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Andrew Wilford is the director of the Interstate Commerce Initiative at the National Taxpayers Union Foundation.

In this installment of Commerce Crossroads, Wilford examines legislative developments on *Wayfair* this session and discusses what other issues states should be considering.

As the six-year anniversary of the Supreme Court's decision in *Wayfair*[1] approaches, some may be tempted to see the issue of economic nexus for sales taxes as a largely settled one. For many state legislatures and revenue departments, it likely is — after all, the revenue source they sought has been turned on.

While state legislation in the wake of *Wayfair* may have left states in a good place, the jury is still out on that question for many small businesses. A rough (and likely conservative) estimate by the National Taxpayers Union Foundation placed the number of remote businesses that are or were out of compliance with their sales tax collection obligations because of economic nexus rules at a minimum of 50,000.[2]

Some of that noncompliance stems from a lack of awareness, but a far greater problem is that the compliance burden for small businesses without a dedicated state and local tax department is prohibitive. The obligation to stay up to date with various rules, definitions, exemptions, and rates for 45 states and the District of Columbia, not to mention local jurisdictions, has been daunting enough to create a shadow economy of small online retailers trying to keep their heads down.

While the initial flurry of state economic nexus laws in *Wayfair*'s wake has largely passed, some states continue to make small changes to the obligations and compliance burdens they place on remote sellers. But while the momentum may be lacking, the underlying reason for states to take up more substantive, comprehensive changes remains strong.

Tinkering Around the Edges

Most of the changes debated in state legislatures over the past year have not been nearly as comprehensive as those that took place in the aftermath of the *Wayfair* decision. Four issues have remained prominent in recent legislative action: safe harbor thresholds, home rule states that lack a centralized tax administration, delivery fees, and marketplace facilitator laws.

Safe Harbor Thresholds

The South Dakota legislation at issue in *Wayfair* included a safe harbor that applied sales tax collection obligations only to sellers with more than 200 transactions and $100,000 in sales within the state — a threshold that has largely been copied by other states. In passing their initial

[1] *South Dakota v. Wayfair Inc.*, 138 S. Ct. 2080 (2018).

[2] Andrew Wilford, "Nearly 50,000 Remote Businesses Out of Compliance With *Wayfair*," National Taxpayers Union Foundation (Nov. 16, 2022).

economic nexus legislation, nearly all states either adopted this threshold or a higher one, though Kansas went without one from 2019 to 2021.[3]

But while most states now have nearly identical safe harbors from a numbers standpoint, some seemingly minor technical differences can have a large impact on businesses. For instance, while some states' safe harbors ensure that collection obligations kick in only after a seller exceeds 200 transactions *and* $100,000 in sales within the state, others require a seller to exceed only one of those thresholds.

That's a difference of "and" versus "or," but the impact on small businesses is significant. An "or" threshold can require a business with a large volume of low-dollar sales to collect and remit sales taxes even if the dollar value of sales into that state is well below the $100,000 threshold. Unfortunately, more than half the states with a sales tax continue to enforce an "or" threshold rather than an "and" threshold.

Lately, some states have moved to do away with this problem by simply eliminating the number of transactions from their safe harbor thresholds. Along with the states that have already done so, legislation to accomplish this has been introduced in Indiana and Utah.[4] Legislation to remove transactions from the state's safe harbor threshold has also been prefiled by the nonpartisan Joint Revenue Interim Committee in Wyoming.[5]

Another technical difference that can make a big impact for businesses concerns the type of sales that count toward thresholds. Many states count gross sales toward their thresholds, but this drags in businesses that primarily sell nontaxable goods into that state, such as wholesalers. A threshold based on gross sales can therefore require businesses to go through the complicated process of collecting and remitting sales tax to a state even when taxable sales are well below $100,000.

The obvious solution to this problem would be to instead base thresholds on taxable sales. More recently, however, states that recognize the difficulties associated with a threshold based on gross sales have been moving away from a threshold based on taxable sales as well. Instead, they have been transitioning to a threshold based on retail sales.

The reason for this is fairly simple: For a business to determine whether it has exceeded a threshold based on taxable sales, it first must find out which of its sales are taxable. The effect is that businesses trying to figure out if they must do the work of understanding a state's sales tax code must first understand the state's sales tax code. A threshold based on retail sales, on the other hand, allows businesses to know whether they have sales tax obligations without first having to calculate them. Several states have already changed their thresholds to retail sales, though the majority continue to use gross sales for their thresholds.

States That Lack Centralized Tax Administration

For remote sellers, economic nexus in most states means one additional set of rules, definitions, exemptions, and rates to comply with — as well as one additional point of contact and potential audit. But home rule states, in which local jurisdictions separately administer their own sales taxes, have the potential to create disproportionate burdens for remote businesses.

Home rule states have not approached this problem in a uniform manner. Alabama has empowered its simplified sellers use tax regime post-*Wayfair*, enabling remote sellers to collect and remit use tax at a single statewide rate with a single point of contact, without having to track which sales went to which jurisdiction. The state Department of Revenue then handles distribution of these funds to local jurisdictions on the back end.

Arguably the opposite approach has been favored by Colorado and Alaska.[6] In these states, it has largely been left up to local jurisdictions to enroll in agreements that promote uniformity and

[3] Michael Austin, Andrew Moylan, and Wilford, "Kansas Must Act to Protect Small Sellers From Remote Sales Tax Law," National Taxpayers Union Foundation and Kansas Policy Institute (Mar. 22, 2021).

[4] S.B. 228, 123d Gen. Assemb. (Ind. 2024); H.B. 17, 65th Leg. (Utah 2024).

[5] L.S.O. 226 (prefiled), 67th Leg. (Wyo. 2024).

[6] Alaska does not have a statewide sales tax, but more than 100 local jurisdictions in the state collect and administer their own sales taxes.

provide remote sellers with a single point of contact for filing and audit procedures. While these are good initiatives, there remains the issue of dealing with nonparticipating jurisdictions.

Another home rule state, Louisiana, has only recently moved to reduce the burdensome nature of its byzantine sales tax system. Louisiana is constitutionally bound to permit parish-level tax administration, making establishment of a single statewide point of contact difficult. This problem was only exacerbated by an unhelpful web portal that often made it impossible for out-of-state sellers to determine what fire district or road taxing district their customer was actually located in.[7]

A lawsuit brought by an Arizona-based business, Halstead Bead, against Louisiana because of its burdens on remote sellers prompted the state to pass H.B. 558,[8] which directs the Louisiana Uniform Local Sales Tax Board to create a single platform through which remote sellers can remit sales taxes to all statewide jurisdictions via a single transaction. H.B. 558 also requires more participation from local taxing jurisdictions in providing timely and accessible updates on any tax changes made at the local level.

Delivery Fees

Colorado was the first state to impose a so-called delivery fee, a flat surtax that retailers selling into Colorado were required to collect and remit on top of the existing sales tax. Seemingly a minor requirement at first glance, the delivery fee has caused significant issues for remote businesses because of the difficulty of incorporating it into compliance software that often does not support fees.[9]

Colorado's reason for instituting an obligation that functions almost precisely the same as a tax and calling it a fee — the desire to bypass a state rule necessitating direct voter approval for any tax increase — is unique to the state. In this regard, it is somewhat surprising that other states have taken up an initiative that caused such disproportionate headaches for businesses.

Nevertheless, that is exactly what has happened. Minnesota passed a similar fee as part of a transportation bill in 2023,[10] while legislation that would have imposed delivery fees between 25 cents and $3 per delivery was introduced in New York last year.[11] Conversely, companion bills have been introduced in Minnesota this legislative session to repeal the state's delivery fee.[12]

Marketplace Facilitator Laws

While all states with economic nexus sales tax laws have also enacted marketplace facilitator laws by this point, controversy remains. States continue to differ greatly in how they define "marketplace facilitators," with broader definitions risking multiple parties being classified as a marketplace facilitator in a single transaction, a single marketplace facilitator having to collect sales tax at two levels of the same transaction, or parties uninvolved in a transaction being held liable for sales tax collection.[13]

At the same time, the question of whether and how to assess tax obligations on retailers that used marketplace facilitators before marketplace facilitator laws went into effect remains a thorny one. For example, some states have sought to go after retailers with inventory stored in in-state warehouses by Fulfilled by Amazon (FBA) services before *Wayfair*, attempting to argue that these retailers had physical presence through this inventory. The counterargument is that these retailers had no control over or awareness of where Amazon placed their inventory, as Amazon took over the entire fulfillment process once inventory was turned over to it.

Different state courts have come down on opposite sides of this question. While California's Court of Appeals sided with the California

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[7] Complaint at 9, *Halstead Bead Inc. v. Lewis*, 604 F. Supp. 3d 342 (E.D. La. 2022).

[8] H.B. 558 (La. 2023).

[9] Wilford, "Colorado Makes Sales Tax Compliance Even Worse With Delivery Excise Tax," National Taxpayers Union Foundation (July 12, 2022).

[10] H.F. 2887, 93d Leg. (Minn. 2023).

[11] S. 5895 (N.Y. 2023); A. 6008 (N.Y. 2023).

[12] H.F. 4504, 93d Leg. (Minn. 2024); S.F. 4772, 93d Leg. (Minn. 2024).

[13] National Conference of State Legislatures Task Force on State and Local Taxation, "State and Local Tax Considerations for Marketplace Facilitator Tax Collection Requirements" (Aug. 2023).

Franchise Tax Board in going after FBA retailers,[14] Pennsylvania's Commonwealth Court instead decided that in-state inventory managed by the FBA program could not create nexus for the retailers.[15] The question whether states have the power to pursue these collections therefore remains unanswered, though the fact that this effectively represents a retroactive tax assessment on businesses that never collected the sales taxes in the first place and have no ability to do so now certainly seems to answer the question whether states *should* do so.

Big Problems Going Unaddressed

Uniformity

In *Wayfair*, the Supreme Court favorably cited South Dakota's participation in the Streamlined Sales and Use Tax Agreement — a multistate agreement to harmonize sales and use tax bases and sourcing rules — as a significant factor in determining that the law at issue did not impose an unconstitutional burden on interstate commerce. Unfortunately, this has not had the effect of encouraging significant voluntary state efforts to promote uniformity — in fact, not a single new state has joined the SSUTA since the *Wayfair* decision.

This is particularly concerning since there is a strong argument to be made that the SSUTA alone is not enough to satisfactorily ameliorate the compliance burdens of collecting and remitting sales taxes nationwide for small businesses. While SSUTA member states address the biggest headaches for businesses, the SSUTA is silent on safe harbors, and the "free" compliance software offered by member states is often unsatisfactory or fails to account for significant software integration costs.[16]

Greater uniformity on not just tax definitions and sourcing rules but also certifying compliance software providers, safe harbor measurement periods, exemption certificates, and other technical matters would go a long way toward bringing multistate sales tax compliance for remote retailers in line with compliance burdens for other types of taxes.

Out-of-Compliance Businesses

As previously mentioned, a significant number of businesses — particularly small businesses — likely remain out of compliance. Businesses that have decided that the obligation to become multistate tax experts is simply beyond their capabilities are risking their livelihoods should states step up enforcement efforts, but the compliance landscape for small businesses is not meaningfully simpler in 2024 than it was in 2018.

At the same time, businesses that were late to the compliance party continue to have a sword of Damocles hanging over their heads in the form of obligations that they incurred before coming into compliance, as well as steadily accumulating penalties and interest. As late as May 2022, an Avalara poll found that less than half of surveyed businesses reported that they were fully compliant with *Wayfair*[17] — a figure that does not account for businesses optimistically reporting compliance when they could be wrong.

Upon its founding, the SSUTA enticed businesses to register by requiring its member states to offer a one-time amnesty to any businesses that registered and complied with that state's sales tax obligations for 36 months. States should consider something similar to offer out-of-compliance small businesses afraid to bring attention to themselves an opportunity to come out of the shadows and into compliance.

Conclusion

While states may be happy with a revenue boost from economic nexus sales tax laws, they should also recognize that making compliance reasonable is in their interests as well as those of businesses. Not only does increased compliance bring increased revenue, but pushing small businesses to risk the consequences of noncompliance because of shortsighted parochial

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[14] *Grosz v. California Department of Tax and Fee Administration*, 87 Cal. App. 5th 428 (Cal. Ct. App. 2023).

[15] *Online Merchants Guild v. Hassell*, 282 A.2d 871 (Pa. Commw. Ct. 2022).

[16] Written statement of Joe Bishop-Henchman et al., "Reforms Congress Must Consider 4 Years After *Wayfair* Ruling," submitted to the U.S. Senate Finance Committee (2022).

[17] Gail Cole, "Survey and Senate Hearing Find Small Businesses Are Not Immune to Impacts of the *Wayfair* Decision," Avalara, June 21, 2022.

refusal to provide meaningful simplification is bad for everyone involved.

Legislators who want to champion small businesses should show it by not allowing thousands of them to suffer silently under a flood of paperwork. The internet is proving to be a great equalizer for smaller businesses, allowing them to access a nationwide market and compete directly with the largest retailers. It would be a tremendous shame if taxes were to restrict this digital playground to businesses with enough accountants to play in it. ■