

# BDO TAX TALK

Summer Webinar Series

## IMPACT OF SOUTH DAKOTA V. WAYFAIR ON SALES & USE TAX COMPLIANCE

June 2018



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# With You Today



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# Agenda

- ▶ Sales Tax 101
- ▶ Nexus Standards and New Use Tax Reporting Requirements:
  - Economic Nexus
  - Click Through Nexus
  - Affiliate Nexus
  - Use Tax Notice and Reporting Requirements
- ▶ SD v. Wayfair
- ▶ Industry Perspective
- ▶ Managing Sales Tax Determination

# Sales Tax 101

# Overview

## Sales Tax

- ▶ Generally defined as a transaction tax that is imposed on the retail sale of tangible personal property (“TPP”) and specifically enumerated services.
- ▶ Why is it important?
  - P.L. No 86-272
  - Constantly Changing
  - Usually “back-burnered” - Not a Priority
- ▶ Sales and use taxes are destination taxes in that the tax is due when title, possession, and/or control of TPP is/are transferred from the seller to the buyer.
- ▶ Sales tax applies to INTRASTATE transactions.

# Use Tax

- ▶ Generally defined as a transaction tax that is imposed on the privilege of ownership, consumption, possession, storage and/or use of tangible personal property (TPP) and specifically enumerated services (when sales tax is not paid at point of sale).
- ▶ Company must self-assess use taxes when it does not pay sales tax on a purchase.
- ▶ Use tax applies to INTERSTATE transactions.

# Even Playing Field Concept

- ▶ Sales and use taxes are complementary.
- ▶ The goal of the complementary taxes is to ensure that out-of-state vendors do not have a competitive advantage over in-state vendors.
- ▶ We'll talk about it more later, but an even playing field is what states (some) and taxpayers are trying to reach that has culminated in *SD v. Wayfair*.

# Sales/Use Tax Standards, Trends and New Use Tax Reporting Requirements

# Sales/Use Tax Nexus Standards

## Sales and Use Tax Standards:

- ▶ Unlike income tax, there is no federal public law similar to P.L. 86-272 to provide guidance or protection for activities considered in determining the existence of sales and use tax nexus.
- ▶ Sales and use tax nexus standards are governed primarily by U.S. Supreme Court cases, and interpretations of the Commerce and Due Process Clauses.

# Sales/Use Tax Nexus Standards

When are activities substantial enough to result in a finding of sales tax nexus?

▶ Old Standard:

- Virtually any physical presence:
  - People: including sales people, service providers, independent contractors
  - Offices
  - Inventory of Consignment

▶ New Standard:

- Economic Nexus
- Affiliate/Agency Nexus
- Click Through Nexus
- Use Tax Notice

# Sales/Use Tax Nexus Trends

## Economic Nexus

### Setting the Stage

- ▶ *Direct Marketing Ass’n v. Brohl*, 135 S. Ct. 1124, 1135 (2015) (“Brohl II”)
  - In his concurring opinion, Associate Justice Kennedy indicated that he believes it is time to reconsider *Quill*’s physical presence standard.
    - “There is a powerful case to be made that a retailer doing extensive business within a State has a sufficiently ‘substantial nexus’ to justify imposing some minor tax-collection duty, even if that business is done through the mail or the Internet. . . This argument has grown stronger and the cause more urgent with time.”
- ▶ *Direct Marketing Ass’n v. Brohl*, No. 12-1175 (10th Cir., Feb. 22, 2016) (“Brohl III”)
  - Circuit Judge Gorsuch may respect the continued validity of *Quill* under the doctrine of stare decisis.
  - However, in *Brohl III* Judge Gorsuch may have felt constrained, as a lower court judge, to overrule a U.S. Supreme Court decision and arguably might have *Quill* “wash away with the tides of time.” *Brohl III*, Slip Op., at 9 (Gorsuch, C.J., concurring).
  - Petition for writ of certiorari denied on December 12, 2016.

# Sales/Use Tax Nexus Trends

## Economic Nexus (con't)

- ▶ Numerous states have enacted economic nexus provisions regarding sales and use tax:
  - Alabama (effective Jan. 1, 2016) (gross sales of \$250,000)
  - Connecticut (On March 28, 2017 DOR announced increased audit efforts aimed at remote sellers with a “substantial economic presence”)
  - Georgia (effective Jan. 1, 2019) (gross sales of \$250,000)
  - Indiana (effective July 1, 2017) (gross sales of \$100,000)
  - Kentucky (effective April 14, 2018) (gross sales of \$100,000)
  - Maine (effective October 1, 2017) (gross sales of \$100,000)
  - Massachusetts (effective July 1, 2017) (gross sales of \$500,000)
  - Mississippi (effective December 1, 2017) (gross sales of \$250,000)
  - North Dakota (eff. contingent on SCOTUS guidance) (gross sales of \$100,000)
  - Ohio (effective January 1, 2018) (gross sales of \$500,000)
  - South Dakota (effective May 1, 2016) (gross sales of \$100,000)
  - Tennessee (effective January 1, 2017) (gross sales of \$500,000)
  - Vermont (eff. contingent on SCOTUS guidance) (gross sales of \$100,000)
  - Wyoming (effective July 1, 2017) (gross sales of \$100,000)

# Sales/Use Tax Nexus Trends

## Economic Nexus (con't)

Proposed:

- ▶ Hawaii (S.B. 620) - introduced
- ▶ Kansas (H.B. 2400) - \$100,000 or 200 annual sales threshold - introduced
- ▶ Texas (S.B. 1713) - \$1 million sales or 2,000 annual sales - introduced



# Sales/Use Tax Nexus Trends

## Economic Nexus (con't)

### Massachusetts

Directive 17-1 (Revoked on June 28, 2017 by Directive 17-2)

- ▶ A remote Internet vendor is required to collect and remit sales tax if:
  - Massachusetts sales for the preceding 12 month period exceed \$500,000; and
  - It made sales for delivery into Massachusetts in 100 or more transactions.
- ▶ The Directive was challenged in state, and it was subsequently revoked by Directive 17-2.
- ▶ However, Massachusetts issued proposed regulations that not only include Directive 17-1's economic nexus provisions, but also add a provision that "cookies" or software downloaded onto a Massachusetts customer's computer, tablet, or device constitutes physical presence in Massachusetts for an internet seller.
  - Proposed 830 CMR 64H.1.7: Vendor Making Internet Sales

# Sales/Use Tax Nexus Trends

## Economic Nexus (con't)

### Ohio

H.B. 49 (effective January 1, 2018)

- ▶ A remote seller is deemed to have substantial nexus with Ohio if it uses in-state software to sell or lease TPP or services and has gross receipts of more than \$500,000 in the current or preceding calendar year from the sales of TPP to Ohio customers.
- ▶ It also provides that a remote seller has substantial nexus if it enters into an agreement to provide a content distribution network in Ohio to accelerate or enhance the delivery of the seller's website to consumers, provided the seller meets the \$500,000 gross receipts threshold.
- ▶ There have been concerns that Ohio could impose "cookie" nexus, even though the Ohio Department of Taxation has denied it.

Notice ST 2017-02: Software Nexus and Network Nexus (October, 2017)

- ▶ "In-State Software Nexus" - An application downloaded onto a customer's computer or phone is software in Ohio.
- ▶ "Network Nexus" - Contracting with a 3P that has a physical presence in Ohio is sufficient to create nexus, if the 3P is providing network access to the company's websites.

# Sales/Use Tax Nexus Trends

## Economic Nexus (con't)

### South Dakota

S.B. 106 (S.D. 2016) (effective May 1, 2016)

- ▶ A remote seller is required to collect and remit sales tax if:
  - The seller's South Dakota gross revenue from the sale of TPP, any product transferred electronically, or services delivered into South Dakota exceeds \$100,000; or
  - The seller sold TPP, any product transferred electronically, or services for delivery into South Dakota in 200 or more separate transactions.
- ▶ A state circuit court held in favor of the remote seller taxpayers on the state's complaint for declaratory judgment. *State of South Dakota v. Wayfair, Inc., et al.*, No. 32CIV16-000092 (Cir. Ct., Mar. 6, 2017)
  - Circuit court also granted taxpayers' motion for summary judgment and declared the sales/use tax economic nexus statute unconstitutional.
  - Despite "changing times and events clearly suggest a different outcome," the court cannot overturn a decision of the U.S. Supreme Court.
- ▶ On September 13, 2017, the Supreme Court of South Dakota ruled in favor of remote seller, affirming the trial court's decision granting the remote seller's motion for summary judgment. *State of South Dakota v. Wayfair, Inc., et al.*, 2017 S.D. 56 (2017).
- ▶ US Supreme Court granted cert and has heard oral arguments. Decision is expected in June of 2018.

# Sales/Use Tax Nexus Trends

## Affiliate Nexus

### Minnesota

H.F. 1 (legislation passed May 30, 2017)

- ▶ Expands the definition of a “retailer maintaining a place of business in this state” to include having a representative such as a “marketplace provider” operating in Minnesota.
  - Subject to an annual \$10,000 threshold.
- ▶ Expands the definition of a retailer’s “affiliate nexus.”
- ▶ However, the new legislation does not become effective until the earlier of:  
(1) July 1, 2019, or (2) the date that *Quill* is overturned by the U.S. Supreme Court, or (3) congressional authorization to impose collection requirements on remote sellers.

# Sales/Use Tax Nexus Trends

## Affiliate Nexus

### Nevada

Affiliate nexus regulations issued (R137-15)

- ▶ Nevada affiliate nexus statute establishes a presumption of nexus and requires a remote retailer collect sales/use tax if it is a member of a “controlled group” of business entities that has a component member with Nevada physical presence, and the component member engages in activities in Nevada that relate to the remote retailer’s ability to make sales in Nevada.
- ▶ Presumption of nexus may be rebutted by showing the component member did not engage in activity that was significantly associated with the remote retailer’s ability to establish and maintain a market in Nevada (the “significantly associated” test of Tyler Pipe).
- ▶ The new regulations provide examples of activities that are “significantly associated,” including:
  - Installation, assembly, repair services
  - Acceptance of returns of merchandise
  - Maintenance of customer relationships such as customer meetings, warranty repairs, training, etc.

# Sales/Use Tax Nexus Trends

## Affiliate Nexus (con't)

### Oklahoma

#### H.B. 2531

- ▶ Amended definition of “maintaining a place of business in this state” to create a rebuttable presumption that a vendor has nexus with Oklahoma for sales and use tax purposes if:
  - Directly, or through a subsidiary, maintains a place of business in Oklahoma;
  - Has an agent operating in Oklahoma; or
  - An affiliate has nexus with Oklahoma and (a) sells a similar line of products as the vendor under the same or similar business name, (b) uses trademarks, service marks, or trade names that are the same or substantially similar to the vendor’s, (c) delivers, installs, assembles, or performs maintenance for the vendor, (d) facilitates delivery of the vendor’s products, or (e) conducts other activities that are significantly associated with the vendor’s ability to establish and maintain a market in Oklahoma.
- ▶ Effective November 1, 2016
- ▶ Oklahoma Tax Commission promulgated amended administrative rules, effective September 11, 2017, which define “maintaining a place of business.”

# Sales/Use Tax Nexus Trends

## Affiliate Nexus (con't)

### Virginia

H.B. 2058

- ▶ Amends the definition of “dealer” to include:
  - A business or entity that is owned or controlled by the same interests that own or control a business located in Virginia; or
  - A business or entity that has a franchisee or licensee operating under the same trade name in Virginia.
- ▶ A dealer is presumed to have nexus with Virginia if any commonly controlled person maintains a distribution center, warehouse, fulfillment center, office or similar location in Virginia that facilitates delivery. A “commonly controlled person” means a person that is a member of the dealer’s “controlled group” under IRC § 1563(a). The presumption is rebutted by showing the commonly controlled person’s activities are not significantly associated with establishing or maintaining a market in Virginia for the dealer.

# Sales/Use Tax Nexus Trends

## “Amazon” - Click-Through Nexus

- ▶ Originated in New York
- ▶ Internet retailers are considered vendors if the seller enters into agreements with New York residents for a commission or other consideration under which they directly or indirectly refer potential customers (“click thru nexus”).
- ▶ Amazon, Overstock and other online sellers severed relationships with affiliate online sellers located in states that enacted expanded nexus provisions.
- ▶ Amazon has negotiated deals with California and other states to defer effective date of legislation to allow for federal legislation.
  - NOTE: Amazon started collecting sales tax on CA shoppers beginning on 9/15/12 (now collecting in AZ, CA, CT, FL, GA, IN, KS, KY, MA, NV, NJ, NY, NC, ND, PA, TN, TX, VA, WA, WV, WI)

# Sales/Use Tax Nexus Trends

## “Amazon” - Click-Through Nexus

- ▶ New York - enacted in 2008 referral for commission (click-thru nexus) N.Y. Tax Law § 1101(b)(8)(vi)
  - Seller enters into agreements with NY residents for website referrals or links.
  - Seller pays commissions or fees for such referrals based on sales.
  - Seller generates total gross receipts from sales (made as a result of all such arrangements) of at least \$10,000 during the preceding 4 quarterly periods.
- ▶ Presumption - A seller that makes taxable sales of TPP or services in a state has nexus when a state resident’s website clicks through potential customers to the seller.
- ▶ Rationale - Link on the website in New York creates a physical presence for the seller when the owner of the website is a resident of New York and acts as a sales agent for the seller.
- ▶ Amazon and Overstock.com challenged the constitutionality of NY’s vendor nexus law.
  - NY Court of Appeals ruled that state’s click-through nexus statute did not violate the Constitution; U.S. Supreme Court declined to review NY Court of Appeals decision.

# Sales Tax Nexus

## Current State Click-Through Nexus

State	Effective Date	Annual Threshold (before required to file)	Statute
Arkansas	October 24, 2011	\$10,000	Ark. Code Ann. Sec. 26-52-117
California	September 15, 2012	\$10,000 and seller has more than \$1,000,000 in CA sales	CA Sec. 6203 of Rev & Tax Code
Colorado	March 1, 2010	None	Colo. Rev. Stat. § 39-26-102
Connecticut	July 1, 2011	\$2,000	Conn. Gen. Stat. Sec. 12-407(a)(12)(L)
Georgia	December 30, 2012	\$50,000	GA. CODE ANN. § 48,8,2(8)(K)
Illinois	July 1, 2011	\$10,000	35 ILCS 105/2 and 110/2
Kansas	July 1, 2013	\$10,000	Kan. Stat. Ann. § 79-3702(h)(2)(C)
Maine	October 9, 2013	\$10,000	Me. Rev. Stat. Ann. § 1754-B(1-A)(C)
Michigan	October 1, 2015	\$10,000 to in state purchasers	Mich. S.B. 658, effective Oct. 1, 2015
Minnesota	July 1, 2013	\$10,000	Minn. Stat. § 297A.66(4a)
Missouri	August 28, 2013	\$10,000	Mo. Rev. Stat. § 144.605
New Jersey	July 1, 2014	\$10,000	N.J. Stat. §54:32B-2(i)
Nevada	October 1, 2015	\$10,000	2015 Nev. A.B. 380
New York	June 1, 2008	\$10,000	N.Y. Tax Law Sec. 1101(b)(8)(vi)
North Carolina	August 7, 2009	\$10,000	N.C. Gen. Stat. Sec. 105-164.8
Ohio	July 1, 2015	\$10,000	Sec. 5741.01(l)(2)(g)
Pennsylvania	September 1, 2012	None	Sales & Use Tax Bulletin 2011-01 (issued 12/1/2011)
Rhode Island	July 1, 2009	\$5,000	R.I. Gen. Laws Sec. 44-18-15
Tennessee	July 1, 2015	\$10,000	2015 Tenn. H.B. 644
Vermont	When adopted in 15 other states	\$50,000	Vt. Stat. Ann. tit. 32, Sec. 9701(9)(l)(H.B. 436)
Washington	September 1, 2015	\$10,000	Sec. 202(1)

# Sales/Use Tax Nexus Trends

## Use Tax Notice and Reporting

### Alabama

S.B. 86, effective July 1, 2017

- ▶ Authorizes the Alabama Department of Revenue “within constitutional limitations” to require use tax notice and customer reporting for remote sellers that do not collect Alabama sales or use taxes on sales to Alabama customers.

# Sales/Use Tax Nexus Trends

## Use Tax Notice and Reporting (con't)

### *Georgia (elective to collect or report)*

H.B. 61 (Eff. January 1, 2019)

- ▶ A “seller” has sales and use tax nexus in Georgia if, during the current or previous calendar year:
  1. Georgia gross revenue exceeds \$250,000 from sales of TPP delivered electronically or physically in GA; or
  2. 200 or more sales of TPP delivered electronically or physically in GA.
- ▶ Allows the Department of Revenue to seek a declaratory judgment that the economic nexus law is applicable and valid against any person it believes meets the definition of a dealer.
- ▶ Sellers are required to register to collect and remit sales tax OR comply with reporting requirements.

# Sales/Use Tax Nexus Trends

## Use Tax Notice and Reporting (con't)

### *Oklahoma (elective to collect or report)*

H.B. 61 (Eff. April 10, 2018)

- ▶ Election must be made by July 1, 2018 (and by June 1 of each CY starting in 2019) .
- ▶ A “marketplace facilitator,” “remote seller,” or “referrer” in the previous 12 calendar months must either:
  1. Obtain sales tax permit and collect and remit sales and use tax due on TPP; or
  2. Comply with notice and reporting requirements.
- ▶ All three terms use a threshold of \$10,000 of sales of TPP delivered into OK within a 12-month period.

# Sales/Use Tax Nexus Trends

## Use Tax Notice and Reporting (con't)

### *Pennsylvania (elective to collect or report)*

2017 Pa. H.B. 542 (Eff. Oct. 30, 2017)

- ▶ Election must be made by March 1, 2018 (and by June 1 of each CY starting in 2019).
- ▶ A “marketplace facilitator,” “remote seller,” or “referrer” in the previous 12 calendar months must either:
  1. Obtain sales tax permit and collect and remit sales and use tax due on TPP by April 1, 2018; or
  2. Comply with notice and reporting requirements.
- ▶ All three terms use a threshold of \$10,000 of sales of TPP delivered into PA within a 12-month period.

# Sales/Use Tax Nexus Trends

## Use Tax Notice and Reporting (con't)

### Rhode Island

H.B. 5175 (effective August 17, 2017)

- ▶ Rhode Island enacted economic nexus standards for “non-collecting retailers,” which are “remote sellers,” marketplace providers,” and “referrers.”
- ▶ A remote seller will have the option of use tax notice and reporting to customers, instead of collecting and remitting sales tax.
- ▶ If a “remote seller” adopts this option, it will be required to:
  - Post a conspicuous notice on its website that that Rhode Island use tax is owed on purchases;
  - Notify its Rhode Island customer at the time of purchase that use tax is due;
  - Notify the customer again by email within 48 hours of the purchase;
  - Send a notice by January 31 each year to all Rhode Island purchasers having total cumulative purchases of \$100 or more during a calendar year of their obligation to remit use tax; and
  - File an attestation with the Division of Taxation by February 15 each year that it has complied.

# Sales/Use Tax Nexus Trends

## Use Tax Notice and Reporting (con't)

### Vermont

#### H.B. 873

- ▶ Noncollecting vendor is a vendor that makes taxable sales to Vermont purchasers, but does not collect sales tax, and must:
  - Notify a Vermont purchaser that sales or use tax is due, and that Vermont requires the tax to be paid on his or her tax return.
    - Failure to provide notice may result in a \$5 penalty for each instance of noncompliance.
  - Send notification to a Vermont purchaser who had made \$500 or more of purchases in the preceding calendar year that shows the total amount paid by the purchaser.
    - Failure to provide notice may result in a \$10 penalty for each instance of noncompliance.
- ▶ Effective the earlier of July 1, 2017, or beginning on the first day of the first quarter after the sales and use tax reporting requirements challenged in *Direct Marketing Assoc. v. Brohl*, 814 F. 3d 1129 (10th Cir. 2016) are implemented by Colorado.



# Sales/Use Tax Nexus Trends

## Use Tax Notice and Reporting (con't)

### Washington (elective to collect or report)

H.B. 2163 (Eff. July 7, 2017)

- ▶ Election must be made by January 1, 2018.
- ▶ A “marketplace facilitator,” “remote seller,” or “referrer” in the previous 12 calendar months must either:
  1. Collect and remit WA sales and use tax due on TPP; or
  2. Comply with notice and reporting requirements
- ▶ “Marketplace facilitator” and “remote seller” use a threshold of \$10,000 of sales of TPP delivered into WA within the current or previous calendar year.
- ▶ However, “referrer” uses the \$267,000 threshold of retail sales sourced to WA.

# Status of Federal Sales/Use Tax Nexus Proposals

## ▶ Marketplace Fairness Act (“MFA”)

- Proposed legislation pending in the U.S. Congress that would enable state governments to collect sales/use tax from remote retailers with no physical presence in their state.
- Destination-based sourcing
- Reintroduced in the U.S. Senate on April 27, 2017 (S. 976)
  - Previously passed on the Senate in 2013 (S. 743), but failed in the House.
  - Was re-introduced in the Senate in 2014 and 2015, but was not passed by the Senate.
- Small Seller Exemption: Exemption threshold in order to avoid the burden of collecting out-of-state sales/use tax is set at only \$1 million of gross sales.
- Remains pending in the Senate Committee on Finance.

# Status of Federal Sales/Use Tax Nexus Proposals

## ▶ Remote Transactions Parity Act of 2015 (“RTPA”)

- The RTPA addresses the Internet sales tax issue using the structure of the MFA.
- The RTPA retains many features of the MFA, but adds protections for remote sellers and certified software providers.
- H.R. 2193 Re-introduced in U.S. House of Representatives, Ways and Means Committee, on April 27, 2017.
  - Originally introduced in the House in 2015 and referred to the Subcommittee on Regulatory Reform, Commercial And Antitrust Law; did not pass the House.
- Would adopt a 3 year phase-in of small seller exemption noted in the MFA.
- Destination-based sourcing.

# Status of Federal Sales/Use Tax Nexus Proposals

- ▶ Online Sales Simplification Act of 2016
  - Circulated, not introduced.
  - Origin-based sourcing.
- ▶ No Regulation Without Representation Act
  - H.R. 5893 was introduced on July 14, 2016 and would codify the physical presence standard for sales tax collection and reporting purposes established in *Quill*.
  - Creates a de minimis threshold for physical presence, provides protection for any person other than a purchaser or seller having a physical presence in the state, and provides specific exclusions.

# Summary of Sales/Use Tax Nexus Rules

State	Click-Through Nexus	Affiliate Nexus	Reporting Requirements	Economic Nexus	Marketplace Nexus
Alabama		8/24/2012	7/1/2017	1/1/2016	
Arizona					Ruling Issued 9/20/2016
Arkansas	10/27/2011	10/27/2011			
California	9/15/2012	9/15/2012			
Colorado	7/1/2014	7/1/2014	7/1/2017		
Connecticut	5/4/2011				
Georgia	7/18/2012	10/1/2012	1/1/2019	1/1/2019	
Idaho	7/1/2018				
Illinois	1/1/2015	7/1/2011			
Indiana				7/1/2017 – Challenged	
Iowa		6/11/2013			
Kansas	10/1/2013	7/1/2013			
Kentucky			7/1/2013	7/1/2018	
Louisiana	4/1/2016	4/1/2016	7/1/2017		
Maine	10/9/2013	10/9/2013		10/1/2017	
Massachusetts				10/1/2017 – Pending	
Michigan	10/1/2015	10/1/2015			
Minnesota	7/1/2013	Delayed			Delayed
Mississippi				12/1/2017	
Missouri	8/28/2013	8/28/2013			
Nevada	10/1/2015	7/1/2015			
New Jersey	7/1/2014				
New York	5/8/2008	6/1/2009			
North Carolina	8/7/2009				
North Dakota				Delayed	

# Summary of Sales/Use Tax Nexus Rules

State	Click-Through Nexus	Affiliate Nexus	Reporting Requirements	Economic Nexus	Marketplace Nexus
Ohio	7/1/2015	7/1/2015		1/1/2018 – Challenged	
Oklahoma		6/9/2010 and 11/1/2016	6/9/2010 and 11/1/2016 and 4/10/2018		4/10/2018
Pennsylvania	12/1/2011	12/1/2011	2/1/2018 and 2/1/2019	2/1/2018 and 2/1/2019	2/1/2018 and 2/1/2019
Rhode Island	7/1/2009 and 8/17/2017	8/17/2017	8/17/2017	8/17/2017	8/17/2017
South Dakota		7/1/2011	7/1/2011	Appealed	
Tennessee	7/1/2015	1/1/2014	3/26/2012	Delayed	
Texas		1/1/2012			
Utah		7/1/2012			
Vermont	12/1/2015		5/24/2011 and 7/1/2017	Effective date pending SD legislation	
Virginia		9/1/2013			
Washington	9/1/2015		1/1/2018	B&O Tax only 9/1/2015 and expanded 7/1/2017	1/1/2018
West Virginia		1/1/2014			
Wyoming				Delayed	

# The Road to Wayfair

# Sales/Use Tax Nexus Trends

## Economic Nexus

### South Dakota

S.B. 106 (S.D. 2016) (effective May 1, 2016)

- ▶ A remote seller is required to collect and remit sales tax if:
  - The seller's South Dakota gross revenue from the sale of TPP, any product transferred electronically, or services delivered into South Dakota exceeds \$100,000; or
  - The seller sold TPP, any product transferred electronically, or services for delivery into South Dakota in 200 or more separate transactions.
- ▶ A state circuit court held in favor of the remote seller taxpayers on the state's complaint for declaratory judgment. *State of South Dakota v. Wayfair, Inc., et al.*, No. 32CIV16-000092 (Cir. Ct., Mar. 6, 2017).
  - Circuit court also granted taxpayers' motion for summary judgment and declared the sales/use tax economic nexus statute unconstitutional.
  - Despite "changing times and events clearly suggest a different outcome," the court cannot overturn a decision of the U.S. Supreme Court.
- ▶ On September 13, 2017, the Supreme Court of South Dakota ruled in favor of remote seller, affirming the trial court's decision granting the remote seller's motion for summary judgment. *State of South Dakota v. Wayfair, Inc., et al.*, 2017 S.D. 56 (2017).
- ▶ US Supreme Court granted cert and has heard oral arguments. Decision is expected in June of 2018.

# The Road to Wayfair

## Historical Perspective

### *Quill Corp. v. North Dakota, US Supreme Court, 1992*

- ▶ Served as the gold standard for states' ability to impose sales/use tax collection responsibility on an out-of-state seller.
- ▶ Requires physical presence to establish collection responsibility (i.e., nexus).
- ▶ State governments are of the opinion that due to shifting of the economy from predominantly brick-and-mortar to an e-commerce economy, the physical presence standard should no longer be valid.

# The Road to Wayfair

## States' responses to circumvent the physical presence

- ▶ The 3 types of Nexus that we just reviewed
- ▶ Use tax notice and reporting
  - An out-of-state retailer who is not required to register for sales/use tax purposes in a state is required to provide the following:
    - Provide use tax reporting notices to customers on **each sales transaction**.
    - Provide an **annual report to customers** the purchases they made during the preceding year.
    - Provide an **annual report to Department of Revenue** sales made into the state during the preceding year.
  - Approximately 10 states have enacted such laws.
  - This law was ruled valid by courts.

# The Road to Wayfair

## States' responses to circumvent the physical presence

### ► Use tax notice and reporting

- “Pick your poison” extortion scheme by taxing authorities to force out-of-state retailers to “voluntarily” register to collect sales/use tax.
- Noncompliance penalty provisions in Pennsylvania and Washington are especially punitive.
  - PA - Annual penalty of lower of \$20,000 or 20% of total PA sales.
  - WA - (1) \$20,000 for failure to provide transaction notice to customers; (2) \$20,000 minimum, or \$25 per customer, for failure to provide sales report to the Department; AND (3) a tiered penalty structure for failure to provide annual report to customers as follows:

<u>Annual WA Gross Receipts</u>	<u>Penalty Amount</u>
Under \$50,000	\$5,000
Under \$150,000	\$10,000
Under \$300,000	\$50,000
\$300,000 and above	\$100,000 + \$20,000 per \$50,000 of additional gross receipts

# The Road to Wayfair

## States' responses to circumvent the physical presence

- ▶ Use tax notice and reporting
- ▶ Marketplace facilitator collection
  - Some states require a marketplace platform provider (e.g., Amazon) to collect sales/use tax on property sold through its platform.
  - Amazon is starting to collect/remit sales/use tax on 3rd party sales transacted through its platform for Pennsylvania and Washington.

# The Road to Wayfair

## *South Dakota v. Wayfair, Inc. et al.*, U.S. No. 17-494

- ▶ Oral argument held before the Supreme Court of the United States on April 17, 2018.
- ▶ South Dakota is one of a number of states that have recently enacted economic nexus for sales/use tax purposes.
- ▶ Conventional wisdom: Court would not take appeal of *Wayfair* if it didn't intend to overrule *Quill*.
- ▶ Focus and questioning of the Justices in oral argument possibly suggest otherwise

# The Road to Wayfair

## What Could Happen?

### ▶ If the Court overrules *Quill*:

- Will the Court remand to the South Dakota Supreme Court on the minimal constitutional sales threshold issue?
  - In conjunction, or separately, Court could remand on the compliance costs issue.
- Likewise, will the Court kick that issue to Congress?
- As a constitutional decision, it should apply retroactively. What will states do?
- Could the Court only “clarify” *Quill* as inapplicable to Internet sellers?

### ▶ If the Court upholds *Quill*:

- Will the Court (again) kick the issue to Congress?
- States should be expected to increase aggressiveness on affiliate and attributional nexus, marketplace vendor nexus, “cookie” nexus, etc.
- Will more states enact use tax notice and reporting statutes in light of Colorado’s victory in *Direct Marketing Ass’n v. Brohl*?

### ▶ Decision should be expected in 2019, and quite possibly as early as June.

# What if Quill is Overturned? An Industry Perspective

# An Industry Perspective

- ▶ Online Services
  - Cloud
  - Infrastructure as a Service (IaaS)
  - Platform as a Service (PaaS)
  - Software as a Service (SaaS)
  - Information Services
  - Data Processing Services
  - Digital Goods
- ▶ Remote Retailers
- ▶ Remote International Businesses

# Managing Sales Tax Determination and Reporting

# What Are My Options?

## Tax Determination

- ▶ Maintain Existing Process at Larger Capacity
- ▶ Acquire a Tax Rate File Subscription
- ▶ Acquire a Third-Party Tax Determination Software
  - What if I already have tax determination software?

## Tax Compliance Reporting

- ▶ Maintain Existing Process at Larger Capacity
- ▶ Acquire a Third-Party Tax Reporting Software
- ▶ Outsource Tax Reporting

# Advantages/Challenges of Options

## Maintain Existing Process

### Tax Determination

Advantages	Challenges
No cash outlay for rate subscription or tax software	Manual maintenance of tax rates
	Customization for special tax calculation rules
	Manual maintenance of taxability research

### Tax Compliance Reporting

Advantages	Challenges
No cash outlay for tax software or outsourcing	Increase in number of tax return filings
	Potential need to hire additional resources

# Advantages/Challenges of Options Acquire Tax Rate File Subscription

## Tax Determination

Advantages	Challenges
No cash outlay for tax determination software	Customization for special tax calculation rules
No manual maintenance of tax rates	Manual maintenance of taxability research

# Advantages/Challenges of Options Acquire Third-Party Tax Determination Software

## Tax Determination

Advantages	Challenges
No manual maintenance of tax rates	Investment in tax determination software
Taxability content provided *	Investment in set-up and testing
State and local tax authorities provided	Configuration maintenance
Source for tax compliance reporting	
Manage customer exemptions/exceptions	
Manage product/service exceptions	
Manage jurisdictional exceptions	
Source for audit support	
Resource re-deployment	

\* (Most but not all products and services)

# Advantages/Challenges of Options Acquire Third-Party Tax Reporting Software

## Tax Compliance Reporting

Advantages	Challenges
Can produce signature-ready tax returns	Investment in tax reporting software
Reduces tax return preparation effort	Web site filings are still necessary
EDI Filing Options	

# Advantages/Challenges of Options Outsource Tax Compliance Reporting

## Tax Compliance Reporting

Advantages	Challenges
No cash outlay for tax reporting software	Cost of outsourcing
Resource re-deployment	

# Cost Considerations

- ▶ Cost to Maintain Existing Process
  - Cost of internal resources
- ▶ Tax Rate File Subscription
  - \$3K - \$15k +
- ▶ Cost of Third-Party Tax Determination Software
  - Depends on your needs
  - \$5K - \$150K +
- ▶ Cost of Third-Party Tax Reporting Software
  - \$10k - \$35k
- ▶ Cost of Outsourcing
  - ~\$30 - \$50 + (Per Return)
  - Add-on costs depending on service provider

# Tax Vendors

## Tax Determination Software

- ▶ Vertex
- ▶ Thomson Reuters (Sabrix)
- ▶ Avalara
- ▶ SOVOS (Taxware)
- ▶ CCH

## Tax Rate Subscriptions

- ▶ Zip2Tax
- ▶ Thomson Reuters
- ▶ Vertex
- ▶ CCH

# Automation with Third-Party Software: Core Steps in an Automation Project

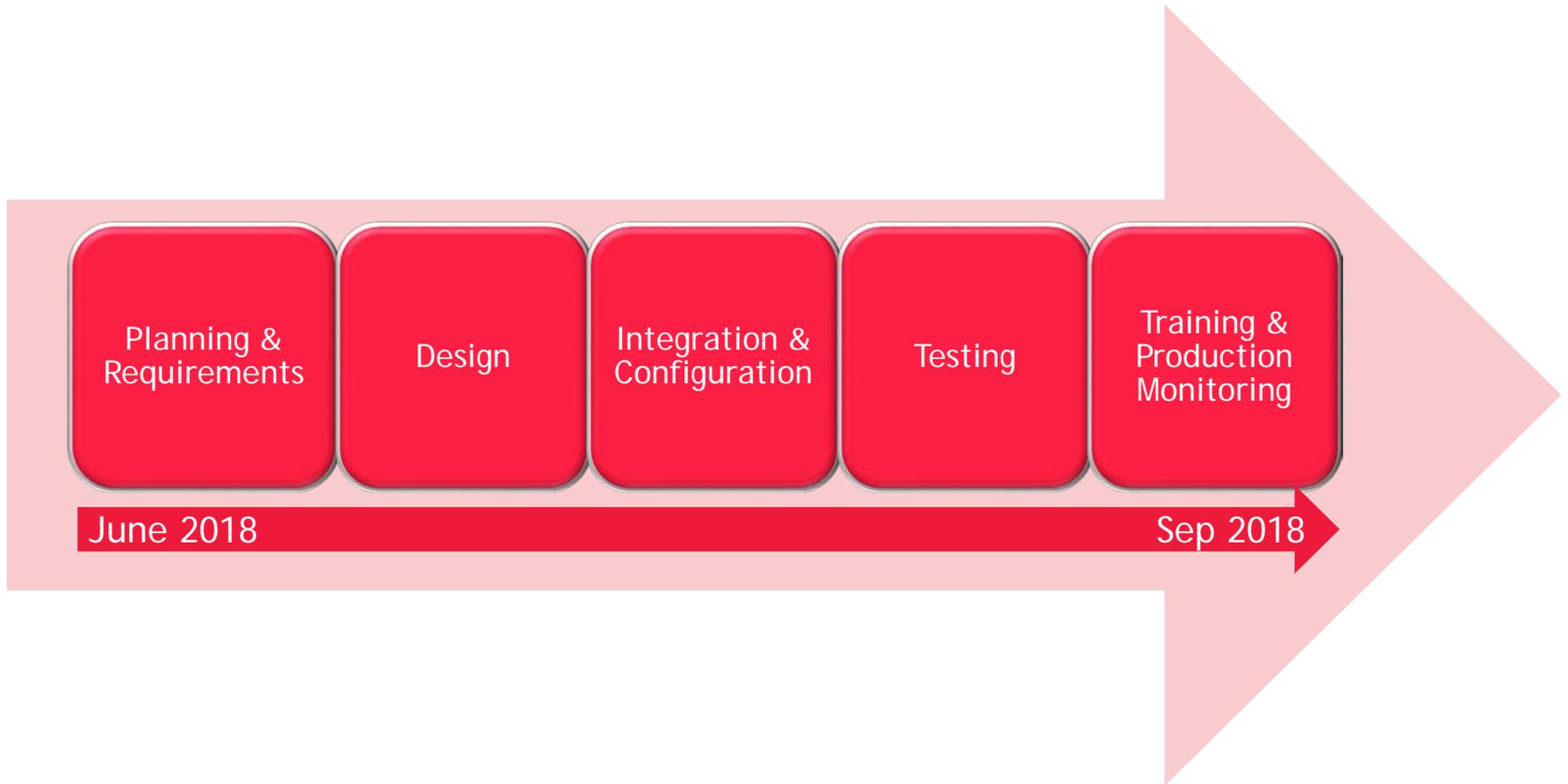
STEP	C	T	S
Determine service provider	√		
Conduct diagnostic review	√		√
Narrow list of tax software vendors	√		√
Schedule product demos	√	√	√
Award software vendor contract	√		
Prepare system environments (Dev, Test, Stage, Prod)	√		
Tax software installation		√	
Tax software connector set up		√	
Develop tax configuration blue-print	√		√
Configure tax system	√		√
Develop test scripts and conduct testing	√		√
Approve results	√		
Training	√		√
Production cut-over	√		√
Post Go-Live monitoring	√		√

(C) Company; (T) Tax Software Vendor; (S) Service Provider

# Automation with Third-Party Software: Investment Scope

- ▶ Software licensing
  - Initial license fee
  - Annual support renewal
- ▶ Software connector
  - Service fee for establishing communication with ERP
- ▶ Implementation
  - Service provider fees covering project lifecycle
- ▶ Internal Resources
  - Project assistance and upkeep after Go-Live

# Automation with Third-Party Software: Common Project Lifecycle



# Automation with Third-Party Software: Common Deliverables

- ▶ Project work plan
- ▶ Roles & responsibilities matrix
- ▶ Business requirements & Gap analysis
- ▶ Functional design document
- ▶ Tax configuration guide
- ▶ Test plan & results
- ▶ Training materials

# Automation with Third-Party Software: Typical Project Resources

## ▶ Company

- Tax representative(s)
- Accounts receivable & billing
- Procurement & accounts payable
- Information Technology (DBA, Network Engineer)

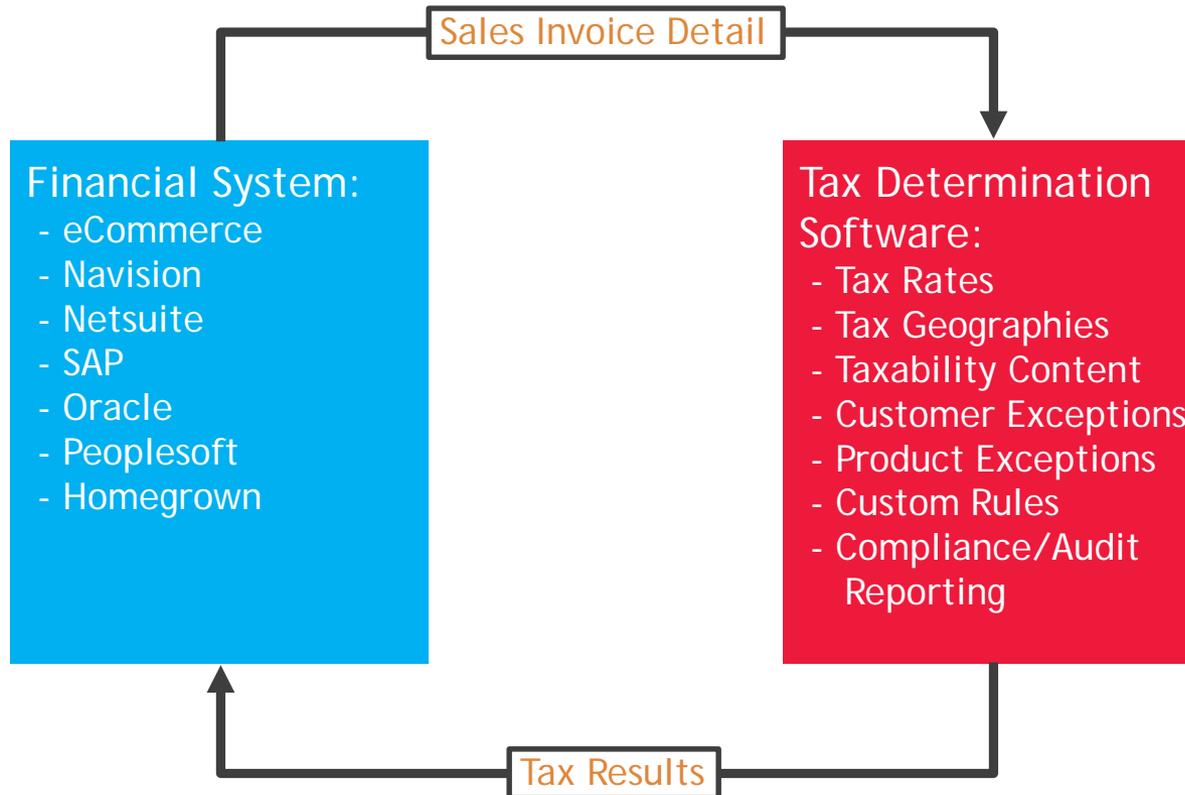
## ▶ Service Provider

- Project team (Director, Manager, Staff Associate)
- Multi-State professionals & Tax Software Expertise

## ▶ Tax Software Vendor

- Software technical consultant
- Professional Services coordinator

# Automation with Third-Party Software: Example Topology



Thank you!

## Questions?

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