

NetChoice Promoting Convenience, Choice, and Commerce on The Net

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Sen. JD Mesnard, Chair
Committee on Finance
Arizona Senate

February 19, 2019

RE: Opposition to HB 2702 – Taxation

Dear Chair Mesnard and members of the committee:

We respectfully ask that you not advance HB 2702 as it fails to provide the adequate simplifications and protections laid out in the US Supreme Court decision *South Dakota v Wayfair*.

Other states have adopted South Dakota’s remote seller tax collection law. But unlike these states, Arizona has failed to undertake the necessary steps to ensure that collection requirements do not violate the factors laid out by the Supreme Court.

In June 2018, the US Supreme Court’s *Wayfair* decision discarded the 60-year precedent of *Quill* and *National Bellas Hess*, so states may now impose sales tax burdens on businesses without a physical presence in their state. The *Wayfair* decision goes on to describe how South Dakota’s sales tax law would likely survive a Commerce Clause challenge as an undue or discriminatory burden on interstate commerce, based on three findings:

“First, the South Dakota law at issue in *Wayfair* applies a safe harbor to those who transact only limited business in South Dakota.” (p.23, *Wayfair*)

“Second, the South Dakota law at issue in *Wayfair* ensures that no obligation to remit the sales tax may be applied retroactively.” (p.23, *Wayfair*)

“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.” (p.23, *Wayfair*)

As you can see in the attached document, Arizona fails to satisfy this third requirement.

Moreover, Arizona then imposes a Constitutionally suspect requirement on marketplaces that merely facilitate transactions. For example, HB 2702 imposes sales tax collection requirements on platforms that don’t even touch the money.

Also, HB 2702 would unconstitutionally discriminate against interstate commerce, by requiring out-of-state businesses to pay the TPT of the location where Arizona purchasers reside. In-state businesses, however, could simply use the TPT rates and rules applying to the business location – regardless of where the customer resides.

We ask that you reject HB 2702 and protect Arizona citizens from a new tax, avoid costly litigation the state is likely to lose.

Thank you for considering our views and please let us know if we can provide further information.

Sincerely,

Carl Szabo
Vice President and General Counsel
NetChoice

The views of NetChoice do not necessarily represent the views of its members.

HB 2702 Does not follow *Wayfair*

The US Supreme Court's *Wayfair* decision discarded the 60-year precedent of *Quill* and *National Bellas Hess*, so states may now impose sales tax burdens on businesses without a physical presence in their state.

The *Wayfair* decision goes on to describe how South Dakota's sales tax law would likely survive a Commerce Clause challenge as an undue or discriminatory burden on interstate commerce, based on three findings:

- 1 "The South Dakota law at issue in *Wayfair* applies a safe harbor to those who transact only limited business in South Dakota."  HB 2702 applies to sellers with more than 200 transactions or \$100,000/year in sales.
- 2 "The South Dakota law at issue in *Wayfair* ensures that no obligation to remit the sales tax may be applied retroactively."  HB 2702 forbids retroactive application of tax collection on remote sellers.
- 3 "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."  Arizona is not a member of SSUTA.

But 3 might be satisfied by doing the following:

 - A single, state level tax administration  Arizona does have state level administration.
 - Uniform definitions of products and services, simplified tax rate structures  Cities have different tax base (except for retail). Cities have tiered / blended tax rates. Cities have different tax rates between classes.
 - Provide sellers access to sales tax administration software paid for by the state.  Arizona lacks sales tax software and has not promised vendor compensation.
 - Sellers who choose to use such software are immune from audit liability.  Arizona fails to provide adequate immunity for sellers who use software.

The *Wayfair* decision confirmed the third prong of the *Complete Auto* test, saying "[t]he Court will sustain a tax so long as it . . . (3) does not discriminate against interstate commerce." 138 S.Ct. 2080 (2018).



HB 2702 would discriminate against interstate commerce, by requiring out-of-state businesses to pay the TPT of the location where Arizona purchasers reside. In-state businesses, however, could simply use the TPT rates and rules applying to the business location – regardless of where the customer resides.

Principles for imposing sales tax obligations on Marketplaces

Neither the *Wayfair* decision nor SSUTA addresses whether or how states can impose sales tax obligations on online marketplaces or marketplace facilitators.

Some states are adopting laws and regulations to tax marketplaces, in ways that will invite legal challenges for undue or discriminatory burdens per the Constitution's Commerce Clause.

States seeking to tax marketplace facilitators can significantly reduce their legal risks by adhering to these principles in their legislation and regulation:

- Uniform definitions, rates, and rules for all localities in the state, regarding taxable and exempt products and the duty to collect sales tax for localities.
- A phase-in period for marketplace sellers and facilitators.
- State tax audits of marketplaces should not extend to audits of marketplace sellers. A marketplace facilitator should be relieved of liability for failure to collect and remit the correct amount of tax to the extent that the error was due to incorrect or insufficient information provided by the marketplace seller.
- Marketplace Facilitators should have the ability to separately report sales tax for the marketplace's own sales, apart from sales the facilitator or its affiliates make directly.
- Marketplace facilitators should not be liable for sales tax collection on sales where the marketplace facilitator requests and receives an agreement, certificate, or other form of proof that the seller is collecting the sales tax.
- A marketplace facilitator should not be liable for tax on sales where it receives a tax exemption or resale certificate from the marketplace seller or the marketplace seller's customer.
- State level administration of local taxes, including a single return and audit on behalf of all local jurisdictions in a state.
- The safe harbor for small businesses applies to direct sales, via the seller's own website, phone numbers, catalogs, or other remote sales channels.
- Non-streamlined states must also provide adequate compensation to marketplace facilitators who collect tax on behalf of marketplace sellers. Any limits on vendor compensation should be aggregated for marketplace sellers, and not a limit on the marketplace facilitator.
- Marketplace Facilitators should not be obligated to collect sales tax on a seller's sales into the state until that marketplace seller has reached \$10,000 in sales on that marketplace over 12-months ending within the most recently completed calendar quarter.
- Marketplace Facilitator tax obligations for Marketplace Seller transactions should apply only when the facilitator is processing payments for customer transactions. Prohibit class action lawsuits against marketplaces for over-collection of sales tax.
- There should be no imposition of retroactive tax liability for sales prior to the *Wayfair* decision.