

DEPARTMENT OF TAXATION

2004 Fiscal Impact Statement

1. **Patron** Timothy D. Hugo

3. **Committee** House Finance

4. **Title** Retail Sales and Use Tax: Constitutional
Nexus; Declaratory Judgments

2. **Bill Number** HB 1463

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would grant circuit courts jurisdiction over civil actions in which a Virginia business seeks a declaratory judgment against officials in other states to prevent such other states from forcing the Virginia business to collect and remit retail sales and use taxes to another state. This bill would also provide that no business is liable for the collection of Virginia retail sales and use tax, unless such business has a substantial physical presence in Virginia.

The effective date of this bill is not specified.

6. **Fiscal Impact Estimates are:** Tentative. (See Line 8.)

6b. Revenue Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2004-05	<\$5,544,000>	GF
2004-05	<\$1,008,000>	TTF
2004-05	<\$1,848,000>	Local
2005-06	<\$5,544,000>	GF
2005-06	<\$1,008,000>	TTF
2005-06	<\$1,848,000>	Local
2006-07	<\$6,204,000>	GF
2006-07	<\$1,128,000>	TTF
2006-07	<\$2,068,000>	Local
2007-08	<\$6,864,000>	GF
2007-08	<\$1,248,000>	TTF
2007-08	<\$2,288,000>	Local

2008-09	<\$7,524,000>	GF
2008-09	<\$1,368,000>	TTF
2008-09	<\$2,508,000>	Local
2009-10	<\$8,184,000>	GF
2009-10	<\$1,488,000>	TTF
2009-10	<\$2,728,000>	Local

7. Budget amendment necessary: Yes.
Page 1, Revenue estimates.

8. Fiscal implications:

The provision of this bill that limits the imposition of the Virginia retail sales to businesses with a substantial physical presence in Virginia would have a negative revenue impact beginning in fiscal year 2005 of \$8.4 million, \$8.4 million in fiscal year 2006, \$9.4 million in fiscal year 2007, \$10.4 million in fiscal year 2008, \$11.4 million in fiscal year 2009 and \$12.4 million in fiscal year 2010.

This bill would have a minimal administrative impact on the Department.

Legislation enacted in 2003 (Chapters 994 and 1006), prohibits state agencies from purchasing goods or services from vendors required under Virginia's sales tax nexus laws to collect use tax on sales of goods delivered into Virginia, but refuse to do so. This bill would prohibit Virginia from requiring such vendors to register and remit tax.

9. Specific agency or political subdivisions affected:

Department of General Services
 Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Declaratory judgments

This bill would expand the jurisdiction of Virginia circuit courts to hear declaratory judgment proceedings in cases involving Virginia businesses and officials in other states. In order to seek a declaratory judgment in a Virginia circuit court, the business must be organized under the laws of Virginia or be qualified to do business in Virginia and the officials in another state must be asserting that the business is obligated to collect sales and use taxes in the other state based on conduct of the business that occurs wholly or partially within Virginia. In making the decision whether to grant a declaratory judgment, this bill would require the circuit court to evaluate whether the demand from the other state constitutes an undue burden on interstate commerce within the meaning of the

United States Constitution and decisions of the federal courts construing Article I, Section 8, Clause 3 of the United States Constitution (Commerce Clause).

In the United States Supreme Court decision in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), the court determined that the Commerce Clause barred a state from requiring an out-of-state mail-order company to collect use tax on goods sold to customers located within the state because the company had no outlets, sales representatives, or significant property in the state.

It appears that in deciding the merits of a declaratory judgment, Virginia circuit courts would be required to apply the tests set forth in *Quill*.

The declaratory judgment provisions of this bill raise issues with respect to whether a declaratory judgment issued by a Virginia circuit court that prohibits an action, legal under the laws of another state, would interfere with the sovereignty of that other state. In order to obtain such a declaratory judgment, the Virginia plaintiff would first have to have proper service of process against the official in the other state. Without the full cooperation of law enforcement officers in the other state, this may be difficult. Finally, such a declaratory judgment by interfering with the ability of the other state to obtain payment from a Virginia business after such a claim has been adjudicated in the other state, could undermine Virginia's reciprocity with respect to the full faith and credit granted to tax collection suits filed by one state in another state to collect unpaid taxes.

Constitutional nexus

Code of Virginia § 58.1-612 sets out the standards for requiring out-of-state dealers to collect the Virginia use tax on sales into the Commonwealth. In *Quill*, the United States Supreme Court ruled that these businesses must have some type of a physical presence within a state in order to require the collection of the tax.

Virginia follows the United States Supreme Court ruling with respect to requiring tax collection by out-of-state dealers, and this bill would not affect the Commonwealth's current position. As a result, businesses that sell to Virginia customers only via the Internet or mail order, are not required to collect Virginia taxes.

However, 2003 legislation allows the Commonwealth to require that businesses and their affiliates who want to do business with the state meet the more stringent state law requirements to register and collect the sales tax. This is not in conflict with the United States Supreme Court cases because the Commonwealth as a purchasing entity has the right to set certain terms and conditions for vendors who wish to do business with Virginia. North Carolina has a similar requirement.

This bill would effectively negate this 2003 legislation.

Senate Bill 668 is identical to this bill.

cc : Secretary of Finance

Date: 2/8/2004 mch