DEPARTMENT OF TAXATION
2017 Fiscal Impact Statement

1. Patron Vivian E. Watts

2. Bill Number HB 2058
House of Origin:
_____ **Introduced**
_____ **Substitute**
_____ **Engrossed**

3. Committee Passed House and Senate

4. Title Retail Sales and Use Tax; Dealer Registration Based on Inventory

Second House:
_____ **In Committee**
_____ **Substitute**
_X_ **Enrolled**

5. Summary/Purpose:

This bill would clarify that the storage of inventory within the Commonwealth gives rise to nexus sufficient to require an out-of-state seller to register as a dealer for the collection of sales and use tax on sales to customers within Virginia.

Under current law, it is not clear whether the presence of inventory in Virginia is sufficient to require a dealer to register with the Department.

The effective date of this bill is not specified.

6. Budget amendment necessary: No.

7. No Fiscal Impact. See Line 8.

8. Fiscal implications:

Administrative Costs Impact

The Department of Taxation considers implementation of this bill as routine and does not require additional funding.

Revenue Impact

State Sales and Use Tax (5.3%)	
GF-Unrestricted (Excluding 0.25% Education)	$ 7,489,381
GF-Restricted (Excluding 0.125% Education)	3,679,646
Transportation Trust Fund	2,973,451
Local Option	3,716,814
HMOF (GF Transfer)	371,681
Regional Transportation Funds	1,375,221
Other Non General Fund	
Education (GF Transfer 0.125%)	464,602
Education SOQ (GF Transfer 0.250%)	929,204
Total General Fund	$ 11,169,027
Total Sales and Use Tax	$ 21,000,000

This proposal would generate new state and local annual revenue totaling $21 million beginning in Fiscal Year 2018. The revenue impact of this bill is included in the Introduced Executive Budget.

9. Specific agency or political subdivisions affected: Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Constitutional Nexus

The Commerce Clause of the U.S. Constitution reserves to Congress the power to regulate commerce among the states and with foreign nations. The U.S. Supreme Court has established a four-prong test to be used in determining whether a state tax on an out-of-state corporation's activities in interstate commerce violates the Commerce Clause. A state may require an entity engaged in interstate commerce to collect taxes on its behalf provided the tax is 1) applied to an activity with a substantial nexus with the taxing State; 2) is fairly apportioned; 3) does not discriminate against interstate commerce; and 4) is fairly related to the services provided by the state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). The U.S. Supreme Court has determined, in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992) 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 when the company had no outlets, sales representatives, or significant property in the state. In this case, the Court determined that only Congress has the authority to require out-of-state vendors without a physical presence in a state to register and collect that state's tax.

Virginia law specifically sets out the standards for requiring out-of-state dealers to collect the Virginia Retail Sales and Use Tax on sales into the Commonwealth. The law provides

that a dealer is deemed to have sufficient activity within the Commonwealth to require that dealer to register to collect the Virginia Retail Sales and Use Tax if the dealer:

- Maintains an office, warehouse, or place of business in the Commonwealth;
- Solicits business in the Commonwealth, by employees, independent contractors, agents or other representatives;
- Advertises in Commonwealth publications, on billboards or posters located in the Commonwealth, or through materials distributed in the Commonwealth;
- Regularly makes deliveries into the Commonwealth by means other than common carrier;
- Continuously, regularly, seasonally, or systematically solicits business in the Commonwealth through broadcast advertising;
- Solicits business in the Commonwealth by mail, provided the solicitations are continuous, regular, seasonal, or systematic and the dealer benefits from any banking, financing, debt collection, or marketing activities occurring in the Commonwealth;
- Is owned or controlled by the same interests which own or control a business located within this Commonwealth;
- Has a franchisee or licensee operating under the same trade name in the Commonwealth, if the franchisee or licensee is required to obtain a certificate of registration; or
- Owns tangible personal property that is rented or leased to a consumer in the Commonwealth, or offers tangible personal property, on approval, to consumers in the Commonwealth.

Actions by Other States

Restricted by the United States Constitution and the Supreme Court's decision in *Quill*, states have limited ability to require remote sellers to collect taxes on sales made into the state. With growing retail sales on the Internet and declining tax receipts, states have taken several different approaches to address to the revenue being lost from sales by out-of-state retailers to the residents of their states. Although individuals who purchase goods from out-of-state firms via the Internet or mail order owe their states of residence use tax on their purchases in lieu of sales tax, states find it difficult to enforce this obligation.

States Challenging Quill

Six states currently have or are contemplating laws or administrative actions that directly challenge the physical presence standard from *Quill* or try to circumvent *Quill* with use tax reporting requirements.

Alabama has adopted Regulation 810-6-2-.90.03, effective January 1, 2016, which creates nexus for out-of-state sellers with sales of $250,000 or more into the state when those sellers do certain other enumerated activities such as use a warehouse or storage place in the state or conduct certain solicitation related activities.

South Dakota enacted S.B. 106 in 2016 requiring sales tax collection for sellers with either annual sales into South Dakota in excess of $100,000 or 200 separate annual transactions within the state.

In 2016, Tennessee put forth Proposed Rule 1320-05-01-129, which would require out-of-state sellers with more than $500,000 of sales in the state who also systematically solicit sales to register for the collection of sales tax.

Wyoming's pre-filed bill H.B. 19 would require remote sellers to collect sales tax when they annually have more than $100,000 in sales or at least 200 sales transactions into Wyoming.

Vermont bill H. 873, signed into law as Act 134, requires out-of-state vendors who do not remit sales tax to provide information on sales tax to Vermont purchasers. This law takes effect on the earlier of July 1, 2017 or the first day of the first quarter after the new sales and use tax reporting requirements are implemented in Colorado.

Colorado Rev. Stat. §39-21-112.3.5 imposes requirements on retailers who do not collect sales taxes to do three things: (1) send a transactional notice to Colorado purchasers notifying them they may be subject to Colorado use tax; (2) send Colorado customers whose purchases total more than $500 an annual purchase summary reminding them of their obligation to pay use taxes; and (3) send the Colorado Department of Revenue an annual customer information report listing their customers' names, addresses, and total amounts spent.

Streamlined Sales and Use Tax Agreement

The Streamlined Sales and Use Tax Agreement (SSUTA) is an agreement that is the result of a cooperative effort of states, local governments, and the business community to simplify sales and use tax collection and administration by retailers and states. To date, twenty-four states have passed legislation to conform to the SSUTA: Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Vermont, Washington, West Virginia, Wisconsin and Wyoming.

The SSUTA eases administrative burdens on retailers by embracing more efficient administrative procedures, tax law simplification, and the utilization of emerging technologies. Sales sax law simplification is achieved through, among other provisions, uniform tax definitions, rate simplification, uniform sourcing, and the state-funding of the administrative cost of participation.

Congressional Efforts

In 2013, the Senate passed the Marketplace Fairness Act of 2013 (S. 743) (MFA) to allow states that joined SSUTA or took action to simplify their sales tax laws to require remote sellers to collect their sales taxes. The legislation stalled in the House. Representative Chaffetz has introduced the Remote Transactions Parity Act of 2015 (H. R. 2775) (RTPA), which is very similar to the MFA.

Representative Goodlatte has circulated an alternative to the RTPA, the Online Sales Simplification Act of 2016 (Draft) (OSSA). The OSSA authorizes states to tax remote sales if they participate in a new remote sales tax regime focused on simplifying sales tax collection for remote sellers. Remote sellers would be required to collect sales tax for each remote sale using the tax base of the state in which the seller is located and the tax rate of the destination state. The OSSA mandates the creation of a clearinghouse which would accept and process tax remittance payments from remote sellers and then distribute those payments to participating states.

Virginia's Sales Tax Nexus

Under current law, the Retail Sales and Use Tax generally applies to sales of tangible personal property to customers within Virginia. However, because the U.S. Supreme Court's held in *Quill* that the Commerce Clause requires physical presence as a prerequisite for nexus, many out-of-state sellers avoid collecting sales tax on their sales to Virginia customers by choosing not to have a physical presence within Virginia's borders. Many remote sellers who sell to Virginia customers store inventory in Virginia fulfillment centers and warehouses owned by unrelated third parties. These sellers typically do not have any other physical presence within the Commonwealth and therefore are arguably not required to register as dealers for sales tax collection under current law because, under Virginia law, having inventory stored within Virginia is not listed as one of the factors requiring registration.

Proposal

Under this bill, the presence of inventory within Virginia in a fulfillment center or warehouse will give rise to an out-of-state dealer's obligation to collect sales tax on sales to Virginia customers. This bill would allow Virginia to exercise the full authority granted to all states under the Constitution as set forth in *Quill*.

Similar Legislation

Senate Bill 962 is identical to this bill.

cc : Secretary of Finance

Date: 2/24/2017 VB
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