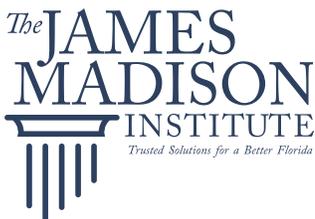


On Wayfair, Tread Lightly

Florida Should Not Repeat Other States' Mistakes on Remote Sales Tax Legislation

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Since the release of the Supreme Court's decision in the 2018 *South Dakota v. Wayfair* case, states have hurried to implement so-called "economic nexus" rules. This approach allows states to impose tax obligations on any business that sells into the state, even if it is located elsewhere. By now, nearly every state with a statewide sales tax has imposed economic nexus obligations in one shape or another. But with the pandemic putting new emphasis on tax revenues, Florida should proceed with a thoughtful and practical approach that identifies and avoids the mistakes made by other states.

Instead of hastily legislating on this issue to chase a modest revenue bump, Florida legislators should carefully examine the experiences of other states to avoid pitfalls that could result in burdensome rules that impose high compliance costs or, even worse, put the state in danger of litigation.



Background: *Wayfair* and Economic Nexus

Before the Court presented its decision in *Wayfair*, a state could only require businesses to collect sales tax on purchases if they had some form of physical presence within that state — be it a retail outlet, a warehouse, or even a sales representative. This “physical nexus” standard applied for decades until 2018, when the Court considered *South Dakota v. Wayfair*. Ultimately, the majority opinion in the case dispensed with the physical nexus standard in favor of “economic nexus,” which allows states to assert sales tax collection liability on any business making sales into the state, even if no other connection exists.

Advocates of these economic nexus rules claimed that states were missing out on billions of dollars in sales tax revenues from out-of-state retailers. Yet it quickly became apparent that these revenue estimates were overblown.

The National Taxpayers Union Foundation (NTUF) [compared estimates](#) made prior to the *Wayfair* decision of how much revenue economic nexus taxes could raise with post-*Wayfair* official estimates from 32 states. Prior to *Wayfair* being argued, the National Conference of State Legislatures had projected that these 32 states would realize around \$19 billion in additional revenue from economic nexus rules if the Court were to allow their imposition. Even the more conservative Government Accountability Office estimated states would gain \$8.6 billion.

After *Wayfair* was decided and states began implementing the authority granted them by the Court, the NTUF analysis found that estimated revenue was a fraction of the pre-*Wayfair* claims by advocates of new tax power. Evaluating official revenue projections found a relatively modest \$3.6 billion in added revenue, or an average of just 0.7 percent of these states’ general funds. In oth-

er words, despite claims to the contrary, there simply is not a big pot of uncollected revenue that can be accessed simply by passing new remote sales tax rules.

Advocates of economic nexus had missed the mark in large part because of how many out-of-state sales were already taxable. Amazon, the giant of the e-retail space, had already [entered into voluntary collection agreements nationwide](#) a year before the *Wayfair* decision, while many other large e-retail businesses had physical presence through their brick-and-mortar operations, such as Walmart, and thus were already required to collect and remit sales tax on all transactions.

Remote Sales Tax in the COVID-19 Era

Memories have been short in this space. Despite the fact that actual revenue estimates were modest at best, some analysts have declared that post-*Wayfair* tax rules were crucial for state budgets in the midst of the pandemic, as lockdowns and social distancing have increased reliance on e-retailers.

One recent analysis specifically compares the sales tax revenue performance of Texas, a state with economic nexus rules, with that of Florida. The analysis [found that](#) Texas’s September 2020 sales tax collections were down 6.1 percent compared to September 2019, while Florida’s June 2020 sales tax collections were down more than 19 percent.¹ From these numbers, it would seem that Florida is missing out a great deal from not having economic nexus rules in place.

But this apples-to-oranges comparison doesn’t tell the whole story. Florida relies a great deal on the tourism and hospitality industries, industries which have been particularly affected by the pandemic. Of course, economic nexus rules would in no way help Florida to make up revenue lost from dips in tourism and hospitality. In fact, [nearly all the state’s sales tax revenue decline](#) comes from these specific industries.

And indeed, as the state has begun to reopen, sales tax revenues have begun to recover. The state’s September 2020 revenues are down a [much less jarring 6.8 percent](#) compared to September 2019 — just about in line with Texas. And even here, the most significant loss to Florida’s sales tax revenues still comes from lost tourism and hospitality industry revenue.

This context means that it would be a mistake to interpret sales tax revenue shortfalls as a mandate to urgently pass economic nexus legislation. While it is possible that Florida could find a small boost to its sales tax collections with economic nexus rules in place, the revenue gain could be more than offset by the potential harm that poorly crafted legislation could do.

Without a false sense of urgency, the Sunshine State can instead take the time to craft legislation that implements economic nexus



rules in the least harmful and burdensome manner possible. With this in mind, here are some first principles that Florida's legislature should follow when crafting its economic nexus law.

Priorities in Drafting Economic Nexus Legislation

A Proper Legislative Process

It should go without saying that a major sales tax change should be passed by the legislature and not bureaucrats in the Department of Revenue, but many other states have dispensed with the need for a legislative process when implementing economic nexus rules. The most notable example of this is Kansas, whose Department of Revenue took it upon itself to implement new tax rules after legislative efforts stalled.

In Kansas, the result was that the Department of Revenue claimed, on a technicality, that it was unable to carve out a safe harbor for small sellers, meaning that a grandmother who sells small crafts on Etsy as a hobby would be required to file sales taxes after even \$1 of sales to the state. This modern-day version of the government demanding sales taxes from a child's lemonade stand came about because bureaucrats at Kansas's Department of Revenue decided to play at being legislators.

A proper legislative process in Florida would avoid absurd technical glitches such as this, as well as allowing for hearings and public input. Given that the out-of-state business owners affected by this legislation lack the ability to weigh in on the legislature's actions via the ballot box, a hearing process is the only opportunity for their voices to be heard.

Additionally, making sure that any changes are statutory in nature ensures that they are more durable and reliable. Any executive or agency action is subject to change at a moment's notice by a future occupant of the office in question, whereas statutory rules

can only be undone by a legislative process that provides notice to affected business of potential changes.

A Reasonable De Minimis Threshold

While Kansas is the only state to have failed to provide for *any* safe harbor for small sellers, many other states have read the *Wayfair* decision far too literally. In that decision, the Court determined that a threshold of 200 transactions or \$100,000 in sales within the state of South Dakota was sufficient to protect smaller businesses without the tax infrastructure to comply with other states' tax regimes.

Most states have taken those specific numbers to heart, also including thresholds of 200 transactions or \$100,000 in sales. That's despite the fact that South Dakota has the 47th largest economy of the 50 states, and is a much smaller market than most other states. It's far easier to hit those thresholds in Florida, a state with an economy [more than 20 times the size of South Dakota's](#).

Other large states, such as [New York, California, and Texas](#), have taken some steps to incorporate the size differential between their economies and South Dakota's into their economic nexus thresholds, with each having set their thresholds at a much higher \$500,000 in sales.² Though even this does not fully realize the size difference between those states and South Dakota, it is certainly a start.

Florida should follow the example of these states, with a sales threshold of at least \$500,000 in sales. Should the state desire to truly emulate the spirit of the *Wayfair* decision, it would set its threshold closer to \$2 million in sales.

Florida should also ensure that its threshold is carefully crafted — specifically, sales which are tax-exempt should not count towards its threshold. This ensures that only taxable sales count toward the threshold, which protects wholesale operations or businesses trading in tax-exempt goods from facing tax paperwork and audit threats despite having little or no actual sales tax liability.

SSUTA Membership

One crucial aspect of South Dakota's law that allowed the Supreme Court to find it constitutional in the *Wayfair* case was South Dakota's membership in the [Streamlined Sales and Use Tax Agreement \(SSUTA\)](#). The SSUTA is a multi-state agreement whereby member states agree to maintain state-level tax administration, standardize tax base definitions, simplify tax rates and exemption administration, and provide a single electronic registration system.

While membership in the SSUTA does not eliminate the compliance burden of registering with a new state, it substantially ameliorates it. Unfortunately, Florida is not currently an SSUTA member state.

Florida should consider making the necessary changes to its sales tax regime to become a member state of SSUTA as part of any legislation to impose economic nexus legislation. Not only would this signal the state's determination to be hospitable to businesses selling into the state, but it would also make any economic nexus obligations it imposes far less burdensome.

While SSUTA membership is obligatory to maintain fidelity with the Supreme Court's guidance in *Wayfair*, the reality is that further simplification of Florida's sales tax regime would have benefits beyond protecting the state from potential litigation.

Endnotes

- 1 Texas's June 2020 tax collections were down by a similar amount compared to June 2019, or about 6.5 percent.
- 2 California and Texas each do not consider the number of transactions for their economic nexus thresholds. New York's is set at 100 transactions, but a seller must *also* reach \$500,000 in sales to qualify.

Business Certainty and Protections

Florida has [flirted with the idea of imposing](#) economic nexus rules going back retroactively in the past. To provide certainty to businesses that they will not be held liable for sales taxes on transactions that took place prior to the state's economic nexus law, Florida should include definitive language that will foreclose any attempt to collect economic nexus taxes retroactively.

The state should also be mindful of the fact that many out-of-state filers will be dealing with the state's tax administration for the first time. As such, an audit clause that protects businesses that make good-faith errors in filing during the period of transition would go a long way towards making the switch more seamless.

Conclusion

E-retail has grown in importance during the COVID-19 era, but it would be a mistake for Florida to rush through economic nexus legislation in the pursuit of an illusory revenue windfall. The Sunshine State should instead learn from the mistakes of others that have set thresholds too low, forced out-of-state sellers to comply with an excessively complicated sales tax regime, or allowed the administrative state to draft economic nexus rules in place of the legislature.

Florida should take heed of the lessons in their failures and be mindful of the potential harm that poorly crafted legislation can do to small businesses that are even less equipped to deal with additional headaches at the moment than usual.



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