Articles

Sales and Use Taxes: Investigating the Administrative and Compliance Costs for U.S. Small Businesses

Amy Cardillo¹, Andrew Holt¹, Scott Schlaufman¹

¹ Department of Accounting, Metropolitan State University of Denver

Keywords: sales tax, Colorado, accounting, micro business, regulatory burden, compliance, costs, tax, small business

<https://doi.org/10.53703/001c.28148>

Small Business Institute Journal

Vol. 17, Issue 1, 2021

Since the 2018 ruling from the Supreme Court on *South Dakota v. Wayfair*, the issue of sales tax collection and its impact on small and micro-sized businesses has become increasingly debated. Investigating how small business owners currently deal with their sales and use tax collection burden is beneficial for aspiring entrepreneurs wishing to learn best practices and state regulators desiring to help ease the compliance burden. This study explores the accounting and administrative burdens that the collection of Colorado sales and use taxes place on small and micro-sized entities, how small business owners attempt to efficiently and inexpensively navigate the requirements, and the role regulatory agencies play in helping navigate this regulatory burden. The project utilizes an interpretivist perspective using data obtained from 50 semi-structured interviews with small and micro-sized business owners and managers in Colorado. In addition, 6 interviews were conducted with representatives from various Colorado tax-regulatory agencies to investigate the levels of sales tax support and guidance currently being provided, and 2 interviews were conducted with tax and accounting professionals to provide a better understanding of the compliance issues. Despite some assistance from tax regulatory agencies, small and micro-sized entities in Colorado face sizeable accounting and administrative regulatory burdens from the sales tax process that consume valuable management time. In the end, the most common way small businesses manage their cost and regulatory compliance burdens is through the use of an accountant or bookkeeper.

INTRODUCTION

Since the June 21, 2018 Supreme Court ruling on *South Dakota v. Wayfair*, the discussion of sales tax collection and its impact on small businesses within the United States (U.S.) has become increasingly heated. This Supreme Court decision, as well as other debates about sales tax, are most commonly viewed from the perspective of large retailers, such as Wayfair and Amazon. However, the impact on the small and micro-sized business owner often remains unexplored. The *Wayfair* decision has granted states the authority to impose sales tax on retailers if it does not impose undue burdens on interstate commerce (Bishop-Henchman et al., 2018). An equally important and unexplored concern is the potential impact of sales tax compliance on small retail entities.

This paper explores how the owners of U.S. small and micro-sized businesses manage the accounting and administrative burdens of sales and use taxes and seeks to determine whether the 2018 Supreme Court ruling has further increased tax-related compliance costs for such entities. To achieve these objectives, the study analyzes interview data from small and micro-sized business entities registered and operating in the U.S. State of Colorado, a state which relies comparatively heavily on revenues obtained from sales and

use taxes. For the purposes of this study, small and micro-sized entities are defined as businesses with fewer than 50 employees. As regulatory and compliance agencies in Colorado typically provide small businesses with educational and technological assistance for tax-matters, the study also investigates the role these institutions play in facilitating sales-tax compliance. These institutions include home rule cities, which are governments that levy and collect sale and use taxes separately from the state. Thus, the overall goal of the study is to gain a better understanding of potential challenges in the sales tax system utilized by the State of Colorado and to determine how successful small business owners navigate these challenges.

Intertwined with the sales tax burden is that of use taxes. While this study focuses primarily on sales tax, use tax is also relevant. The *Wayfair* decision, as well as prior cases surrounding sales tax, concentrated heavily on use tax when discussing sales and purchases outside of a state. Use tax is required to be paid to the state if a purchase of an item is made outside of the domicile state but will be used in the domicile state. Colorado first began collecting use tax on sales of online retailers, but brick and mortar retailers are also subject to use tax. Online retailers that sell to customers in Colorado must notify their customers of potential use tax and must file a report with the Colorado Department of Revenue. The report includes the names of local

residents, their addresses and amount spent on their purchases (Erb, 2016).

BACKGROUND TO THE STUDY

Sales taxes within the United States are a crucial part of the country's economic structure. A 2012 study estimated that sales tax accounted for nearly one-third of state taxes and a quarter of state and local taxes (Bruce, 2013). Sales and use taxes in the US are highly complex because the tax rates are not only different in every state, but can also be different in each locality of every state. Due to the complexity of sales tax, the "reliance on vendors is necessary because it would be infeasible for state revenue departments to collect retail sales taxes on 'countless' transactions on their own" (Cornia, 2000, p. 1327).

Despite such a large reliance on sales and use tax on a national level, few research studies have explored the burdens that tax collection imposes on small businesses. In the National Small Business Association's 2017 survey of small business regulations (National Small Business Association, 2017a), only 8 percent of small businesses reported sales tax as the most burdensome tax from an administrative perspective. However, the report also asked respondents about other potential burdens related to sales tax. When specifically discussing sales tax, 57 percent had "significant concern" about navigating various state tax rules and deadlines, 56 percent had the same level of concern about keeping abreast of state tax rate and payment date changes, and 45 percent of respondents had significant concern about the threat of tax liability resulting from inadvertent errors and the threat of increased audits (National Small Business Association, 2017a, p. 10). The report also estimated that one-third of sales tax filers spent at least a full work week each year on sales tax compliance issues.

The 2017 Colorado Department of Revenue Report estimated that one-third of the State of Colorado's income is based on sales tax and that home rule cities rely on sales tax for up to 80 percent of their revenue each year (Colorado Department of Revenue, 2017, p. 4). Because of the reliance on sales tax, Colorado's sales tax structure can be complicated. As of 2013, there were 294 different sales tax jurisdictions within the state, including 69 home-rule cities, 51 counties, 152 statutory cities and towns, as well as special districts. As a result, sales tax rates may vary within a city or zip code due to overlap between taxing jurisdictions. In total, there are currently approximately 756 different sales tax rates and bases within Colorado (Colorado Department of Revenue, 2017, p. 2).

Colorado uses information from multiple databases to help businesses determine their tax rates. Nevertheless, a state-conducted audit of tax year 2014 discovered that nearly 11 percent of reviewed businesses were found to be paying tax to the incorrect jurisdiction, which resulted in \$3.3 million in over-collection and \$3.8 million in under-collection (Colorado Office of the State Auditor, 2015, p. 1). Each of these jurisdictions may also change what is or is not taxable at their specific sales tax rate. At a state level, Colorado offers exemptions on 15 categories of items such as food for home consumption, farm equipment, and property used in space flight. Individual jurisdictions have the ability

to remove these exemptions and apply their sales tax to that specific category. For example, while the state may not tax groceries, cities may still impose their tax to the sale. These exemptions can vary widely from place to place, as can the definition of items under each category.

The collection of these taxes can be equally complicated. While the state collects for smaller cities and a majority of the counties, home rule cities require businesses to make separate payment directly to that governing body. Businesses must acquire a separate sales tax license for these cities and pay them directly. The remittance methods can also vary by location, with some cities opting for online remittance only, while others may only take paper payments, and others offer both methods. Navigating this complex and cumbersome taxation process is challenging, but despite this fact, small and micro-sized entities in Colorado are relied upon to accurately collect a significant portion of Colorado tax revenues.

Colorado governments have started to recognize these burdens. In 2017, the Colorado state legislature created the Sales and Use Tax Simplification Task Force. The purpose of the task force is to simplify the entire taxation process by adopting uniform definitions for product types and evaluating the feasibility of implementing a centralized remittance system that would allow businesses to pay taxes to state-collected entities and home-rule cities from one place. Positive strides, discussed later in this paper, have taken place that may begin to help alleviate sales tax compliance burdens, but the road is still steep.

LITERATURE REVIEW

Regulation plays a key role in many aspects of society. Kitching writes that the primary purpose of regulation, from the perspective of government, is to maintain and enhance the conditions that enable an advanced market economy to function (Kitching, 2008, p. 800). He continues by writing that, "as far as any particular small business is concerned, regulation can affect it directly or indirectly" (Kitching, 2008, p. 801). An example of direct influence includes tax payment.

Regulation, if not designed and implemented properly, can adversely affect small businesses. Patton suggests that, "small businesses are a vital source of economic growth in the United States. Reducing their cost for complying with the tax code may free up resources to expand, hire new employees, and contribute to the growth of the U.S. economy" (Patton, 2016, p. 7). Since tax payment directly affects a small business, it causes certain burdens to the business and its owners. Research has highlighted that tax compliance burden includes time and money spent by the business to meet its tax obligations (Patton, 2016). Patton (2016) continues, writing that, "time spent on tax activities can include working with a paid professional, tax planning, keeping records, completing forms, submitting forms, learning tax laws, and working with IRS on tax issues while monetary burden can include expenses for hiring a paid professional to file taxes, investing in a tax software system, paying for payroll services, and legal fees" (p. 7). Furthermore, in a study by the IRS about the cost of regulatory compliance, it was apparent that as a business grows, so does its overall

compliance cost (DeLuce, 2007).

Within the NSBA's 2017 *Small Business Regulations Survey*, 58 percent of respondents viewed federal regulations as the most burdensome to their business, and 23 percent saw state regulations as being burdensome (National Small Business Association, 2017a). In the NSBA's 2017 *Small Business Taxation Survey*, the largest burdens posed by the federal tax code were ranked as follows; financial cost to the business (38 percent), complexity and the concern over getting audited (22 percent), administration of tax forms and the time it takes (14 percent), and amount of paperwork that must be completed (8 percent). As financial and administrative issues are major issues for most small businesses, sales tax represents one of the most burdensome taxes that most small businesses face after income taxes, payroll taxes, and state and local tax compliance (National Small Business Association, 2017b). A 2004 study conducted by PricewaterhouseCoopers, LLP (PwC) found that the average sales tax compliance cost for small businesses within the United States (US) was more than six times greater than that of large retailers (PricewaterhouseCoopers, LLP, 2004). Pedro Alfonso, NSBA Chair, and Todd McCracken, NSBA President, suggest that "while the financial tax liability for small firms is a huge issue, administrative complexity continues to pose an even bigger problem", and that "unfortunately, the current U.S. Tax Code is becoming an insurmountable hurdle for the growth of existing businesses and creation of new firms" (National Small Business Association, 2017b).

PROBLEM AND PURPOSE STATEMENTS

PROBLEM STATEMENT

The general problem to be addressed is to ascertain how the burden of sales tax compliance is currently being managed by small business owners, especially after the changes introduced by the *Wayfair* decision. State legislatures acknowledge that Colorado receives an "F" when scoring its ease of sales tax compliance. Consequently, Colorado is attempting to make regulatory changes to reduce sales and use tax compliance costs (Frieden & Nicely, 2018). Since small businesses are subject to sales and use tax laws, understanding how successful small business owners manage the compliance cost processes may offer valuable insight to both regulators and aspiring entrepreneurs.

PURPOSE STATEMENT

The purpose of this qualitative study is to acquire an understanding of how Colorado small business owners perceive and manage their sales and use tax compliance process. When small business owners were asked who in the business spent the most time on regulatory compliance, forty percent responded that the owner was personally responsible (National Small Business Association, 2017a). While larger firms usually rely on tax professionals to manage tax compliance issues, the small business owner personally manages these compliance and regulatory burdens (National Small Business Association, 2018).

Relatively little literature is available on sales and use tax compliance, as other tax and regulatory burdens weigh

more heavily on the small business owner (National Small Business Association, 2017a). However, with the recent Supreme Court ruling on the *Wayfair* case, an increased focus on sales and use taxes has already started to occur (Luscombe, 2018). As new regulations emerge, the small business owner is continually tasked with staying abreast of the changes and facilitating the additional workload that may accompany those changes. Understanding how a successful small business owner manages this process may not only help offer guidance to emerging entrepreneurs, but may also help enlighten regulators to burdens not easily discovered through purely quantitative methods alone.

The specific aims of this paper are to investigate the following research questions.

1. How do Colorado-based small businesses successfully manage the burden of the collection and payment of sales and use taxes?
2. What role do governmental agencies play in assisting small businesses with the collection and payment of sales and use taxes?

By adding new findings to the limited research presently available on the topic, the study will reveal new insight about the problems small businesses face and how they successfully manage their sales tax compliance responsibilities.

The next section outlines the research design and methodology for the study. Separate sections then examine the interview data from the perspective of both regulators and small businesses. The conclusion section then draws these together to explain how the study contributes to the existing literature on understanding how sales and use taxes affect small businesses.

METHODOLOGY

This study will use a narrative research approach by conducting personal, semi-structured interviews with approximately 50 successful Colorado small business owners and/or managers, defined as businesses with under 50 employees. The overall aim of the interview is to understand the owner's perception of the sales and use tax process and how she or he manages the process, and to recommend on ways to improve the compliance process. This study will also interview state regulatory personnel with the aim of understanding what the state is attempting to do, if anything, to help ease the compliance burden.

The project adopted an interpretivist perspective using interviews to explore "data on understanding, opinions, what people remember doing, attitudes, feelings and the like, that people have in common" (Arksey & Knight, 1999, p. 2). A survey-based study was rejected due to its inability to elicit detailed data from the respondents since the subject matter concerned the tax compliance practices of interviewees who may be reluctant to be truthful about such issues in a formal survey. Semi-structured interviews were conducted with two populations of interviewees: tax regulators and business owners/managers of small and micro-sized entities.

In total, 165 businesses and 11 regulatory agencies in Colorado were approached as potential interviewees. From

these contacts, a total of 58 interviews of 20-40 minutes were completed with interviewees, including:

- 50 representatives of small and micro-sized entities (2 interviews within one business)
- 6 representatives from Colorado-based tax regulatory agencies, including interviewees from the Finance and Tax & Licensing Department and the Colorado Sales and Use Tax Force.
- 2 tax professionals / certified professional accountants

Interviewees were given information about the nature and purpose of the research, and permission was required to record the interviews. They were made aware that the report would include anonymous quotations and that identifying information would be removed prior to publication of the final report. Most of the interviews were recorded, and interviewees were offered a copy of the final research report.

The 49 small and micro-sized businesses within the interview sample were located in a variety of locations within the Denver metropolitan area and represented a wide range of industry-types, including retail, food and beverage, general merchandise, miscellaneous services, non-profits and on-line retailers. All 49 companies employed fewer than 50 employees, with the majority having between two to eight full-time staff. Additionally, nearly half of the businesses have been in business for more than five years

Most small business interviewees were from entities that collect more than \$300 per month in sales tax. Identifying this characteristic is vital. Entities that collect more than \$300 per month in sales tax must file monthly sales tax returns, while those that collect between \$15 - \$300 per month in sales tax must file quarterly (Colorado Department of Revenue, 2017).

Of the businesses interviewed, 53 percent used a dedicated software package at point of sale to help charge and track sales tax receipts, and a further 12 percent used computer-based spreadsheet packages to assist with tax record keeping. Forty-two percent of business owners acknowledged the use of third-party accounting and tax advisors to help manage the collection and payment of sales tax collection. This regulatory compliance cost is potentially a barrier for entry into the small business marketplace, but the use of third-party accounting and tax advisors appears to be the most common method for small business owners to deal with their sales tax compliance burdens.

FINDINGS

The interviews were analyzed using a thematic approach, which entailed identifying themes from interviewee's responses and grouping them into categories that share a common characteristic. The themes were first identified separately for both the government interviews and the business interviews. Further analysis was done to identify where themes from the interview sets may have overlapped. The next sections report on the sales tax-related themes discovered during the interviews.

FINDINGS FROM THE REGULATORY INTERVIEWS

All local regulatory interviews were conducted with representatives with home rule cities. To better understand the tax structure and the responses, a brief discussion of Colorado's taxing entities is necessary. Colorado's taxing entities can be broken into four different groups.

1. Self-collected home rule cities/counties — these are government entities that administer and enforce their city-specific sales and use tax. The methods of enforcement and collection are up to the specific governing body. Remittance of this tax goes directly to the government instead of through the state.
2. State-collected cities/counties — these are government entities that have specific sales tax but rely on the state for enforcement. All remittance is done through the state website and then disbursed to the respective entities.
3. Regional Transportation District (RTD) and Scientific and Cultural Facilities District (CD) Taxes — these are state-collected taxes that apply to specific areas within the Denver metropolitan area. RTD taxes go to the regional transportation district and CD taxes go to the Cultural Facilities District.
4. Special District Taxes — Similar to the RTD and CD taxes, these are state-collected taxes for different purposes, such as local improvement districts or transportation systems around the state.

These taxes overlap with each other, meaning that in one transaction, a business may be required to collect and remit RTD, CD, state, and county tax through the state portal, in addition to a separate city tax. There are 756 possible taxing combinations within the state of Colorado due to the taxing structure of the state. The Colorado Sales and Use Tax Simplification Task Force estimated that sales tax within Colorado produces 69 percent of municipal tax revenues which is much higher than the municipalities of other states, estimated at 17 percent.

The themes discovered during the interviews, including the regulatory perspective on the small business burdens created by sales and use tax, will now be discussed in more detail.

Reliance on sales tax. As noted above, Colorado's home rule cities rely very heavily on sales tax, which was something clearly noted by all government representatives. Sales taxes are the number one driver of revenue for the cities; so collection is paramount.

*"Ultimately we need it to fund the services we provide ... if we have a 1 percent variance in our sales and use tax, that's 2.3 million dollars that we lose out on."
(Government 5)*

Problems auditing small business sales tax collections. The primary methods home rule cities use for enforcement are a mix of comparative statements and audits. The comparatives use previous data, either from the business being audited or a similar type of business, to find potential issues. Full sales tax audits of small businesses were surprisingly rare, both due to the huge number of such entities and the fact the regulatory agencies had limited staff

to perform audits.

"The problem for us is that we only have three auditors and 6,000 businesses. They average 20 to 30 audits a year, so they're really going after the big guys."

(Government 4)

In addition, regulators were more concerned with investigating businesses with higher, material taxable liabilities.

"We engage in audits, more of the bigger businesses, but at times the smaller businesses. Again, it's hard to know that every single business is paying the right amount because we can't audit everybody. We just don't have the manpower to do that."

(Government 2)

Confusion on tax rates and exempt items. The government representatives interviewed indicated that it was generally easy to determine the sales tax rates within their city. The larger concern is with exemptions on different kinds of items. While the state exempts certain classes of items from taxation, every other taxing jurisdiction can choose whether those items can be taxed within that jurisdiction.

"A small business that doesn't have a background in tax struggles with that. They say 'Oh, this stuff is nontaxable,' so they'll file the state return and use the same numbers for the (city) return. Well, they neglected to pay taxes on stuff that's taxable here."

(Government 5)

"Colorado has a very fragmented system. Sales tax requirements in (city) are different than (neighboring cities) and all over the place, so that definitely causes confusion, especially for those people that operate multiple facilities throughout the region. That's a real concern."

(Government 3)

"From a staff perspective, it gets confusing as well. At least on the economic development side, we'll have prospects that come in and ask about sales tax, what will they pay sales tax on, what won't they pay sales tax on, sometimes it's not a cut and dry answer. We're going back and saying 'What category does this business fit in?' ... We're constantly going back to the code and looking to make sure we are following our own rules."

(Government 1)

One government official also raised concerns with compliance on items such as candy, which can be subject to different taxes based on its jurisdiction. The definition of "candy" can vary between locations. During the interview, this government representative pulled out a grocery bag full of items and asked the interviewers to help decide what was "candy" and what was not. An item like a Kit Kat bar, which contains flour-based wafers covered in chocolate, is not taxed as a candy because it contains flour, where a bag of M&Ms does not and will be taxed as a candy. Similarly, items with similar packaging and branding may or may not be subject to tax based on a small list of ingredients.

Sales tax education and understanding for small businesses. All of the government representatives interviewed for the project suggested multiple ways for small business owners to better understand the sales tax system. All the interviewees stated that their city offered online and/or in-person educational classes and provided auditing

assistance to new businesses. Many of the cities also have small business development centers, which offer an array of resources for upstart businesses. One government official even noted that meetings with new businesses can be relatively simple, depending on their records.

"A lot of these are pretty quick. The biggest challenge in the small business environment is the computer system. Some have good ones, some have cash registers."

(Government 4)

Businesses of concern. Delivery-based and mobile businesses, such as food trucks and sign companies, were the types of business that all the government representatives consistently described as being at the most risk for sales tax related errors. These types of businesses usually operate in multiple jurisdictions, thereby compounding the difficulty of sales tax compliance.

"Home Depot charges (city) tax because you bought it there but a printing press company, a guy who installs solar, someone who does heating and air conditioning. Depending on how they define their item, they can technically be selling it at a different location and it's a completely different tax. ... We get a lot of pushback from those companies going 'What the hell?'"

(Government 3)

"If I've got QuickBooks or some other system that's sophisticated enough, ok. But if I'm a small business person humping it to make money, I may not take the time to figure it out. All of a sudden I do a \$500 job and a \$10,000 deal here, a \$10,000 deal there, I don't know whose it is and that becomes hard."

(Government 3)

Push for online filing. Within Colorado, there is no standard system that small businesses use for remitting sales tax receipts. Although the State has an online portal for the state-related monies, each of the home rule cities uses their own bespoke systems. Some collect through independent online filing systems, while some still only offer paper remittance, and others offer both. Despite the differing systems, there was a strong preference for online systems, even if cities have not fully implemented them.

"Not being able to offer that for a lot of businesses is a nuisance to them that they have to file on paper. I think a lot of people want to get out of that. It's just an extra, cumbersome process." (Government 5)

One government official said online systems have the potential to eliminate overpayment or underpayment of taxes.

"The online calculator basically helps to eliminate mistakes. If you key in sales, it's going to calculate everything for you."

(Government 4)

Steps towards simplification. While there may be points of confusion, governmental agencies throughout Colorado have started working together to help simplify the sales tax process and facilitate better understanding of the rules by both regulators and businesses. The Colorado Municipal League, a nonprofit and nonpartisan organization

that acts as a voice for the cities and towns around Colorado, is in the process of implementing a project to standardize definitions for 106 different items and categories of items. The standardized definitions have been adopted by 53 different cities and towns as of August 14, 2019.

“Over the last three-plus years now, there’s been an effort to standardize our sales tax definitions so that ‘grocery food’ means the exact same thing in all 79 cities. Some may tax it, but the definition is standardized, which eliminates some of the gray of ‘what do you mean by it’, is it really taxable or exempt. We’ve really done a lot of work to standardize definitions.” (Government 2)

Additionally, Colorado legislature formed a Sales and Use Tax Simplification Task Force prior to the 2017 session. The task force investigated multiple ideas, including both the standardized definitions project and the potential for a single website that would allow business to remit their tax to both the state and the home rule municipalities. The governments believe that this would make compliance easier for business owners, especially those who owe tax in multiple places.

“Currently somebody like that would have to pay each city separately. They’d have to go into each website to remit online or, in some cases, mail in a paper form and a check and they have to do it all over the place. We’re trying to work towards a platform online where those businesses can go in, and in one shot they file their returns for all their obligations and do one wire transfer into that portal and have the portal disburse the funds to everybody and make it easier for them.” (Government 2)

As of September of 2020, Colorado now has a single web portal for sales tax collection where businesses can look up sale and use tax information as well as file and remit to all jurisdictions at one time. Uniform definitions have not yet occurred and only a small portion of jurisdictions have signed on to use the portal (Joint Technology Committee, 2020). However, this is a positive step in helping to simplify the taxing burdens for small business owners in Colorado.

Other tax issues raised. While most of the interviews focused on sales tax, use tax was a high concern for nearly all the interviewees. The tax essentially levies a sales tax on an item purchased outside of the taxing area, with the idea that if the item had been purchased there, it would have been subject to the sales tax. Like sales tax, use tax can vary between places. One government representative interviewed only had a small number of items subject to use tax in his jurisdiction, while the others interviewed had a much broader scope of use tax and placed it as a high priority.

“That is the most prevalent situation where businesses underpay is in use tax area and that’s the primary revenue that our auditors find when they conduct audits of business.” (Government 2)

With that in mind, multiple government representatives said smaller businesses tend to pay the required sales tax on the front end of a transaction.

“A lot of smaller businesses, it’s more likely they’ll be pur-

chasing things they use in their business from a local retailer. The audit staff definitely pays attention to, and has on their work plan, ways to look at the businesses that have a use-tax obligation.” (Government 1)

“The bigger businesses have figured it out and complied pretty well. A lot of the smaller businesses choose to just pay sales tax up front.” (Government 4)

DISCUSSION OF THE REGULATORY INTERVIEWS

Colorado’s regulatory bodies recognize that there are weaknesses in the sales and use tax collection system and have started to proactively make changes that will allow them to collect their share of revenue, while also making things easier for the businesses that must remit the taxes. The standard definitions project should allow for more clarity about what items fall under which categories, and having each jurisdiction fully embrace the statewide remittance system could make compliance significantly easier for businesses operating in multiple jurisdictions.

FINDINGS FROM THE INTERVIEWS WITH SMALL BUSINESSES

During the small business interviews, several common issues emerged: (1) proper filing of sales tax; (2) administrative support; (3) interaction with the regulators; (4) sales tax collection for cash businesses; and (5) the risk of a sales tax audit. The themes of the interviews with the small businesses are below.

SALES TAX FILING

There are different sales tax requirements within the state of Colorado dependent upon amount of revenue, type of business, or location of the business entity. All businesses have the option of either filing their stated state sales tax returns online or on paper, however, some municipalities still require paper filing. (At the time of this study, the statewide portal was not yet in use so the interviewees had only had experience with the current online system). The 2017 Annual Report of the Colorado Department of revenue found that 82 percent of returns were filed online. This is a dramatic increase from 2013 where only 50 percent of businesses filed their sales tax returns online. With most of the businesses interviewed filing either monthly or quarterly, a minimum of four filings per year allowed the interviewees ample opportunity to form opinions about the filing requirements. While utilizing online filing is done for convenience, the general feedback of the online system was negative for those businesses that filed their own sales tax returns.

“The website is atrocious, clickable items are determined by color but you have to move your mouse across the page to see if something can be clicked on. We are a trapped party we have to figure this out. If you evaluated their website and presented it in a way an independent person could figure it out, it would be better.” (Retail Store 12)

Those who filed their own sales tax returns generally reported a confusing and negative experience with online filing. However, those who used sales tax software, a spreadsheet package such as Excel, or tools built into online sales platforms, did not find the actual filing of taxes difficult.

"It was a piece of cake. I just filled out the information on their online form and submitted it. They verified I was living at the address, was going to do this and that, and mailed it to me and I was ready to go."

(Online Retailer 1)

Small business owners that used a software package to track sales tax use provided that it was not the dollar amount of sales tax that negatively affected their businesses, but rather the time it takes to file.

"In [my line of work], it is commonplace to have a hundred clients a year – each in their own city/county combination. At the end of the quarter, it takes me a solid weekend to compile all the jobs I had into Avalara, and make the appropriate payments."

(Retail Store 16)

"The first year I did it, I underestimated how long it was going to take to make the payments to all the governments. Each one had their own system and it took an entire week to figure each one out."

(Service Provider 1)

Some of the small business owners also expressed that doing business in other jurisdictions would be too complicated and time consuming with the different tax rates. As a result, they only operate where they are comfortable.

"When I was looking into opening a second location in Longmont a few years back, I was shocked at all the additional licenses I needed to acquire and additional expenses." (Service Provider 2).

ADMINISTRATIVE AND TECHNICAL SUPPORT

Over half of the small business owners and representatives interviewed used a software package or Point of Sales system to track their sales tax obligations. An additional 12 percent used readily available software packages, such as Excel or QuickBooks, to track their own sales tax obligations.

"We use a POS System that tracks every single transaction, it tracks every single discount, every single voided transaction. It also breaks down individual line items. On our end it's really easy because we have this automated system, we're not in the Stone Ages where we have to calculate everything on paper."

(Food and Beverage 4)

Most notable was the fact that over half of the small business owners interviewed retained an accountant or bookkeeper to track and remit their tax obligations. When looking at small business owners who had been in business for over five years, more than 92 percent hired an accountant or bookkeeper to handle their tax requirements. However, all who did pay for outside help indicated that the cost was substantial, which is prohibitive for small business owners that do not have the income to support paying for adminis-

trative help.

"Having someone do accounting work for you is a big cost. If you can do it all yourself, you can save a lot of money, but it's not easy to do it all yourself."

(Food and Beverage 2)

"Administrative costs are my biggest [non-COGS] expenditure. Between dealing with insurance companies and with paying my CPA to prepare my quarterly taxes, compliance costs are about to run me out of business."

(Service Provider 3)

Some businesses did not hire an accountant or a bookkeeper at first, but when their sales started to increase, they realized that the administrative burden of sales tax filing was too much for them to handle.

"I had to hire an American accountant to manage all of the U.S. taxes. I was making it work until I hit a trade threshold which added additional requirements. I worked a deal with my chartered accountant, so she only takes a flat percentage of each [product] sold, making [compliance something that] I can afford."

(Online retailer 3)

"I don't even want to think about all the overhead costs I've spent on CPAs to figure out who I owe, and how much I owe."

(Retailer 17)

INTERACTION WITH REGULATORS

In discussing interactions between regulators and the small business owners, the interviewees' immediate response was to describe audit experiences. Because only five percent of the small businesses included in the study, had been audited for tax purposes, the majority of the businesses had little to no interaction with regulators. Of the audited businesses, all had been operating for more than five years and filed their sales tax monthly. However, as sales tax in Colorado was a major revenue source for the state, cities, and counties, small business owners clearly saw pressure for their entities to comply with relevant sales tax laws.

"When you screw up from not knowing you are flagged in that system forever. They're gonna keep an eye on you. They're gonna come after you again."

(Gen Merch Store 8)

"Regulators are pretty vigilant during events. They go around and make sure everybody is collecting and charging sales tax."

(Retail Store 6)

However, ideally, interactions with regulators should include more than audit experiences. The regulators who were interviewed indicated that the various municipalities offer multiple areas of education and support for small business owners. When further pressed regarding interaction with regulators, many of the small business owners indicated that they did not receive support, that they were not aware of the services, or that they chose not to utilize the services provided.

"I vaguely remember seeing ads for 'Contact these people if you want support' but no one in the government took the time to reach out to me."

(Online Retailer 1)

"I know that exists but it, to me, has the stigma of the DMV. Like, I don't want to go down there and wait an hour to ask a couple of questions and they might belittle me or talk down to me, so I would rather ask someone I know or find information on the internet". (Food and Beverage 2)

It is apparent from these responses that there is a disconnect between what the local municipalities offer for small-business support and how the small business owners view this interaction with the regulators. Open communication without fear of retribution would create a substantial improvement in the regulator to small-business-owner relationship.

CASH BUSINESSES

For businesses with Point of Sale systems, credit-card processing, and CPAs or bookkeeping software, sales tax compliance, as discussed above, is costly, but less burdensome in regards to time. However, the businesses interviewed that deal mainly in cash seldom have sophisticated accounting software, so these businesses creatively manage their sales tax burdens. According to Colorado's Sales and Use Tax General Information and Reference Guide, "the law requires that you list sales tax separately from the purchase price of the items you sell on all invoices, billing and business records" (Department of Revenue, 2017, p. 2). However, this may not be the case for most small cash businesses in the study that will usually offer one cash price, in which sales tax is included.

"I do my price, I do a percent for tax and do another for profit. Usually people think better when they don't pay tax." (Gen Merch Store 6)

Cash businesses from the study included small businesses with seasonal stands and bazaar vendors. Most of their sales are cash payments, which commonly involve a flat rate for their sales instead of the purchase price and sales tax together. Many of the cash businesses stated that they would "cover" the sales tax charge if customers paid in cash. If a customer paid with a credit card, sales tax was then charged as it is reflected in the credit card processing system.

One cash business owner admitted that they did not report the actual amount of cash received, *"I report an estimate of cash; some of it gets lost or stolen"* (Food and Beverage 6). This business owner reported that he had been operating for more than a decade, and with various locations. He said, due to the logistics, they cannot keep track of all cash receipts. Thus, they use estimates based on past years to file for sales tax.

CONCLUSIONS AND RECOMMENDATIONS

Although this study only includes interviewee data from 49 small business owners and managers within a single metropolitan geographical area, it was apparent that better com-

munication, better record keeping and a more convenient sales tax remittance system would greatly improve the relationship between small business owners and regulatory agencies. Additionally, the potential for more accurate sales-tax remittance would also be appreciated. The purpose of this study was twofold: to determine 1) how Colorado small businesses successfully manage the burden of the collection and payment of sales and use taxes, and 2) what role governmental agencies play in assisting small businesses with the collection and payment of sales and use taxes. The findings and recommendations are summarized below.

CONCLUSIONS AND RECOMMENDATIONS FOR SMALL BUSINESSES

To ease the burden of sales tax compliance for the Colorado small business owner, the answer found within these interviews is, unfortunately, costly. The small business owners interviewed that had been profitable for longer than five years overwhelmingly used the help of an accountant or a bookkeeper to manage their sales and use tax burden. This cost is burdensome to many and potentially prohibitive for those looking to start a small business.

While the primary desire of small business owners is to successfully manage their own operations, this cannot be accomplished without acknowledging and understanding the regulatory piece of the business. Home rule cities in Colorado rely heavily upon sales tax collection in order to maintain the operations of the city. Additionally, a significant portion of the state government is also funded through sales tax collection. While taxation is seldom, if ever, a positive topic of conversation, without the support of state and local governments, many small business owners would be unable to be successful. This study has shown that open communication with local governments and proper record-keeping can be beneficial, not only to help small business stay in compliance, but also to help the locality in which the small business is located.

Although many of the small business owners interviewed indicated that trying to deal with the government can be daunting, concerned and engaged small businesses would be better served if they attempted to openly communicate any questions or concerns to their local government. This study revealed that many of the home-rule municipalities have auditors or small business advocates to help business owners that have questions or concerns about regulatory compliance. The local city governments have a vested interest in collecting the appropriate sales tax from its business owners. They provide personnel who are trained and willing to help answer questions, hear concerns, and help reduce management anxiety. In addition to communicating with the local government, small business owners should also place more importance on proper record keeping for tax collections. Manual data collection systems, such as a log book, maintaining an Excel spread sheet, or keeping a Word document are a cost effective way to keep track of business transactions. For a marginal cost, a point of sale system or accounting software can also help a small business owner maintain proper records. Professional bookkeepers or accountants are also available for those business owners who

need this level of expertise. Whatever the method, proper records can be the difference between an easy audit and a difficult one. Many of businesses interviewed stated that once they had a good accounting system in place to record sales tax, the system was easy to follow. Taking the time to implement and maintain a proper and thorough record-keeping system will save time in the future, as calculating and remitting the proper sales tax will be easy to perform.

CONCLUSIONS AND RECOMMENDATIONS FOR REGULATORS

Regulatory agencies understand the importance of sales tax on their revenue, so have attempted to ease the burden by offering electronic filing for small businesses, yet some businesses still find sales tax filing, especially online, difficult. Although regulatory bodies provide free trainings for small businesses to understand sales and use tax filing and remittance, business owners tend to shy away from these trainings simply because of the notion that an interaction between an ordinary individual and a government representative is not comfortable.

While many small business owners may not view the local or state government favorably, these government agencies offer many services and tools for small business owners. As stated above, the revenue from sales tax collection is vital for government solvency. This study has shown that many of the owners interviewed stated that they had little or no contact with any of their taxing governments, even though some described the remittance of sales tax as burdensome. As regulators are aware that few business owners willingly interact with them, this study has shown that local and state governments could engage in more community outreach, as well as create a more user-friendly tax remittance system.

Local and state governments could attempt to find better forms of small business community outreach as it may be valuable to help encourage compliance, as well as boost their reputation with the small business community. While classes are regularly offered, attendance is low because the small business owners must research to find the information. Regulators could reach out to small business owners, either through personal visits to their places of business, mailers or phone calls, which advertise the classes offered (often at no cost). Regulators could also schedule “non-au-

dit” visits where the sole purpose is to help business owners with sales tax questions and to help them become compliant without penalizing them if deficiencies are found. If regulators wanted small business owners to fear the government less, providing help without fines and penalties would more rapidly help achieve this goal.

The emergence of the nonprofit Colorado Municipal League is also a positive development for the small business owner. As this nonprofit is working to standardize definitions for taxable items, and many cities and towns are adopting these definitions, the determination of what is taxable and what is not will help ease the complexities of compliance for businesses that operate in multiple jurisdictions.

The newest online sales tax compliance portal is another move in the right direction. As more jurisdictions embrace its use, the potential to help small business owners to stay in compliance with their tax requirements is greatly enhanced. However, until definitions are standardized and jurisdictions embrace the one sales tax system, the burden of successful sales and use tax compliance will continue to be placed upon the small business owner.

LIMITATIONS OF THE STUDY AND IDEAS FOR FURTHER WORK

The main limitation of the research is that data was obtained from 50 interviews with small and micro-sized entities in a single U.S. State. Additionally, very few online retailers were interviewed, allowing limited, if any, discussion on the impact of the *Wayfair* ruling. This does not detract from the objectives of the paper, which were to better understand the burdens that sales and use taxes place on small businesses, what successful small business owners do to navigate their compliance burdens, and the role that regulatory agencies play in helping the small business owner navigate the sales and use tax process. Nevertheless, it is desirable to follow up this research with more extensive interview data obtained from small business owners and online retailers across the USA.

Submitted: March 01, 2020 MST, Accepted: September 10, 2021 MST

This is an open-access article distributed under the terms of the Creative Commons Attribution 4.0 International License (CCBY-4.0). View this license's legal deed at <http://creativecommons.org/licenses/by/4.0> and legal code at <http://creativecommons.org/licenses/by/4.0/legalcode> for more information.

REFERENCES

- Arksey, H., & Knight, P. (1999). *Interviewing for Social Scientists*. SAGE Publications, Ltd. <https://doi.org/10.4135/9781849209335>
- Bishop-Henchman, J., Walker, H., & Grabe, D. (2018). Post wayfair options for states. *Journal of Multistate Taxation and Incentives*, 28(8), 6–42.
- Bruce, D. a. (2013). *An Analysis of Internet Sales Taxation and the Small Seller Exemption* (pp. 1–4). Small Business Administration, Office of Advocacy. <http://advocacy.sba.gov/2013/11/01/an-analysis-of-internet-sales-taxation-and-the-small-seller-exemption/>
- Colorado Department of Revenue. (2017). *Annual Report*. Colorado Department of Revenue. https://www.colorado.gov/pacific/sites/default/files/2017_Annual_Report.pdf
- Colorado Office of the State Auditor. (2015). *Local Sales Taxes Performance Audit* (pp. 1–70). Colorado Office of the State Auditor. <https://leg.colorado.gov/audits/local-sales-taxes>
- Cornia, G. C. (2000). An Analysis of the Feasibility of Implementing a Single Rate Sales Tax. *National Tax Journal*, 53(4.3), 1327–1350. <https://doi.org/10.17310/ntj.2000.4s2.04>
- DeLuce, D. (2007). Proceedings of the 2007 IRS Research Conference. In *IRS Research Conference* (pp. 147–184). The IRS Research Bulletin. <https://www.irs.gov/pub/irs-soi/07resconfdeluca.pdf>
- Department of Revenue. (2017). *Colorado Sales and Use Tax General Information and Reference Guide*. Department of Revenue. https://leg.colorado.gov/sites/default/files/images/committees/2017/17-0711_sales_and_use_tax_colorado_sales_and_use_tax_presentation.pdf
- Erb, K. P. (2016, December 13). “Tattletale” Tax Law Will Stand After Supreme Court Declines To Hear Case. *Forbes*. <https://www.forbes.com/sites/unicefusa/2018/07/25/inside-a-mexican-shelter/#264da7607afb>
- Frieden, K., & Nicely, F. (2018, April). The best and worst of state sales tax systems. *Council on State Taxation*. <https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/the-best-and-worst-of-state-sales-tax-systems-august-17-2018-final.pdf>
- Joint Technology Committee. (2020, September 14). Sales and use tax simplification update. *Colorado Department of Revenue*. https://leg.colorado.gov/sites/default/files/images/dor_suts_presentation.pdf
- Kitching, J. (2008). A burden on business? Reviewing the evidence base on regulation and small business regulation. *Environment and Planning C: Government and Policy*, 24(6), 799–814. Kingston University Research Repository. <https://doi.org/10.1068/c0619>
- Luscombe, M. A. (2018). Tax trends: The impact of the Supreme Court’s Wayfair decision. *Taxes*, 96(9), 3–4, 57. <https://www.answerconnect.cch.com/document/19696ac27d141000982ed8d385ad169404/journal/tax-trends-the-impact-of-the-supreme-court-s-wayfair-decision>
- National Small Business Association. (2017a). 2017 NSBA small business regulations survey. <https://www.nsbabiz/wp-content/uploads/2017/01/Regulatory-Survey-2017.pdf>
- National Small Business Association. (2017b). NSBA 2017 Small Business Taxation Survey. NSBA. <https://www.nsbabiz/wp-content/uploads/2017/04/Tax-Survey-2017.pdf>
- National Small Business Association. (2018). 2018 NSBA Small business taxation survey (pp. 1–12). NSBA. <https://nsbabiz/wp-content/uploads/2018/04/Tax-Survey-2018.pdf>
- Patton, S. (2016). *Small Business Tax Compliance: Burdens and IRS Response Efforts*. Nova Science Publishers.
- PricewaterhouseCoopers, LLP. (2004). *Retail sales tax compliance costs: A national estimate* (Joint Cost of Collection Study). <https://netchoice.org/wp-content/uploads/cost-of-collection-study-sstp.pdf>