

South Dakota v. Wayfair Inc.: A Brief Overview

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Background on Sales/Use Taxation

Article IX, §8 of the Constitution of Michigan of 1963 states:

“Except as provided in this section, the Legislature shall not impose a sales tax on retailers at a rate of more than 4% of their gross taxable sales of tangible personal property.”

In most states, the sales tax is imposed on the end purchaser, and the retailer merely acts as a collection agent. Michigan is different in that the sales tax is levied on the retailer as a privilege for doing business in the state.

The use tax is a companion to the sales tax, and applies if there is a transaction that would normally be subject to the sales tax on which no taxes were collected and remitted by the seller.

Sales Taxation and Remote Sales

National Bellas Hess v. Department of Revenue of Illinois (1967)

- Established physical nexus as the standard for sales/use tax liability
- Bellas Hess had no sales people, outlets, or any other physical presence in Illinois
- “...the Court has never held that a State may impose the duty of use tax collection and payment upon a seller whose only connection with customers in the State is by common carrier or the United States mail.” – Potter Stewart

Quill Corporation v. North Dakota (1992)

- Although parts of *Bellas Hess* were overturned, the U.S. Supreme Court maintained that Quill did not have substantial nexus under the Commerce Clause of the U.S. Constitution.
- Compliance costs would be excessive.

Estimated Revenue Loss from Remote Sales

- If the seller doesn't collect and remit the sales tax, the responsibility falls upon the buyer to remit a use tax.
- The estimated revenue loss has grown substantially in recent years due to online shopping.

Fiscal Year	Traditional Mail Order	E-Commerce	Total Foregone Revenue
2000	\$149.3	\$37.3	\$186.7
2005	\$188.4	\$160.3	\$348.7
2010	\$174.1	\$173.5	\$347.6
2015	\$162.9	\$281.6	\$444.5
2017	\$168.0	\$300.1	\$468.1

Source: Michigan Department of Treasury

Attempts at Enforcement

- Collecting use tax on the Michigan individual income tax return (effective TY 1999)

Tax Year	Number of Returns Filed	Number Reporting Use Tax Liability	Total Use tax
1999	4,414,720	64,650	\$2,895,475
2010	4,459,933	104,707	\$4,056,857
2015	4,662,493	105,435	\$6,669,182
2018	4,784,036	93,035	\$5,593,960

Source: Michigan Department of Treasury

- Main Street Fairness (2014 PA 553 and 2014 PA 554)
Established “click-through” or affiliate nexus
Sometimes platforms dropped affiliate partners to eliminate the nexus

Enter Wayfair

In a 2015 case tangential to *Quill*, Justice Kennedy wrote “it is unwise to delay any longer a reconsideration of the Court’s holding in *Quill*.”

“Kill *Quill*” bills were introduced in a number of state legislatures to require out-of-state sellers to collect and remit sales taxes. South Dakota’s legislation required out-of-state sellers with more than 200 transactions or more than \$100,000 in sales to South Dakota over the prior twelve months to collect and remit sales taxes.

Wayfair, New Egg, and Overstock sued South Dakota, and the case was eventually heard by the U.S. Supreme Court, which in a 5-4 decision in June 2018 voted to overturn *Quill* and establish the principle of “economic nexus.” It was deemed that the perceived compliance costs were no longer an issue. In addition, the South Dakota law contained provisions to protect small businesses.

Michigan's Response

The Department of Treasury issued Revenue Administrative Bulletin 2018-16 on August 1, 2018 to apply the concept of economic nexus to sales and use tax collections in Michigan. Michigan adopted the same 200 transaction/\$100,000 gross receipts thresholds as the South Dakota law, but applied a slightly broader timeframe by applying the thresholds to the prior calendar year as opposed to the prior 12 months.

Out-of-state vendors were responsible for collecting and remitting sales/use taxes beginning October 1, 2018.

Current projections are \$168 million in FY 2018-19, \$225 million in FY 2019-20, and \$240 million in FY 2020-21.

The Next Step — Marketplace Facilitators

Marketplace facilitators (or platforms) such as Amazon, eBay, Walmart, Etsy, etc. can be classified as the vendor as opposed to the individual sellers. If the platform exceeds 200 sales or \$100,000 in sales, it becomes subject to the tax.

More than 20 states have already adopted marketplace facilitator laws, and legislation is being considered in at least a dozen other states.

Many of the laws contain a carve out for those platform participants that already meet the economic nexus standard.

Questions?

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