The Supreme Court's *Wayfair* Decision and its Impact on the Association of Service and Computer Dealers and the North American Association of Telecom Dealers

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INTRODUCTION: Why are we here?

- The ASCDI-NATD (Association of Service and Computer Dealers and the North American Association of Telecom Dealers) is a not for profit association of companies that buy, sell and service computer, telecom and other technical equipment and solutions.
- Many dealers have operations and a physical presence in a single state or a few.
- Many dealers historically were not required, by law, to bill, collect and remit sales taxes on transactions with purchasers in states outside of those where the dealer "triggered" the "physical presence" nexus test established by the Supreme Court's 1992 *Quill* decision.
- The Supreme Court's 2018 *Wayfair* decision overturned *Quill* and supplanted the traditional physical presence test with an "economic nexus" test, thus setting the foundation for states to implement sales taxes on "Remote Sellers."
- ASCDI-NATD members previously unaffected by sales taxes in distant states may now be required to bill, collect and remit sales taxes in dozens of states.

Agenda

- ❑ *What is nexus?*
- ❑ *Identify and Compare Nexus Standards*
- ❑ *State Responses*
- ❑ *Legal Risks, Uncertainty and Opportunities*

NEXUS BASICS

What is nexus?

- The **determining** factor of whether a business is liable for collecting taxes on sales within a state.

- Describes the **amount or degree of business activity** that must be reached before a state can **impose taxes** on a company's income or revenue.

Nexus Tests

- **Physical Presence (*Quill*)**
  - *If a company has a physical presence (equipment, offices, telecom infrastructure, employees/contractors) in a jurisdiction, it has nexus with that jurisdiction.*
- **Economic Nexus (*Wayfair*)**
  - *If a company earns more than the threshold from selling services/goods in the state, the company has nexus for tax purposes.*

Complicating Factors

Nexus for One, Nexus for All

- Generally, nexus must be independently evaluated for EACH tax type.
- If a company establishes nexus with a jurisdiction for income (or other) tax purposes, it may ALSO establish nexus for purposes of sales, use, or other taxes.

Remote Sales

- Online (e-commerce) sales
- Other remote (phone) sales

Implications of Establishing Nexus

✓Registration

➢ *Required to register with Department of Revenue*

✓Collection and Remittance

➢*Required to collect and remit sales/excise tax*

✓Tax Engine/Calculation/Billing Software

➢*Must invest in a billing system that enables the company to calculate, appropriately bill, and collect taxes in all applicable jurisdictions*

✓Resale Compliance

➢*Must implement a resale compliance program (for selling services on a wholesale basis)*

NEXUS TESTS:
Physical Presence (*Quill*)

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The Rule Before Wayfair- *Quill Corp. v. North Dakota*

- In 1992, the United States Supreme Court decided *Quill Corp. v. North Dakota*, which required a meaningful **physical presence** for remote sellers within the state to be subjected to the sales tax nexus of a state.

- Physical presence included, but was not limited to:
  - *possessing inventory in a jurisdiction;*
  - *owning or leasing real tangible property or personal property;*
  - *conducting services in the jurisdiction;*
  - *having employees conduct in-person solicitation activities within the jurisdiction.*

The Rule Before *Wayfair- Quill Corp. v. North Dakota*

- Brick and mortar retailers complained that this gave remote out-of-state sellers an unfair business advantage, as their goods and services would not be subject to sales tax.
- State legislatures also complained that they were losing tax revenue on goods sold within their jurisdiction, as asking individual taxpayers to calculate their own use tax was unrealistic.
- In response, states began to devise work-arounds to the *Quill* rule, including an “Economic Nexus” sales tax formula.

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NEXUS TESTS:
Economic Nexus (*Wayfair*)

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The *Wayfair* Rule: "Economic Nexus"

- On June 21, 2018, the U.S. Supreme Court declared that a 2016 "economic nexus" sales tax formula administered by South Dakota was constitutional.
- This ruling, *Wayfair v. South Dakota*, explicitly overruled the physical presence rule as required by *Quill* for both **domestic** and **foreign companies.**
- However, in so doing, the Supreme Court did not endorse **all** economic nexus formulas, just the formula used by South Dakota.
- It also made clear that the Commerce Clause and due process requirements of the U.S. Constitution still mandate that state taxes are neither discriminatory nor unduly burdensome to interstate commerce.

Factors considered by Supreme Court for Constitutionality

- In finding South Dakota's law constitutional, the Supreme Court analyzed the law's threshold for determining nexus.
- The South Dakota law only applies to a seller selling more than $100,000 of goods or services into South Dakota or engaging in 200 or more transactions in the state each year.
- Based on this analysis, the Court, without discussing the weight of each factor, identified six factors it considered in determining the South Dakota law did not discriminate or unduly burden interstate commerce, including:
  - *Inclusion of a safe harbor for a seller that transacts limited business in South Dakota (the $100,000 or 200 transaction thresholds);*
  - *Prospective-only application of the law (the law does not apply retroactively); and*
  - *Adoption of the Streamlined Sales and Use Tax Agreement, which requires:*
    - A single, state-level tax administration;
    - A simplified tax rate structure, including uniform definitions of products and services; and
    - The state to offer free sales tax software and immunity from audit liability for a seller who uses the state's software.

Uncertainty Surrounding Economic Nexus Requirements

- The potential for other states to adopt economic nexus rules that differ from South Dakota's rules is a significant source of uncertainty and potential risk for businesses.
- And, unbeknownst to many retailers, there are a handful of states, in addition to South Dakota, that have implemented and are enforcing a variety of economic nexus requirements on out-of-state sellers.
- Thus, retailers must understand and contend with existing economic nexus requirements, as well as plan for anticipated state reactions to *Wayfair* in the form of new and varied economic nexus requirements.
- Further, the impact of *Wayfair* could extend beyond state sales taxes. Many states impose other taxes, the application of which on out-of-state providers will likely be governed by *Wayfair* and similar economic tax considerations.
- And, in many states, localities have their own taxing regimes and authority. Thus, providers must consider potential economic nexus requirements at both the state and local levels, over hundreds of taxing jurisdictions.

Legal Uncertainty

- There is additional uncertainty surrounding the compliance with and enforcement of both existing and newly created standards during the inevitable legal battles that will come as states experiment with different economic nexus rules in the wake of *Wayfair*.
- A number of economic nexus laws also remain subject to litigation, including South Dakota's law, which the Supreme Court remanded to the South Dakota Supreme Court for further consideration.
- While this litigation continues, businesses must make determinations about how and whether to collect and remit transaction taxes in a number of jurisdictions.
- Moreover, changes may occur to a seller's obligations in a given state depending on the outcome of legal proceedings that may not get significant press coverage outside the sales tax or trade press.
- This underscores the importance of retaining expert legal and accounting professionals to help monitor the changing economic nexus landscape and to ensure timely compliance with new economic nexus requirements.

Legal Uncertainty

- After contending with a range of state decisions regarding economic nexus thresholds, a seller will also need to determine its sales tax liability in each state in which it has economic nexus.
- Taxability questions can be as or more difficult than determining whether a seller has nexus in the first place. And, like the variation in economic nexus thresholds, the taxability of certain goods and services varies widely from state to state and from locality to locality.
- It is critical for a provider to consult legal counsel to help the provider understand the tax implications of the seller's offering and to develop a strategy to minimize exposure to applicable taxes.

Potential Variability in Different State Approaches

- The variability among the states' approaches to economic nexus considerations can include the following:
  - *Wide variation as to economic thresholds, with some state thresholds being as high as $500,000 in annual sales or as low as $10,000 in annual sales;*
  - *Thresholds being determined by the number of annual transactions vs. the amount of annual revenue;*
  - *The application of economic considerations to local taxes;*
  - *The application of economic considerations to all transaction taxes; and*
  - *Whether economic nexus requirements will be applied retroactivity, the availability of amnesty, and/or the availability of voluntary disclosure programs.*

State by State Variance

- With *Wayfair*, the Supreme Court did the easy part, paving the way for states to impose sales tax collection requirements on remote online sellers.
- Now states and, more importantly, businesses are left with the hard part, figuring out exactly how to collect sales taxes from remote sellers in different jurisdictions across the country.
- To date, more than thirty states have already passed economic nexus laws that are either already in effect or will take effect soon. A number of these states have adopted laws that mirror the South Dakota law at issue in *Wayfair.*
- For example, Hawaii, Iowa, Illinois, and Indiana all have economic nexus laws with an economic nexus threshold of $100,000 in sales or 200 transactions in the state.

State by State Variance

- However, there are a number of outlier states with economic nexus thresholds and rules that differ significantly from those upheld by the Court in *Wayfair*. The lack of uniformity among the states may lead to confusion and frustration for sellers that are attempting to develop a nationwide (or multi-state) sales tax strategy.
- For example, several states have implemented laws with larger thresholds before a seller triggers economic nexus in the state.
- Alabama and Mississippi opted to set their thresholds for economic nexus at $250,000 in annual sales in their states; Connecticut requires $250,000 in annual sales and 200 or more transactions in the state; and Tennessee only imposes economic nexus on sellers with more than $500,000 in sales in the state during the previous 12-month period.

State by State Variance

- In contrast, and potentially more problematic for sellers, other states have enacted economic nexus laws with extremely low thresholds that could potentially be triggered by a single large purchase order in a state.
- Specifically, Minnesota and Pennsylvania stand out for their low economic nexus thresholds. In both states, a seller with more than $10,000 in sales during the prior year can be subject to sales tax collection and remittance requirements.
- In Minnesota, the impact of the low economic nexus threshold is somewhat mitigated by a state law caveat that a remote seller only has nexus with the state if it makes sales through an Internet marketplace provider or through any other third party maintaining a place of business in Minnesota.
- As a result, Minnesota's system may be more accurately viewed as a hybrid economic/affiliate nexus structure. While this hybrid nexus structure may allow some businesses to avoid sales tax liability in Minnesota, it adds yet another factor retailers must take into account when structuring their tax compliance strategies.

State by State Variance

- Similarly, Pennsylvania has somewhat diluted the impact of its lower economic nexus threshold by allowing sellers to either collect and remit sales taxes or comply with the state's "notice and reporting" requirements.
- Approximately a dozen states have adopted notice and reporting requirements as an alternative for remote sellers that opt not to register with the state and remit sales taxes.
- With respect to Pennsylvania, the Commonwealth requires any seller that selects the notice and reporting option to:
  - *Post a notice on its sales forums informing customers that sales or use tax may be due on purchases;*
  - *Provide a written notice on all invoices, order forms, sales receipts, or similar documents (whether in paper or electronic form) notifying the purchaser of the potential sales tax liability in Pennsylvania;*
  - *Provide an annual report to the purchaser by January 31 of each year notifying the purchaser that Pennsylvania sales or use tax may be due on purchases from the prior year; and*
  - *Send an annual report to the Pennsylvania Department of Revenue by January 31 of each year that provides the Department with each purchaser's name, billing address, delivery address, last known mailing address (if different), and the total dollar amount of purchases from the remote seller.*

State by State Current Economic Nexus Regulation

State	Economic Nexus Threshold	Effective Date
Alabama	$250,000 (Annual sales)	1/1/2019 for third-party marketplace facilitators, 10/1/2018 for all others
Colorado	$100,000 OR 200 Transactions	12/1/2018
Connecticut	$250,000 AND 200 Transactions	12/1/2018
Georgia	$250,000 OR 200 Transactions	1/1/2019
Hawaii	$100,000 OR 200 Transactions	7/1/2018
Illinois	$100,000 OR 200 Transactions	10/1/2018
Indiana	$100,000 OR 200 Transactions	10/1/2018
Iowa	$100,000 OR 200 Transactions	1/1/2019
Kentucky	$100,000 OR 200 Transactions	10/1/2018
Louisiana	$100,000 OR 200 Transactions	1/1/2019

State by State Current Economic Nexus Regulation

State	Economic Nexus Threshold	Effective Date
Maine	$100,000 OR 200 Transactions	10/1/2017
Maryland	$100,000 OR 200 Transactions	10/1/2018
Massachusetts	$500,000 AND 200 Transactions	10/1/2017
Michigan	$100,000 OR 200 Transactions	10/1/2018
Minnesota	$10,000	10/1/2018
Mississippi	$250,000	9/1/2018
Nebraska	$100,000 OR 200 Transactions	1/1/2019
Nevada	$100,000 OR 200 Transactions	11/1/2018
New Jersey	$100,000 OR 200 Transactions	11/1/2018
North Carolina	$100,000 OR 200 Transactions	11/1/2018
North Dakota	$100,000 OR 200 Transactions	10/1/2018

State by State Current Economic Nexus Regulation

State	Economic Nexus Threshold	Effective Date
Ohio	$500,000	1/1/2018
Oklahoma	$10,000	7/1/2018
Pennsylvania	$10,000	4/1/2018
Rhode Island	$100,000 OR 200 Transactions	10/1/2018
South Carolina	$100,000 OR 200 Transactions	11/1/2018
South Dakota	$100,000 OR 200 Transactions	11/1/2018
Utah	$100,000 OR 200 Transactions	1/1/2019
Vermont	$100,000 OR 200 Transactions	7/1/2018
Washington	$100,000 OR 200 Transactions	10/1/2018
West Virginia	$100,000 OR 200 Transactions	1/1/2019
Wisconsin	$100,000 OR 200 Transactions	10/1/2018
Wyoming	$100,000 OR 200 Transactions	2/1/2019

Risks for Businesses

- Retroactivity
  - *Backward-looking tax liability*
  - *Risk that companies will be required to pay out of pocket, rather than pass through to customers*
    - Hawaii confirmed it will not retroactively administer economic nexus rules
    - More aggressive states could back date exposure to the *Wayfair* decision
  - *Depending on exposure, some companies may choose to accrue for potential retroactive findings*
- Evolving State Economic Nexus Requirements
  - *New states will change laws to take advantage of Wayfair. For example, Texas is planning to change its rules in early 2019.*
  - *Conversely, states like NH, without sales tax, are taking steps to protect their businesses. NH set up a Commission to study how to protect its businesses from paying remote sales tax. (One idea: force a foreign Dept. of Revenue to register and pay a fee to NH's Dept. of Justice).*
- Congressional Action Could Change the Rules
  - *Legislation like the Marketplace Fairness Act could create a nationwide sale tax nexus regime.*
  - *Legislation could create thresholds that determine whether a company is subject to the law.*
  - *As with any legislation in today's Congress, it is unlikely to pass.*

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Practical Next Steps: What Should You Do?

- Step 1 – Take a fresh look at your Company's current policies & practices vis-à-vis sales tax compliance
  - *Are you still relying on a "physical presence" test?*
  - *Are you a pure wholesaler relying entirely on tax exemption from your resellers?*
  - *How are you sourcing revenue to determine which state's taxes or exemption certificate applies to your transactions?*
- Step 2 – Self-Help
  - *Do your own research! Here, let us help:*
    - https://www.salestaxinstitute.com/resources/remote-seller-resources
    - https://www.avalara.com/us/en/learn/sales-tax/south-dakota-wayfair.html
- Step 3 – Identify your concerns and formulate your questions
  - *Seek guidance from the experts!*

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Practical Next Steps: How Can We Help?

- We can help you determine whether your Company's current practices trigger "Remote Seller" tax issues
- We can help you determine whether your Company's current practices give rise to "Economic Nexus"
- We can help you evaluate whether changes to current practices can minimize or eliminate your Company's exposure to Remote Seller taxes
- We can introduce you to vendors of sales tax solutions that help with compliance:
- Our consulting affiliate can help with:
  - *Tax registrations*
  - *Tax return prep and remittance*
  - *Tax exemption management*

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Questions?

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