



VIEW*S* & VISIONS

A publication of Bowles Rice LLP

Summer 2018



E-Commerce Sales and Use Tax Changes Coming

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Robert S. Kiss, a partner in the Charleston office of Bowles Rice, practices in the areas of tax, estate planning and commercial law. From 2013 to 2016, he served as Cabinet Secretary of the Department of Revenue under former West Virginia Governor Earl Ray Tomblin.

During his tenure with the Tomblin administration, Kiss also presided as the state budget director and the governor's designee for the Board of Treasury Investments.

He first joined Bowles Rice in 2003, after serving 19 years in the West Virginia House of Delegates. He served as Speaker of the House from 1997 to 2006 and House Finance Chairman from 1993 to 1996. Pursuant to his legislative duties, Kiss was extensively involved in more than a decade of major economic and fiscal legislation, including the West Virginia School Building Authority; water and sewer infrastructure development; state tax policy; state health care plans, including PEIA and Medicaid; state retirement systems; the workers' compensation system; and the Tax Increment Financing (TIF) legislation.

State tax collection agencies, tax practitioners and hundreds of thousands of businesses throughout both the state of West Virginia and the United States are now on the verge of perhaps one of the most significant shifts in tax policy ever caused by a judicial decision.

Since 1992, the United States Supreme Court ruling in *Quill Corporation v. North Dakota*, 504 U.S. 298 (1992), required remote internet sellers to collect and remit state sales tax only if those sellers had a physical presence in the state. The Court's ruling was based upon the United States Constitution's Commerce Clause and established legal doctrines preventing states from interfering with interstate commerce unless authorized by Congress.

In order to understand the possible paradigm shift we now face, one must recognize that the U.S. Supreme Court's decision in *Quill* was decided before Amazon.com or eBay were founded (1994 and 1995), and that the scope and magnitude of consumer internet purchases now dwarfs the extent and scope of those type of sales in the 1990s. Now, when Amazon fills an order for goods from its own inventory for a customer located in a state where it has a physical presence (e.g. due to having one of its fulfillment centers there) or for goods from the inventory

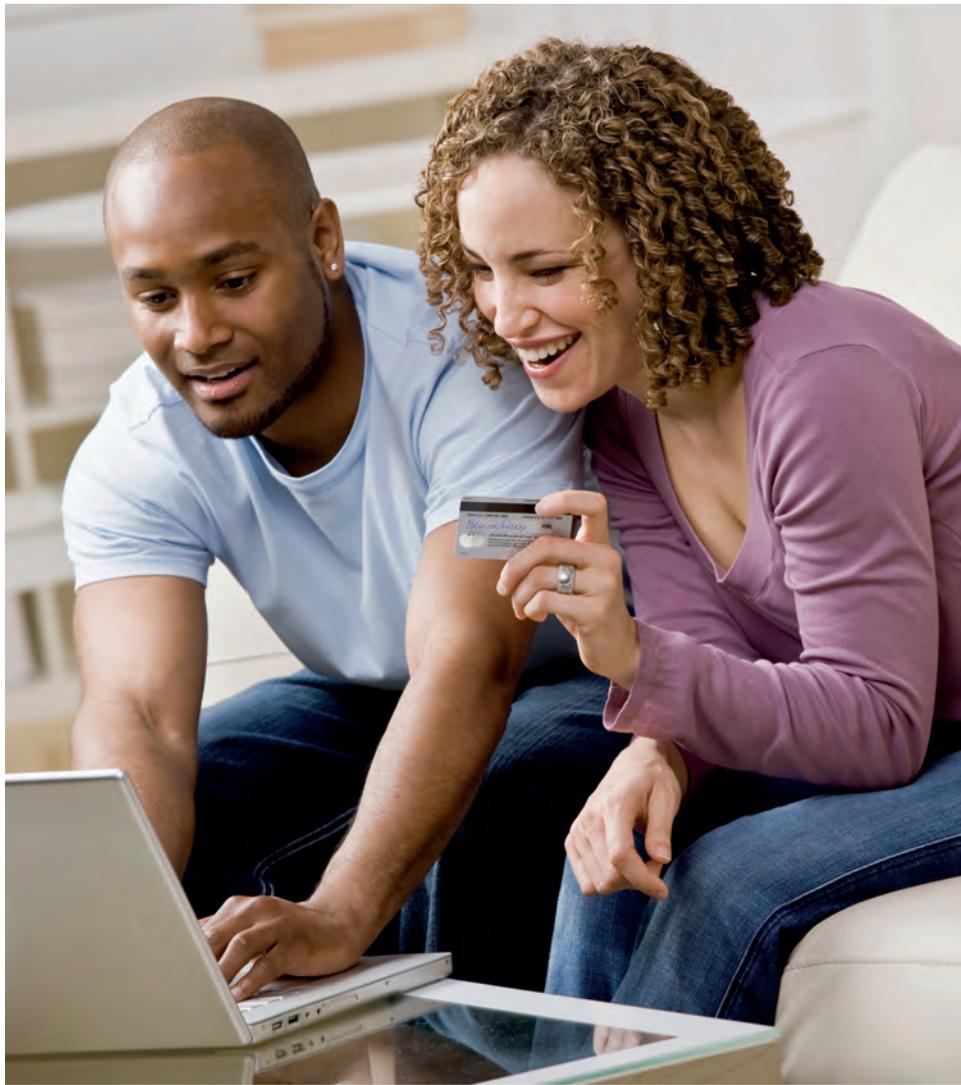
of a third-party vendor that has a physical presence in that state, it charges that state's sales tax. However, as is often the case, if the vendor (whether Amazon or the third-party vendor) does not have such a physical presence in the customer's state, the tax is not charged.

Estimates suggest that but for *Quill*, state and local governments could have collected an additional \$13 billion in 2017 in sales tax payments from online sellers. Recent action by the U.S. Supreme Court overturning *Quill* will have enormous fiscal implications for state and local government taxing authorities in the United States, not to mention the implications for businesses and taxpayers who are now required to collect and remit sales tax on a much broader scope of sales.

So, what could cause this seismic shift in sales and use tax administration and potential collections in the United States? The U.S. Supreme Court recently decided the case of *South Dakota v. Wayfair, Inc.*, 2018 U.S. Lexis 3835, an appeal from a decision by the Supreme Court of the state of South Dakota.

In 2016, the South Dakota legislature and governor passed legislation that was a pre-designed attempt to cause the U.S. Supreme





The Court's decision overturned *Quill* and ruled that a narrowly crafted economic nexus standard, which otherwise minimized any burden on interstate commerce, was enforceable by the state and not a violation of the United States Constitution's Commerce Clause.

However, the reasoning of the Court's decision may be critical to the success or failure of what is now certain to be a flood of other states and jurisdictions attempting to impose a similar economic nexus standard, particularly if those standards are not narrowly crafted.

In upholding the South Dakota Statute, the Court pointed favorably to its following features:

1. The South Dakota statute was not retroactive.
2. The state created a safe harbor for those who transact only limited business in South Dakota.
3. South Dakota was a signatory to the Streamlined Sales and Use Tax Agreement, which standardizes sales and use taxes to reduce administrative and compliance costs.
4. The state allows sellers access to state sales tax administration software, and provides sales and use tax audit immunity for those who use it.

States and other taxing jurisdictions would be well advised if they pursue South Dakota's approach adopting an economic nexus to carefully follow South Dakota's blueprint. Although West Virginia is also a party to the Streamlined Sales and Use Tax Agreement, and its statutes have long contemplated collection of its use tax by out-of-state vendors if they have constitutional economic nexus with the state, refinements of those statutes adding the above key features of the South Dakota law would appear to be a prudent course. ▽

Court to reconsider its position in *Quill*. South Dakota took this action based upon its belief that the state's inability to effectively collect sales tax from internet sellers was causing significant harm to both the state treasury and local brick-and-mortar retailers in South Dakota.

Instead of requiring a physical presence, the South Dakota legislation implements an economic nexus standard requiring remote sellers without a physical presence in the state to collect and remit sales tax if certain gross revenue or transaction thresholds are met.

It appears that *Quill's* demise was pre-ordained by the lightning speed at which the scope and magnitude of internet sales has exploded in the last 20 years. That explosion created significant economic challenges for the many state

and local jurisdictions that impose a sales and use tax. Only five states in the country – Alaska, Delaware, Montana, New Hampshire and Oregon – do not impose sales taxes.

The U.S. Census Bureau estimates that in 2016 total e-commerce sales in the United States exceeded \$300 billion and accounted for approximately eight percent of total retail sales compared to similar data, which in 2001 indicated total e-commerce sales were estimated to be slightly more than \$30 billion and only approximately one percent of total retail sales.

On January 12, 2018, the U.S. Supreme Court granted the state of South Dakota's petition for appeal. Oral arguments were heard in April of 2018 and the Court's decision was issued June 21, 2018.