Part Five

Accountants are being pulled in to the trend of the online marketplace. The ease offered by online ecommerce platforms means even small clients can suddenly be mired in complexities of multistate tax rules from their very first sale.

Michael T. Dillon • May. 14, 2018

If Quill is Overturned, What Does This Mean for Remote Sellers?

So we wake up one morning in late June to find that the Supreme Court has overturned *Quill*. The sky has not fallen…the birds are still chirping. What does it mean? Well, it all depends on the manner in which the Court decides *Wayfair*.

As we discussed in Part Four of this article, on September 13, 2017, upon challenge by

South Dakota v. Wayfair, Inc. et. al. [*South Dakota v. Wayfair Inc., et. al.*, 901 N.W.2d 754 (S.D. September 13, 2017); *cert. granted* (U.S. January 12, 2018) (No. 17-494)] At issue is whether the Court should abrogate *Quill's* sales-tax-only, physical-presence requirement?

The Tax Foundation provides a useful map of state efforts to tax remote sales. [https://taxfoundation.org/congress-act-scotus-online-sales-taxes/] Currently, there are 14 states plus the District of Columbia that require *Quill* physical presence nexus for a remote seller before the state may assert sales tax compliance requirements. As such, these states would arguably have to address this legislatively, or administratively, prior to requiring remote sellers to collect sales tax on sales to customers in their jurisdiction. This leaves 31 states that have adopted some method for imposing sales tax compliance obligations on remote sellers, either considering certain activities to constitute physical presence, or by ignoring the physical presence requirement.

Of these states, as I note in Part Three (need link) of this article, and as summarized in the Tax Foundation map, we observe the following:

- 22 states have adopted click-through or affiliate nexus laws. Such laws may be insufficient to assert nexus over a remote seller before the state may assert sales tax compliance requirements. For example, while tens of thousands of remote sellers utilize click-through and affiliate relationships (e.g., Amazon) to market their products, many remote sellers do not utilize such platforms.
- Ten (10) states have adopted Colorado-style notice and reporting requirements. The Court is not addressing the constitutionality of these laws, so it remains unclear how or if states would continue to exploit these requirements to "encourage" remote seller compliance.

- As such, each of these states may have to address this legislatively, or

remote seller exceeds a certain sales threshold in the state.
- Six states (South Dakota, Indiana, Maine, North Dakota, Vermont and Wyoming) have adopted economic nexus laws with limitations, which balance the needs for state collection against the need for uniformity, rate simplification, a *de minimis* threshold of $100,000 in annual sales or 200 individual transactions, and barring retroactive application. [S.D. S.B. 106] South Dakota's law also seeks to meet the Court's four-pronged test set forth in *Complete Auto Transit v. Brady*, ensuring that it does not discriminate against interstate sales and only taxes the state's fair portion of activity in the state. [430 US 274 (1977)]

Notably, South Dakota is a member of the Streamlined Sales Tax Project (SST), meaning they have already simplified their sales tax laws to promote simple and uniform application on interstate commerce. The most recent Federal bills promoting taxation of interstate commerce (*See* Marketplace Fairness Act and Remote Transaction Parity Act) both require similar simplification efforts by a state prior to the state requiring remote sellers to collect sales tax. Each of the other states have adopted the South Dakota template in their law.

Ideally, if the Court were to overturn *Quill*, it would do so within the confines of the South Dakota law. This would encourage other states to adopt the same law in order to require remote sellers to collect sales tax on sales to customers in their jurisdiction. States would be able to do so with certainty that the law will withstand constitutional scrutiny. This would also promote uniformity among the states, providing taxpayers with a bright line standard for the type or level of activity that will create nexus. States would be able to address the level of activity by making the *de minimis* threshold higher or lower, depending on their fiscal needs.

Most important, the law provides for prospective only treatment, which eliminates concerns relating to the retroactive application of the Court's decision and historical

liabilities for every taxpayer that has relied on the physical presence standard as a

third parties that facilitate the sale of a remote seller's product through a marketplace. Even under the existing *Quill* physical presence standard, most state and local tax professionals will agree that this establishes physical presence for sales tax purposes. Though the argument exists that such remote sellers are not "retailers" within state sales tax laws, but that the marketplace facilitators are the actual "retailers" required to collect the sales tax, this issue is not before the Court in *Wayfair*.)

However, the *Wayfair* Court could potentially take a different approach in overturning *Quill*. For example, the Court could:

- Uphold the South Dakota nexus standard only, yet provide no clear guidelines as to what other state nexus standards are constitutional. This approach would only benefit the five other states that have adopted the same South Dakota law, and would otherwise merely serve to support and proliferate the nexus standards that the remaining states adopt to expand their taxing authority, causing even more damage and uncertainty in state taxation.
- Uphold the South Dakota nexus standard by removing the physical presence requirement for sales tax nexus, and allowing for state's to adopt their own interpretation of what nexus means. This could lead to a free-for-all, in which states would adopt myriad nexus standards, leaving taxpayers with no clear bright line standard for the type or level of activity that will create nexus. Again, this approach would cause even more damage and uncertainty in state taxation.
- Uphold the South Dakota nexus standard by removing the physical presence requirement for sales tax nexus, and providing specific criteria under which a state's sales tax laws applicable to remote sellers will properly establish substantial nexus given repeal of the physical presence standard. In other words, it could establish a new standard without specifically limiting the standard to the South Dakota law. This too could lead to a free-for-all, in which states would

adopt myriad nexus standards, leaving taxpayers with no clear bright line

to realize its practical implications, and then – ideally – states will need to legislatively or administratively adopt principles by which they seek to require remote sellers to collect sales tax.

We can, however, expect that some states will seek to simply issue a bulletin and/or mass mailing simply informing remote sellers that they are now required to register and collect sales tax. As such, there will remain countless arguments about state authority to impose their laws on remote sellers, only furthering the need for Federal legislation in this area.

Ultimately, if *Quill* is overturned, and states are able to require remote sellers to collect and remit sales tax, remote sellers who historically have not collected sales tax will now have to implement sales tax compliance protocol and will no longer maintain a competitive advantage over retailers who have long had to collect sales tax. Obviously, this will even the playing field not only for large big box retailer, but also for remote sellers who already collect state sales tax regardless of physical presence.

Currently, there are several good pieces of legislation before Congress that address these issues, and such legislation can be enhanced by the Supreme Court's *Wayfair* decision, should it overturn *Quill*. Both the Senate and the House continue to pursue legislative measures to enable states to impose sales tax collection obligations on out-of-state retailers, regardless of whether they maintain a 'physical presence' or not. [Marketplace Fairness Act (S.976); Remote Transaction Parity Act (HR 2193)] In the Senate, since 2013, several legislators have presented versions of the Marketplace Fairness Act (MFA), most recently in 2017, which would give states more power to collect sales taxes from businesses that don't have a physical location within their borders, so long as the state participates in the Streamlined Sales Tax Project (SST), or implements the simplification requirements and liability provisions of the MFA.

Its earliest version (The Marketplace Fairness Act of 2013) passed with ease in the

Project, or implements the simplification requirements and liability provisions of the RTPA. Like its Senate sibling, the RTPA is completely voluntary for states, provides a small seller exception, and would require a minimum six month waiting period before a state can begin requiring remote sellers to collect sales tax.

However, there are several notable differences between the MFA and the RTPA, including the size and applicability of the small seller exception, as well as potential audit liability for remote sellers and potential audit liability for sales tax automation solution providers. There are many unanswered questions in both versions as well. For example, liability of a remote seller to a customer for over- or under-collection of sales tax, how the legislation applies to remote sellers in foreign countries, whether state or federal courts have jurisdiction over cases involving administration of state taxes under these laws, penalties for noncompliance and the lack of uniformity in tax treatment of products and services among state participating in the Streamlined Sales Tax Project.

To the extent Congress does respond to the Court's *Wayfair* decision, just as with the manner in which the Court decides *Wayfair*, the manner in which Congress responds could cause more harm than good if Congress overreacts to a *Quill* reversal. If Congress enacts legislation that grants states too much authority to tax interstate commerce, it will open the floodgates to state taxation in a manner that cedes too much of its Commerce Clause power to the states. If Congress enacts legislation that is too restrictive, or imposes too high of a small seller exemption, states may not realize sufficient sales tax revenues associated with remote sellers, and may begin the post-*Quill* aggressive tactics all over again.

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