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Proposed Sales and Use Tax Nexus Legislation: More Problems for Interstate Businesses

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Although it is still early in the 2012 legislative session, many states are already considering amendments to their sales and use tax nexus laws. The bills discussed in detail below are examples of the types of troublesome legislation that have been proposed to date and illustrate that, continuing the trend of recent years, movement in the nexus area is aimed at taxing out-of-state retailers through aggressive affiliate nexus and click-through nexus laws.

With continuing state budgetary woes, this trend is likely to continue and will merit careful attention as legislative sessions unfold. A recent quote from Justice Anthony Kennedy during oral arguments debating the constitutionality of the federal health care law seems somewhat apropos to the trend of nexus legislation: "Could you help – help me with this. Assume for a moment – you may disagree. Assume for a moment that this is unprecedented, this a step beyond what our cases allow…."[1]

The Honorable Supreme Court? Congress? Could you help? Would you please considered the magnitude of the burden that these expanding nexus provisions impose on interstate commerce, particularly for small and start-up businesses?

This article raises but a small sample of the problems that arise from the recent trend of nexus legislation aimed at regulating out-of-state taxpayers.

Proposed Affiliate Nexus Legislation

Arizona S.B. 1338 would broaden the definition of "retailer" for purposes of use tax to include any person who makes sales of tangible personal property intended for storage, use, or other consumption in Arizona if any *other* person maintains a distribution center, warehouse, fulfillment center, or similar place of business within Arizona that facilitates the delivery of property sold by the person to the person's customers. **Problem:** These types of provisions raise significant Due Process and Commerce Clause concerns if the person maintaining the Arizona place of business serves as neither the sales force, nor an employee or agent for the out-of-state seller (i.e., someone who would typically receive a W-2 or 1099 from seller).

[1] Transcript of Oral Argument at 11, *Department of Health and Human Services v. Florida*, No. 11-398 (Tuesday, March 27, 2012).

Indiana H.B. 1119 defines "retail merchant engaged in business in Indiana" to include any retail merchant who: (1) makes retail transactions in which a person acquires personal property or taxable services for use, storage, or consumption in Indiana; and (2) enters into an arrangement with any person, other than a common carrier, to facilitate the retail merchant's delivery of property to customers in Indiana by allowing customers to pick up property sold by the retail merchant at a place of business maintained by the person in Indiana. Additionally, a person would be required to collect and remit gross retail tax or use tax as a retail merchant if the activities conducted by any person in Indiana are significantly associated with the retail merchant's ability to establish and maintain a market in Indiana. **Problem:** Similar to provisions proposed by the other states, the application of this type of provision exceeds the farthest boundaries established by the Supreme Court in *National Geographic v. California Bd. of Equalization,* 430 U.S. 551, 556 (1977)(nexus requires a connection beyond the means of the instruments of interstate commerce being conducted) and *Quill Corp. v. North Dakota,* 504 U.S. 298 (1992)(nexus requires physical presence beyond minimum contacts).

Oklahoma H.B. 2586 would modify the definition of "maintaining a place of business in this state" by including any retailer that has agents in the state delivering, installing, assembling, or performing maintenance services for the retailer or other persons conducting other activities in Oklahoma that are significantly associated with the retailer's ability to establish and maintain a sales market in Oklahoma. The definition of "maintaining a place of business in this state" also includes persons using trademarks, service marks, or trade names in Oklahoma that are the same as or substantially similar to those used by an out-of-state retailer, as well as persons who facilitate a retailer's delivery of property to Oklahoma customers by allowing the pickup of goods at an office, distribution facility, warehouse, storage place, or other similar place in the state. **Problem:** Provisions attempting to impose nexus by use of similar trademarks, service marks or tradenames raise significant Due Process and Commerce Clause concerns, particularly in situations where the persons are not commonly controlled, and are thus not a unitary business.

Utah H.B. 384 would expand sales and use tax collection and remittance obligations to out-of-state sellers with substantial ownership interest in in-state businesses or to sellers that make sales to in-state purchasers by mail, telephone, the internet, or other media and have contractual relationships with in-state sellers to perform installation, maintenance, or repair services for those in-state purchasers. **Problem:** These types of provisions are a step beyond what the current Supreme Court cases have allowed and raise concerns of both lack of a substantial nexus to the seller being regulated and fair apportionment of sales transactions occurring in interstate commerce.

Proposed Click-Through Nexus Legislation

Indiana H.B. 1119 creates a rebuttable presumption that a retailer is engaged in business in Indiana if the retail merchant enters into an agreement with one or more residents of Indiana under which the resident directly or indirectly refers potential customers to the retail merchant. The presumption is applied only where the cumulative gross receipts from the sales by the retail merchant to customers in Indiana who are referred to the retail merchant by all residents are greater than $10,000 during the preceding 12 months.

The new law would be effective from the earlier of January 1, 2014, or the third month after the Indiana State Budget Agency certifies that a requirement for sellers to collect use tax on remote sales has been enacted into law by the United States Congress. The Indiana provision is similar to the California click-through nexus bill passed last year which also included a tie to federal

legislation. Indiana's proposed legislation may signal a trend towards further adoption of this controversial type of provision by other states. **Problem:** These type of provisions attempt to impose a significant burden on countless (often struggling) interstate businesses to monitor and adjust to the constantly changing the requirements of tens of thousands of state and local taxing jurisdictions. Businesses operating solely in one state have a huge economic advantage. Particularly where states have other less burdensome options to collect taxes owed by their own citizens, the burden of such use tax collection laws greatly outweighs the benefit of the convenience of mandating that out-of-state businesses become tax collectors.

Maryland S.B. 152, pursuant to Maryland governor Martin O'Malley's budget proposal, is a click-through nexus bill expanding the definition of "seller" to include any out-of-state retailer entering contracts under which residents refer customers to the out-of-state retailer's web site through an internet link, creating a rebuttable presumption of nexus. Like many proposals, this proposed law would apply only to retailers whose revenues from the referrals exceed $10,000 in a 12-month period. The presumption of nexus could be rebutted by proof that the resident did not engage in any solicitation in the state on behalf of the out-of-state retailer. **Problem:** As noted in the discussion of the Indiana proposed legislation, this type of provision significantly burdens interstate commerce with a cost not imposed on instate businesses. Even the burden of monitoring these types of legislative changes can be overwhelming to most businesses.

Minnesota H.B. 1849 would define "solicitor" for purposes of sales and use tax as any resident in the state who directly or indirectly refers potential customers to a seller through an internet web site or similar link for a commission or other consideration. The bill would create a rebuttable presumption that a retailer has nexus if the total receipts of sales to Minnesota customers generated by internet referrals made through web sites operated by Minnesota residents exceed $10,000 in a 12-month period. This bill is explicitly modeled on "affiliate nexus" bills that have been passed in New York, Rhode Island, North Carolina, Connecticut, Illinois, and Arkansas. **Problem:** The piling on of more states that assert the ability to regulate out-of-state businesses to the level of requiring the monitoring of the residence of every person who directly or indirectly refers customers to the company compounds the burden on interstate commerce at a level that the Supreme Court has never sanctioned.

The Honorable Supreme Court and Congress of the United States, please hear our plea!

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