Impact of the Wayfair decision

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1/16/19

Vermont's sales tax

- 6% of the sales price on the retail sale of tangible personal property
- Collected by vendors on behalf of the State at the point of sale – a "trust tax"
- When a state relies on someone else to collect and remit a tax, it has to be able to exercise jurisdiction over that person to enforce the obligation.
- How far can a state reach beyond its borders to enforce its laws?

Commerce Clause

- Congress has the power to regulate commerce among the States.
- Drafted to avoid the economic balkanization that plagued relations among the colonies.
- State regulation may not:
  - Discriminate against interstate commerce
  - Impose an undue burden on interstate commerce

Quill v. North Dakota (1992)

- Quill office supply company solicited and sold goods in South Dakota via US mail
- Under Commerce Clause, US Supreme Court ruled that a state cannot force seller to collect and remit sales tax unless the seller has a physical presence in the state – undue burden case
- In the internet age, this means that online retailers who lacked a physical presence in Vermont are not obligated to collect and remit the sales tax

Use tax compliance

- If, under Quill, a seller is not going to collect and remit, then the purchaser owes use tax
- But use tax compliance is low
  - Nationally in the range of 1-3%
  - Vermont has taken steps to improve its use tax compliance, but it is still only about 10%
- Since most people do not pay use tax, result is that most out of state purchases are not taxed

Two equity problems

- As online sales increase as a proportion of all sales, sales and use tax revenue in Vermont goes down
  - Online sales have increased nearly tenfold since 2000
  - Currently about 10% of all sales
- If online retailers do not collect and remit, they gain a competitive edge over brick and mortar retailers

State responses to Quill

- There were a number of state responses to Quill over the years, but in light of subsequent legal developments, there are only two that bear mention now:
  - Streamline Sales and Use Tax Agreement
  - Direct legal challenges

Streamline Sale and Use Tax Agreement

- Interstate agreement with 23 states, including Vermont – adopting a common set of definitions and administrative provisions
- Designed to simplify sales tax compliance and administration
- Was created to counter the concern that subjecting businesses to multiple sales tax regimes would burden interstate commerce – a response to Quill's "undue burden" analysis
- Vermont realizes about $1 million each year from participating in the agreement

Direct Legal Challenges

- A number of states began passing laws or adopting regulations which extended jurisdiction to vendors who had an "economic presence" in the state, but no physical presence
- Direct challenge to Quill's requirement
- Hoped that the U.S. Supreme Court would overturn Quill

Wayfair

- South Dakota passed a law that required any vendor to collect and remit the sales tax if:
  - $100,000 in sales or
  - 200 individual transactions
  - Physical presence not required
- US Supreme Court ruled that in light of subsequent developments, the physical presence requirement of Quill is “incorrect and unsound”

Wayfair

- Physical presence rule not a necessary interpretation of prior nexus cases
- Quill created, rather than resolved, market distortions
- The physical presence test was overly formalistic and inconsistent with the Supreme Courts overall approach to the Commerce Clause, which tends to be more of a case-by-case analysis

Wayfair

- Court concluded that South Dakota’s economic presence test did not create an undue burden
- Specifically mentioned how the law excluded smaller vendors ($100,000/200 transactions)
- Specifically mentioned that South Dakota was a streamline state, reducing the burden on compliance
- The result is a sense that there is a clear “safe harbor” – if a state comes with the South Dakota economic presence requirement, it should be able to reach out of state vendors who lack a physical presence

Vermont anticipated

- In 2017, Vermont adopted South Dakota type requirements:
  - $100,000/200 sales
  - Plus Vermont is also a SSUTA Agreement state
- Made effective on the first day of the first quarter after Quill was overturned
- After Quill, these provisions became effective July 1, 2018
- Happy ending! .... Right?

How internet sales work

- In the old days:
  - Website
  - Direct sales and fulfillment by the vendor
- Nowadays, vendors also sell through other businesses that provide a marketplace for online sales:
  - Promote products
  - Facilitate payments
  - May or may not handle fulfillment
  - Other services, such as accounting, inventory tracking

Marketplace Facilitators versus Marketplace Sellers

- Marketplace facilitator:
  - A business that that contracts with third party sellers to promote their sale of physical property, digital goods, and services through an online marketplace.
  - Think Amazon or Ebay
- Marketplace seller:
  - A business that contracts with a marketplace facilitator for services to assist in the sale of their products.
  - Think a producer of widgets

Vermont is only part way there

- Wayfair + Vermont’s current statutory system means that Vermont can collect and remit on direct sales into Vermont by a vendor who is not located here.
- However, marketplace facilitators, such as Amazon, are not required to collect and remit for indirect, or facilitated third party sales.

Why is this a problem?

- Compliance issues to collect and remit from every far flung individual vendor
  - MFs aggregate a huge number of sellers
    - 55% of Amazon's total sales were third party sales in 2017
    - 25% of Amazon's third party sales in 2017 were from non-US global sellers
  - As Amazon has begun collecting sales tax on direct sales, its third party seller services have boomed
- Threshold problems – some small vendors could split sales to avoid the tax

Marketplace legislation beginning

- As of 11/18, ten states had some form of marketplace facilitator language. More coming.
- Multistate Tax Commission organized a working group in 2018 to outline marketplace facilitator issues moving forward.

Marketplace Facilitators versus Marketplace Sellers

- Broad or narrow definition of MF
  - Too broad and there could be compliance problems; too narrow and there could be avoidance problems
    - Example: MFs want access to payment data. If defined too broadly, some MF models may not have access to payment data. If defined too narrowly, MFs could structure their businesses to claim they don't have access to payment data.
  - A broader approach could also anticipate future changes in technology

Other issues

- Who registers?
- Who gets audited?
- How are the economic thresholds applied?
  - MF: to direct sales and facilitated sales?
  - MS: to direct sales only? Or to direct and sales facilitated by someone else?