



SENATE BILL 81: Sales Tax Economic Nexus For Remote Sales.

2017-2018 General Assembly

Committee:	Senate Rules and Operations of the Senate	Date:	June 8, 2017
Introduced by:	Sens. Tucker, Brock, Tillman	Prepared by:	Cindy Avrette Staff Attorney
Analysis of:	Second Edition		

OVERVIEW: *Senate Bill 81 would do the following:*

- *Require a person who facilitates a sale in this State to collect and remit North Carolina sales and use tax. Section 1 would become effective September 1, 2017. Section 1 also modernizes the statutes and provides that a facilitator of an accommodation may also be a person who provides a forum or platform to market the accommodation.*
- *Require a seller who, in the previous calendar year, made gross sales of more than \$100,000 sourced to North Carolina or who made 200 or more separate sales transactions sourced to this State to collect and remit North Carolina sales and use tax. Section 2 would become effective January 1, 2018.*
- *Require a marketplace provider to collect and remit a sale sourced to this State to collect and remit North Carolina sales and use tax. Section 3 would become effective July 1, 2019.*

CURRENT LAW: Sales and use tax is payable by the consumer. However, the most cost-effective manner to collect the tax is to require the retailer to collect and remit it. A state cannot require a seller to collect and remit its sales and use tax unless the seller has a physical presence in the state. North Carolina has deemed that a seller has a presence in this State if the seller makes a remote sale. The term "remote sale" is defined. North Carolina has defined a remote sale broadly, but within the constitutional confines of "physical presence".

BILL ANALYSIS: Senate Bill 81 would do three things to help ensure the collection and remittance of sales and use tax payable on sales sourced to North Carolina:

- It clarifies that a retailer includes a person who facilitates the sale of property or a service on behalf of a third party. This section becomes effective September 1, 2017. The term "sale" means the transfer for consideration of title, license to use or consume, or possession of property or the performance of a service. However, based upon a long-interpretation of the Department of Revenue, boat and aircraft brokers¹ do not collect or remit sales tax on the sale of those items and it appears the rationale for the decision may be that the broker did not possess title to the item. That interpretation differs from the language of the statute. This change clarifies that a person who facilitates a sale is engaged in business as a retailer and must collect and remit sales tax on the sales price.

¹ Often a person who sells items, such as boats, may have in its inventory items it owns or possesses the title to as well as items it holds on the lot for a third party. A purchaser would not recognize the difference. However, based on the current DOR interpretation, one item is subject to tax and another is not.

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- It expands the definition of a remote sale to include a minimum number or amount of sales in North Carolina during the previous calendar year. A seller who makes sales in North Carolina that exceed \$100,000 annually, or who makes more than 200 separate transactions in North Carolina annually, is a retailer engaged in business in this State, and thus required to remit and collect the State's sale and use tax. This change becomes effective January 1, 2018. This expansion would conflict with the constitutional physical presence requirement; at least 17 states have enacted similar legislation.
- It expands the applicability of the sales tax to include sales at retail facilitated by a marketplace provider. A marketplace provider is a person who facilitates a sale in this State through a forum or platform in which, or by means of which, the retail sale takes place, the offer of sale is accepted, or payment is collected. It would include transactions made through a mobile phone application, Amazon, eBay, etc. This change becomes effective July 1, 2019. One state, Minnesota, enacted similar legislation last week. The bill provides that the marketplace provider and the retailer may have an agreement that stipulates the retailer, rather than the marketplace provider, will remit the sales tax on the facilitated sale. A marketplace provider would not be liable for failure to collect and remit sales tax if the marketplace provider demonstrates that the error was due to incorrect or insufficient information given to the marketplace provider by the retailer.

The bill also does the following in Section 1 of the bill, which becomes effective September 1, 2017:

- Modernizes the definition of "engaged in business" through the use of "transacting business"; this term is currently part of the remote sales statute, G.S. 105-164.8.
- Provides for a more equitable administration of the sales tax on accommodations by requiring facilitators that either only market or collect the rental fees for the rental of an accommodation to collect the tax from the consumer. The provision will help reduce the avoidance of sales and use taxes, as well as occupancy taxes, through the use of separate entities.

EFFECTIVE DATE: Except as otherwise noted in the **Bill Analysis**, the bill would become effective when it becomes law.

BACKGROUND: Sales and use tax is payable by the consumer. However, the most cost-effective manner to collect the tax is to require the retailer to collect and remit it. In 1967, the U.S. Supreme Court ruled in *National Bellas Hess Inc. v. Department of Revenue* that a state could not require an out-of-state retailer to collect its use tax unless the retailer has enough contacts with the state to subject it to the state's taxing jurisdiction. Part of the discussion in this court decision was the burden it placed on a business located in one state to collect sales tax for every other state.

In the 1980s, states around the country became increasingly aware of the revenue loss associated with taxpayer avoidance of the use tax. North Dakota attempted to require Quill, a corporation that did not have a physical location in North Dakota, to collect and pay use tax on sales shipped into the State. However, in 1992, the Supreme Court reaffirmed the physical presence standard for the collection and remittance of sales tax in *Quill Company v. North Dakota*. The Supreme Court opined that Congress had the power to resolve the issue through legislation.

Many online retailers have used this ruling to justify not charging sales tax on online sales, giving online sales a competitive advantage over Main Street retailers. For the past 25 years, states have sought to solve this issue through several means:

- Urging Congress to pass legislation requiring out-of-state retailers to collect and remit states' sales and use tax.

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- Simplifying the administration of sales and use tax laws.
- Participating in interstate agreements, such as the Streamlined Sales Tax Agreement (SSTA). North Carolina is a founding member of the SSTA. The State has been very active in the Streamlined Sales Tax Project since its inception.
- Requiring taxpayers to submit use tax annually when they file their state tax returns.
- Enacting laws that seek to more broadly define "physical presence". For example, a retailer is engaged in business in this State if it has representatives in the State that solicit business or if it has a "click-through" contractual agreement with a North Carolina resident to solicit business for it.
- Encouraging out-of-state retailers to collect sales and use tax. For example, in 1999, North Carolina prohibited the State from contracting with a vendor for goods or services if the vendor did not collect sales and use tax on remote sales.

South Dakota recently enacted a law that requires remote sellers to collect sales tax if they have annual sales in excess of \$100,000 or 200 separate transactions in the state. As a matter of law, this statutory change is prohibited by the *Quill* ruling. South Dakota hopes the law will be a vehicle to get to the U.S. Supreme Court in a challenge to *Quill*. On Monday, March 6, 2017, a state trial court in South Dakota struck down the state's remote sale tax law. The state filed an appeal of the decision to its state supreme court on March 8, 2017. The case is expected to be ultimately appealed to the U.S. Supreme Court.

States are increasingly considering and enacting legislation that will erode the physical presence requirement:

- Economic nexus. – Set aside "physical presence" as the standard. Implement a bright-line sale threshold. The most common standard used is \$100,000 in sales or 200 separate transactions. Senate Bill 81 adopts this approach, and uses the same thresholds that South Dakota used: \$100,000 in annual sales or 200 separate transactions. At least 17 states have legislation introduced in 2017 advocating this approach.
- Expanded nexus. – Aim to extend physical presence to constitutional limit. Examples include affiliate nexus, click-through nexus, and drop ship nexus. At least 10 states have legislation introduced in 2017 in this category. North Carolina already defines a remote sale to include sales that extend the physical presence to constitutional limits.
- Reporting requirements. – Require out-of-state sellers to inform buyers about responsibility to pay use tax on their purchases, as well as requiring out-of-state sellers to report sales made in a state to the state. The Tenth Circuit has found that a reporting requirement is constitutionally permissible. A handful of states have legislation introduced in 2017 that impose reporting requirements on out-of-state sellers.
- Marketplace providers. – Requires a person who facilitates a retail sale sourced to this State to collect and remit sales tax on the sales price.