

This Tax Facts is designed to explain how sales and use tax applies to attorney services. If this Tax Facts does not answer your specific question, please call the Department's toll-free Helpline at 1-800-TAX-9188 between 8:00 AM – 6:00 PM CST, Monday through Friday.

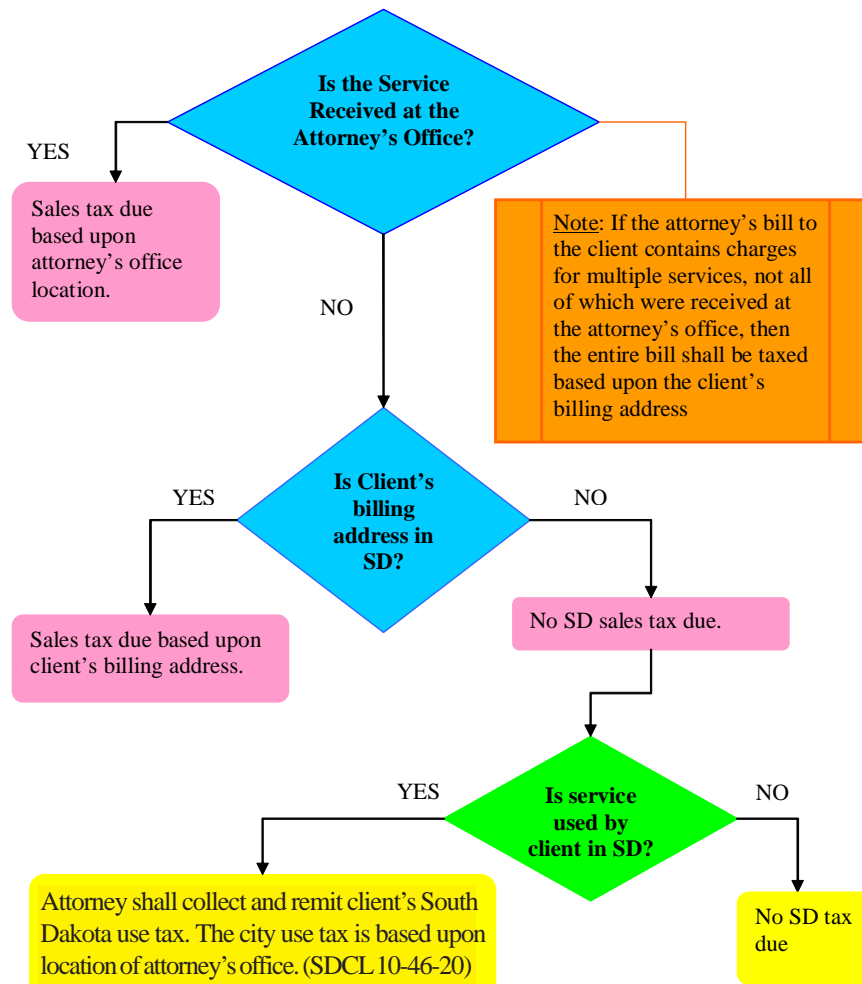
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## Attorney Services

Attorney services are subject to the 4% state sales tax, plus applicable municipal tax. Based on ARSD 64:06:01:63 the following rules determine where sales tax applies to attorney services. The customer is the person that hires the attorney.

As a general rule, the services of an attorney will be subject to either sales or use tax because most services are inherently used in South Dakota. The following explanation and flow chart are designed to help determine the proper tax to remit.

1. If the service is received at the attorney's office, then the service is first used and received by the client at the attorney's office. Sales tax should be remitted using the tax rate applicable for the attorney's office.
2. If the service is not received at the attorney's office, then the service is received at the client's billing address. Sales tax should be remitted using the tax rate applicable for the client's billing address.



## Sales Tax and Probate Work

Services provided to South Dakota estates are subject to either sales or use tax because there is some inherent use in South Dakota.

## Nonresident Attorneys

Nonresident attorneys performing legal services pursuant to SDCL 16-18-2 must have a South Dakota sales tax permit and may be subject to sales tax.

Nonresident attorneys that are not required to comply with SDCL 16-18-2 may also be required to have a South Dakota sales tax license. If the attorney or an employee, agent, or representative of the attorney enters South Dakota for purposes of doing business the attorney must have a sales tax permit and report the applicable sales tax.

The sales tax is applied based on the same rules for both resident and nonresident attorneys.

## Use Tax on Attorney Services

Sales tax applies to attorney services at the attorney's office or the customer's address, based on the above rules. The seller is responsible for reporting and remitting the sales tax.

Use tax, on the other hand, is based on where the service is used. The purchaser or consumer is legally responsible for the use tax.

The attorney is responsible for sales tax in those jurisdictions that tax attorney services. If the attorney's customer receives the service in a jurisdiction that does not tax the attorney's service, but the customer will owe the South Dakota use tax, the attorney shall collect and remit the use tax on behalf of their customer. City use tax should be remitted using the tax rate applicable for the attorney's office.

The attorney will not be held liable for the client's use tax if the attorney makes a good faith effort to collect the use tax but the client refuses to pay. In such case, the Department shall require payment directly from the client.

## Reimbursable Expenses

Licensed attorneys may deduct from their gross receipts amounts that represent charges to clients for tangible personal property or services purchased by the attorney, if the following criteria are met:

1. The amount to be deducted represents an expense incurred for a particular client;
2. The property or service is not purchased as a sale for resale; and
3. The amount is itemized and separately billed as a reimbursable expense by the attorney.

If sales or use tax is not paid on the purchase, the receipts for the reimbursable expense are taxable. However, services or items exempt from sales tax, such as filing fees paid to a governmental entity, may be deducted as a reimbursable expense provided the above criteria are met.

If the attorney charges more for the item or service than the amount the attorney paid for the item or service, the entire receipts are subject to sales tax, even if sales or use tax was paid on the purchase. Charges for reimbursable expenses should not be included in the gross receipts line of the sales tax return.

Expenses incurred in the day-to-day operation of an office are not reimbursable expenses and cannot be deducted from the gross receipts even if they are itemized on the client's invoice. Services provided by employees are not reimbursable expenses; these services are not purchased on behalf of a specific customer.

Services contracted for a specific client may be taken as a reimbursable expense. However, services contracted for use by many attorneys or for use on work for multiple customers cannot be taken as a reimbursable expense.

### **Examples**

1. An attorney contracts with a paralegal to work on John Doe's case. The paralegal charges sales tax on her service. The attorney may deduct this amount as a reimbursable expense.
2. A law firm contracts with a paralegal to provide services to the firm for six months. The paralegal's fee to the law firm is subject to sales tax. Because the paralegal's service is not purchased for a specific customer, the service cannot be taken as a reimbursable expense.

### **Examples of items or services that can be taken as reimbursable expenses if the above criteria are met:**

- Court reporter fees
- Filing and recording fees
- Investigative agent services
- Medical records
- Paralegal services
- Photocopying fees from a third party or in house\*
- Postage
- Expert consulting and testimony
- Service of process
- Telephone and FAX charges if itemized by the phone company\*
- Travel expenses including:
  - Airfare
  - Meals
  - Mileage (Expense of own vehicle, not to exceed \$.45 per mile)
  - Motels
  - Vehicle Rentals

\* If an average charge is used instead of actual expense, the average must be based on actual expense and is subject to audit by the Department.

Examples of items and services that cannot be deducted as a reimbursable expense are:

- Office supplies
- Employee services-Secretarial
- Telephone monthly charges and local calls that are not itemized per call by the phone company
- Services purchased for resale
- Temporary help agency services, unless purchased for a specific customer

### Examples

1. An attorney from Sioux Falls takes a deposition for a customer in Pierre. The attorney bills the customer for his service, and the cost of the motel room, meals, and court reporter. Sales tax was paid on the purchase of the motel room, meals, and court reporter.

The attorney does not include the motel room, meals, or court reporter charges in his taxable receipts because the charges are itemized on the customer's invoice and are not marked up.

2. An attorney hires a secretary from a temporary help agency for help on a specific case. Because the help is for a specific customer, the attorney does not include the temporary help charges in his taxable receipts if sales tax was paid to the temporary help agency and the cost was passed on without being marked up.
3. An attorney issues an exemption certificate to a private investigator for work on a case. The investigator does not charge the attorney sales tax. The attorney must include the investigator charges in their receipts subject to the 4% state sales tax, plus applicable municipal tax.
4. An attorney bills a customer \$2.00 per long distance call based on the average expense of calls. Because the average expense represents an expense incurred for that customer, and the charge is itemized, this charge is not included in the attorney's taxable receipts.

## Purchases for Resale

As a general rule an attorney cannot purchase supplies and services the attorney uses exempt from sales tax. However, services can be purchased for resale if the following criteria are met:

1. The service is purchased for or on behalf of a current customer;
2. The purchaser of the service does not use the service; and
3. The service is delivered or resold to the customer without any alteration or change.

Attorneys must give an exemption certificate to their suppliers to purchase services for a specific customer exempt from sales tax.

Services and items purchased for resale for a specific customer **cannot** be taken as a reimbursable expense. Receipts for services and items purchased without sales or use tax are included in the attorney's taxable receipts.

### Examples

1. An attorney contracts with a court reporter to take a deposition for a client. The attorney may purchase the court reporter's service for resale because the purchase is for a specific client, is not used by the attorney, and is passed on unchanged. If an exemption certificate is issued the attorney cannot deduct the court reporter's fee as a reimbursable expense and will owe sales tax on their receipts for the court reporter's service.
2. An attorney contracts with a doctor to testify on behalf of a customer. The attorney can purchase the doctor's service for resale because the purchase is for a specific client, is not used by the attorney, and is passed on unchanged. If an exemption certificate is issued, the attorney cannot deduct the doctor's fee as a reimbursable expense. The receipts for the doctor's service are included in the attorney's taxable receipts.

State law requires exemption certificates to be complete and accurate. The seller is responsible for obtaining a completed exemption certificate. The buyer will be held responsible for properly completing an exemption certificate. Exemption certificates may be obtained from the department's website at [www.state.sd.us/drr](http://www.state.sd.us/drr), or by calling 1-800-TAX-9188.

## Court Reporters

Court reporter fees are subject to the 4% state sales tax, plus applicable municipal sales tax. Sales tax applies where the court reporter's customer receives the report.

## Expert Consulting and Testimony

Except as provided below, expert consulting services and expert testimony associated with litigation are subject to the 4% state sales or use tax, plus applicable municipal tax. Sales tax applies where the customer receives the service. If the receipt of service is not known, or if the service is received at multiple locations, sales tax will apply based on the customer's address.

### **Example**

Attorney Brown contracts with Dr. Smith to testify in a malpractice suit as to the condition and appropriate treatment of the plaintiff, John Doe. John Doe is not Dr. Smith's patient. Although Dr. Smith reviewed the plaintiff's medical records and took the appropriate x-rays and tests, this information was used by Dr. Smith to form an opinion that was presented at the trial and was not used to treat the plaintiff. Dr. Smith meets with Attorney Brown to discuss the findings prior to testifying in court. Dr. Smith is providing an expert witness service subject to sales tax.

Dr. Smith's receipts for the expert witness service, including receipts for x-rays and tests, are subject to the 4% state sales tax, plus applicable municipal tax. Because the service is not received at Dr. Smith's office, sales tax applies based on Attorney Brown's address. The attorney will owe sales tax on charges to his customer, including charges for x-rays, lab tests, and doctor fees, if sales tax is not paid to the service provider. If sales tax is paid to Dr. Smith, the attorney may deduct the charge for Dr. Smith as a reimbursable expense.

Medical consulting or testimony concerning the diagnosis or treatment of the healthcare professional's patient is not subject to sales or use tax.

### **Example**

Dr. Smith's patient, Jim, was in a car accident. Jim's attorney paid Dr. Smith to testify in a lawsuit concerning Jim's injuries from the accident. Dr. Smith does not owe sales tax on the receipts for testifying because the services were associated with the diagnosis or treatment of Jim.

Jim's attorney may deduct the charge for Dr. Smith's service as a reimbursable expense even though sales tax was not charged, because this is an exempt health care service.

## Retainer Fees

Retainer fees are subject to the 4% state sales tax, plus applicable municipal tax. Retainers placed in a trust are subject to the 4% state sales tax, plus applicable municipal tax when the fees are withdrawn from the trust to pay for legal services. Sales tax applies to the fees based on the rules provided on page one.

## Barter Fees

The value of real property, tangible personal property, or services received in exchange for legal services are taxable to the attorney.

### **Example**

An attorney bills a client for \$25,000 and receives \$5,000 cash plus 40 acres of land, valued at \$20,000. \$25,000, less applicable reimbursable expenses, is subject to sales tax.

## Patents

Attorney services for filing patents are subject to the 4% state sales tax, plus applicable municipal tax. Sales tax applies at the attorney's office if the service is received there. Otherwise, the sales tax applies based on the client's address.

The client will owe use tax on the attorney fees based on the client's location if the attorney is out of state and unlicensed.

## Use Tax

Supplies, materials, or services purchased from an unlicensed business are subject to use tax. The state use tax rate is 4%, plus applicable municipal use tax, and is payable to the Department of Revenue and Regulation in the filing period in which the attorney receives the supplies or services.

Tangible personal property delivered into South Dakota is subject to the South Dakota sales or use tax, even if the supplier charges another state's sales tax.

When a purchase is made out-of-state and possession is taken out-of-state the supplier may charge that state's sales tax. If the other state's sales tax is the same or more than South Dakota's tax, there is no South Dakota use tax due. If it is less than South Dakota's, the difference is due in use tax. The state use tax plus applicable municipal use tax must be added together to determine if additional tax is owed.

### **Examples of use taxable items are:**

Computers	Furniture
Software	Law Books
Office Supplies	Internet Database Services
Equipment	Maintenance Agreements

## Municipal Tax

Many municipalities in South Dakota have a sales and use tax in addition to the state tax. If the customer receives a product or service in one of these cities, the product or service is subject to that municipality's sales or use tax. A list of municipal tax rates are available on our website at [www.state.sd.us/drr](http://www.state.sd.us/drr).

It is the attorney's responsibility to remit the correct sales tax. If the attorney relies on the customer's representation of their taxing jurisdiction and that information is incorrect, the attorney will be responsible for any additional sales tax due.

TaxMatch, the department's GIS system, will help users quickly find the correct tax rate and codes for locations throughout South Dakota. Users will enter any South Dakota address into Tax Match, the system will then provide all the applicable tax codes and rates for that address. For quick and easy access, look for the GIS icon on the department's web site at [www.state.sd.us/drr](http://www.state.sd.us/drr).

## Exempt Entities

Accredited schools, non-profit hospitals, approved relief agencies, and government entities are exempt from sales and use tax.

Government entities must provide an exemption certificate to the vendor or the vendor must keep documentation to show the purchase was paid from government funds. Documentation may include a purchase order or a check stub.

Relief agencies and religious or private schools must provide an exemption certificate to purchase products and services exempt from sales and use tax.

The attorney must keep copies of payment documents received from the exempt purchaser in their records.

When an attorney is hired by a client to represent them in a case against an exempt entity, the exempt entity may send payment of the customer's award or settlement directly to the attorney. The attorney then retains a portion of the customer's settlement as pay for their service and remits the balance to the client. The amount kept by the attorney is subject to sales tax.

If an attorney provides a service for a taxable customer, but his/her fees are paid by an exempt entity, the gross receipts are subject to sales tax when received. **To be exempt, the service must be provided to and paid by the exempt entity.**

### Example

Joe Smith hires attorney Sam Jones to represent Joe in a case involving the federal disability office. The court awards Joe the amount of his claim plus legal fees. The federal disability office sends payment of the full amount to attorney Sam Jones. Sam's customer is Joe Smith, not the government. The attorney is responsible for remitting sales tax on the amount received.

However, court appointed attorneys are exempt from sales tax on fees received directly from government funds.

## Required Records

Attorneys must have a South Dakota sales tax license for each place of business within the state. Records, such as purchase and sales invoices, bills of lading, books of all receipts and sales, cash register receipts, and other pertinent papers and documents, are required to be kept for at least three years and be available for inspection during business hours.

## Talk to Us!

If you have a tax problem or question, call the South Dakota Department of Revenue & Regulation toll-free at 1-800-TAX-9188. Visit us on the web at [www.state.sd.us/drr](http://www.state.sd.us/drr), email us at [bustax@state.sd.us](mailto:bustax@state.sd.us) or write us:

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