

Questions frequently asked about sales tax issues and AvaTax ST:

>> What exactly *is* AvaTax ST?

AvaTax ST is a sales and use tax calculation service which works in the background of your accounting system, via a secure internet connection. It has three capabilities: Address Validation (for correct identification of tax jurisdiction), sales and use tax calculation, and secure data storage for tax filing and reporting. AvaTax ST is the easiest, most economical, most accurate sales and use tax calculation solution available.

>> Is “use tax” different than sales tax?

Sales tax is a levy placed by states on goods or services purchased from a business that has a physical presence in the same state as the consumer. Use tax is a compensating tax owed when retail sales tax was due, but was not paid at the time of sale. This can occur when items are purchased by mail or over the Internet and the out-of-state business is not registered to collect sales tax. Use tax may also be owed by businesses that use items from inventory and do not pay the sales tax. Use tax is the customer’s responsibility to pay, but is increasingly being collected by vendors on their behalf.

>> What is nexus?

Nexus is a legal term which means connection to the state. Different state and federal courts have inconsistent definitions of what it means to have sufficient connection to the state to be subject to

tax. Nexus is typically defined by physical presence, but may also be defined by business activity, affiliation or other kind of presence, such as sales people calling on customers in the state. Businesses may owe sales or use tax based on nexus.

>> What constitutes a taxable sale?

Sale means any transfer of title to tangible personal property for consideration. It includes exchange and barter. The sale occurs at the time title passes. Unless otherwise explicitly agreed, title passes to the buyer at the time and place at which the seller delivers the goods, even though a document of title is to be delivered at a different time or place.

>> What is the Streamlined Sales and Use Tax Project (SSTP)?

The Streamlined Sales Tax Project is an effort created by 43 of the 45 state governments who collect sales tax, with input from local governments and the private sector, to simplify and modernize sales and use tax collection and administration. The Project’s proposals include tax law simplifications, more efficient administrative procedures, and emerging technologies to substantially reduce the burden of tax collection. The Project’s proposals are focused on improving sales and use tax administration systems for both Main Street and remote sellers for all types of commerce. Once SSTP is adopted, the burden of collecting sales and use taxes, particularly



for e-commerce, will be much simpler for companies who utilize the services of a SSTP-Certified vendor such as Avalara.

>> Is sales tax owed if a product is purchased through mail-order or on the Internet?

When you purchase items on the Internet and they are shipped to you in your state, the items you purchase are likely subject to sales tax. Some retailers who do not have a presence (nexus) in your state are not required to collect your state's sales tax. If you are not charged "sales tax" on your purchase, you likely owe "use tax."

>> What percentage of state's revenues come from sales and use taxes?

Nearly half of state revenues come from sales and use taxes. Some states rely even more heavily on sales and use tax income.

>> What items are taxable?

Typically all retail sales, leases, rentals, and services are taxable. Specific taxable items vary by state, such as food and prescription drugs. In other cases clothing may be taxed at a lower rate.

>> Are shipping and handling charges taxable?

This varies by state. Shipping and handling charges may or may not be taxable depending on whether the charges are part of the selling price of the tangible personal property being sold. If the seller and the buyer contract for the shipping and handling charges separately from the selling price of tangible personal property and the charges reflect the actual costs of such shipping and handling, then the charges may not be taxable.

>> What is a resale certificate?

A resale certificate is a standard business form that is used by registered businesses making purchases of goods and certain services which they intend to resell in the normal course of business without intervening use. The use of a resale certificate allows for purchases without paying sales tax. A resale certificate is usually required for all wholesale sales. Otherwise, sales tax must be charged. The specific rules for use of resale certificates vary by state.

>> Who must file sales/use taxes?

Most states require any person or business who holds a seller's permit to file sales and use taxes. These taxes must be filed and paid

in accordance with the state's regulations. Many states also require individuals to report use tax on their state income tax return. Specific requirements vary by state.

>> How often are sales and use taxes filed?

It varies by state, but typically sales and use tax returns must be filed and paid monthly, usually by the 20th of the month. When taxable receipts are less than a certain defined amount per quarter, then the vendor is only required to file and pay the taxes quarterly. These quarterly/monthly thresholds are defined by each individual state.

>> What is the likelihood of getting audited?

Since sales and use taxes are such a large piece of state revenue, states are getting more aggressive and have started increasing audit activity. States use several sources in selecting businesses for an audit, including Internal Revenue Service information; information-sharing programs with other states or other intra-state agencies; computer based random selection; state department of revenue database information; and business publications, periodicals, journals and directories. The average company faces an audit every seven years, based on studies of state audits.

>> What are the penalties if found to be delinquent?

Again, this varies by state. Most states charge penalties and interest for late payments, underpayments or not filing. States can also revoke the business license, shut down the business, and issue tax warrants for the business owner's arrest.

>> Do nonprofit organizations have to pay sales tax?

Most religious, charitable and nonprofit organizations are required to pay sales tax on the purchase of goods they buy for their own use and collect tax when they make taxable sales. Laws may vary from state to state.

>> In the AvaTax ST tax calculation service, how is security handled over the Internet?

Security is maintained by encapsulating the entire "conversation" (client to web service) using Secure Socket Layer (SSL) encryption, and establishing "best-practice" standards in username/password combinations. Account keys are generated through a 4 step process that includes using "one-way hash" and SHA encryption, creating

a “public/private” key setup that ensures that your client is uniquely identified and is the only software that can access your account and data. Once your data is on our systems we ensure its security using multiple layers of firewalls, IDS (intrusion detection systems), active traffic monitors, redundant storage systems and a thorough backup and disaster recovery process.

>> What is a “service?”

A web service provides integrated software functionality as a “plug-in object” that works in combination with your ERP application as if it were part of your software system. The Avalara service adds significant value, not only by enhancing the functionality of your system with address verification and automated sales and use tax calculation, but additional cost-saving features like dynamic reporting and automatic tax table updates.

>> How does AvaTax ST work with my accounting package?

Avalara establishes an integration bridge between the AvaTax ST service and your accounting package such as Great Plains, Quick Books etc. This bridge ties the AvaTax ST server and tax calculation and reporting functions directly to the order entry and invoicing process of your system. Setup inside your accounting package involves updating your configuration settings, identifying which customers are exempt, and which products have exceptions. Nexus states, type of nexus, and product taxability (product exceptions) are set up in the Avalara Administrative Console. Once set up, AvaTax ST correctly calculates sales and use tax calculations invisibly in the background and storing all transaction information for tax filing and reporting. AvaTax ST eliminates many hours of manual work.

>> How does the AvaTax ST service’s performance compare against competing software solutions?

A key feature of AvaTax ST is its address verification component which is based on the Federal Post Office address standard. By tying the tax calculation to the geo-code of a delivery street address, the discrepancies that can occur when a zip code overlaps two or more tax districts is avoided. Of course the AvaTax ST addressing component provides the additional benefit of verifying and keeping your customer demographic and shipping information up to date and accurate.

>> How can AvaTax ST achieve accuracy in the thousands of tax districts in the US and Canada?

Avalara has a focused team of state and local tax experts who constantly research the changing rates in all jurisdictions throughout the United States and Canada. To confirm accuracy, we run our own internal audits as well as contract independent audit agencies to review our calculations and check our compliance. Last year, with over 900 rate changes occurring throughout 7,500 state and local tax jurisdictions in the US, independent auditors found our calculations to be 100% correct.

>> How are the tax rates I use updated and how often?

Updates for the most current taxation statutes and tax rates, jurisdictions and address changes in the U.S. and Canada are provided from our database automatically so you never are required to update tax tables in your own system. The Avalara tax expert staff updates these central tables on a daily basis before changes take effect.

>> How are exemption situations (like a customer, a product or states) handled?

AvaTax ST enables users to easily manage all combinations of their tax rate exemptions and or exceptions and special tax situations by combining the notation of customer exemptions in the set up screens in your ERP system as well as product taxability matrix (product exemptions) in AvaTax ST. Set up once, and AvaTax calculates the rate based on these criteria automatically from there on.

>> How does AvaTax ST handle Use Tax?

AvaTax ST enables you to accurately calculate use tax, by selecting a product and invoicing it based on the receiving address. This use tax amount is compared to the tax on the vendor invoice and the balance is accrued in your GL distribution. In the case of a direct pay permit, AvaTax ST will calculate the required sales tax instead of the use tax. This methodology is in step with forthcoming SSTP standards.

>> How is taxability of a product defined?

AvaTax ST has a built in product taxability matrix which defines product exceptions, product types and categories. The majority of products are taxed under the standard rate for the applicable state and local tax district. As the manager of the system, you define what is and is not taxable for your business using these tools.

>> **How is the point of sale tracked?**

AvaTax ST calculates the sales tax due on a line item basis, while also tracking the total value of the invoice and any cumulative tax changes that result from accumulated values on the invoice. AvaTax ST utilizes the point of sale defined by your ERP system to determine the applicable address. In the case of a pickup, the pickup location is used. In the case of a delivery, the delivery address is used.

>> **What is the likelihood of Avalara's Internet connection being interrupted?**

Rest assured, an Internet failure at the Avalara is nearly impossible. Avalara's datacenter has direct connections to 7 discrete major backbone providers. If one of them goes down, there are six more backup connections to keep service active. This level of redundancy is extremely unusual, and ensures a constant connection.

>> **What happens if my Internet connection is down?**

If you experience a loss of your Internet connection during sales order processing, AvaTax ST will alert you of the connection failure, protecting you from accidentally posting, printing and mailing an invoice with incorrect sales tax. While your Internet connection is down you may still continue taking orders and preparing shipments. Once your Internet connection is restored, AvaTax ST will calculate the correct tax before you print order confirmations or post and print the invoices. If you suspect your internal network may go down, consider implementing a dial-up connection as a backup when needed. The amount of data passing is minimal, delivering satisfactory response times.

>> **What is the process for installing AvaTax ST?**

Unlike other solutions, AvaTax ST takes only a few hours to set up — not days, weeks or months. AvaTax ST is a hosted Internet service. Installation begins with downloading the small, non-invasive AvaTax ST Client from the Avalara web site and following the installation wizard. Next, configure your ERP/accounting package by following the instructions provided with the download. Last, go to the Avalara Administrative Console (secure website) to setup your nexus and taxability specifications. AvaTax ST will now accurately calculate all sales and use taxes transparently in the background each time you create a purchase invoice or sales invoice.

>> **Does new data ever need to be uploaded or installed?**

The AvaTax ST databases (residing on our servers) are updated continually (invisible to you) ensuring that you're using the most current information possible every time you create an invoice. You don't have to worry about monthly data CD updates to install or downloads to coordinate. Although complex in the background, the AvaTax ST service is transparent and seamless to your normal work flow.

>> **Do Client upgrades ever need to be installed?**

The AvaTax ST Client (residing on your local computer) is a simple "connector" to the AvaTax ST service. If and when future updates are provided, all you'll need to do is download and run a simple update patch.

>> **How is filing taxes done, who does it?**

AvaTax ST presents a report that provides all the information you need to complete and file required tax returns. We have an optional feature of automatically filling out your tax returns through a third-party service. And we do not believe in holding your data hostage — you may download it into Microsoft Excel any time you like.

>> **Am I charged for every transaction?**

No matter the size of your business, AvaTax ST is affordable. With AvaTax ST's service-based pricing you pay a monthly fee based on an estimated transaction volume for the first year. If the transaction estimate is exceeded, you have the option of upgrading to the next level of service or continue by paying a small per-transaction fee. Our pricing method allows medium-sized and small business to affordably take advantage of AvaTax ST's power. Large companies will find AvaTax ST provides more thorough capabilities than competing solutions which cost several times more. A transaction is an invoice. You are only charged once per invoice, even though the invoice may call on AvaTax ST data several times per invoice.

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