



“The Tax Case of the Millennium”

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How Did We Get Here?

- 1967 - In *National Bellas Hess v. Department of Revenue of Illinois*, the Supreme Court held that states and local governments cannot require a business to collect sales tax unless the business has a **physical presence** in the state.



The Quill Rule

- In 1992, USSC reaffirmed *Bellas Hess* physical presence test citing state sales tax requirements were too complex and burdensome.
- ND tried to get Quill, an Illinois-based office supply mail order retailer, to pay taxes on sales shipped into the state.
- Quill's only contacts with ND were by mail or phone.
- The Court signaled that Congress could resolve this issue.



Substantial Nexus

- Rooted in dormant Commerce Clause interpretation.
- **Complete Auto Transit v. Brady** (1977) – 4-factor test to determine whether a state tax violates the Commerce Clause.
- “Substantial nexus” factor is the focus here; **Quill** held that a state cannot tax a company that is not “substantially connected” to the state through physical presence.



What’s Congress Been Doing?



Congress continues to stall on various proposals:

- **Marketplace Fairness Act of 2017** - would authorize states meeting certain requirements to require remote sellers that do not meet a “small seller exception” to collect their state and local sales and use taxes.
- **Business Activity Tax Simplification Act** - would define the level of activity that gives rise to business taxes.
- **Remote Transactions Parity Act** - would require states to simplify their sales taxes before they could collect sales taxes on internet transactions.
- **Mobile Workforce** - would limit state income tax collection to only those in the state for 30 days or longer.
- **No Regulation Without Representation Act of 2017** - would, in part, codify **Quill**'s physical-presence standard.

Setting the Stage

Direct Marketing Association v. Brohl (2015)

“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

- “...And *Quill*'s very reasoning...seems deliberately designed to ensure that *Bellas Hess*' precedential island would never expand but would, if anything, wash away with the tides of time.”

— Judge Gorsuch



The Perfect Storm

- Explosion of e-commerce
- Congressional inaction
- States' strapped revenues
- Judicial green light



“Economic Presence”



- South Dakota's 2016 “economic presence” law
- Online retailers are required to collect sales taxes if a business has more than \$100,000 in annual sales to South Dakota residents or more than 200 separate transactions with state residents.
- Intentionally written to tee up a constitutional challenge.

In This Corner...



- The new retail landscape renders *Quill* obsolete.
- A majority of states, through Streamlined, have significantly simplified their sales tax systems and software exists to help with sales tax collection.
- The inability of states to collect these sales taxes harms their ability to manage government resources without raising other taxes, especially for states wholly dependent on sales taxes for revenue.
- *Quill* discriminates against brick-and-mortar stores since online stores can offer the same products at lower effective prices.
- The National Retail Federation, along with 40 other states joined in South Dakota's petition. The state was also supported by President Trump's Administration.



...And in This Corner

- *Stare decisis*—the legal principle that favors maintaining current precedent.
- Burdensome compliance costs and exposure to audit.
- Remote sellers have always operated at a fundamental cost disadvantage to local businesses because remote sellers must charge shipping fees to deliver their products to consumers.
- Potential for retroactive tax liability.
- Congress is the appropriate forum to resolve this issue.
- 23 *amicus curiae* briefs were filed in support of the companies' position.

Justices Kennedy & Gorsuch line of questioning seem to indicate they remain anti-Quill.

Said nothing at oral argument but has rejected the Dormant Commerce Clause since *Quill*.

Most vocal champion of overturning *Quill*.

Led the charge defending *Quill*.

Particularly sympathetic to South Dakota's position. Suggested if *Quill* was overturned, states would "grab everything they could" rather than exempt small businesses from having to collect.

Members of both sides. His questions about South Dakota focused on the small businesses to whom the state is honoring Congress's protection of the way they are.

Asked about the case. After reading both sides, he concluded both positions were "right." He looked to the attorneys for help sort out issues including how much money is on the table, whether it is easy and inexpensive to collect sales tax, and whether tax collection should be retroactive.

Number of questions expressing the view that Congress should overturn *Quill*, if it is clear that Congress can craft a more equitable solution than the court can.

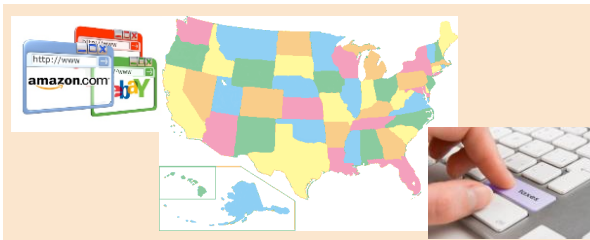
If South Dakota wins...

- Other states may enact economic presence-type statutes. Marketplace provider legislation likely to spike.
- States could gain sales tax revenues.
- Consumers could pay more for online purchases.
- Congress could take action, either reversing USSC decision or granting states more authority to collect and imposing restrictions.
- While SD's "economic presence" threshold will be sufficient, there are more issues to be resolved.
 - How much presence constitutes a substantial nexus?
 - What about states that have not adopted a South Dakota economic nexus type statute?
 - What about potential retroactive application?



If Wayfair wins...

- Would leave entire issue unresolved.
- Status quo with regard to consumer use tax obligations.
- Another state would likely step forward to challenge Quill.
- Erosion of sales tax as viable revenue source, esp. for states heavily reliant on it.



Remote Seller Legislation Trends in Other States

I Know What You Bought Last Summer

- Notice & Reporting Approach – Some states require retailers to notify customers about use tax obligation or require companies to share information with states about customer purchases.

Example

SUBTOTAL (3 ITEMS)	\$69.95
SHIPPING	FREE
If you didn't pay California tax here then you likely owe use tax	
	\$0
GRAND TOTAL	\$69.95



Cookie Nexus

- MA & OH count the internet cookies retailers place on customers' computers as a physical presence in the state.



Marketplace Providers



- A "marketplace provider" is a website where third party sellers list and sell their products, like Amazon, eBay, or Etsy.
- Makes the platform available, incl. listing or advertising sales
- Communicates offer and acceptance between buyer and seller.
- Collects and transmits payment.
- May ship goods to consumer.



Marketplace Providers



- This type of legislation requires marketplace provider to collect and remit sales tax on behalf of third party seller.
- Typically tracks "economic nexus" language by requiring threshold # of transactions or monetary minimum sourced to that state.
- The future of marketplace provider laws hinge on *Wayfair* case.



Questions?

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