

# STATE AND LOCAL TAX IMPLICATIONS OF *SOUTH DAKOTA V. WAYFAIR*

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LSBA Tax Section LDR Liaison Meeting  
September 28, 2018

# AGENDA

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- *South Dakota v. Wayfair*
  - Overview
  - Holding
  - Louisiana Response
  - Other States' Responses
  - Other Issues
  - Income Tax Implications
  - Related Issues
    - Information Reporting
    - Affiliate/Marketplace/"Dealer" Nexus

# *SOUTH DAKOTA V. WAYFAIR* – OVERVIEW

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- *South Dakota v. Wayfair, Inc.*, Dkt. No, 17-494, 585 U.S. \_\_\_ (June 21, 2018)
- Guiding dormant Commerce Clause Principles
  - State regulation may not discriminate against interstate commerce
    - Per se invalid
  - State may not impose undue burden on interstate commerce
    - State law that regulates even handedly to effectuate a legitimate local interest will be upheld unless the burden on interstate commerce is clearly excessive in relation to the putative local benefits (*Pike v. Bruce Church*, 397 U.S. 137 (1970))

## *SOUTH DAKOTA V. WAYFAIR* – OVERVIEW (CONT.)

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- *Quill* is flawed on its own terms
  - Physical presence rule not necessary interpretation of the substantial nexus requirement
  - Creates rather than resolves market distortion
  - Imposes arbitrary, formalistic distinction disavowed by modern Commerce Clause jurisprudence
- “Extraordinary imposition by judiciary on States’ authority to collect taxes and perform critical public functions”
  - Judicially created tax shelter

## *SOUTH DAKOTA V. WAYFAIR* – OVERVIEW (CONT.)

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- *Stare decisis* rejected
  - Court may not prohibit a state from exercising its lawful power in our federalist system
  - Inappropriate to ask Congress to resolve a false constitutional premise created by the Court
- Congress can resolve any problems associated with overturning
- *Quill* and *Bellas Hess* overruled

# SOUTH DAKOTA V. WAYFAIR – HOLDING

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- Creation of a Substantial Nexus Sufficiency Test
  - For purposes of the substantial nexus prong of *Complete Auto Transit v. Brady*,
    - “[Substantial nexus] is established when the taxpayer [or collector] ‘avails itself of the substantial privilege of carrying on business’ in that jurisdiction.”
- Taxpayers satisfied test
  - “[B]ased on both the economic and virtual contacts”
  - “[R]espondents are large, national companies that undoubtedly maintain an extensive virtual presence”
- Remanded to South Dakota Supreme Court

# *SOUTH DAKOTA V. WAYFAIR* – HOLDING – NEW SUBSTANTIAL NEXUS SUFFICIENCY TEST

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- New undefined types of contacts
  - “Substantial virtual connections”
    - “Extensive virtual presence”
  - Passive vs. Interactive?
  - Targeting required?
  - Non-economic contacts?
  - Tacit endorsement of cookie/software nexus
- Minimum threshold undefined for lower courts to determine
  - How much contact is enough?
  - *Wayfair* now only existing guidance
  - No fact specific analysis in *Wayfair* opinion

# *SOUTH DAKOTA V. WAYFAIR* – HOLDING – NEW SUBSTANTIAL NEXUS SUFFICIENCY TEST (CONT.)

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- Distinction between Commerce Clause and Due Process
  - Muddies or removes the distinction between Commerce Clause and due process analysis?
    - Similar to income tax economic nexus cases?
    - Similar to due process minimum contacts and purposeful availment?
    - Unrelated?

# *SOUTH DAKOTA V. WAYFAIR* – HOLDING – NEW SUBSTANTIAL NEXUS SUFFICIENCY TEST (CONT.)

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- Other Commerce Clause Principles
  - *Pike v. Bruce Church* undue burden analysis required even if *Complete Auto* test satisfied?
    - Regulation vs. tax levy
- Retroactivity
  - Constitutional decision retroactive
  - Limits on retroactivity?
- Financial statement implications
  - Q2 event
  - Potential for significant tax reserves

# *SOUTH DAKOTA V. WAYFAIR* – HOLDING – NEW SUBSTANTIAL NEXUS SUFFICIENCY TEST (CONT.)

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- Future SALT Jurisprudence
  - Increased deference to states?
  - More aggressive tax laws?
- Increased emphasis on Due Process
- Tax Planning and M&A Implications
- Prospect for Post-*Wayfair* Congressional Action

# *SOUTH DAKOTA V. WAYFAIR* – SALES AND USE TAX IMPLICATIONS

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- General Principles
  - Safe harbor for those who transact limited business;
  - No retroactivity;
  - Reduced administrative and compliance costs by:
    - Providing single level tax administration;
    - Providing uniform definitions of products and services;
    - Providing simplified tax rate structures, and other uniform rules;
    - Is Streamlined Membership required?
  - Access to software paid for by the taxing authority; and
    - Sellers who choose to use that software immune from audit liability

# *SOUTH DAKOTA V. WAYFAIR – LOUISIANA RESPONSE TO WAYFAIR*

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- Tax Foundation Red Light State
- Louisiana Sales and Use Tax Commission for Remote Sellers
  - Established within the Louisiana Department of Revenue by Act 274 of the 2017 Regular Session
  - Act 5 (H.B. 17) 2018 Second Extraordinary Session
    - \$100,000 or 200-transaction threshold
  - Currently meeting
- Uniform Local Sales Tax Board
  - On a parallel track

# *SOUTH DAKOTA V. WAYFAIR – LOUISIANA RESPONSE TO WAYFAIR (CONT.)*

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- Remote Sellers Information Bulletin 18-001 (Aug. 10, 2018)
  - Prospective Enforcement - January 1, 2019
  - Notice and Reporting Requirements (Act 569 of 2016 Regular Session)
  - La. R.S. 47:302(K) – Direct Marketer Sales Tax Return

# *SOUTH DAKOTA V. WAYFAIR – LOUISIANA RESPONSE TO WAYFAIR (CONT.)*

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- HCR7 (2018 3<sup>rd</sup> Extraordinary session)
  - Creates the Sales Tax Streamlining and Modernization Commission as the successor to the original commission created by Act 405 in the 2015 Regular legislative session and continued by Act 564 in the 2016 Regular legislative session.
  - The goal is to ensure both revenue stability and taxpayer equity through the adoption of proven contemporary tax policies.

# *SOUTH DAKOTA V. WAYFAIR – OTHER STATES’ RESPONSES TO WAYFAIR*

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- Measured Response

- Many states appear to be attempting to comply with the roadmap in *Wayfair*
  - But some states imposing (or proposing to impose) higher thresholds
  - Threshold measurement periods vary
    - Previous calendar year
    - Previous or current calendar year
    - Preceding 12-months
    - Preceding 12-months measured as of a specific date
    - “Annual sales” or “Annually”
- States appear to be enforcing prospectively but
  - Some state guidance, such as Hawaii, contains retroactive “catch-up” language (see Hawaii Dept. of Tax’n, Announcement No. 2018-10, amended July 10, 2018)
- Non-Streamlined states do not appear to view lack of participation as a barrier
- Some states appear to be willing to negotiate prospective compliance

# *SOUTH DAKOTA V. WAYFAIR – OTHER STATES’ RESPONSES TO WAYFAIR (CONT.)*

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- Enforcement Dates
  - Several states asserting an October 1, 2018 enforcement date
  - Other states looking to 2019 either because of effective dates in enacted legislation or because legislative action is required in the 2019 session
  - Outliers
    - July 1, 2018 – HI, ME, VT
    - September 1, 2018 – MS
    - November 1, 2018 – NC, SC and SD
    - December 1, 2018 – CT

# *SOUTH DAKOTA V. WAYFAIR – OTHER POTENTIAL ISSUES*

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- Other Potential issues
  - Mass. and Ohio cookie/software nexus
  - Local enforcement
  - Lack of safe harbor
    - Nexus threshold?
  - Marketplace facilitators
    - Prospect of multiple dealers
    - Multiple sets of guidance required?
  - Ongoing audits, existing assessments and pending litigation

# *SOUTH DAKOTA V. WAYFAIR* – INCOME TAX IMPLICATIONS

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- More aggressive enforcement
  - Undefined floor - Nexus threshold
  - Retroactive?
  - Economic Nexus
  - Factor Presence Standards
  - Non-economic nexus?
- P.L. 86-272
  - Virtual contacts that exceed solicitation
- Tax Planning and M&A
  - Choice of entity
  - Business structuring

# *SOUTH DAKOTA V. WAYFAIR – RELATED ISSUES – USE TAX REPORTING REQUIREMENTS*

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- Act 569 (H.B. 1121) 2016 Regular Session
  - Wayfair has no impact on notice and reporting requirements
  - Louisiana has adopted Colorado-style remote seller reporting requirements on ‘remote retailer’ sales to in-state customers
  - For purposes of the law, a remote retailer is a retailer that avails itself of the benefits of an economic market in Louisiana and:
    - 1) is not required by law to collect Louisiana sales and use taxes
    - 2) makes retail sales of taxable property or services delivered into Louisiana and the cumulative annual gross receipts from those sales exceeds \$50,000 per calendar year
    - 3) does not collect and remit Louisiana sales and use taxes

# ***SOUTH DAKOTA V. WAYFAIR – RELATED ISSUES – USE TAX REPORTING REQUIREMENTS (CONT.)***

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- Act 569 (Cont.)
  - Remote retailer must:
    - Notify the in-state purchaser that a purchase is subject tax unless it is specifically exempt, and that use tax liability must be paid annually
    - Mail Louisiana customers an annual notice by Jan. 31 containing the amount paid by the purchaser for purchases made in the preceding calendar year
    - Provide an annual statement to the Louisiana Department of Revenue by March 1 including the total amount paid by each of the retailer's customers
  - Similar to Colorado legislation at issue in *Direct Marketing Assoc. v. Brohl*
  - Effective July 1, 2017

## *SOUTH DAKOTA V. WAYFAIR – RELATED ISSUES – AFFILIATE/MARKETPLACE/“DEALER” NEXUS*

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- *Normand, v. Wal-Mart.com*, Dkt. No. 769-149 (La. 24th Judicial Dist. Ct. March 2, 2018)
  - Marketplace facilitator was a dealer for purposes of Louisiana sales and use tax laws solely because it engaged in solicitation of a customer market and despite that fact that it never owned or sold the good at issue
  - Currently on appeal
    - Oral argument scheduled October 11, 2018

# QUESTIONS

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