

Quill, Then and Now

June 13, 2017

2017 FTA Annual Meeting

Commissioner Kevin Sullivan, Connecticut

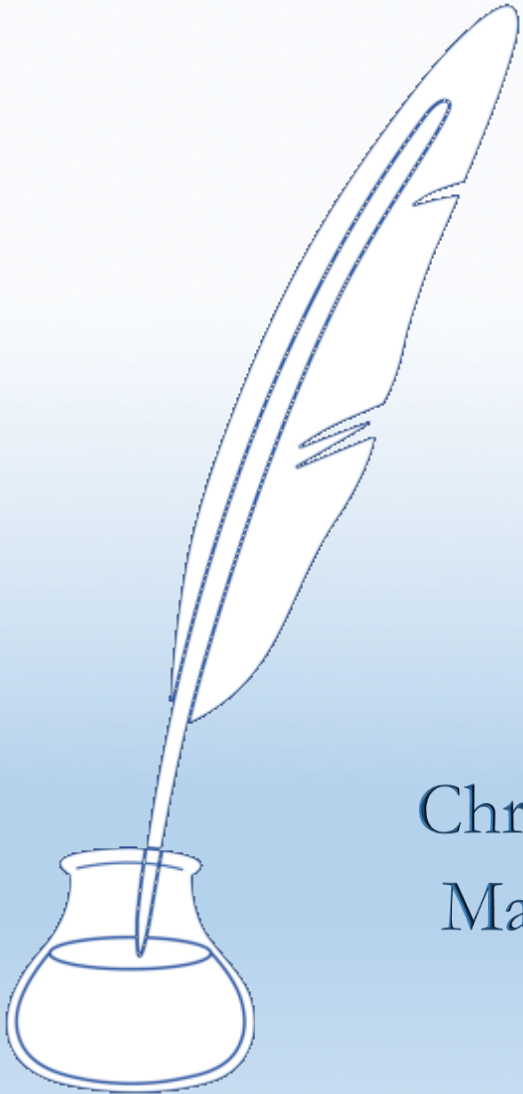
Secretary Andy Gerlach, South Dakota

Commissioner Nonie Manion, New York

Christine Mesirow, Ohio Office of the Attorney General

Max Behlke, National Conference of State Legislatures

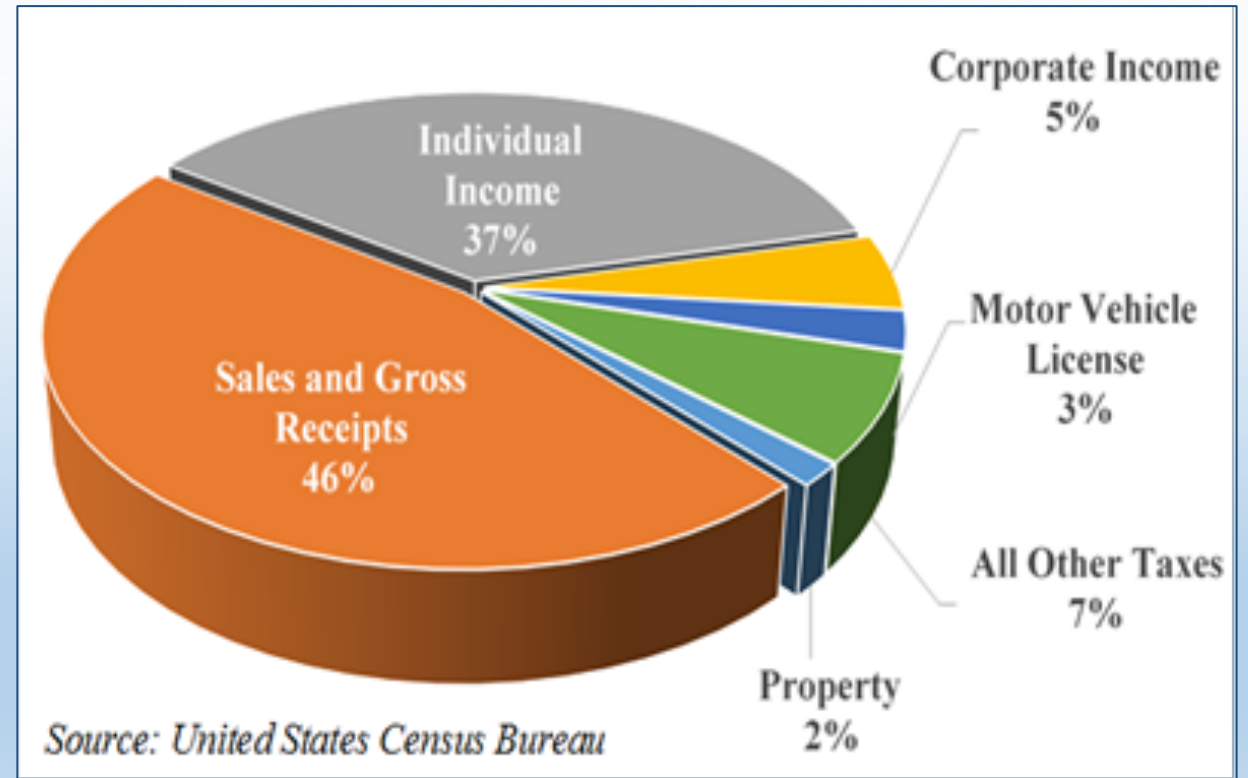
Fred Nicely, Council on State Taxation



Sales Tax and State Revenue

- **Sales Tax** alone accounts for **34%** of state revenue.
- Online commerce continues to grow.
- This past Black Friday, for the second consecutive year, more people shopped online than did in stores.
- For the last five years, e-commerce grew annually by **15%** and now accounts for **10%** of all retail sales.

Average of the 50 State Revenue Sources



Sales Tax Collection: Congressional Action – Or Lack Thereof

113th Congress

- Marketplace Fairness Act (S. 743)
(Passed Senate 69-27 on May 6, 2013)

114th Congress

- Marketplace Fairness Act (S. 698)
(24 sponsors but never received a hearing)
- Remote Transactions Parity Act (H.R. 2775)
(69 sponsors but never received a hearing)
- Online Sales Simplification Act
(Never Introduced)

115th Congress

- Marketplace Fairness Act (S. 976)
(24 sponsors)
- Remote Transactions Parity Act (H.R. 2193)
(11 sponsors)
- No Regulation Without Representation Act

Recent Congressional Efforts

Marketplace Fairness Act (MFA)/Remote Transactions Parity Act (RTPA)

- Destination Sourcing
- A single state-level entity to administer all sales and use tax laws
- A single audit for all state and local taxing jurisdictions within the state
- A single sales and use tax return for remote sellers to file with the state-level entity
- A uniform sales and use tax base among the state and its local taxing jurisdictions
- Information regarding the taxability of products and services, along with any product and service exemptions
- A rates and boundary database
- A 90-day notice of rate changes, along with liability relief to both remote sellers and Certified Service Providers (CSPs)

Recent Congressional Efforts

Online Sales Simplification Act



“Hybrid Origin Sales Tax”

Only one thing you need to know about this proposal...

Just say “No”

State Sales Tax Collection Efforts

NCSL Task Force on State and Local Taxation

In 1999, the NCSL Executive Committee established the Task Force on State and Local Taxation to review the issue of collection of sales and use taxes from out-of-state transactions and then recommend legislative solutions to Congress.

That was 18 years ago....



States are No Longer Waiting for Congress...

Task Force Discussion Regarding a State Solution

➤ November 20-21, 2015

➤ January 8, 2016

- Task Force members heard from a Supreme Court expert and discussed a state legislative proposal.
- Proposal was sent to legislative leaders and tax chairs across the country.



State Legislative Considerations

States are considering three primary options:

- I. Reporting requirements
- II. Nexus expansion provisions to increase the scope of state ‘doing business’ language.
- III. Marketplace collection/reporting provisions to require online and other marketplaces to collect and remit, or report, sales and use tax if a retailer sells products on the marketplace.

States Shift to the Courts

“Given these changes in technology and consumer sophistication, it is unwise to delay any longer a reconsideration of the Court’s holding in *Quill*. A case questionable even when decided, *Quill* now harms States to a degree far greater than could have been anticipated earlier.”

– Justice Kennedy in *DMA v. Brohl*, March 3, 2015

Reporting Requirements

Typically require non-collecting businesses who have a defined amount of in state sales to:

- Inform customers that they may be subject to use tax;
- Send an annual purchase summary to customers who purchase a defined amount of taxable goods in one year, along with a reminder of their use tax obligation; and/or
- Provide the Department of Revenue with annual customer information (names, addresses, and amount of purchases).

States With Reporting Requirements

- Colorado (2010)
- Louisiana (2016) – For sellers with +\$50,000 in sales. Effective July 1, 2017
- Oklahoma (2016) – Report only to Customers
- Vermont (2016) – Colorado-style. Effective July 1, 2017

Colorado's Reporting Requirement

On February 22, 2016, the United States Court of Appeals for the Tenth Circuit upheld the constitutionality of the Colorado law.

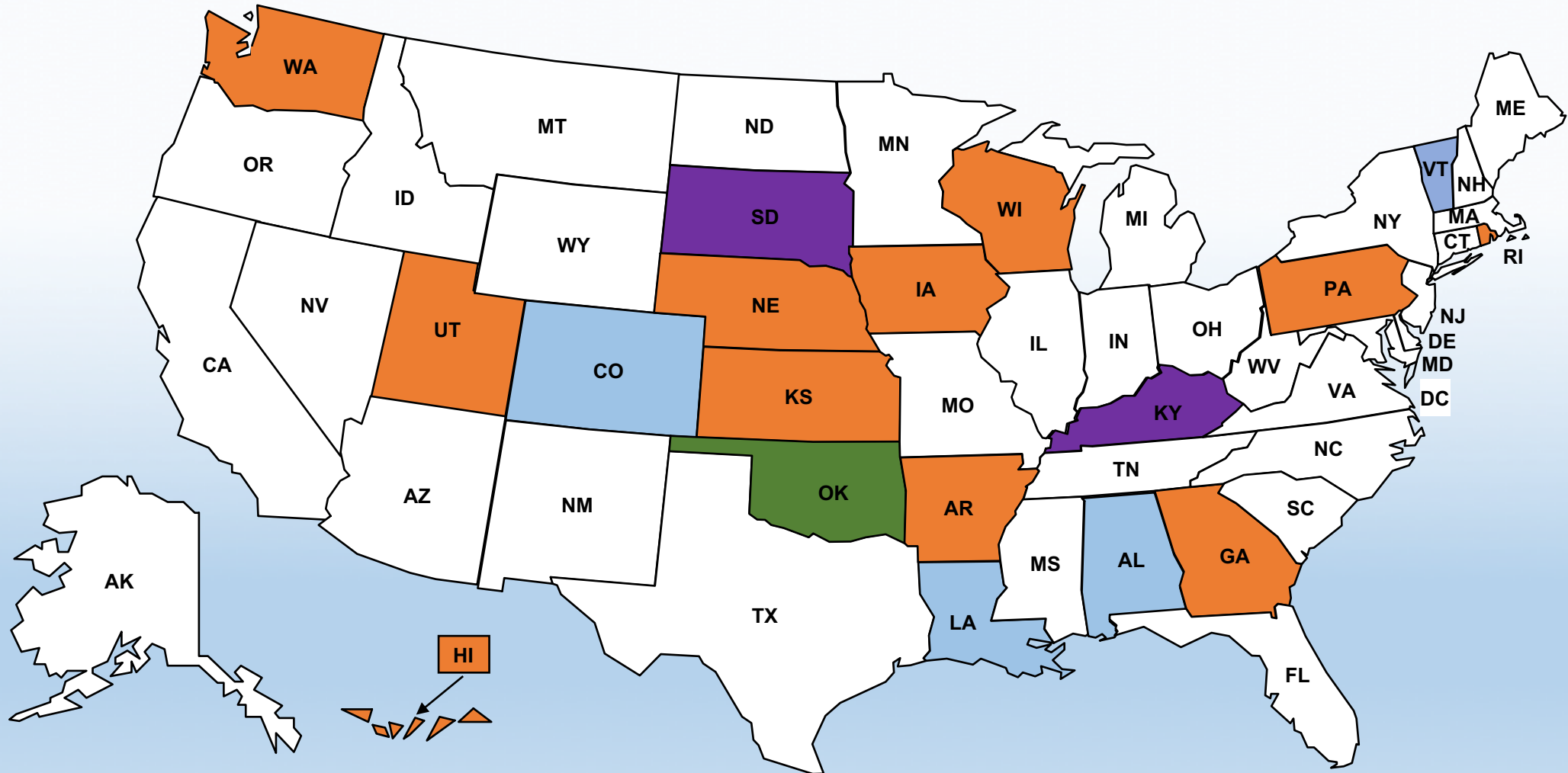
The court held that the notification and reporting requirements do not violate the Commerce Clause because they do not discriminate against or unduly burden interstate commerce.

On December 12, 2016, the United States Supreme Court denied DMA's petition to hear the case, thus allowing the Colorado to begin enforcing its law.

On February 22, 2017 the state's Department of Revenue and DMA reached a settlement agreement where the DOR agreed to waive penalties for noncompliant retailers until July.

Notice and Reporting in 2017 – Sales Tax

- legislation introduced in 2017
- taxpayer and the Department
- taxpayer only
- notification only

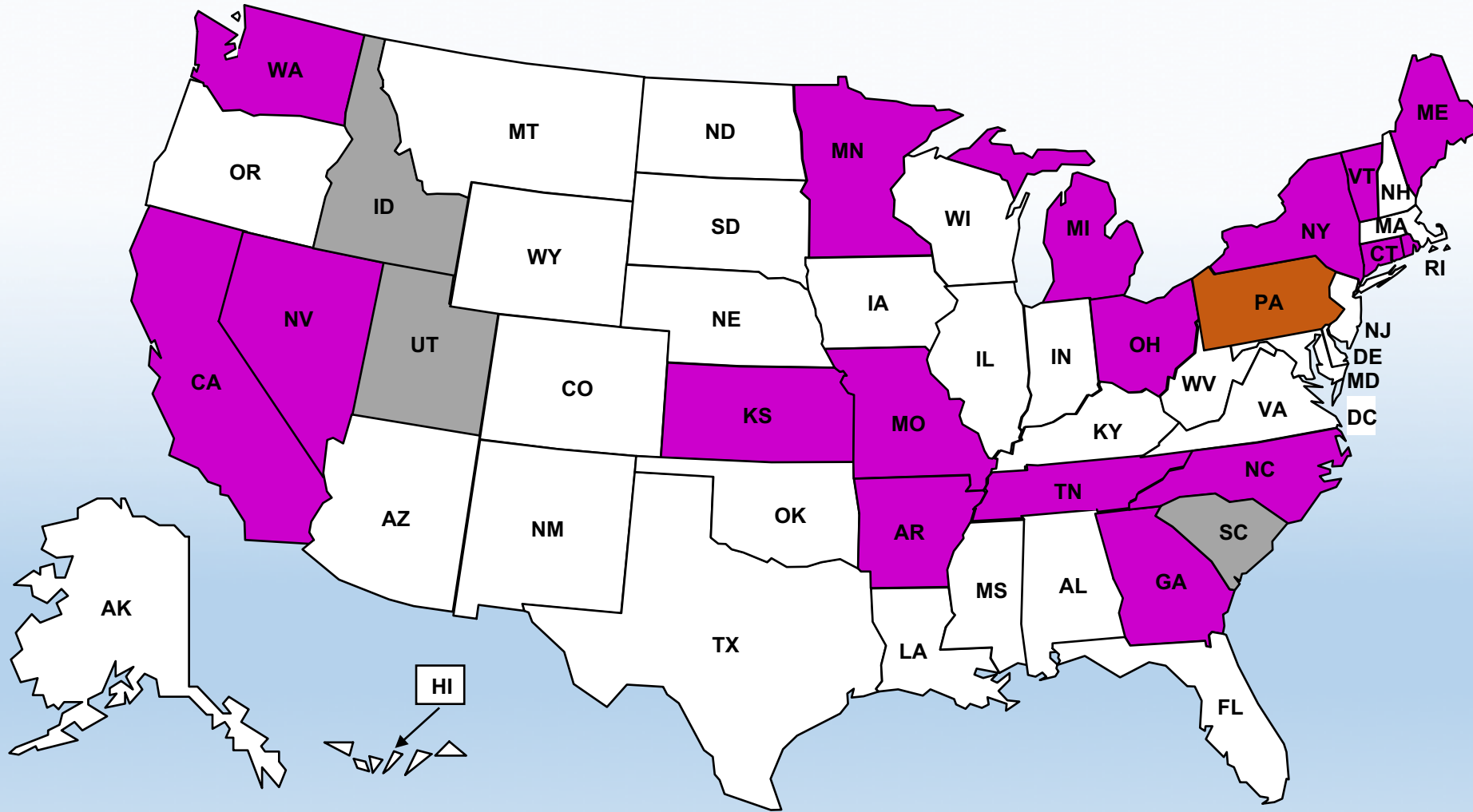


Expanded Nexus

- Amend definitions, such as “vendor” or “doing business in the state”
- Economic Nexus
- Expands to include storage of inventory

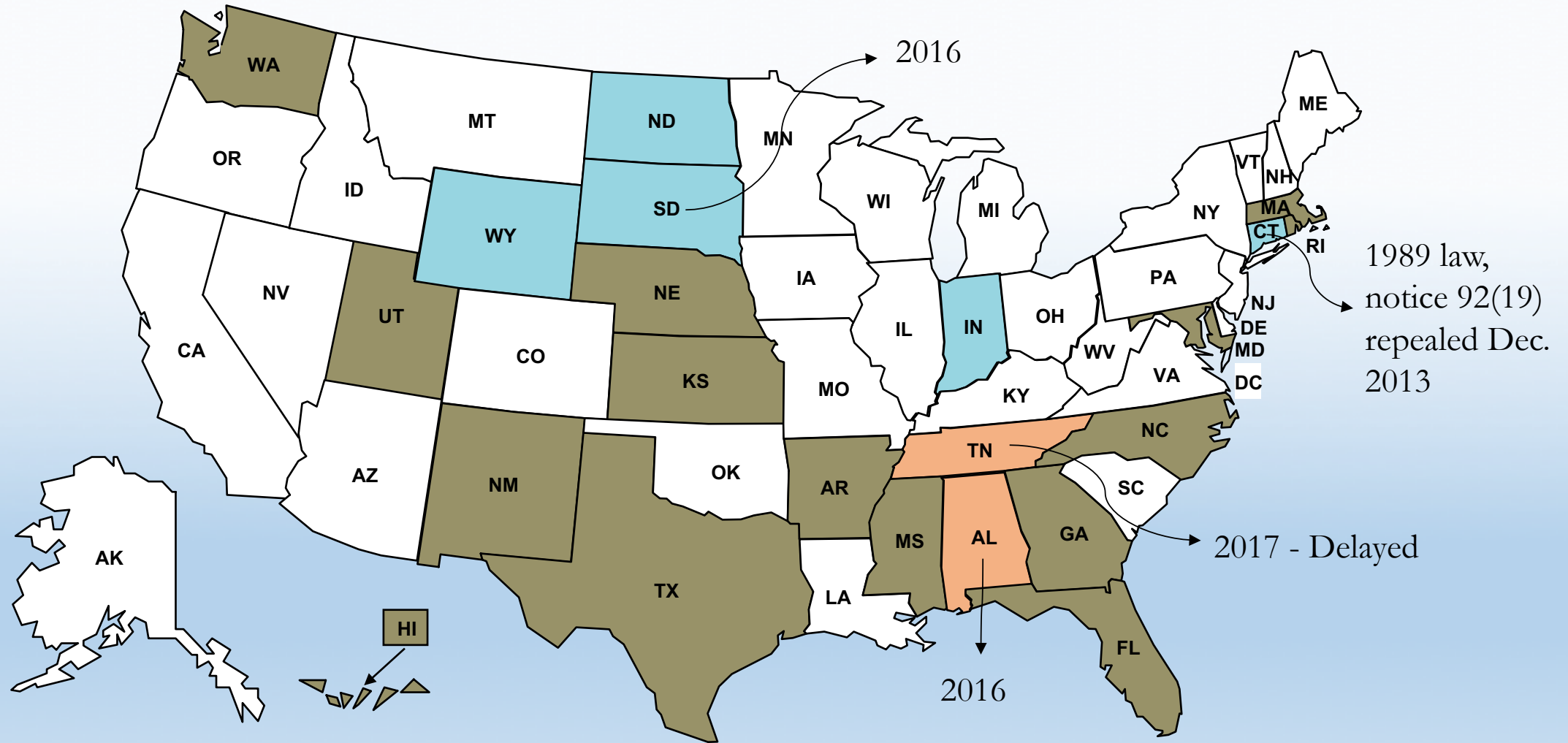
Click-Through Nexus in 2017 – Sales Tax

● legislation introduced in 2017 ● enacted by legislation ● enacted by regulation



Sales Factor/Transactional Nexus – Sales/Use Taxes

● legislation introduced in 2017 ● enacted by legislation ● enacted by regulation



Marketplace Provisions

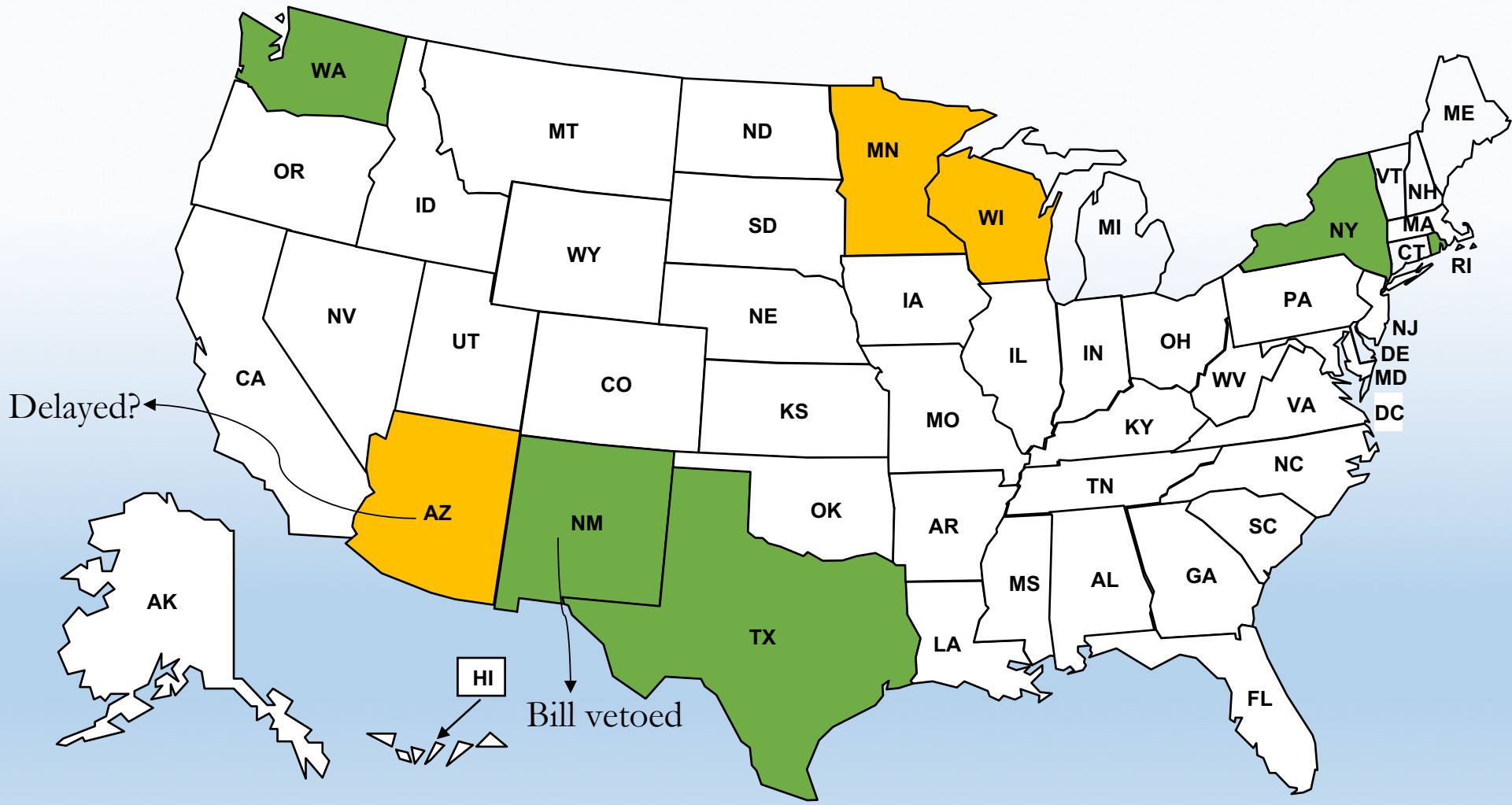
Marketplace collection provisions aim to require online and other marketplaces to collect and remit sales and use tax if a retailer sells products on the marketplace.

Types of Marketplaces:

- 1) “standard” or “traditional” marketplaces where multiple sellers sell products, sometimes the same products, on a single platform.
- 2) “referral” marketplaces is where customers may search for products and are then referred to a place to purchase those products.

Marketplace Provider in 2017 – Sales Tax

● legislation introduced in 2017 ● enacted by legislation/regulation



Summary: Notable Activity in 2016

- 22 states introduced legislation to collect sales taxes from remote purchases.
- Notable Enacted Legislation
 - Louisiana (Expanded Nexus & Reporting)
 - Oklahoma (Reporting)
 - South Dakota (Economic Nexus)
 - Vermont (Colorado-style Reporting)
- Administrative Rules
 - Alabama (\$250,000 Economic Nexus)
 - Tennessee (\$500,000 Economic Nexus)

Summary: Notable Activity in 2017

- Legislation has been introduced in at least 30 states to address the remote sales tax collection problem
- Notable legislation enacted so far this year in:
 - Alabama (Reporting requirement)
 - Indiana (South Dakota Model of Economic Nexus)
 - Minnesota (Marketplace Provider, Effective July 1, 2019)
 - North Dakota (Contingent upon federal collection authority)
 - Virginia (Adds "storage of inventory" to definition of nexus)
 - Wyoming (South Dakota Model of Economic Nexus)
- Notable Regulations:
 - Massachusetts
 - Mississippi

An In-Depth Look at Several States

Protectionism: Constitution UPSIDE DOWN



- Whether characterized as affirmative or dormant, the fundamental negative purpose of the Commerce Clause was and is to assure that state governments do not unreasonably *burden* commerce among the states through unfair trade barriers that *disfavor* out-of-state commerce.
- The Commerce Clause cannot possibly mean that the Constitution gives out-of-state competitors the *advantage* of an un-level playing field by evading equal responsibility for taxation and tax collection.

CONNECTICUT



“[I]t is highly unlikely that the language of *Quill* that a state’s ability to ‘compel a vendor to collect a sales and use tax may turn on the presence in the taxing State of a small sales force, plant or office...was intended as a definitive description of other contacts that might demonstrate the existence of a substantial nexus....”

(Scholastic Book Clubs, Inc., Connecticut Supreme Court, 2012)

CONNECTICUT ACTS



CGS 12-407(a)(15)(A) “engaged in business in the state” includes:

- Selling or any activity in this state in connection with selling tangible personal property.
- Retail sales made outside the state to an in-state destination even without a place of business in the state.
- Regular or systematic solicitation by electronic means for the purpose of effecting sales.
- Agency, control, assignment, independent contracting.
- Including hosted click-through sales.

CGS 12-426(4) enforcement:

- Examine the books, papers, records and may investigate in order to verify the accuracy of any return or, if no return, determine the amount to be paid.



Senate Bill 106 Background

- Inability to collect sales tax from remote sellers threatens South Dakota's efforts to sustain a broad tax system, which allows South Dakota to keep taxes low.
 - Because South Dakota doesn't have a state income tax, sales and use tax revenue are essential in funding state and local services.
 - The growth of online retail ensures further erosion to our sales tax base.

Remote Sellers must remit South Dakota sales tax if they meet one of two criteria

- The seller's gross revenue exceeds \$100,000.
 - The sellers made 200 or more separate transactions into South Dakota.
-
- Any sales tax obligation required by this act cannot be applied to past sales.



2016 – 17

- On April 28, 2016, the State of South Dakota filed a declaratory judgment action in the Sixth Judicial Circuit Court, Hughes County, against four remote sellers: Newegg, Overstock, Systemax, Wayfair.
- On May 25, 2016, Defendants file notice of intent to move from State court to US District Federal Court.

- On January 17, 2017, Opinion entered to grant State's motion to remand back to state court.
- On March 6, 2017, South Dakota Sixth Circuit Court Judge Mark Barnett enters order granting Defendant's Motion for Summary Judgement.
- On March 8, 2017, South Dakota files Notice to Appeal Circuit Court's ruling to the Supreme Court of South Dakota.

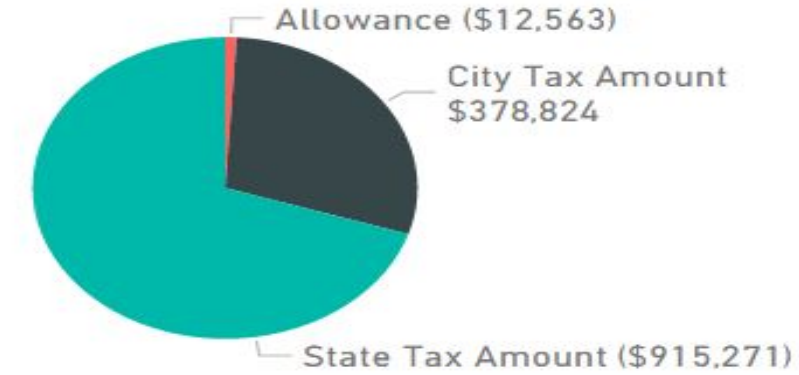


The Returns

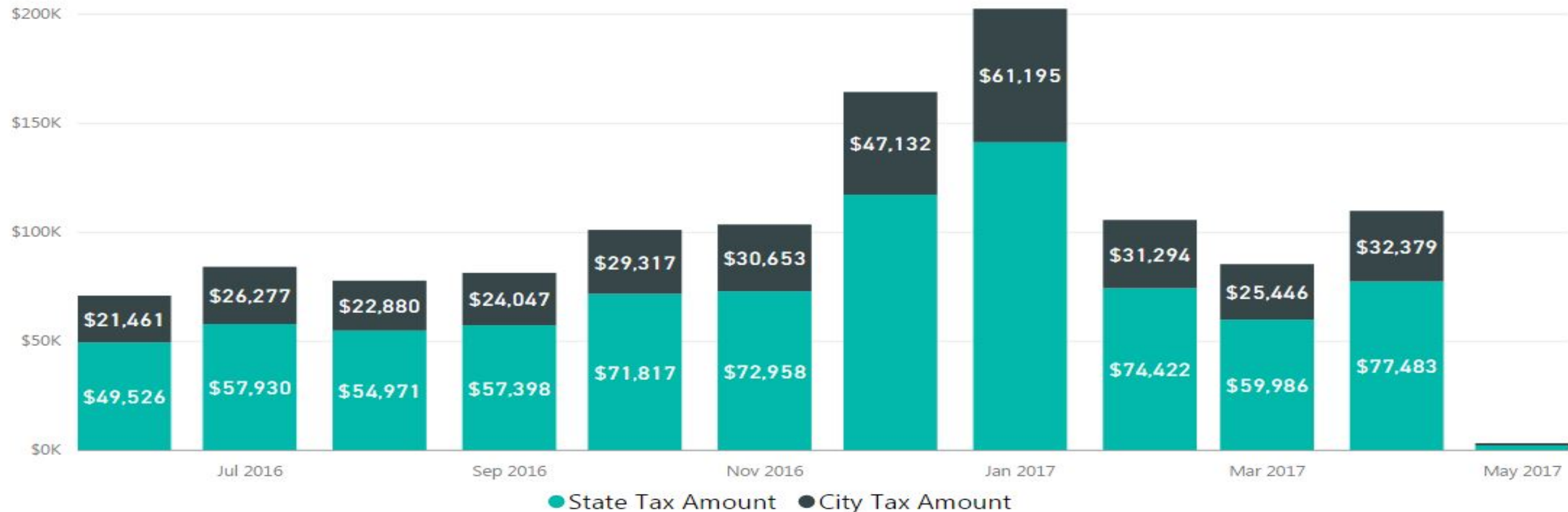
Tax Due Reported since June 2016

\$1,281,532

Tax Due Reported to Date



Reported Tax Due by Month Processed



Ohio Budget Bill

Department of Taxation

Main Operating Appropriations Bill

H. B. 49

Executive

As Passed by the House

TAXCD61

Use tax collections by certain out-of-state retailers

No provision.

R.C. 5741.01, 5741.17; Section 803.150

Requires, beginning January 1, 2018, an out-of-state seller with annual Ohio sales in excess of \$100,000 or 200 or more Ohio transactions to collect and remit use tax, regardless of whether or not those sellers have a physical presence or a substantial nexus with Ohio.

Fiscal effect: Uncertain increase in use tax revenues. Sales and use tax revenue is deposited in the GRF.

New York Marketplace Language

FY 2017-18 Marketplace Provider Budget Proposal

- Legislative proposal to expand sales tax collection responsibilities to online marketplace providers
- Purpose: Online marketplaces such as Amazon Marketplace, eBay, Etsy, Walmart.com and various “app stores” represent a large and growing share of online retail sales.
- Under the typical online marketplace business model, the marketplace provider:
 - 1) provides a forum in which third-party sellers are able to display their products and transact sales; and
 - 2) facilitates the collection and processing of payments for these third-party sellers.
- As a general rule, online marketplaces do not collect sales tax as part of their service.

New York Marketplace Language

- The Tax Department has documented sales tax compliance problems with online marketplaces.
 - Desk audits – 21 selected, only one collecting
 - Field Audits – 2 not registered, 12 under reporting
 - Information from marketplace – marketplace collects
 - 20% not registered or under reporting taxable sales
 - NEW YORKERS PAID – 3rd PARTY DID NOT REMIT!
- Current- inefficient and costly compliance
 - Marketplace third party sellers not collecting must register and file returns
 - Numbers are high – could double the 600K registered
- Marketplace efficiencies – one registration, one filing
 - Note many voluntarily collect and remit (Sears.com, Apple's App store)

New York Marketplace Language

Proposal:

- Tax would be collected and remitted by the marketplace provider on sales to New Yorkers by all third-party sellers, including those that do not have a presence (nexus) in the State.
- Approximately additional \$275 million 1st year (State and local)
 - growth of 15% to 20% annually is expected for the foreseeable future.
- The tax collection requirement only to sales of tangible personal property. Part X also applied to sales of services, hotel occupancy, and admission tickets.
- Small start-up online marketplaces would be excluded from the collection requirement with the inclusion of a sales threshold (i.e., \$100 million in annual sales).

U.S. Supreme Court Watch

- The recent focus has been on South Dakota's and Alabama's litigation of their law/regulation directly challenging *Quill*
- However, Irwin Naturals, a company based in California that sells nutritional products, will likely request the U.S. Supreme Court review a Washington Court of Appeals decision, see Docket 16A1078; cert. petition due 7/14/2017, that addresses *Quill's* separation of the states' authority to tax under the Due Process Clause and Commerce Clause
 - Irwin Naturals, citing *Norton v. IL Dep't of Rev.*, 340 U.S. 354 (1951), is arguing its retail sales shipped to customers in WA should be dissociated with its wholesale sales made to retailers and distributors in WA
 - While *Norton* addressed a gross receipts tax, Irwin Natural asserts that should also apply to sales/use taxes and that the Court's holding in *Nat'l Geographic Soc. V. Cal. Bd. of Equal.*, 430 U.S. 551 (1977), which held a taxpayer's presence in the state did not have to be directly related to its sales activity for California to impose a sales/use tax collection and remittance obligation on a business
 - Irwin Naturals argues that in the Court's 1992 *Quill* decision, where the Court distinguishing Due Process Clause "minimum contacts" from the Commerce Clause's "substantial nexus," the Court made *Nat'l Geographic* no longer relevant because the Court's analysis in that case was based on the Due Process Clause and not the Commerce Clause
- Could this case be a vehicle for the Court to address *Quill*?

Predictions

- Will the Highest Court of a State Overrule *Quill*?
 - If not, would the Court still take up the case?
- What would be the nexus standard if *Quill* is reversed?
- Is Retroactivity still a concern?
- Will Congress act?
 - Does it depend of whether the U.S. Supreme Court takes up a Case?
 - Will membership in the SSUTA be needed?

