

Wayfair for Montana Businesses and Policymakers

Montana Legislative Finance Committee
Financial Modernization and Risk Analysis Study Committee
September 14, 2020

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Outline

Overview- Why are we discussing a sales tax case

Discuss:

- U.S. Supreme Court cases- *Quill* and *Wayfair*
- Impact on Montana
- Current Environment and Impact on Business
- What we can and cannot do

Questions

Dakota Developments

In 1992, U.S. Supreme Court reaffirmed a physical presence requirement for asserting jurisdiction over remote sellers in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

- Relied on dormant commerce clause to create a bright line rule
- Determined a bright line rule was required to avoid undue burden on interstate commerce
- Eliminated physical presence requirement for due process

In 2016, South Dakota passed, SB 106, a remote seller sales tax act imposing an economic nexus test

- Was for the express purpose of creating an opportunity to revisit *Quill*
- Supported the act by declaring a revenue emergency based on the erosion of sales tax collections from remote sales.

The act was immediately challenged by Wayfair, Inc., Overstock.com, Inc. and Newegg, Inc.

In 2018, U.S. Supreme Court overruled *Quill's* physical presence requirement and determined that SB 106 satisfied the substantial nexus requirement

Wayfair- Background

Under Sales and Use Tax regimes, taxes are imposed on the buyers:

- Seller collects and remits a **sales** tax to the State if subject to state jurisdiction
- Buyer remits a **use** tax to the State if seller is not subject to state jurisdiction
- Use taxes are notoriously underreported (South Dakota estimated lost revenue between \$48 and \$58 million)

Respondents all sold and shipped goods into South Dakota, so taxability of the transactions was not at issue

- Sales of goods are a local transaction taxable by the State

Issue was whether South Dakota could require remote sellers to collect sales tax

- Under *Quill*, sellers with no property or employees in a state were not required to collect

Wayfair Decision

The Court overruled the physical presence requirements of *Quill* and a prior case, *National Bellas Hess*

- Noted the competitive disadvantage *Quill* imposed on local sellers
- Goal of decision was to resort some type of even playing field between local and remote sellers
- In today's economy, physical presence is artificial distinction

Significant decision because it is rare for U.S. Supreme Court to overrule prior, long-standing precedent.

- Court explained that *stare decisis* cannot justify continuing a judicial prohibition on states' sovereign right to collect taxes on local transactions.

Court relied on “far-reaching systemic and structural changes in the economy” in the Cyber Age as part of the basis for overruling *Quill*.

Remanded the case to South Dakota to determine whether the remote seller act violated any other Commerce Clause requirements.

- Case was settled on remand, and remote sellers agreed to collect and remit tax

Constitutional Restraints Today

Wayfair Court left in place other long-standing precedents, including four part *Complete Auto* test:

- Substantial nexus with the taxing state
- Fair apportionment
- Non-discrimination
- Related to services provided

Not all activity in a state will create tax nexus

- Must avail itself of the substantial privilege of carrying on business in the jurisdiction
- SD law imposed a dollar and transaction threshold

Non-discrimination- SD law took steps to minimize administrative and compliance costs

- Streamlined Sales and Use Tax Agreement
- State provided compliance software

No retroactivity- The collection requirement did not apply prior to the settlement

Congress could change the rules

Post *Wayfair* Impacts

41 States have enacted remote seller collection statutes

E-Commerce has continued to increase dramatically

- During Q2 of 2020;
 - Overall retail sales were down 3.6%
 - Online retail sales were up 31.8% over Q1 and 44.5% over 2019
 - Now 16.1% of total sales (were 10.8% in 2019)

State Revenue-

- Average increase of remote sales tax collections- 30%
- ND has seen a 500% increase in one year

State enforcement is increasing

Why Does this Matter in Montana

Montana business selling out of state may be subject to sales tax collection obligations in other states

Provides a road map if Montana decides to impose a sales tax in the future

Will inform decisions regarding nexus/jurisdiction in other tax areas, including income and business activity taxes

Compliance Suggestions for Businesses

Determine the sales tax collection thresholds and requirements for the States into which your business is doing business

Determine whether your goods or services are taxable

- most sales of taxable goods to exempt entities are still counting toward the thresholds

Consult with accountant or software vendor to set up a compliance program

Determine whether your business may be subject to other taxes in those states

- Under market based sourcing, multi-state income tax apportionment may source sales to customer location

Current Environment

Most states had previously taken or are currently taking steps to enhance remote seller provisions (Only four remaining, and are expected to enact during next session)

In some states, has required a simplification process to account of variety of local jurisdictions

Most impose a sales or transaction threshold:

- CA- \$500,000
- ID- \$100,000
- ND- \$100,000
- SD- \$100,000 or 200 transactions
- WA- \$100,000
- WY- \$100,000 or 200 transactions

What can we do about *Wayfair*

Support efforts in Congress to limit States' ability to tax remote sellers-

- Online Sales Simplicity and Small Business Relief Act of 2019
- Bills Introduced by Representatives and Senators from New Hampshire, Oregon and Wisconsin
 - Co-sponsors from California, North Carolina, Wisconsin, Arizona, Kansas, South Carolina, Tennessee
- Subcommittee Hearing on the topic in March, but no Bills have been assigned to committee or received any hearings
- Drafts would limit retroactivity and create exceptions for businesses with less than \$10 million in sales.

Take as an opportunity to determine whether remote seller collections creates an opportunity to reexamine Montana's overall tax structure

What we **cannot** do about *Wayfair*

Ignore it

Pass a tax just on remote sales or out of state businesses

Protect Montana businesses from other States' tax laws

- New Hampshire is trying ([Senate Bill 242](#))
- Almost uncertainly unenforceable and unconstitutional

Protect Montana main-street business from competition from remote sellers

Other issues to consider

Montana businesses are being impacted by competition from remote sellers

Remote Sellers (and their customers) are escaping the taxes being paid by local businesses and their customers

Other states are increasing the burden on Montana businesses selling into their markets

- They are aggressively pursuing tax from remote sellers in an effort to preserve state and local revenue source and maintain fairness for local businesses

Montana is trending the opposite, as business property taxes are increasing at the same time competition from remote sellers is eroding revenues

Questions?

Presenter-

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Mike's practice focuses on state and local taxation advice and litigation in Montana and North Dakota. Mike is a frequent consultant to the Montana Taxpayers Association and other statewide groups regarding state tax matters. Mike routinely assists clients in planning, and represents clients before administrative agencies as well as Montana, North Dakota and federal courts. Mike and Wiley Barker recently achieved positive decisions for taxpayers from the Montana and North Dakota Supreme Courts. Mike also practices in the areas of utility regulation, employment advice and litigation, and other administrative and regulatory matters.