SOUTH DAKOTA V. WAYFAIR: HOW WILL IT AFFECT YOU?

July 17, 2018
South Dakota v. Wayfair: How will it affect you?

CPE Credit: 1.0

Sponsored by:

© 2018 RSM US LLP. All Rights Reserved.
This material may not be reproduced by anyone outside of RSM US without the firm’s express written consent.
Today’s presenters

Mo Bell-Jacobs
Manager
• Member of Washington National Tax
• In addition to examining state and local tax issues and the impact of legislation on middle market companies, Mo serves as a technical resource who tracks legislation, reviews significant court developments and provides client service

Brian Kirkell
Principal
• Member of Washington National Tax
• Brian is RSM’s State & Local Tax (SALT) leader. He focuses on sales and use tax, credits and incentives, income and franchise, and property tax issues.

Michael Giannettino
Partner
• Leads RSM’s Northeast state and local tax indirect technology practice
• Michael’s experiences span various types of indirect taxes including, sales/use, gross receipts, excise tax, and he has extensive experience with unclaimed property.
<table>
<thead>
<tr>
<th>Topic</th>
<th>Minutes</th>
</tr>
</thead>
<tbody>
<tr>
<td>South Dakota v. Wayfair</td>
<td>10</td>
</tr>
<tr>
<td>Current economic sales tax landscape</td>
<td>10</td>
</tr>
<tr>
<td>State and congressional responses to Wayfair</td>
<td>10</td>
</tr>
<tr>
<td>Wayfair FAQ</td>
<td>10</td>
</tr>
<tr>
<td>Recommended next steps</td>
<td>15</td>
</tr>
<tr>
<td>What’s Next</td>
<td>5</td>
</tr>
</tbody>
</table>
Objectives

By the end of this course, you will be able to:

• Describe recent developments in the *South Dakota v. Wayfair* decision
• Identify how economic nexus may impact your business
• Understand what the short-term impact of *Wayfair* will be over the next six months
South Dakota v. Wayfair
Quick recap and litigation update
South Dakota v. Wayfair: Recap

• For about 50 years, sales tax nexus has been based on a concept of ‘physical presence’
  – Businesses selling taxable products or services must be physically present in a state before that state can obligate the business to collect sales tax
• Physical presence includes offices, inventory, and employee travel
• Two prior U.S. Supreme Court cases have addressed physical presence nexus
South Dakota v. Wayfair: Recap (cont.)

- Three major events have caused the states to take a more aggressive approach to remote sellers
  - Exponential growth of remote commerce (e-commerce)
  - Weak sales and use tax collections compared with the amount of economic activity
  - An invitation from the U.S. Supreme Court to re-litigate the issue
South Dakota v. Wayfair: Recap (cont.)

• Sales and use tax ‘economic nexus’
  – In 2016, states begin to directly challenge the physical presence standard by enacting or promulgating so-called economic sales and use tax nexus laws
  – These laws establish nexus for remote sellers with no physical presence when certain total sales or transaction thresholds are achieved
    • A ‘market presence’

• This was the central question of the South Dakota v. Wayfair case that will be decided by the U.S. Supreme Court
South Dakota v. Wayfair, Inc.

- Senate Bill 106 imposes a sales tax collection and remittance obligation on remote sellers without physical presence in South Dakota when gross revenue from sales of TPP or services exceeds:
  - $100,000, or
  - Sales occur in 200 or more separate transactions
- South Dakota Supreme Court overturned the law under Quill
- U.S. Supreme Court agreed to hear the case in January

On June 21, 2018, SCOTUS overrules Quill in a 5-4 decision
- “Flawed on its own terms”
South Dakota v. Wayfair: Recap (cont.)

- **Quill** physical presence standard overturned
- **Wayfair** has been remanded to consider any other claims under the Commerce Clause, *i.e.*, **Complete Auto** test
  - Discrimination/undue burden
  - Substantial nexus
- **Characteristics of the South Dakota law that prevent undue burden or discrimination against interstate commerce**
  - South Dakota had adopted the Streamlined Sales and Use Tax Agreement
    - System of standardization and simplification, administrative software
  - The rule is prospective only
  - Activity thresholds create small-seller exception
South Dakota v. Wayfair: Litigation update

- The parties in Wayfair (Wayfair, Newegg, and Overstock) have discussed settlement with the state of South Dakota.
- Settlement could effectively end the litigation, allowing South Dakota’s economic sales tax nexus provision to become law.
- Impact?
  - No economic sales tax nexus provision will have received substantive review under the Complete Auto test by a state court.
  - Litigation continues in Indiana, Tennessee, Wyoming.
What does *Wayfair* not do?

- *Wayfair* does not find South Dakota’s law constitutional under *Complete Auto* test
- *Wayfair* does not change the taxability discussion
- *Wayfair* does not impose South Dakota’s law on the 46 state sales tax jurisdictions. *Wayfair* overrules *Quill* and opens up the possibility for economic sales tax nexus provisions
- *Wayfair* is not limited to only internet sellers
Current economic sales tax landscape
What states have addressed economic sales tax nexus?
States that have addressed economic sales and use taxes

- CA
- OR
- WA
- NV
- UT
- AZ
- NM
- CO
- MT
- WY
- ID
- ND
- SD
- KS
- NE
- IA
- MN
- WI
- MI
- OH
- IL
- IN
- KY
- TN
- MS
- AL
- GA
- SC
- NC
- VA
- WV
- MD
- DC
- FL
- HI
- AK

**South Dakota styled laws**
# Current economic sales tax nexus laws

<table>
<thead>
<tr>
<th>State</th>
<th>Current Status</th>
<th>Statute or Rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>Oct. 1, 2018</td>
<td>Regulation</td>
</tr>
<tr>
<td>Connecticut</td>
<td>Dec. 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Georgia</td>
<td>Election to collect: Jan. 1, 2019</td>
<td>Statute</td>
</tr>
<tr>
<td>Hawaii</td>
<td>July 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Illinois</td>
<td>Oct. 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Indiana</td>
<td>In litigation</td>
<td>Statute</td>
</tr>
<tr>
<td>Iowa</td>
<td>Jan. 1, 2019</td>
<td>Statute</td>
</tr>
<tr>
<td>Kentucky</td>
<td>July 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Louisiana</td>
<td>Not yet effective as effective date is based on constitutionality of South Dakota's law. Anticipate Louisiana legislature to change law in light of Wayfair</td>
<td>Statute</td>
</tr>
<tr>
<td>Maine</td>
<td>Oct. 1, 2017</td>
<td>Statute</td>
</tr>
<tr>
<td>Massachusetts*</td>
<td>Oct. 1, 2017</td>
<td>Regulation</td>
</tr>
</tbody>
</table>

*cookie nexus*
## Current economic sales tax nexus laws

<table>
<thead>
<tr>
<th>State</th>
<th>Current Status</th>
<th>Statute or Rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mississippi</td>
<td>Dec. 1, 2017</td>
<td>Regulation</td>
</tr>
<tr>
<td>North Dakota</td>
<td>June 21, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Ohio*</td>
<td>Jan. 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Oklahoma</td>
<td>Election to collect: July 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Pennsylvania</td>
<td>Election to collect: March 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Rhode Island</td>
<td>Election to collect: Aug. 17, 2017</td>
<td>Statute</td>
</tr>
<tr>
<td>South Dakota</td>
<td>In litigation, remanded to the South Dakota Supreme Court</td>
<td>Statute</td>
</tr>
<tr>
<td>Tennessee</td>
<td>In litigation</td>
<td>Regulation</td>
</tr>
<tr>
<td>Vermont</td>
<td>July 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Washington</td>
<td>Election to collect: Jan. 1, 2018</td>
<td>Statute</td>
</tr>
<tr>
<td>Wyoming</td>
<td>In litigation</td>
<td>Statute</td>
</tr>
</tbody>
</table>

*cookie nexus
Other nexus expansion

- Economic sales tax nexus is far from universal adoption
- States will continue to enforce other existing nexus rules, regardless of economic nexus
- Other current nexus expansion
  - Marketplace provider nexus
  - Click-through nexus
  - Affiliate nexus
  - Use tax notification and reporting
Use tax reporting and notification

• In 2010, Colorado enacted use tax notice and reporting requirements
  − Notify Colorado purchasers that tax is due on their purchases
  − Annual notices to customers with more than $500 in annual purchases to remind them to pay
  − Annual reporting to the Colorado Department of Revenue
• In 2017, those requirements were finally effective after years of litigation
• A number of other states have since enacted or authorize use tax reporting and notification
  − Alabama, Colorado, Georgia, Iowa, Kentucky, Louisiana, Oklahoma, Pennsylvania, Puerto Rico, Rhode Island, South Dakota, Vermont, Washington
State and congressional responses to *Wayfair*
The states respond almost immediately

<table>
<thead>
<tr>
<th>State</th>
<th>Response to <em>Wayfair</em> decision</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hawaii</td>
<td>Confirmed sellers meeting the sales thresholds will require GET license, file returns, and remit the tax</td>
</tr>
<tr>
<td>Iowa</td>
<td>Confirmation that recently enacted statute will begin Jan. 1, 2019</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>Concludes that current regulation (threshold and presence requirement) is unaffected</td>
</tr>
<tr>
<td>Minnesota</td>
<td>Analyzing the decision with guidance expected by July 21, 2018</td>
</tr>
<tr>
<td>Mississippi</td>
<td>Remote sellers must collect if thresholds are met</td>
</tr>
<tr>
<td>New Hampshire</td>
<td>Considering legislation that would require other states to receive permission to enforce collection by New Hampshire-based businesses</td>
</tr>
<tr>
<td>New Jersey</td>
<td>Economic sales tax bill introduced day of decision, pending with governor</td>
</tr>
<tr>
<td>Texas</td>
<td>Guidance that rule updates will be reviewed and any changes will not be retroactive</td>
</tr>
<tr>
<td>Vermont</td>
<td>Economic nexus statute which was contingent on <em>Quill</em> overturned is effective July 1</td>
</tr>
<tr>
<td>Wisconsin</td>
<td>Nexus &quot;otherwise limited by federal law&quot; provision was affected by <em>Wayfair</em>; intends to collect sales tax on remote sales beginning October 1. (law changes pending)</td>
</tr>
</tbody>
</table>
Congress responds too

• Stop Taxing Our Potential (STOP) Act of 2018 (S.3180)
  – Introduced on June 28 by senators from states without a sales tax (New Hampshire, Montana, Oregon)
  – Do not want businesses that have never collected a sales to have to collect those taxes
Existing federal proposals

- Remote sales tax solutions proposed in 2017
  - Marketplace Fairness Act (MFA)
    - Remote sellers with more than $1 million in annual remote sales collect and remit sales tax on taxable sales delivered to in-state purchasers
    - Sale sourced to the location where the product or service is received by the purchaser
  - Remote Transactions Parity Act
    - Similar to MFA
  - No Regulation Without Representation Act
    - Physical presence with 15-day threshold
- Other notable proposals
  - Online Sales Simplification Act (draft language only)
Policy groups respond

- National Counsel of State Legislatures
  - Compiled “principles of implementation” of Wayfair, encouraging states to wait until Jan. 1, 2019 to collect, or if the state has existing law, provide clear guidance on implementation
Wayfair FAQ
Wayfair FAQ

• Retroactivity considerations
  – Current economic sales tax nexus laws enacted earlier
  – Broad-based nexus statutes

• When does remote sales tax collection begin?

• Will the states wait for Congress to act before enacting their own economic nexus provisions? Should businesses wait for Congress?

• Will more states adopted the Streamlined Agreement?

• Does registering for sales and use tax purposes in a state result in other tax exposure in that state?

• Will states honor other state exemptions?
Wayfair FAQ

- Does physical presence still create nexus under economic nexus?
- What about use taxes? Do we still owe use taxes under economic sales tax nexus regimes?
- What is the impact of the *Wayfair* decision on income taxes?
Recommended next steps
Do you know...

• In the context of the *Wayfair* decision, do you know where you need to collect sales tax?
What questions are relevant?

- What are the correct tax rates?
- What is taxable (an item that’s exempt in one state may be taxable in another)?
- How often must a return be filed?
- Must I register with the state and when?
- Are local sales taxes also due?
- When will the first sales taxes be due?
- Do I need to expand my exemption certificate maintenance system?
- Do I need to update my tax software?
- Do I need to purchase a software solution and how much will this cost?
- What if I’m unable to prepare in time?
- How do I source sales for sales and use tax purposes?
Post-Wayfair to-do list

• Post-Wayfair to-do: Urgent – address immediately
  – **Understand current nexus footprint.** When was the last nexus analysis conducted? Consider voluntary disclosure agreements (VDA) and amnesties for significant noncompliance to catch-up with new nexus framework. **Understand your current activity.** Where do you currently sell products and services and into what states? Understand your sales and transactions thresholds – determine whether you can identify this information.

  – **Understand your products and services.** Items and services may be exempt from the sales tax in one state, and taxable in another. Understanding how those items are characterized is important for multistate sales tax compliance. Taxability is not universal among the states.
Post-Wayfair to-do list

- **Post-Wayfair to-do: Urgent – address immediately**
  - **Consider ASC 450.** Previous noncompliance with economic sales tax nexus provisions.
  - **Automate your tax compliance.** Consider a technology/automation solution. Does your ERP track “ZIP+4” shipping address, individual line item taxability on an invoice, customer exemption status by state, and export sales into a return software? Determining sales tax compliance obligations in 10,000 jurisdictions requires using the right tools. Technology and ERP solutions are not necessarily one size fits all and should be considered with the needs of the business.
Post-Wayfair to-do list

- **Post-Wayfair to-do: Recommended**
  - **Maintain state legislative** and regulatory **tracking** of nexus expansion. Anticipate a wave of new economic nexus laws.
  - **Re-evaluate current approach to** sales tax **collection**. Although not every state currently has an economic sales tax nexus rule. Some businesses may want to proactively begin nation-wide collection.
  - **Re-evaluate current planning**. Those currently pursuing complex planning to avoid sales and use tax obligations may want to consider alternative plans, or delaying those strategies until there is more certainty from the court.
Post-Wayfair to-do list

- Post-Wayfair to-do: Relevant questions
  - Do you have a salesforce?
  - Do you know what activities that salesforce conducts and where the salesforce travels?
  - Do you have mobile assets or inventory?
  - Who is responsible in your business for pulling together relevant stakeholders? (IT, tax, management, etc.)
  - Have you considered factor-presence thresholds for income/franchise tax nexus?
What’s next?
What’s next?

• Congressional action
  – At least three remote seller bills have been introduced
  – HJC Chairman was against the Court deciding this issue
  – Mobile Workforce (federal legislation impacting states 2-for-1 special?)

• Almost 40 state legislatures are adjourned for the year
  – Expect states in full-year sessions to address a S.D.-style law (New Jersey)
  – Special sessions to address
  – States have begun to respond with guidance (North Dakota, Minnesota, New Jersey)

• Further litigation over the South Dakota law
  – Complete Auto review
Thank you

Mo Bell-Jacobs
Manager
mo.bell-jacobs@rsmus.com
+1 202 370 8175

Brian Kirkell
Principal
brian.kirkell@rsmus.com
+1 202 370 8245

Michael Giannettino
Partner
michael.giannettino@rsmus.com
+1 212 372 1761 / 1 914 396 6657