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## **South Dakota v. Wayfair Inc.**

**Most Vendors Required to Collect Sales Tax on Internet Sales**

**What All Internet Vendors Must Do**

June 22, 2018

By Attorney Morris Robinson, CPA, LLM  
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# South Dakota v. Wayfair, Inc.

## Most Vendors Required to Collect Sales Tax on Internet Sales

### What All Internet Vendors Must Do

By Attorney Morris N. Robinson, CPA, LLM<sup>1</sup>

June 22, 2018

On June 21, 2018, the United States Supreme Court handed down its 5-to-4 decision in South Dakota v. Wayfair, Inc. ([click here to read the slip opinion](#)). The majority opinion, authored by Justice Kennedy, held that states may lawfully collect sales taxes from out-of-state internet vendors who sell tangible personal property or services to in-state residents even though these out-of-state vendors do not have a physical presence within the state.

The law under constitutional examination applied “only to sellers that deliver more than \$100,000 of goods or services into South Dakota or engage in 200 or more separate transactions for the delivery of goods and services into the State on an annual basis. S. B. 106, §1.” (Wayfair, Pages 22-23.) Thus, out-of-state vendors with less than \$100,000 of in-state sales or less than 200 separate in-state transactions

were exempted from the obligation to collect and remit sales taxes to South Dakota. The majority noted that the South Dakota statute satisfied both the “due process clause” and the “commerce clause” requirements of the United States constitution, which help create and maintain a common market throughout the United States. Specifically,

#### **Observation:**

The majority noted that the South Dakota statute satisfied both the “due process clause” and the “commerce clause” requirements of the United States Constitution.

South Dakota’s tax system includes [three] features that appear designed to prevent discrimination against or undue burdens upon interstate commerce. First, the Act applies a safe harbor to those who transact only limited business in South Dakota. Second, the Act ensures that no obligation to remit the sales tax may be applied retroactively. S. B. 106, §5. Third, South Dakota is one of more than 20 States that have adopted the Streamlined Sales and Use Tax Agreement. This system standardizes taxes to reduce administrative and compliance costs: It requires a single, state level tax administration, uniform definitions of products and services, simplified tax rate structures, and other uniform rules. It also provides sellers access to sales tax administration software paid for by the State. Sellers who choose to use such software are immune from audit liability. (Wayfair, Page 23. Emphasis added.)

In light of Wayfair, we can expect additional states to join the Streamlined Sales and Use Tax Agreement, discussed above. We can also expect many additional states to promptly adopt statutes similar to South Dakota’s.

(continued)

In light of Wayfair, what must internet vendors do? Allow me to suggest an effective three-part strategy of evaluation, compliance and voluntary disclosure.

## 1. Evaluation

All internet vendors will want to reevaluate their exposure to sales tax laws, state-by-state, based on the following five types of nexus.<sup>2</sup>

- (1) Economic Nexus. The South Dakota law, described above, is an example of economic nexus. Under economic nexus laws, an out-of-state vendor is required to collect sales taxes if the out-of-state vendor has either (1) a significant number of in-state sales or (2) a significant dollar amount of in-state sales.
- (2) Click-Through Nexus. Under these laws, an out-of-state vendor is required to collect sales taxes on internet sales if the website used by the out-of-state vendor to make the in-state sale was maintained by a person or entity with nexus in the state.
- (3) Agency Nexus. Under these laws, an out-of-state vendor is required to collect sales taxes on in-state sales if the out-of-state vendor has in-state agents who, for example, (1) set-up or repair tangible personal property for the out-of-state vendor; or (2) receive returns of merchandise.
- (4) Affiliate or Attributional Nexus. Under these laws, an out-of-state vendor is required to collect sales tax on in-state sales if the vendor is affiliated, such as through common ownership, with an entity with nexus in the state.
- (5) “Old-Fashioned” Nexus. Under these laws, an out-of-state vendor is required to collect sales tax on in-state sales if the vendor has employees, offices, inventory or other property in-state. Thus, a vendor who is exempt from in-state income taxation under Public Law 86-272 (because its in-state salespeople merely solicit sales) is nonetheless required to collect sales taxes on in-state sales.<sup>3</sup>

## 2. Compliance

Internet vendors who meet the statutory requirements of any one of the above-listed laws should collect and remit the sales tax. Intentional noncompliance with the sales tax laws is not good business policy and may even be a crime. If vendors do not collect a legally valid sales tax, the states may collect the tax, penalties and interest from so-called “responsible parties,” who are typically members of the vendor’s management. We have successfully represented so-called responsible parties. These cases are typically expensive and distracting for vendors and their managements. These cases are also time-consuming and difficult for the audit-defense team.

Compliance, however, can be a challenge. Commentators note that there are something like 12,000 separate and sometimes overlapping sales tax jurisdictions. Therefore, most vendors will want to work with service providers who can provide computerized mechanisms for remitting sales taxes, filing the related sales tax returns, and obtaining resale certificates and exemption certificates. As the majority in Wayfair noted, over 20 states provide sales tax software free of charge and internet vendors who use this software are immune from audit liability. Most vendors will want to consider using such compliance software.

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In light of Wayfair, what must internet vendors do? Allow me to suggest an effective three-part strategy of evaluation, compliance and voluntary disclosure.

### 3. Voluntary Disclosure

The Wayfair decision overruled Quill Corp. v. North Dakota, 504 U.S. 298 (1992), which held that imposition of state sales tax against an out-of-state vendor that solicited in-state customers with mail-order catalogs violated the dormant Commerce Clause. Based on Wayfair, states can expand the sales tax base on a going-forward basis. The Wayfair majority suggests that it might be unfair to *retroactively* apply a sales tax law based on economic nexus against out-of-state internet vendors who had not collected in-state sales taxes in reliance on the tax exemption provided by Quill.<sup>4</sup> Economic nexus, however, is only one form of nexus. As noted above, there are at least four other forms of nexus. These additional types of nexus were not overturned by the Wayfair case. Therefore, there is no unfairness involved when out-of-state vendors with other types of nexus exposure are required to collect sales taxes on in-state sales for prior periods.

It follows that all internet vendors should determine, on a state-by-state basis, if they have existing exposure to sales tax liability. Vendors with significant exposure are strongly advised to make a voluntary disclosure. The benefits of voluntary disclosure typically include (1) avoidance of criminal responsibility and (2) avoidance of penalties that typically can add an additional 50 percent or more to the underlying sales tax liability. A voluntary disclosure can be made either (1) on a state-by-state basis or (2)

“wholesale” under the Multistate Tax Commission voluntary disclosure program. For details on the benefits and mechanics of voluntary disclosure see my article entitled [State Voluntary Disclosure Programs: An Overview](#) (*State Tax Notes*, January 18, 2016).

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#### **Additional Information Available**

For additional information about the Wayfair case and its practical implications for e-commerce sellers, please call the author of this article, Attorney Morris N. Robinson, at 617-428-6900.

*End of Article*

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<sup>1</sup> Attorney Morris N. Robinson, CPA, LLM is Managing Director of M. Robinson Tax Law, a tax law firm boutique located in Boston’s Financial District. His practice emphasizes tax planning, tax audit defense, and tax compliance for businesses and individuals. He acknowledges the invaluable assistance of Attorney Yale Yechiel N. Robinson, Associate and Joseph Kelley, Paralegal.

<sup>2</sup> Nexus is the constitutional authority of a state to obligate out-of-state vendors to collect the sales tax.

<sup>3</sup> Public Law 86-272 only exempts an out-of-state vendor from in-state income taxation.

<sup>4</sup> The Wayfair majority noted that “[T]he Act ensures that no obligation to remit the sales tax may be applied retroactively.”