

From the editors of **Internet Retailer**

THE ONLINE SALES TAX SHOWDOWN:

what it means for online retailers



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EXECUTIVE SUMMARY



ONLINE SALES TAX IS ONCE AGAIN A HOT TOPIC

2017 will mark the 25th anniversary of a U.S. Supreme Court decision that has exempted many online retailers from having to collect sales tax on purchases. It could also be the year when that exemption ends, and online retailers must be ready to respond to what would be a major change in their competitive position.

While legislation to set a national rule on online sales tax collection has been blocked in Congress by conservative Republicans in the House, pressure is growing from state governments. States such as South Dakota and Alabama have passed laws or imposed rules that directly challenge the 1992 Quill v. North Dakota ruling by the U.S. Supreme Court that blocked states from requiring sales tax collection by retailers that do not have a physical presence in that state.

There is growing pressure to require the collection of sales tax on most online orders. That could significantly change the competitive position of online retailers vis-à-vis bricks-and-mortar stores.

South Dakota has sued major web-only retailers that refused to comply with the law and trade associations representing web and catalog retailers have countersued, setting up a showdown that could well wind up at the Supreme Court.

The states have been encouraged by the current Supreme Court's seeming willingness to revisit the Quill decision. In 2013, the high court refused to review a

ruling that let stand a New York State law significantly broadening the definition of what constitutes physical presence. And in 2015 Justice Anthony Kennedy openly invited a challenge to Quill, which he noted was a case decided before the explosion of online shopping that has changed the retailing industry.

If an online retailer has to collect and remit sales tax it could significantly increase the price of its goods. Consumers in Chicago, for example, pay a combined 10.25% local and state sales tax, and several other cities are at 10%. 45 states and the District of Columbia has sales taxes and two other states, Montana and Alaska, allow localities to impose their own sales taxes. In all, there are about 10,000 sales tax jurisdictions within the United States, according to the Tax Foundation.

The possibility that online retailers would be required to collect sales tax in all states raises a variety of issues that are covered in this e-book. They include whether the sales tax would be determined by the location of the consumer or the seller—the concept of basing the tax on the seller's location has been floated by Rep. Bob Goodlatte, the power House Judiciary Chairman, as a way of avoiding the problem of requiring every web retailer to be up to date on the taxes charged in each of the 10,000 local and state jurisdictions that impose sales tax.

Related questions being debated by proponents of changing the status quo are how much to subsidize online retailers for the software they will need to keep up with state and local tax rules and rates. A related effort to standardize what items are subject to tax and at what rate has been the remit of the Streamlined Sales Tax Project, which has been hacking away at this thorny problem since 2000. As of now, 23 states have joined the project with one other, Tennessee, holding the status of associate member.

Another question up for debate is whether all online

EXECUTIVE SUMMARY, cont.

retailers will be subject to any national sales tax on online orders. The proposals under consideration offer varying exemptions, with most seeking to avoid the burden of requiring very small e-retailers to collect sales tax.

It was not many years ago that bills introduced in state legislatures designed to require out-of-state online retailers were called “Amazon tax” bills to reflect the growing influence of Amazon.com Inc., which until recently only collected sales tax in a handful of states. But that has changed as Amazon has built out a nationwide network of distribution centers so that it could offer free and fast delivery. As of mid-2016, Amazon was collecting sales tax in 28 states representing 84% of the U.S. population. That has removed Amazon from the center of the debate, and made the question of Amazon collecting sales tax moot.

Amazon’s move to collect sales tax in many more states in recent years has allowed researchers to test how much sales tax influences the buying decisions of online shoppers. As reports in this e-book show, the data

is mixed. An Ohio State study two years ago indicated collecting sales tax cut significantly into Amazon’s sales. But more recent data from Slice Intelligence shows no significant impact.

Some argue that consumers increasingly shop online for convenience more than price and that collecting sales tax would have little impact on online retailers. That remains to be seen. What the articles in this e-book document is that there is growing pressure to require much broader collection of online sales tax, which will impact companies selling online to businesses as well as consumers.

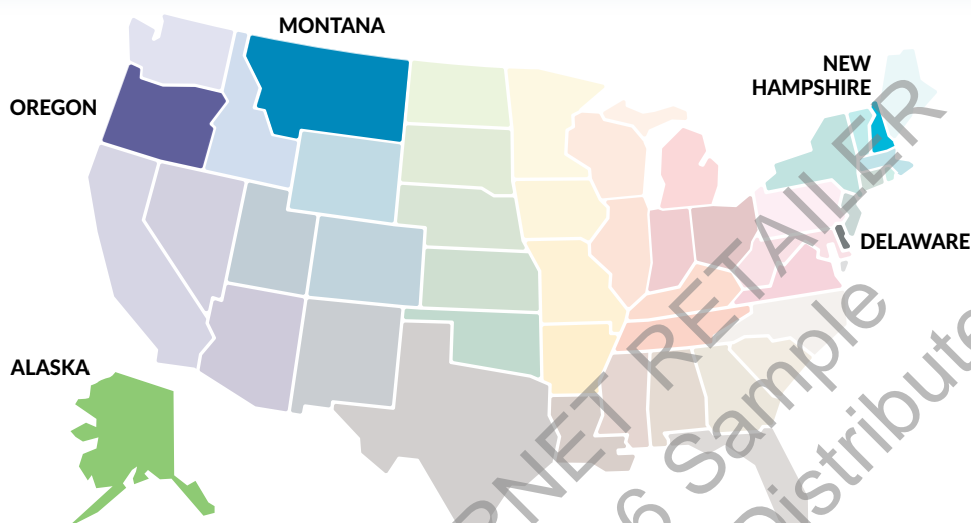
The next year or two may well see a resolution of this long-simmering conflict and a significant shift in the competitive positions of bricks-and-mortar versus web-only retailers. This e-book seeks to provide a detailed look at the situation today, the proposals in play, and their likely impact for retailers of all types and sizes.

Don Davis, editor in chief

Internet Retailer

BY THE NUMBERS

U.S. STATES WITH NO STATEWIDE SALES TAX



28 States where Amazon collects sales tax

84% Percentage of U.S. population in states where Amazon collects sales tax

Source: Amazon.com Inc., Internet Retailer

6.97%

Median combined state and local sales tax rate in the 45 states that have a **statewide sales tax**.

Source: Tax Foundation

10,000

Approximate number of state and local jurisdictions in the U.S. that **levy sales tax**.

Source: Tax Foundation



23 NUMBER OF FULL MEMBERS IN THE STREAMLINED SALES AND USE TAX AGREEMENT

(Tennessee is an associate member)

Source: Streamlined Sales and Use Tax Agreement



**\$15
BILLION**

Estimate of how much in **additional sales tax** state and local governments would take in if **all online orders** were **subject to tax**.

Source: Internet Retailer

THE BATTLE IN WASHINGTON

Pressure builds for Congress to act on online sales tax.

By Heather Lalley and Don Davis



Congress could pass a law requiring online retailers to collect and remit sales tax on all orders, but years of debate have failed to produce action. That's not likely to change in 2016, but pressure from state governments and the courts could prompt action by the 115th U.S. Congress when its session begins in January 2017.

Two forces could lead to congressional action: increasingly aggressive state challenges to the prevailing federal law that exempts many web-only and catalog retailers from collecting sales tax, and strong signals from the U.S. Supreme Court that it recognizes it's time to revise its 1992 decision that for now allows many e-retailers to sell without collecting sales tax.

That decision in a case known as *Quill Corp. v. North Dakota* prohibited states from requiring a seller to collect sales tax on purchases made by consumers in states where that retailer has no physical presence, or nexus in legal terminology. The high court decided that case long before online shopping was popular, as Supreme Court justice Anthony Kennedy noted in a 2015 decision on a related case. "The legal system should find an appropriate case for this court to re-examine *Quill*," Kennedy wrote.

States have taken heed and have adopted laws or regulations that openly flout the *Quill* decision, hoping to provoke legal challenges that could lead the Supreme Court to revise the *Quill* decision and enable states to

THE BATTLE IN WASHINGTON, cont.

require online retailers to collect sales tax on web purchases and submit those taxes to state and local authorities, just as bricks-and-mortar retailers do.

As reported in articles later in this report, South Dakota enacted a law in March 2016 that requires out-of-state online retailers that sell at least \$100,000 worth of merchandise to state residents or complete at least 200 transactions in a year to register and collect sales tax. When a deadline for registration passed in late April the state sued several big web-only retailers that had not complied, including Overstock.com Inc., Systemax Inc. and Wayfair Inc.

South Dakota openly says the Supreme Court would have to reverse its stance on online sales tax to uphold a new state law.

In its lawsuit the state made clear its intent to challenge the Quill decision, writing: “The State acknowledges that a declaration in its favor will require abrogation of the United States Supreme Court’s decision in Quill corp. v. North Dakota.” The American Catalog Mailers Association and NetChoice, a trade association of online retailers, in turn sued the state over the law, raising constitutional issues that could lead to the case ultimately being decided in federal courts.

Meanwhile, the Alabama Department of Revenue adopted a rule in early 2016 that requires online retailer—including those with no offices, stores, warehouses or other presence in the state—to collect and remit sales tax. Alabama also acknowledged that the rule flouts the Quill ruling. The Department of Revenue in neighboring Tennessee has announced plans for an August 2016 hearing on adopting a similar rule.

The state actions could end the stalemate in Congress, some say. “What’s going on in the states this year has really put a lot of pressure on Congress to act,” says Max Behlke, manager of state-federal relations for the National Conference of State Legislatures.

But there remains entrenched opposition, primarily from conservative House Republicans who view any law that would require broader collection of sales tax on online purchases as a new tax, which they oppose. Backers of a federal law that would require online sales tax collection argue that consumers already are required by state law to submit the sales tax they would owe when making purchases with out-of-state retailers—although it’s widely acknowledged that hardly any shopper does send in those payments to his state or local government.

The discussion on Capitol Hill in 2016 has centered on two bills pending in Congress and a third circulating in draft form that would in various ways give states authority to require sales tax collection on web purchases. Two would base the sales tax on the location of the seller, while the third takes the novel—and controversial—approach of basing the tax to be collected on the residence of the shopper.

One of the bills is the Marketplace Fairness Act of 2015, introduced by Sen. Michael Enzi, a Wyoming Republican. This is an updated version of a similar bill that the Senate passed in 2013, but died in the House. The bill was referred to the Senate Finance Committee, which has shown no signs of acting on it.

The bill authorizes states that comply with the Streamlined Sales and Use Tax Agreement—a multistate compact designed to harmonize the widely varying sales tax laws among the 10,000 U.S. jurisdictions that charge sales tax—to require out-of-state retailers to collect sales tax. (23 states are full members of the SST, as it is known, and Tennessee has complied with most of its provisions.) The act would exempt retailers whose sales outside of their own state fall under \$1 million.

Many smaller online retailers complained that the Marketplace Fairness Act would be too expensive to implement, given that there are so many jurisdictions with different rates and varying rules on what items are taxed. That led Rep. Jason Chaffetz, a Republican from Utah, to submit the Remote Transactions Parity Act of 2015, which offers more help to smaller retailers.

The act would require states to belong to the SST to be able to require sales tax collection, to designate a single

THE BATTLE IN WASHINGTON, cont.

entity to handle all state and local tax administration and auditing, create a single tax return for remote sellers and establish a uniform sales tax rate and base of what products are taxed. It also would compensate remote sellers for the software they would need and phase in compliance, exempting sellers with under \$10 million in sales the first year, \$5 million the second and \$1 million the third.

That bill was referred to the House Judiciary Committee, chairman by Virginia Republican Rep. Bob Goodlatte. "The bill remains with the Judiciary Committee and forward movement is at the discretion of that chairman," says a Chaffetz spokeswoman. In other words, it appears to be going nowhere.

That's because Goodlatte has publicly stated that any law requiring out-of-state online retailers to collect sales tax must be simpler for the online and catalog merchants affected. With that in mind, Goodlatte has circulated a draft of a bill that would be called the Online Sales Simplification Act.

His proposal takes the radically different approach of basing the sales tax on the location of the seller, not the shopper. In other words, if a company is based in a locality where the prevailing sales tax rate is 7% that is the sales tax it would charge on all orders, regardless of where the consumer lives. Sales taxes collected would go to a national clearinghouse to be created under the proposal, which would distribute funds to the state where the consumer lives.

States would have to agree to terms of the law, which would limit their authority to impose additional taxes on remote sellers, in order to get those distributions. Otherwise, the state of the seller would keep the sales tax.

The proposal seeks to address the possibility that online retailers would relocate to the five states with no statewide sales tax—Alaska, Delaware, Montana, New Hampshire and Oregon. E-retailers in those states would have to either apply a flat sales tax to all orders or to report all sales by state to the clearinghouse. That would include reporting not only the amount of the purchase but the name and address of the consumer who made the purchases. That could allow the consumer's home state to demand that she pay the use tax—the equivalent of the sales tax—owed on the purchase, which could lead to protests over undue state interference

in consumers' personal lives.

Opponents say basing the tax on the seller's state still could lead states to compete to lower sales taxes to lure online retailers, leading them to have to raise property or income taxes. They also say the proposal amounts to taxation without representation in that a consumer in California could be forced to pay a sales tax in Ohio that she has no control over.

Nonetheless, this proposal is generally viewed by online retailers and their lobbyists as less onerous than having to comply with a crazy quilt of state and local sales tax laws. And Goodlatte's position as Judiciary Committee chairman makes him effectively the gatekeeper of any tax legislation that this Congress might consider. "If anything happens this year, it will be driven by Goodlatte," says Steve DelBianco, executive director of the Washington, D.C.-based NetChoice online commerce trade association, which represents web-only retailers and favors the status quo.

Still, many observers believe action will have to wait until at least the next session of Congress. "It's just not an easy thing to resolve. There are too many moving parts," says Bill McClellan, vice president of government affairs for the Washington, D.C.-based Electronic Retailing Association, which represents merchants that sell primarily through TV infomercials and thus fall under the heading of remote sellers.

There is "no chance" of an online sales tax bill being passed this year, says Howard Gleckman, senior fellow at the Urban Institute, a Washington, D.C. think tank. "There is no urgency and with Congress only in session for a very limited period for the rest of this election year, it is unlikely it will do anything except a budget of some sort and a few other must-pass bills," Gleckman says.

Things could look very differently in January, however. The November elections could shift the power balance in both the House and the Senate, and a new president will surely fill the vacant seat on the Supreme Court, potentially altering the conservative-liberal balance. Add in the pressure from the states and the Supreme Court's apparent willingness to revisit Quill and 2017 shapes up as the year in which Washington might finally bust up the online sales tax logjam.

THE BATTLE IN WASHINGTON, cont.

A NEW TAKE ON SALES TAX

Backers of a national online sales tax keep coming up with new proposals, but Congress seems in no hurry to act.

By Matt Lindner

Jonathan Johnson, chairman of web-only mass merchant Overstock.com Inc., was at one time among the most vocal opponents of an online sales tax. But times changed.

Johnson is now supporting the Remote Transactions Parity Act, or RTPA for short, an online sales tax collection bill introduced in June 2015 by Rep. Jason Chaffetz, a Utah Republican. The RTPA would require online retailers to collect sales tax from customers in the 45 states plus the District of Columbia where there is a sales tax in place. It would also require states to provide and install the necessary software for retailers to collect these taxes.

The legislation, Johnson says, offers a workable resolution to the longstanding battle over sales tax collection between merchants who maintain physical stores and those who only operate online. Johnson says Overstock provided some unspecified commentary on drafts of the bill before it was formally introduced.

"We want Congress to find a solution so there's not this patchwork of state laws that make it difficult for Internet companies to know when and where they have to collect

taxes," Johnson says. "We've taken a position that it's appropriate for Congress to act."

If Congress doesn't act, he says Overstock plans to continue fighting individual states that seek to force retailers without an office, warehouse or other presence in that state from collecting sales tax. The prevailing federal law, based on a 1992 Supreme Court decision, is that retailers need only collect sales tax in states where they have a physical location. As e-commerce has grown, states have clamored for the power to force sales tax collection by all online-only retailers, and bricks-and-mortar merchants have backed those efforts because web retailers effectively offer lower prices when they don't collect sales taxes. Congress has been unable to agree on a plan, but Chaffetz's bill and other proposals put the question back on the table. However, lawmakers will have to act quickly because if an online sales tax bill fails to pass this year, there likely won't be any action on the sales tax front until 2017, after the upcoming election cycle, experts say.



THE BATTLE IN WASHINGTON, cont.

Further roiling the debate is a comment early this year made by U.S. Supreme Court Justice Anthony Kennedy, who suggested that the court might reconsider the 23-year-old ruling that established the framework for the online sales tax debate, preventing states from forcing a retailer to collect sales tax on purchases from consumers in states where the retailer has no physical presence.

In the 1992 case, *Quill Corp. v. North Dakota*, the Supreme Court ruled that Quill, which sold office supplies by catalog, didn't have to collect sales tax from North Dakota residents because it had no physical presence in the state. When online shopping caught on, federal courts applied the same logic to online retailers.

A Supreme Court justice says the prevailing online sales tax law harms states more than could have been anticipated.

But as U.S. e-commerce has grown into a \$304.91 billion market, the Quill ruling might be outdated, Kennedy wrote. "Given these changes in technology and consumer sophistication, it is unwise to delay any longer a reconsideration of the Court's holding in Quill," he wrote. "A case questionable even when decided, Quill now harms States to a degree far greater than could have been anticipated earlier." Kennedy's comments came in his concurrence with the Supreme Court's ruling in *Direct Marketing Association v. Brohl*, a ruling that prevented the state of Colorado from requiring sales tax collection from web retailers that don't have a physical presence in the state.

Matthew Schaefer, a partner with law firm Brann & Isaacson who focuses on state and local tax issues and was one of the lawyers representing the Direct Marketing Association in that case, says he doesn't think Kennedy's words are putting any pressure on lawmakers just yet.

"Justice Kennedy's concurrence was not joined by any other member of the Supreme Court," he says. "Moreover,

to the extent that Justice Kennedy argued that the Court should look for an opportunity to re-examine Quill's physical presence standard, lawmakers who do not view federal legislation as a priority might interpret his comments as a reason for Congress not to act now, on the expectation that perhaps the Supreme Court will revisit the issue." In other words, by muddying the waters, Kennedy may have made it even less likely Congress will act quickly.

The Chaffetz bill, the RTPA, has much in common with the Marketplace Fairness Act, which passed the Senate in May 2013 before dying in the House during the congressional session that ended last year. Many conservative House Republicans opposed it on the grounds that it amounted to a tax increase on consumers. (Consumers are legally obligated to pay sales tax to their home state when they purchase online, but few do pay it if the retailer doesn't collect it at checkout.) The Marketplace Fairness Act was subsequently reintroduced in March of this year looking almost the same as the previous version.

"The only difference is that the 2015 MFA delays slightly the date when states that meet the law's eligibility requirements can begin to exercise authority to require sales tax collection on remote sales," Schaefer says. If passed, states could not begin to require tax collection by remote sellers for a year after the effective date of the bill becoming law, and also could not start tax collection during the peak holiday season the first calendar year after enactment. That means that, in the unlikely event Congress quickly passes the MFA, the first holiday season it could be in effect would be in 2017.

Both bills provide exceptions for small sellers. The 2015 version of the Marketplace Fairness Act exempts companies that do \$1 million or less in remote sales within the United States. (Remote sales are sales outside of the retailer's home state.) Chaffetz's bill is more generous with the exemption totals at first, but includes another caveat. It exempts in the first year retailers with less than \$10 million in U.S. online sales, then the second year lowers the exemption to \$5 million, and the third year only exempts e-retailers with less than \$1 million in web sales. However,

THE BATTLE IN WASHINGTON, cont.

Chaffetz's bill also says any seller who sells through an online marketplace would be required to collect sales tax right away.

Much like the MFA before it, Chaffetz's bill enjoys the support of the National Retail Federation, which seeks to eliminate what it calls online retailers' advantage in that many don't collect sales tax. Rachelle Bernstein, NRF's vice president and tax counsel says the RTPA creates "parity" between merchants with physical stores and those that only sell online.

As e-commerce continues to gain market share, the onus is on the states to recoup sales tax revenue that they previously collected from stores, she says. "As states look at revenue lost from this lack of sales tax, their alternatives are going to be either raise sales tax more because they're not able to collect from the noncompliant or they're going to have to move to alternative forms of taxes," she says. "Politically, many states prefer sales taxes to income taxes or property taxes."

Some online retailers seem resigned to the idea that they won't be able to avoid collecting sales tax forever. "It really isn't a question of if an online sales tax will happen, but when it will happen," says Kyle Goguen, founder and CEO of online pet treats retailer Pawstruck LLC.

Pawstruck would fall under the small business exemption as outlined in the 2015 MFA, as Goguen is projecting online sales of about \$500,000 this year. But the e-retailer wouldn't be exempt under the RTPA, because it sells through Amazon's and eBay's marketplaces. That's why, if a law does move forward, he'd prefer it be the MFA. "The main determining factor is that the RTPA's small seller exception doesn't include larger marketplaces," he says. "This means that any seller—regardless of overall revenue—that uses marketplaces like Amazon or eBay won't be eligible for the small seller exemption. We currently sell on both of those channels in addition to our own website."

The largest online retailer, Amazon.com Inc., in 2012 reversed its stance against national legislation over sales

tax collection on online purchases and now supports it. Amazon changed its position as it began building warehouses throughout the country to ensure fast delivery of online orders. Those warehouses constitute the kind of physical presence that requires Amazon and other retailers to collect sales tax, and Amazon now collects tax in states that represent 77.5% of the U.S. population.

While Amazon backs federal legislation and Overstock has spoken out in support of the RTPA, other retailers say the bill will cause problems for online retailers. The heart of the problem is knowing how much to charge each shopper on each item. It's not only states and the District of Columbia that charge sales tax—nearly 10,000 cities, counties and other jurisdictions in the United States charge sales tax, too. Further, the rates vary and so do the rules as some, for example, tax clothing or food, while others do not.

While the RTPA does place the burden on states to provide, install and maintain the software necessary to collect online sales tax from consumers in all these jurisdictions, online retailers say they're concerned that the tax collection requirement would be a significant burden.

"I would be required to start interviewing different vendors and evaluating how to comply with something in hopes that it doesn't interfere with my regular day-to-day business," says Corey Frons, CEO of web-only lightbulb retailer BulbAmerica.com. And vendors are taking note. Frons says he has received a number of sales calls from vendors pushing software they say would put BulbAmerica.com in compliance with the RTPA or any similar legislation.

Jill Scalisi, owner and operator of Scalisi Skincare, which manufactures and sells skincare products online, agrees. "Compliance in charging, tracking and then payment would all be very difficult," she says. Commercial software vendors might be able to add sales tax features, she says, but retailers that built their own e-commerce

THE BATTLE IN WASHINGTON, cont.

software would likely face big problems. “The websites built off major platforms like Shopify should be OK with compliance and tracking, but (websites that aren’t built off major e-commerce platforms), and there are many, would need to be rebuilt.”

“The changes that would be required to implement MFA or RTPA are significant,” says Harley Duncan, managing director of state and local tax with accounting and consulting firm KPMG. “They will require substantial changes in operations by many sellers.”

There’s also the elimination of what has been, to date, a competitive advantage.

Brian Baugh, a finance Ph.D. student at Ohio State University, in 2014 co-authored a paper that studied the impact that implementing sales tax had on Amazon’s sales when the retailer began collecting sales tax in five states from 2012 to 2013, tracking the purchasing behavior of approximately three million households. Baugh and his co-authors found that not only did shoppers in those states spend around 10% less on Amazon once Amazon began collecting sales tax, they also spent 2% more at bricks-and-mortar retail locations.

While the Chaffetz bill has attracted much of the recent attention, there are other options. For instance, Rep. Bob Goodlatte, a Republican from Virginia and chairman of the House Judiciary Committee, in January introduced the Online Sales Simplification Act, which he said would lessen the burden on web retailers of collecting sales tax. It would address the issue of the many taxing jurisdictions by requiring an online retailer to collect the sales tax required by the state in which it is located. The e-retailer would keep

records of the home states of the customers who made purchases, and then give the money collected from out-of-state consumers to a commission that would distribute it to the other states.

Steve DelBianco, executive director of online retail lobbying group NetChoice, and Overstock both support the proposal. “Goodlatte’s concept is a new twist on an old rule where businesses rely upon the tax rules where they’re based,” DelBianco says. “The sellers, when they remit the money to their home state, submit a report with the amount of money from states they sold to. You let the states allocate the money based on where the customers came from.” That takes the burden of filing with many jurisdictions off of the web merchant.

But are any of these proposals likely to pass? It does not look likely. Neither the House nor the Senate has acted on the Marketplace Fairness Act of 2015 or the Remote Transactions Parity Act. No hearings on either have been held and, as of press time, none are scheduled.

“It is difficult to forecast the prospects for passage for either bill,” Schaefer, of Brann & Isaacson, says. “Both the MFA and the Chaffetz bill have Democratic and Republican sponsors. At the same time, Judiciary Committee Chairman Goodlatte has issued a set of seven basic principles that any federal legislation to expand state authority to impose sales tax collection obligations on remote sellers with no physical presence in a state should satisfy, which neither the MFA nor the Chaffetz bill come close to achieving.”

In other words, if Congress does not act quickly, any tax reform may amount to all talk and no action until another Congress is seated in January 2017.

THE BATTLE IN WASHINGTON, cont.

THE SUPREME COURT GIVES E-RETAILERS A WIN ON SALES TAXES, BUT IT MAY BE SHORT-LIVED

The high court reinstated a lawsuit against a Colorado law that required online retailers to notify Colorado of purchases by state residents. But the court hints at another legal objection to the lawsuit.

By Bloomberg News

The U.S. Supreme Court gave Amazon.com and other direct marketing retailers a victory in March 2015 with one hand, then used the other hand to take it back.

Formally, in *Direct Marketing Association v. Brohl*, the court unanimously reinstated a lawsuit brought by a direct retailer to block a Colorado law requiring them to notify the state about purchases that fall under Colorado's sales or use tax. That much was a win for the direct shippers. But in a nonbinding message, the court strongly hinted that the appeals court should block the suit on different grounds than it used the first time, which would give the victory back to Colorado.

I know, I know, this kind of reasoning is what gives lawyers a bad name. Don't kill the messenger, at least not before I've explained what the heck the court actually did. That'll take a couple of minutes of your time—no more, I promise.

The federal district court that first heard the challenge to the Colorado law hated it. Relying on Supreme Court precedent, the trial court said that by requiring direct marketers to provide Colorado with information about who made online or other out-of-state purchases, how much they bought, and where they lived, the state was violating the U.S. Constitution. Specifically, the court said that the law violated a doctrine known as the "dormant commerce clause."

If word "dormant" sounds irritatingly legal, that's because it is. We should probably call it the negative commerce clause, except that sounds kind of negative.

The commerce clause itself says only that Congress may regulate interstate commerce. But over the centuries, the



Supreme Court has come to interpret it to include the distinct idea that the states may not themselves interfere with interstate commerce.

That idea is "dormant" because, well, it's a sleeper: Though based on an inference from the structure of the Constitution, it has far-reaching consequences. The simplest way to think about it is that the dormant commerce clause functions as a kind of American version of the European Union's foundational Maastricht Treaty. It facilitates a single unified national economy by blocking the states from gumming up the works.

The federal trial court thought that Colorado was in effect impeding the smooth flow of interstate commerce by trying to tax the direct marketers.

On appeal, the U.S. Court of Appeals for the 10th Circuit reversed the marketers' win. It relied on a law called the Tax Injunction Act of 1937. Court aficionados or those with long memories may remember that law from the first Affordable Care Act case, in which Chief Justice John Roberts and the rest of the court's majority held that the individual mandate was not a tax for purposes of the Tax

THE BATTLE IN WASHINGTON, cont.

Kennedy spoke only for himself, but the other justices pretty clearly are sympathetic to the states that are losing sales tax revenue.

Injunction Act but was a tax for purposes of congressional authorization.

The Tax Injunction Act says that federal courts “shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State.” That means essentially that the federal courts can’t issue an opinion blocking a state tax if the state courts could address the issue easily. The 10th Circuit said that under this law, the federal courts lacked the authority to hear the direct marketers’ case—as they could’ve gone to the state courts to get a remedy.

The appeals court decision vacated the direct marketers’ victory before the district court, so the direct marketers went to the Supreme Court. The justices unanimously reversed the 10th Circuit’s reversal. They held that the appellate court had misapplied the Tax Injunction Act. Because the Colorado law only requires the marketers to inform the state about purchases and does not actually require anyone to pay taxes, the court said, it didn’t count as “the assessment, levy or collection of any tax.”

Logically, of course, the reversal of a reversal should’ve left the original district court opinion in place, which would be a huge win for the direct marketers.

But that logic is precisely what stands between an intelligent person and a lawyer. Justice Clarence Thomas writing for the court added two paragraphs containing what lawyers call “obiter dicta,” usually just shortened to “dicta,” which means legally nonbinding observations that the parties and the courts below are supposed to listen to if they’re smart.

Thomas’s dicta said that “we take no position” on whether the 10th Circuit should dismiss the case again on the grounds of “comity,” defined by the court as a doctrine that “counsels lower federal courts to resist engagement in certain cases falling within their jurisdiction.” According to the doctrine of comity, the courts technically could decide an issue, but choose not to out of respect for the state courts. In a footnote to its opinion, the 10th Circuit had said that the comity doctrine “militates in favor of dismissal.”

Lawyers are trained to read such dicta as a kind of telegraphic message directing the lower courts what to do without requiring them to do it. Thomas was basically telling the 10th Circuit to go back to the drawing board and re-reverse the district court’s decision in favor of the direct marketers, but using different logic.

Why on earth did the court go to so much trouble to do this? The answer can be gleaned from Justice Anthony Kennedy’s solo concurrence. Kennedy simply stated that although under current Supreme Court doctrine the direct marketers’ case should succeed in the dormant commerce clause that doctrine was in serious need of transformation in the light of changing economic circumstances and the rise of direct marketing on the Internet.

Kennedy spoke only for himself, but the other justices pretty clearly are sympathetic to the states that are losing sales tax revenue—not to mention local retailers, who suffer a competitive disadvantage by having to charge sales tax.

But the court would like to spare the trouble of overturning its dormant commerce clause doctrine. It therefore apparently wants the lower courts to find a way to uphold Colorado’s law—just not using the Tax Injunction Act. All that clear? Well, at least it was faster than going to law school.

You can also say “dictum” to refer to a single nonbinding statement or observation, but that technically correct usage is fading fast from legal discourse, and it might make you seem pretentious, like you know Latin grammar or something embarrassing like that.

THE BATTLE IN WASHINGTON, cont.

Editor's note: Two big e-retailers challenged a New York law that extended the state's ability to require sales tax collection on online orders. The next two articles describe the challenge to the law and the Supreme Court ruling, which signaled the court's growing sympathy with the states on the sales tax issue.

AMAZON AND OVERSTOCK TAKE TAX FIGHT TO THE U.S. SUPREME COURT

The e-retailers want the U.S. Supreme Court to overturn a New York ruling.

By Paul Demery



After failing in March 2013 to persuade New York State's top court to overturn a state law that ties sales tax collection to in-state affiliate sites, online retailers Amazon.com Inc. and Overstock.com Inc. sought in August 2013 a better deal from the U.S. Supreme Court.

"New York's courts made a bad law that ignored the U.S. Supreme Court's precedent regarding retailers' responsibility in collecting sales, and we have a higher hope that Supreme Court justices will follow prior Supreme Court law," says Jonathan Johnson, executive vice chairman of Overstock. The U.S. Supreme Court ruled in 1992 that states can require retailers to collect sales tax only when retailers have an in-state physical presence, such as stores or distribution centers.

Overstock filed a petition with the Supreme Court in August 2013, followed a day later by a petition filed by Amazon. Both retailers want the high court to review a March 28, 2013, decision by the New York State Court of Appeals, the state's highest court, that upheld a lower court ruling in favor of the state's so-called Amazon Tax law. Technically speaking, each retailer has filed a petition for a "writ of certiorari," which is a request to have the high court review the lower court's ruling.

That law, which New York enacted in 2008, requires online retailers to collect sales tax from New York residents if the merchants get sales leads from consumers clicking links on affiliate web sites based in New York State, such as information sites or blogs. The state contends that such arrangements with affiliates amount to an in-state physical presence or nexus in legal terms, making a retailer responsible to collect sales tax.

An Amazon spokesman declined to comment on the retailer's petition, citing "a long-standing company policy of not commenting on active litigation." Following the court defeat in March, Amazon said the state's Court of Appeals ruling "conflicts" with the U.S. Supreme Court's precedents, but gave no indication that it would appeal the ruling.

Johnson, however, repeated this week what he said in March, that the U.S. Supreme Court would be more likely than New York's courts to consider views opposing the connection between web site affiliates and nexus. "To get a fair hearing in court, we have to go to the U.S. Supreme Court," he says.

THE BATTLE IN WASHINGTON, cont.

AMAZON AND OVERSTOCK LOSE TO NEW YORK ON A SALES TAX LAW

The Supreme Court lets stand a ruling that allows New York State to force sales tax collections by retailers that do get referrals from New York-based websites.

By Allison Enright



New York State can continue to tie online sales tax collection to in-state affiliate sites after the U.S. Supreme Court in December 2013 declined to hear an appeal from Amazon.com Inc. and Overstock.com Inc.

The two large web-only retailers each filed petitions with the U.S. Supreme Court asking it to clarify when states can require retailers to collect sales taxes on online orders placed by consumers in those states.

The e-retailers were appealing a New York State Supreme Court ruling from March that upheld a 2008 New York law. That law makes it easier to require online retailers to collect taxes on orders placed by consumers in New York because it interprets more loosely the definition of what it means for e-retailers to have a physical presence, or nexus, in the state. Most states

interpret nexus as having a physical store, office or distribution center in the state. The New York law, however, says that if a retailer works with affiliate marketers—such as coupon sites and bloggers based in New York that post ads or refer traffic to an e-retailer's site in exchange for a cut of any sale that results—the retailer has a physical presence in New York and must collect sales tax from New York consumers.

The U.S. Supreme Court's refusal to take on the appeals means the ruling of the New York Supreme Court stands. In October, the Illinois Supreme Court overturned a similar law, saying it went against existing federal law that restricts states to mandating

sales tax collection only when a retailer has an in-state physical presence. After the Illinois court overturned the law both Amazon and Overstock said they would re-start their affiliate programs in Illinois. The e-retailers have cut off affiliate programs in states that enacted similar laws, including Connecticut and Rhode Island. Neither currently have affiliate programs in New York.

"We're not surprised, but we are disappointed," says Jonathan Johnson, executive vice chairman of Overstock. "I really think the Supreme Court non-decision today is an invitation for Congress to find a workable solution to the tax issue. The Marketplace Fairness Act isn't it."

The Marketplace Fairness Act—which passed the Senate by a wide margin in May and is now before the House Judiciary Committee—as currently written

THE BATTLE IN WASHINGTON, cont.

would allow states to mandate sales tax collection by online and catalog retailers whether or not they have a physical in-state presence such as stores or distribution centers. In effect, the legislation would overturn the 1992

'We're not surprised, but we are disappointed.'

Supreme Court ruling in *Quill vs. North Dakota*. Johnson says Overstock supports a set of principles released in September by the House Judiciary Committee as the way forward.

Amazon.com, responding to a request for comment on the Supreme Court's decision today, reiterated its support of the Marketplace Fairness Act. "The Supreme Court already has addressed the sales tax issue, saying in *Quill* that Congress can and should act to resolve it," the e-retailer said. "The Marketplace Fairness Act now pending before Congress would protect states' rights to make their own revenue policy choices while allowing them to collect more than a fraction of the revenue that's already owed."

Rebecca Madigan, executive director of the Performance Marketing Association, a trade group that represents affiliate marketers, expressed disappointment in the U.S. Supreme Court's refusal to take on Amazon's

and Overstock's appeals. "There are over 80,000 online affiliate marketers in the U.S. who have had their incomes devastated by various states' attempts to regulate interstate commerce," she says. "These state laws need to be shut down, and that's what we hoped from a Supreme Court ruling."

She says the only viable solution to the question of affiliate marketers and nexus is to require all retailers to collect sales tax for all states. "Maybe the House will show more interest now that there's not a Supreme Court ruling in the wings," she says.

The Supreme Court's refusal to take on the appeals coincides with Cyber Monday, the most-hyped online shopping day of the year. Steve DelBianco, executive director of NetChoice, a lobbying group for retail companies and organizations including eBay Inc., Overstock.com Inc. and the Electronic Retailing Association, says that e-retailers will collect more sales tax today than ever before. "This is the first Cyber Monday where Amazon is collecting sales tax for over half the country, and next year it will be even more," he says. "A new online tax system is not going to save main street stores from their big-box competitors. New tax burdens will extinguish their last hope of reaching new customers, and expose them to audits from dozens of distant state tax collectors."

THE BATTLE IN WASHINGTON, cont.

Editor's note: Rep. Robert Goodlatte's criticism of the Marketplace Fairness Act, described in the following 2014 article, foreshadowed his subsequent introduction of a substantially different bill that would empower states to require sales tax collection from many online retailers.

'DEFECTS' MAR A FEDERAL TAX BILL, A CONGRESSMAN SAYS

At a hearing for the Marketplace Fairness Act, U.S. Rep. Robert Goodlatte points to three flaws in the bill.

By Thad Rueter

A federal online sales tax bill that passed the U.S. Senate and now before the U.S. House contains significant "defects," according to a leading Republican congressman.

U.S. Rep. Robert Goodlatte (R, VA), chairman of the House Judiciary Committee, said in March 2014 that the Marketplace Fairness Act is flawed in three ways:

- The public views the bill "as Congress taxing the Internet." He cited Gallup poll data that shows 57% of U.S. consumers opposed the bill.
- E-retailers would face significant challenges in complying with the bill. That's because while the bill as it stands requires states to provide free tax compliance software, the cost of integrating the software remain unaddressed, he says. Goodlatte also says that "compliance costs estimates vary widely. There are over 9,600 taxing jurisdictions, and the Affordable Care Act experience has left voters wary of highly touted software solutions."
- The federal sales tax bill would leave e-retailers exposed to "multiple audits in jurisdictions in which they have no voice," Goodlatte says.

The Marketplace Fairness Act would allow states to mandate sales tax collection by online and catalog retailers even if they have no physical in-state presence such as stores or distribution centers—a legal concept known as nexus. Current federal law says states can only mandate tax collection by retailers with an in-state physical presence such as stores or distribution centers.

The U.S. Senate passed the Act in May 2014. Its version exempts retailers with less than \$1 million in remote

sales—that is, sales to customers in states where they have no physical presence and no existing requirement to collect sales tax. *[Editor's note: The House of Representatives never voted on the Marketplace Fairness Act and the Senate bill died with the end of that congressional session.]*

The bill is supported by retail chains and industry groups including the National Retail Federation and Retail Industry Leaders Association, as well as Amazon.com Inc., the world's largest retailer by web sales. Amazon is No. 1 in the Internet Retailer Top 500 Guide. The bill is opposed by many online retailers, including eBay Inc. and Overstock.com Inc., that are represented by industry lobbying groups such as NetChoice.

Obamacare 'has left voters wary of highly touted software solutions.'

Amazon, eBay and Overstock did not immediately respond to requests for comment today. A spokesman for the National Retail Federation sounded a note of optimism.

"It is evident from yesterday's House Judiciary Committee hearing that online sales tax fairness remains a priority for the committee and its members," says the spokesman. "NRF looks forward to working with the committee throughout the process and we look forward to the day that retailers can compete for customers no matter their preferred channel."

THE BATTLE IN WASHINGTON, cont.

AUTOMATED SALES TAX MANAGEMENT HELPS RETAILERS ACHIEVE AND MAINTAIN TAX COMPLIANCE



Scott Peterson, director of government affairs, Avalara

Tax compliance has always been a thorn in the side of traditional bricks-and-mortar retailers, and it's become even more complex now that more and more merchants are selling online.

Today, e-retailers are confronted with a myriad of tax compliance challenges—from navigating the thousands of product taxability rules and tax regulations to determining if or when they're required to charge state sales tax to remote customers (commonly referred to as "nexus"). It's no wonder that even the most experienced online retailers often find themselves struggling to understand their tax obligations.

"The majority of ecommerce retailers try their hardest and do their best to manually manage tax compliance, but the complexity makes it nearly impossible to get it right," says Scott Peterson, director of government affairs at Avalara, a leading provider of tax compliance automation for business.

One of the biggest challenges that retailers face, according to Peterson, is navigating the more than 70,000 tax jurisdictions that exist globally. "No matter how big or small, any online retailer can be required to collect and remit taxes for all the taxing jurisdictions in their home state—at the very least—and quite possibly many other states as well," Peterson explains. "This is due to the changing state of the law surrounding which businesses need to pay tax in which states."

Additionally, Peterson says, many of these jurisdictions apply different rates to different products. Apparel and food may be taxed differently than durable goods, such as appliances. "Retailers face changes to sales taxability of particular products when new exemptions are created or old ones expire or are removed by law," Peterson says. "They have to contend with changing sales tax rates and make sure they're maintaining a record of all tax-exempt transactions and the exemption certificates that make those transactions valid—as well as a host of other obligations."

Another huge tax challenge for retailers is understanding when nexus (taxability of sales to remote customers) applies. "When a retailer has nexus—as many of them do—they're liable to collect and remit sales tax for all transactions that come from that state," Peterson explains. "The concept is simple, but figuring exactly when and where the retailer has nexus gets tricky."

Because many states define nexus differently, Peterson says, it's important that online retailers understand state-specific nexus rules. Location also plays a role in determining if nexus applies. For example, traveling to trade shows, attending meetings or having employees in other states may create nexus. Additionally, using third-party marketing strategies, such as remote ad placements, may create nexus. And if a retailer uses Fulfillment by Amazon for orders placed on its Amazon Marketplace site, it might have nexus in the states where Amazon has warehouses and distribution facilities.

"Today, any number of standard business activities can result in a tax obligation," Peterson says. "Every state's regulations are different, so it's important to have a nexus assessment performed periodically if your business makes sales to out-of-state buyers."

THE BATTLE IN WASHINGTON, cont.

Adding to these complications, Peterson says, is that changes to tax requirements are happening all the time—especially with regard to nexus. “The biggest issue now is that states are trying to significantly expand nexus, which will have a huge impact a number of companies,” Peterson adds.

While Congress debates over the proposed Marketplace Fairness Act (MFA) and other legislation, state governments are aggressively taking matters into their own hands and focusing on nexus rules in an effort to reduce budget deficits. “New rules from states such as Alabama and Louisiana, to name a few, will have a big impact many remote sellers,” Peterson says.

Retailers will ultimately need to automate their manual tax compliance processes and do so in a way that complements their existing technology and existing operations,” says Peterson. “Everything from capturing and storing exemption certificates to filing and remittance needs to be integrated with a company’s ERP, e-commerce, accounting, and shopping cart software—all without creating extra steps or adding complexity.”

Peterson adds that one of the keys to streamlining the compliance process is to use cloud-based technology, like Avalara, which automatically calculates sales tax for every invoice line item, in the real-time “magic moment” of ecommerce. Avalara helps reduce the tedious work and complexity of calculating taxes for millions of products and services across the U.S., Canada, Europe, and dozens of other international jurisdictions, giving customers more time to focus on driving their own business success. In

addition, Avalara offers tax return preparation, filing, and remittance services with a single payment.

Avalara’s many retail customers, such as Life is Good, Christian Louboutin, and David Yurman, have found success with Avalara’s Compliance Cloud™ platform.

One of the biggest challenges that retailers face, according to Peterson, is navigating the more than 70,000 tax jurisdictions that exist globally.

“The reports we get from Avalara enable us to develop a smooth process for pulling the information we need, preparing the returns and filing on time,” says Bob Romano, vice president of finance at Life is Good. “Avalara’s accurate tax decision engine and excellent reporting capabilities make an easy transition possible. And our process is better because we have the information we need.”

As the tax compliance landscape continues to become more challenging, Peterson encourages retailers to adopt tools that will automate the process and keep them fully compliant. “Avalara tackles the big pain points so our customers don’t have to worry about missed tax filing deadlines, errors in rate calculation, or expired or invalid exemption certificates,” Peterson says.

THE BATTLE IN THE STATES

SOUTH DAKOTA SUES FOUR BIG ONLINE RETAILERS OVER SALES TAXES

In a separate lawsuit, catalog and e-retailer trade associations sued the state. The legal battle could end up at the U.S. Supreme Court, which previously ruled e-retailers do not have to collect sales tax in states where they have no physical presence.

By Sandra Guy

The state of South Dakota has filed a lawsuit in April 2016 against four big online retailers seeking to force them to comply with a new state law that requires them to collect and remit sales tax even if they have no physical presence in South Dakota.

The state sued Newegg Inc., No. 17 in the Internet Retailer 2016 Top 500 Guide; Overstock.com Inc. (No. 29); Systemax Inc. (No. 32); and Wayfair LLC. (No. 24) in a circuit court in Hughes County, where the state capital of Pierre is located. The suit seeks the court to affirm that South Dakota may require the four web-only retailers to collect and remit sales tax.

The lawsuit is explicitly aimed at forcing the U.S. Supreme Court to reverse its 1992 ruling in a case known as *Quill Corp. v. North Dakota* in which the high court rules that only a company with a physical presence in a state—such as a store, office or warehouse—could be required to collect sales tax from state residents. The lawsuit says in the first paragraph of the summary, “The State acknowledges that a declaration in its favor will require abrogation of the United States Supreme Court’s decision in *Quill Corp. v. North Dakota*.”

Matt Strathman, associate general counsel at Newegg, said Friday, “This lawsuit is a direct attack on established U.S. Supreme Court precedent that retailers around the nation have relied upon for decades. Newegg believes South Dakota’s new law is unconstitutional, and intends to defend itself vigorously.” Wayfair declined to comment. The two other retailers named in the lawsuit did not immediately respond to requests for comment.

The lawsuit is based on legislation that South Dakota Gov. Dennis Daugaard signed into law March 22. It requires retailers to register by April 25 with the state Department of Revenue, committing to comply with the law as of May 1. Or retailers can notify the state that they do not meet the requirements of the law, which only apply to out-of-state merchants that sell at least \$100,000 or complete at least 200 transactions annually with South



South Dakota Gov. Dennis Daugaard

THE BATTLE IN THE STATES, cont.

Dakota residents. The law authorizes the state to sue retailers that fail to register without having to first levy assessments on those retailers.

The state Department of Revenue sent notices to 206 retailers saying they likely would meet the criteria set out in the law, and 40 have registered to collect the tax so far, a department spokesman says. In its lawsuit the state says the Revenue Department developed a formula based on its own data to determine which retailers would be required to register under the law. He would not elaborate on the formula, or comment on why Amazon.com Inc. (No. 1 in the Top 500) wasn't among those sued.

Amazon, which has opened over 100 distribution and sorting centers around the country, collects sales tax in 28 states, but not in South Dakota. Amazon declined to comment.

Meanwhile, the American Catalog Mailers Association and NetChoice, trade associations for catalog and online retailers, on Friday sued South Dakota, challenging the constitutionality of the state's law. That suit also was filed with the circuit court in Hughes County, South Dakota.

The trade associations allege South Dakota's new sales tax law violates federal law, and ask that the law be set aside immediately, says Steve DelBianco, NetChoice executive director. The groups' suit claims the South Dakota law violates the U.S. Constitution's Commerce Clause and guarantees of due process. The Commerce Clause says Congress alone can regulate interstate commerce, and the due process provisions require a definite link and minimum connection between the state and a person it seeks to tax. "An out-of-state retailer whose only connection with South Dakota is to fulfill the South Dakota customers' requests does not meet the minimum contact test of the due process clause," DelBianco says.

"The South Dakota law acknowledges it would require a change in federal constitutional doctrine," DelBianco says. "The law was designed to fast-track to the state Supreme Court and on to the U.S. Supreme Court this challenge to the Quill doctrine."

South Dakota doesn't like that bricks-and-mortar retailers collect the sales tax but online retailers don't, says Stephen P. Kranz, partner with McDermott Will & Emery LLP, the law firm that successfully represented Quill before the U.S. Supreme Court in the 1992 case. Quill Corp. was a catalog retailer of office supplies and equipment that subsequently was acquired by Staples Inc., No. 5 in the Top 500 and No. 21 in the 2016 B2B E-Commerce 300, which ranks the leading companies in North America by their online sales to businesses, government agencies and other enterprises.

This lawsuit is a direct attack on U.S. Supreme Court precedent that retailers have relied upon for decades.'

"They (South Dakota) are trying to force all retailers to collect sales tax or haul those who don't up to the U.S. Supreme Court," Kranz says. The aim is to try to overturn the 1992 Supreme Court decision that protected companies without a physical presence in a state from collecting sales tax, Kranz says.

"The questions being raised are ultimately constitutional questions that would need to be reviewed by the U.S. Supreme Court," Kranz says of both lawsuits.

Kranz says more than 12 state legislatures have enacted laws challenging the 1992 Supreme Court decision and he expects as many as eight more will do so this year.

South Dakota has now joined Alabama and Colorado in becoming the front-line aggressors in this battle, Kranz says. Louisiana this year tried to force out-of-state online retailers to collect sales tax by defining relationships with marketing websites that send traffic to retailer sites as constituting a physical presence in the state. That prompted Amazon to cut off ties to affiliate websites in Louisiana to avoid having to collect sales tax there.

THE BATTLE IN THE STATES, cont.

BLUE NILE STOPS SHIPPING TO SOUTH DAKOTA

Web-only jewelry retailer Blue Nile reacted to a new state law that, effective May 1, requires retailers without a physical presence in South Dakota to collect sales tax on online orders.

By Matt Lindner



At least one major online retailer has stopped doing business in South Dakota as a direct result of the state's new online sales tax collection law.

A spokesman for online jeweler Blue Nile Inc., No. 82 in the Internet Retailer 2016 Top 500 Guide, said in early May 2016 the company would halt shipments to the state for the foreseeable future.

"Unfortunately, South Dakota's law is in direct contradiction to federal law and we made the difficult decision to temporarily suspend shipping to South Dakota until this unconstitutional law can be addressed," the

spokesman says. "I can't comment on specific sales figures, but we are disappointed we can no longer ship to our customers in South Dakota."

The new law aims to force the U.S. Supreme Court to reconsider its 1992 ruling in *Quill Corp. v. North Dakota*, which effectively had allowed web-only retailers to avoid collecting sales tax in most states. That case found that only a company with a physical presence in a state—such as a store, office or warehouse—could be required to collect sales tax from state residents. The South Dakota lawsuit says in the first paragraph of the summary, "The

THE BATTLE IN THE STATES, cont.

State acknowledges that a declaration in its favor will require abrogation of the United States Supreme Court's decision in *Quill Corp. v. North Dakota*."

As of May 1, large online retailers that sell in South Dakota had to begin complying with a new law that requires them to collect sales tax and remit it even if the retailer does not have a physical presence in the state. The Remote Seller Compliance law (Senate Bill 106) was signed into law by Gov. Dennis Daugaard on March 22 and requires all retailers who do more than \$100,000 in sales in South Dakota or complete at least 200 electronic transactions in a calendar year to collect sales tax, even if they do not have a physical presence. South Dakota's sales tax rate is currently 4%; it will go up to 4.5% on June 1.

South Dakota notifies hundreds of e-retailers that they may be subject to the new law.

Top500Guide.com data shows Blue Nile had \$480.1 million in web sales in 2015, up 1.4% from \$473.5 million. A spokesman for the South Dakota Department of Revenue did not return a request for comment on Blue Nile's decision to stop shipping to the state.

More retailers may follow Blue Nile's lead, however.

David Escobar, senior manager of digital marketing for Florida-based department store chain Bealls Inc. (No. 359 in the Top 500), says he was never notified about the change in South Dakota's online sales tax collection policy. He says if he had been notified, he would have acted swiftly.

"If we are now on the hook for sales tax, the first thing we will do is fire all affiliates and marketing partners who reside in the state," he says. "We would then do anything else to reduce/eliminate nexus there." Nexus is a legal term for a physical presence in the state. Some states have passed laws declaring that an online retailer is deemed to have nexus if it works with online affiliates based in the state.

South Dakota sent notices to 206 retailers informing them

that they might be affected by the new law.

Online wine retailer NakedWines.com Inc. (No. 322) began shipping to South Dakota in January, before the legislation went into effect. NakedWines.com winemaker Ryan O'Connell says the company was required to register to collect and remit sales tax in South Dakota before being able to obtain its direct wine shipper's permit to the state.

At the beginning of this year, South Dakota began requiring all wineries shipping to its residents to obtain a \$100 annual permit, which requires wineries to collect any city sales tax in addition to state sales tax.

"We've taken taxes into account for sales into South Dakota since the beginning of shipping to that state, so there won't be any difference for our (customers)," O'Connell says.

David Wolfe, CEO of online-only mattress retailer Leesa, learned of the new law when Internet Retailer contacted him.

"We are now looking at it," he says. "If it applies to us we will register."

A spokesman for the South Dakota Department of Revenue says more than 40 remote sellers have registered for a South Dakota Sales Tax License because of the new law, though he declined to say which ones.

Online retail group Etailz Inc. (No. 267) did register with South Dakota. Etailz owns and operates several retail websites, including GreenCupboards.com, EcoMom.com and Vault Electronics.com.

Chief financial officer Bill Kinzel says the state first reached out to Etailz about two months ago to inform the retailer of the new law.

"It was just a letter that they mailed out that said effective X date, you have to be registered and collecting sales tax in the state," he says. "They were pretty aggressive in reaching out from what I can tell. That's one of the first states that's reached out to Etailz directly and said, 'We want you to register.'"

Etailz registered because collecting the tax felt almost inevitable, Kinzel says. "The alternative is to put your head in the sand and either pretend that it doesn't exist or fight it in the courts," he says. "It's a gamble that we don't want to take."

THE BATTLE IN THE STATES, cont.

AMAZON ENDS ITS AFFILIATE PROGRAM IN LOUISIANA OVER A SALES TAX LAW

The online retailer reacts to the so-called Amazon tax by terminating its affiliates in Louisiana, as it has done in other states.

By Sandra Guy

Amazon.com Inc. shuttered its affiliate program in Louisiana in April 2016 after the Legislature passed a law to force online retailers to collect sales tax when a sale results from a referral from an affiliate website based in Louisiana. It's the latest in a long-running legal battle over the issue.

Affiliates receive a commission comprising a percentage of the sales price when online shoppers buy products after clicking on an affiliate's website link to a product on Amazon.com, No. 1 in the Internet Retailer 2015 Top 500 Guide, or other retailers. The Louisiana law, enacted during a recent 25-day special session of the legislature, deems an online retailer to have a physical presence in the state, or "nexus" in legal terms, if it works with online affiliates based in Louisiana. That nexus triggers the requirement to collect sales tax and remit it to the state. The law took effect April 1.

Amazon did not respond to a request for comment or say how much its affiliates might lose in revenues, but its affiliate website lists Louisiana residents as being ineligible to participate. Other states whose residents cannot participate in the program are Arkansas, Maine, Missouri, Rhode Island and Vermont.

Richard Carbo, communications director for Louisiana Gov. John Bel Edwards, says the state is "in a severe budget crisis" and the so-called Amazon tax was one of many options the legislature approved to raise money.

Carbo says state officials were not clear how or when Amazon, which has no employees or physical presence in Louisiana, would respond to the new law.

Amazon's move is the latest in a lengthy battle over whether states can require out-of-state retailers or their affiliates to pay use taxes or sales taxes on online purchases. A 1992 U.S. Supreme Court ruling declared that an out-of-state retailer without any physical presence in a state, such as a store or warehouse, could not be required to collect and remit sales tax to that state. Two states—Colorado and Alabama—have enacted laws that appear to contradict that ruling in hopes they can get either a vote in Congress or bring the issue back to the U.S. Supreme Court for a review that would take into account the growth in online shopping. Of the 45 states and the District of Columbia that collect sales taxes, 24 states have instituted some form of simplified collection process for out-of-state online and catalog retailers who voluntarily collect the tax. Another 13 states are considering legislation requiring the sales-tax collection, according to the National Conference of State Legislatures. Five states—Alaska, Delaware, Montana, New Hampshire and Oregon—do not have a sales tax.

Yet states have less to gain than when the debate started, because Amazon now collects sales tax in 28 states where it has a physical presence, in many cases fulfillment centers. Those states comprise 84% of the U.S. population based on U.S. Census Bureau data.

THE BATTLE IN THE STATES, cont.

BATTLE LINES FORM AGAIN OVER ONLINE SALES TAX RULES

States aim for either a vote in Congress or a U.S. Supreme Court ruling to open the way for requiring e-retailers to collect and remit sales tax.

By Sandra Guy

The question of whether online retailers must collect sales tax is on the agenda again, as state officials seek to push either Congress or the U.S. Supreme Court to act on a national mandate.

The front lines in this battle now are in two states: Colorado and Alabama.

In Colorado, a federal appeals court in February 2016 reversed a lower court ruling against a state law that requires out-of-state retailers to inform consumers of their obligation to pay “use tax”—effectively the same thing as a sales tax—on online, telephone and mail-order purchases and to report purchases by Colorado residents to the state Department of Revenue.

The Alabama Department of Revenue, meanwhile, adopted a rule Jan. 1, 2016, requiring out-of-state retailers to collect sales tax. Joe Garrett, Alabama’s deputy revenue commissioner, says they took that step knowing that the rule contradicts a 1992 U.S. Supreme Court ruling that says states can only require companies with a physical presence in the state to collect and remit sales tax. Thus, online retailers without a store, warehouse or office in a state must not collect sales tax from consumers in that state. The consumer is legally obligated to pay the sales tax, but few do.

The Alabama tax-collection agency is hoping a retailer will sue the state and start the process of getting a resolution either in Congress or at the U.S. Supreme Court, Garrett says. He says state officials are frustrated by the lack of action in Congress but encouraged by an opinion



U.S. Supreme Court Justice Anthony Kennedy wrote last year in which he said that “dramatic technological and social changes” since the 1992 Supreme Court ruling have made the states’ position stronger. Kennedy wrote that “the legal system should find an appropriate case” for the court to reconsider its 1992 ruling.

While seeking to provoke a legal battle, Alabama also took steps last year to address online retailers’ complaints that a national sales-tax collection requirement would force them to collect sales tax in some 10,000 taxing jurisdictions around the United States, each with its own rates and rules about which items are covered. Alabama said online and catalog retailers based outside the state could pay a single sales tax rate and submit to a single audit, regardless of the location in Alabama of the consumer making the purchase. The first collections

THE BATTLE IN THE STATES, cont.

were due Feb. 20, and more than 30 remote sellers are adhering to the process, Garrett says. He could give no total amount collected so far.

In Colorado, the appeals court ruling revived a law passed in 2010 but never implemented. The law would require retailers with \$100,000 or more in annual sales to Colorado residents to provide those consumers with a report of their past year's purchases and notify them of their responsibility to pay use tax on those purchases. The law also required the retailers to provide the state with an annual report listing the names, billing addresses, shipping addresses and the total amount of purchases for each of their Colorado customers.

Alabama is inviting a challenge to its new online sales tax rule, as a way of getting the issue into federal court.

The Colorado law was never implemented because the presiding judge in the case, Robert Blackburn, of the U.S. District Court of Colorado, wrote that it placed unique burdens on out-of-state retailers and was discriminatory. That ruling came in a lawsuit brought by the Direct Marketing Association, a trade group for direct-to-consumer retailers.

But the 10th U.S. Circuit Court of Appeals reversed that ruling this week. The appeals court upheld the law's constitutionality, saying it doesn't discriminate or unduly burden interstate commerce. The appeals court sent it back to the Colorado district court for a re-hearing and final ruling. The circuit court ruled the law made no distinction between in-state and out-of-state retailers and provides no advantage to in-state over out-of-state retailers.

Forty-five states and the District of Columbia have sales taxes. Of those, 24 states have instituted some form of simplified collection process for out-of-state online and

catalog retailers who voluntarily collect the tax. Those 24 states pay for software to automatically tally the tax for the remote sellers who volunteer to collect it, according to Neal Osten, director of the Washington, D.C., office of the National Conference of State Legislatures, which supports bills that have been submitted to Congress in recent years requiring retailers to collect and remit sales tax on online and catalog orders, regardless of where the retailer is based.

Another 13 states are considering legislation requiring the sales-tax collection, the NCSL says.

Organizations such as the National Retail Federation, whose members are primarily store-based retailers, also back such legislation, arguing that online retailers get an unfair advantage because consumers consider they get a discount when they buy online and don't have to pay the sale tax they would pay in a local store.

Such online sales tax legislation passed the U.S. Senate in 2013, but has been blocked primarily by conservative House Republicans who oppose it as a new tax. Yet Senate Republican leaders vow to bring up some form of the legislation for a vote this year, according to an eBay blog post.

University of Tennessee economist Don Bruce estimated in 2009 that states were losing \$23 billion a year in revenue by being unable to collect the sales tax on all goods, even if bought online or via catalog. Since that calculation was made, Amazon has started collecting sales tax in 28 states that cover 84% of the U.S. population, thus reducing the amount states would gain if web-only and catalog retailers had to collect sales tax. Bruce says he hasn't updated his forecast, but he believes the obvious solution is a national approach.

"You've got transactions that are identical—two shoppers are buying the same item—but they're being taxed differently based on how the transaction is being completed," Bruce says "That's an issue of fairness because that is a tax disadvantage to local retailers trying to run their businesses."

AMAZON AND THE SALES TAX DEBATE

HAS COLLECTING TAXES HURT AMAZON'S SALES?

By Don Davis

The big question for retailers that sell primarily through websites or catalogs is: Would collecting sales tax hurt my sales? Recent data about the sales of Amazon.com Inc. suggest perhaps not.

Amazon provides a good test because it collects sales tax in a lot more states now than it did just a few years ago: 28 as of mid-summer 2016, versus six states four years earlier. Amazon, which for years limited its warehouse footprint to avoid collecting sales tax, has to collect in many more states now that it has covered the United States with more than 100 distribution centers in recent years as part of its strategy to offer shoppers fast and often free delivery.

Ohio State University researchers released a study in 2014 that examined five states in which Amazon had begun collecting sales tax in 2012 or 2013—California, New Jersey, Pennsylvania, Texas and Virginia—and concluded that requiring payment of sales tax reduced Amazon's sales in those states by 9.5%. They noted that there was an even bigger decline—15.5%—in purchases over \$150, suggesting consumers might be more put off by paying the tax on higher-priced items.

But more recent data tells a different story. Slice Intelligence, which collects purchasing data from the email receipts of some 4 million consumers, in 2016 analyzed purchases on Amazon in two states where Amazon had begun collecting sales tax—Colorado and South Carolina—and compared Amazon's sales growth and market share in those states to those in surrounding states.

The Slice data shows Amazon's sales in Colorado were growing 8% slower in Colorado than in seven adjacent

states before it began collecting sales tax, and an identical 8% slower afterwards. In South Carolina, Amazon's sales were growing 3% faster in the pre-tax period than in three adjacent states and 5% faster after it began collecting sales tax. In both cases, says Slice vice president and principal analyst Ken Cassar, "Statistically, there is no difference."

Cassar says Amazon Prime, which offers consumers free, two-day shipping for a year for a \$99 fee, has made Amazon shoppers less price-sensitive. "They value the convenience more than they value the tax saving," he says. "The growing importance of convenience is one of the key trends impacting the e-commerce space today, beyond just Amazon. Price and selection are still key pillars of the channel, but they aren't as dominant as they used to be."

Amazon has a big advantage over most competitors in that it has signed up 63 million households for Prime, and those households represent 52% of Amazon shoppers, according to Consumer Intelligence Research Partners LLC, an equities research firm. That's a lot of consumers who may be willing to pay sales tax if it means getting free and fast shipping.

There's not a great deal of recent data on how consumers would respond to paying sales tax on online purchases. Two surveys by Bizrate Insights of more than 5,000 U.S. online shoppers offers mixed signals. When asked in 2013 what they would do if asked to pay sales tax on a purchase that's not taxed today 26% said they would buy more locally instead of online, while 28% said it would not impact their purchase. But in 2011, asked whether they considered not making an online purchase because the total included sales tax, 75% said no.

AMAZON AND THE SALES TAX DEBATE, cont.

Today's online consumers are not likely to be overly deterred by the requirement to pay sales tax at e-retail sites, says Steve DelBianco, executive director of e-commerce trade association NetChoice, who says he's seen no data that shows higher shopping cart abandonment after sales

tax is applied to online orders. "Consumers go online for choice, value and convenience," DelBianco says, "not to avoid paying sales tax."

Given the growing pressure in favor of online sales tax collection, online retailers can only hope he's right.

What consumers say about how online sales tax would influence them

Question: If sales tax starts being applied to online purchases where it isn't today, which of the following best describes the potential impact to your online shopping behavior?

No change—other factors that influence my choice to shop online are more important: 28%

I will put more effort into finding online coupons, discounts and promotions: 27%

I will buy locally more often instead of online: 26%

I will use price comparison shopping engines more heavily: 16%

Other: 2%

Source: Bizrate Insights, August 2013 survey of 5,723 U.S. online consumers

AMAZON IS LOSING ITS SALES-TAX ADVANTAGE

A report says that web taxes drive consumers to shift spending to competitors and bricks-and-mortar merchants.

By Thad Rueter

Online shoppers spend less with Amazon.com Inc. in states where the e-retailer must collect sales taxes, according to a report released in April 2014 by researchers at Ohio State University. Competing retailers, meanwhile, absorb some of that lost spending, the report says.

Amazon collects sales taxes in 20 states, according to the brand new Internet Retailer 2014 Top 500 Guide, released this week. Research that focused on five of those states—California, New Jersey, Pennsylvania, Texas and

Virginia—found that taxing online purchases led to a 9.5% drop in the value of products bought by households from Amazon. Sales tax rates in those states range from 5.0% to 8.2%.

The total amount spent with Amazon, No. 1 in the 2014 Top 500 Guide, in those states decreased by 2.8%, says the report, "The 'Amazon Tax': Empirical Evidence from Amazon and Main Street Retailers." Those five states enacted online sales taxes in 2012 and 2013.

AMAZON AND THE SALES TAX DEBATE, cont.

- For orders costlier than \$150, consumers in those taxing states have decreased their Amazon spending by 15.5%. For orders of \$300 or more, spending has declined by 23.8%.
- The overall likelihood of consumers shopping at Amazon in any given week has declined by 0.7 percentage points. The number of transactions per week dropped 4.2% after taxes were enacted.
- Consumers in those states have shifted spending to other retailers in the wake of new taxes. Other online retailers experienced a 23.7% increase for purchases of more than \$300; the report analyzed purchases from 25 top retailers listed in Stores magazine to arrive at that conclusion. Overall, online purchases from Amazon's competitors increased 19.8% after tax collection started.
- Local bricks-and-mortar retailers also benefited from online sales taxes, gaining a 2.0% increase in sales.

"We conclude, to a small degree, [that] tax legislation achieved its objective of restoring retail activity to local communities, though most of the gains in 'leveling the playing field' are garnered by the online operations of retailers," states the report, written by Ohio State University finance professor Itzhak Ben-David and finance doctoral students Brian Baugh and Hoonsuk Park.

Consumers buying high-ticket items are more likely to be sensitive to a web retailer collecting sales tax.

Though other e-retailers face having to collect sales taxes under various state laws—Overstock.com Inc., No. 31 in the Top 500, has aggressively opposed the spread of web sales taxes—the levies typically go by the moniker "Amazon

Tax." That not only acknowledges the scope of Europe and North America's largest online retailer—the new Top 500 Guide shows a 20.3% year-over-year sales increase for Amazon in 2013—but the tendency of such taxes to hit Amazon purchases hardest of all, either directly through its e-commerce site or via affiliates that take commissions for Amazon purchases stemming from their blogs.

Consumers residing in the states in which Amazon collects sales tax comprise nearly 60% of the U.S. population, according to a recent estimate from global supply chain and logistics consulting firm MWPVL.

Amazon, judging the direction of the wind and speeding to expand its fulfillment network, has thrown its support behind a federal Marketplace Fairness Act. It would allow states to mandate sales tax collection by online and catalog retailers even if they have no physical in-state presence such as stores or distribution centers—a legal concept known as nexus. Current federal law says states can mandate tax collection only by retailers with an in-state physical presence such as stores or distribution centers. Overstock and eBay Inc. oppose the bill, which remains before the U.S. House of Representatives.

Amazon has negotiated deals with various state officials to build more fulfillment centers near major cities—part of the e-retailer's push to get quicker deliveries to more shoppers—and those deals have often involved Amazon promising to support the Marketplace Fairness Act or a delay in state sales tax collection.

Amazon offers no comment today about specific parts of the new sales-tax report. A spokesman for the e-retailer says: "As analysts have noted, Amazon offers the best prices with or without sales tax." The Ohio State study provides no speculation on what Amazon might do make up for the diminishing advantage of not having to collect sales taxes. At least one recent supply chain and Amazon fulfillment expert has said the e-retailer will have to raise the bar on its service, perhaps through more same-day e-commerce deliveries.

AMAZON AND THE SALES TAX DEBATE, cont.

SEVEN OF NINE US CONSUMERS PAY SALES TAX WHEN SHOPPING ON AMAZON

The largest online retailer now collects sales tax from 77.5% of the U.S. population.

By Matt Lindner

With the recent addition of Ohio, the largest U.S. online retailer now collects sales tax from more than three-quarters of the population of the United States.

Amazon.com Inc., No. 1 in the 2015 Internet Retailer Top 500 Guide, in June 2015 started collecting sales tax from Ohio residents, making Ohio the 25th state in which it collects sales tax. Ohio has a state sales tax rate of 5.75%. According to the U.S. Census Bureau, that means

247.2 million people, or 77.5% of the U.S. population, now live in states where Amazon collects sales tax. [Editor's note: As of Oct. 1, 2015, Amazon began collecting sales tax in Michigan, the last of the 10 most populous states where it collects tax. As of mid-2016 Amazon collected sales tax from 28 states representing 84% of the U.S. population.]

Five states—Alaska, Delaware, Montana, New Hampshire, and Oregon—do not have a statewide sales tax.

In February, Amazon began collecting sales tax from Illinois residents. But an investment analyst who covers Amazon said at the time that he did not think collecting sales tax would have much of an impact on Amazon's overall sales in the state.

"Our checks have suggested there is a short-term benefit to their business in the months leading up to the start of tax collection, followed by a slowdown that lasts a few months after they begin collecting," says Colin Sebastian, an analyst with Robert W. Baird & Co. "However, there is little data to support the view that taxes have a longer-term negative impact on Amazon."

Sebastian says he thinks any negative overall impact that adding a sales tax might have on Amazon is mitigated by the fact that people shop the site primarily for convenience and selection.



AMAZON AND THE SALES TAX DEBATE, cont.

Editor's note: As Amazon began expanding its distribution around the United States it negotiated with states over when it would begin collecting sales tax. Here are two examples from California in 2014 and New Jersey in 2012.

AMAZON BARGAINS WITH STATES ON TAXES

Amazon.com Inc. announced in August 2014 open its fifth warehouse in California, this one in Redlands, located in San Bernadino County east of Los Angeles.

The e-retailer's announcement today represents the latest fruit from Amazon's September 2011 deal with state officials that requires larger retailers to collect sales taxes from residents. Part of the deal called for Amazon to build more fulfillment centers in the state.

Amazon, No. 1 in the Internet Retailer Top 500 Guide, opened its first California warehouse two years ago, with the other facilities located in the cities of San Bernardino, nearby Moreno Valley, and Patterson and Tracy, both of which are located near the San Francisco Bay Area. In total, the e-retailer operates nearly 5-million square feet of warehouse space in the state.

The Redlands warehouse will spread over 700,000 square feet, Amazon says. Redlands workers will "pick, pack and ship large items to customers such as big-screen televisions or kayaks, for example," Amazon says. The web-only merchant did not say when the warehouse would open. Clarion Partners will own the Redlands building

while Trammel Crow Co. will manage construction.

"We have found great talent in the state and we're excited to be growing quickly to serve our customers," says Mike Roth, Amazon's vice president of North America operations.

Amazon keeps increasing its spending on fulfillment, devoting \$4.70 billion to such operations in the first half of 2014, up 29.5% from the same period last year, according to the e-retailer's Q2 financials. As that spending increases, Amazon also expands its same-day delivery services. It recently made it easier for consumers in Baltimore, Dallas, Indianapolis, New York, Philadelphia and Washington, D.C., to receive same-day deliveries of certain products.

The e-retailer operates more than 100 warehouses around the world and maintains nearly 50 million square feet of fulfillment space in North America, according to Scot Wingo, CEO of ChannelAdvisor Corp., which helps retailers sell on Amazon, and Colin Sebastian, a

longtime Amazon observer and e-commerce analyst who works for Robert W. Baird and Co.



New Jersey: Gov. Chris Christie announced in May 2012 that Amazon.com would start collecting sales taxes next year for purchases made by New Jersey residents,

The agreement called for the retailer, No. 1 in the Internet Retailer Top 500 Guide, to begin collecting taxes on July 1, 2013, and for Amazon to build two warehouses in New Jersey. Amazon had similar deals in other states, including Virginia, Indiana and Tennessee.

AMAZON AND THE SALES TAX DEBATE, cont.

"Today's announcement marks a first step toward a long-term relationship with Amazon," New Jersey Gov. Chris Christie said in announcing the deal at a press conference. Also speaking was Amazon vice president of global public policy Paul Misener who said the e-retailer would explore further opportunities to expand in New Jersey. "We have a history of growing in the states that have welcome us," Misener said. Among those favored states has been Kentucky, where Amazon operates four fulfillment centers and recently announced plans for a customer service facility. Amazon has collected sales tax in Kentucky since 2005.

Christie said Amazon's new fulfillment centers would bring some 1,500 full-time jobs to the state as well as thousands of seasonal and part-time jobs. The investment in the warehouses could amount to \$130 million, he said.

"I'm pleased Amazon is committed to helping New Jersey grow and create quality jobs," Christie says.

The general sales tax rate in New Jersey is 7%, according to the state's taxation division. As is the case in many other states, New Jersey residents are already required to remit taxes for online retail purchases, though state officials have said few shoppers do so.

Christie said it was likely that Amazon would seek financial assistance from the state's Economic Development Authority to pay for the new warehouses.

In its previous deals with other states Amazon promised to work to support proposed federal legislation that would require more online retailers to collect sales tax. Under existing federal law, states can only require sales tax collection by retailers who have a physical in-state presence like stores or distribution centers.



A REMINDER FOR B2B ONLINE SELLERS

ONLINE SALES TAX—WHAT B2B SELLERS SOMETIMES FORGET

By Paul Demery



With all the hoopla over pending new federal legislation that could force many more online retailers to collect sales tax, the legislation also pertains to online B2B sellers. Those companies need to ensure they're crossing their T's in tax forms or potentially face tough audits, a tax attorney cautions.

When the U.S. Senate overwhelmingly passed a bill in 2013 designed to let states force a widespread increase in sales tax collection by online and catalog-based sellers, it rekindled alarm among retailers concerned about the cost and liabilities the legislation would bring if passed in the House and signed into law. Retailers are worried about the cost of collecting and remitting tax across about 10,000 taxing jurisdictions and about having to face tough tax audits in any of the 45 states plus the District of Columbia with sales tax laws.

But the bill, known in the Senate as the Marketplace Fairness Act, also carries legal implications for online and catalog wholesalers and others involved in business-to-business commerce.

The wholesale industry, for example, is generally exempt from processing sales tax as long as a purchaser is buying something for resale. For example, if an apparel manufacturer is buying buttons for sweaters that it will then resell to retailers or to consumers, it does not need to pay sales tax on its button purchases. However, if a manufacturer is buying office supplies, for example, for its own use, it would have to pay sales tax, just as a consumer would. There are also numerous industry-specific exemptions from sales tax, such as when an agricultural business buys products for agricultural purposes.

Even when the transaction is exempt from sales tax, however, the buyer is required by tax laws to provide to the seller an exemption certificate, and the seller must be prepared to show that it requested that certificate in order to justify not collecting sales tax from the customer.

It's likely many online B2B sellers are not doing that, says Stephen Kranz, a Washington, D.C.-based partner who specializes in sales tax law at Chicago law firm McDermott Will & Emery LLP. Current federal law says states cannot require an online seller to collect sales tax in states where it does not have a physical presence,

A REMINDER FOR B2B ONLINE SELLERS, cont.

or nexus, such as sales offices or distribution centers. Kranz says many wholesalers and other B2B online and catalog sellers may not bother to require tax-exemption certificates from their business customers in states where a company has no nexus, as they may look at the recording of customers' tax-exemption certificates as an unnecessary chore and expense.

Online sales tax laws apply equally to companies selling to businesses as to consumers.

However, if the Marketplace Fairness Act or similar legislation gets enacted, B2B online and catalog sellers will face the same responsibilities as retailers to collect sales tax and remit it to states, regardless of whether they have nexus in a state. "Online and catalog wholesalers will need to care about the Marketplace Fairness Act, because it will require them to gather and maintain tax-exemption certificates," Kranz says. "They should be doing that today, anyway, to maintain proper records on customers."

The most common ways sellers run into problems, he adds, is through one-off situations where a buyer with a specific sales tax-exemption either purposely or unwittingly uses it to buy a product not covered by the exemption. That would include a manufacturer buying office supplies for its own use, or a wholesaler purchasing a computer for an executive. "Most problems are usually not in the resale area," Kranz says, noting that wholesalers, manufacturers and others usually develop a sound routine for recording tax-exemption certificates from customers who resell what they purchase.

Problems more often occur, he says, when a buyer at a business with, say, a tax-exemption certificate for agricultural purposes, purchases a product like a television that may not obviously have an agriculture-related purpose. It may be hard to justify not collecting sales tax in a state tax audit. Kranz cautions that online B2B sellers need to ensure that their web sites have conspicuous and easy-to-use forms for submitting information on tax-exemption certificates, and that they properly store that information where it can be easily accessed if necessary for an audit.