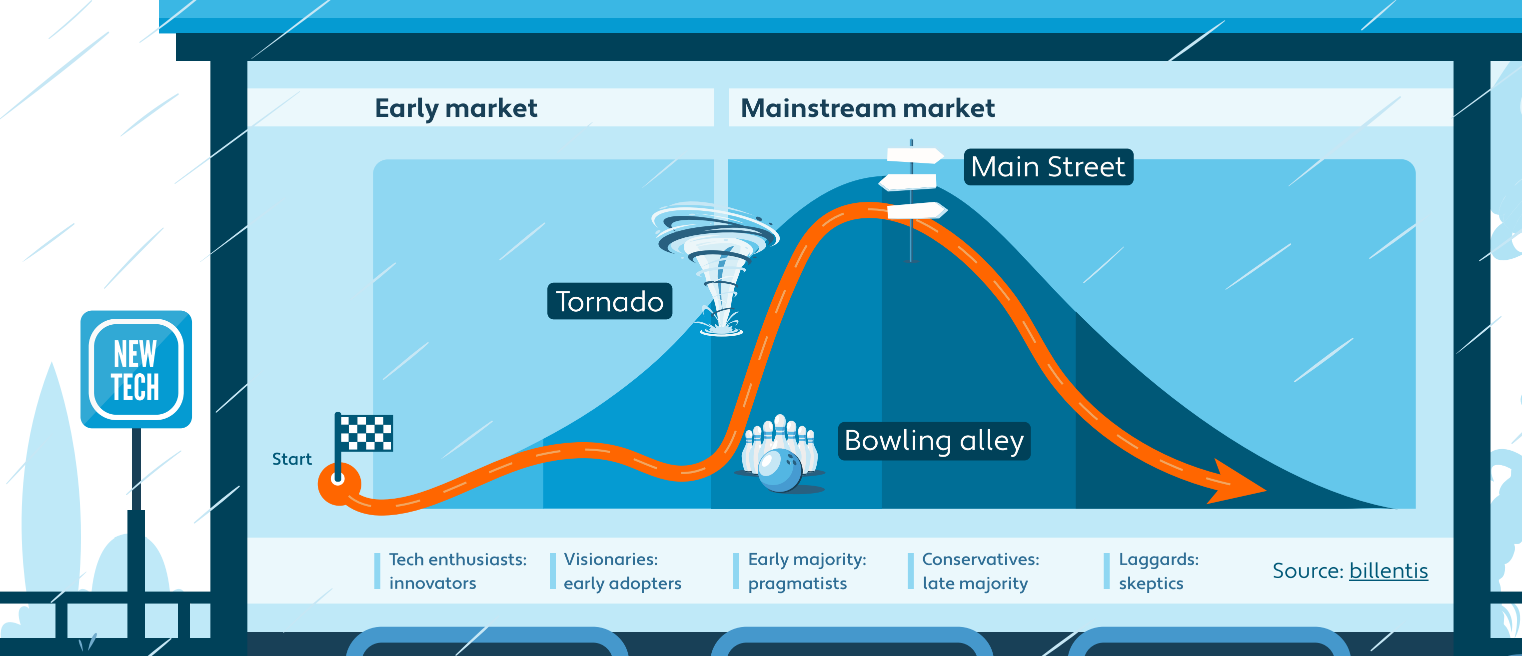
Despite the delays, e-invoicing adoption could gain momentum

Although we've seen numerous delays, alterations, and postponements to e-invoicing plans and mandates across global regions, e-invoicing is inevitable. According to a recent **billentis report**, e-invoicing is entering a "tornado" – a phase of rapid and widespread adoption of new technology and its consequent changes in the market.

Geoffrey Moore's "Inside the Tornado" – cited in the report – identifies five groups in various stages of adopting new technology: "Innovators" are typically first to embrace new technology; they're followed by "early adopters," "early majority," "late majority," and last of all, the "laggards." Adoption tends to peak at early majority, forming a bell curve.

Despite a large number of countries being unable to implement – or choosing to postpone – their original timelines for mandatory e-invoicing, huge changes in the economic landscape are imminent. Businesses therefore need to prepare for the widespread and global market adoption of e-invoicing and e-invoicing solutions.

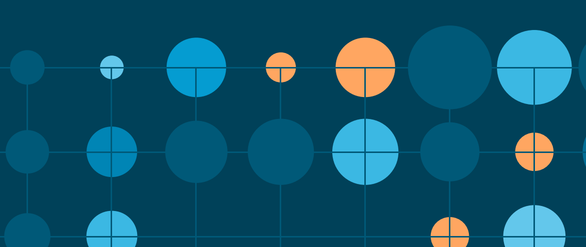


How Avalara can help

The tax compliance landscape is constantly evolving. Requirements, mandates, and government priorities often shift, change, or are delayed. Automation can help you keep up and stay compliant. Whatever the size, type, or industry of your business, Avalara can help you navigate global tax compliance challenges as you pursue your goals and grow. Learn more about Avalara automated solutions for VAT returns, e-invoicing mandates, and more.

EXPLORE SOLUTIONS

Up next: Looking ahead



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Looking ahead

It's impossible to cover every sales tax change in one report, so we aimed to spotlight the biggest headlines impacting the tax landscape and your business. Leading tax experts take a deeper dive into some of the most pressing issues affecting tax compliance in our 2025 tax changes webinar.

WATCH WEBINAR

For more resources:

Stop by the Avalara Tax Desk for breaking tax news — READ THE BLOG

Read about VAT changes in the EU and U.K. — LEARN THE LATEST

Check out the Avalara resource center for extensive tax compliance content — DISCOVER MORE

Learn how tax changes may affect your tax obligations — KNOW YOUR NEXUS

Or give us a call at 877-224-3650. Avalara is committed to ensuring tax compliance doesn't interfere with the growth or success of your business. Discover how automating tax compliance helps businesses track and comply with ever-changing tax laws around the world.