

Internet sales tax held constitutional

By Robert W. Wood

Californians, both consumers and those in business, should be watching the roiling sales and use tax disputes. And they should be paying sales or use tax. You pay sales tax when you make a retail purchase in the state or via phone, mail or Internet from a merchant with a California presence. You pay use tax when you buy from an out-of-state retailer who does not charge you California sales tax.

Your act of bringing or shipping the goods into California triggers your use tax liability. Those who can't quite bring themselves to pay use tax should keep some money aside to pay it later if they have to. But let's start with what's happening in New York.

New York's Amazon sales tax – requiring tax collected at time of purchase by online sellers with affiliate programs – has been held constitutional by the New York Court of Appeals. See *Overstock.com, Inc. & Amazon.com, LLC v. New York State Department of Taxation and Finance*, 2013 NY Slip Op. 02102 (N.Y. Mar. 28, 2013). There were two giant plaintiffs in the case, Amazon and Overstock, and they failed to convince the New York court that the application of New York's Amazon law (which is similar to California's) was unconstitutional.

Do we care about this decision in California? We should. California, even more than New York, faces a budget crisis. The days of looking the other way are fast disappearing.

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Any California tax practitioner will tell you that California has always been more aggressive in tax matters than the IRS, and there are suggestions this notorious toughness is growing even more accentuated. And although some online merchants both large and small may tell you otherwise, the days of no sales and use tax on online purchases are probably coming to a close.

Curiously, though, Amazon and Overstock, the two plaintiffs in the New York case, are unlikely to be affected. Despite its no-tax past, Amazon now supports nationwide sales tax rules.

Overstock stopped its New York affiliate program, which was the nexus that required Overstock to collect New York's sales tax under the now upheld law. Apart from the nuances of the New York law and our own California sales and use tax law, the writing is on the wall. For big and small merchants everywhere, this is yet another indication that we all better pay.

Sales tax applies in 45 states and D.C., so why does it surprise us when we order online and get stuck with tax? Online sellers are already required to collect sales tax from customers in their own states. Tax also applies to phone, mail or online orders if the merchant has a presence like a store in our state.

So says *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), the 1992 U.S. Supreme Court case that is still good law. It says retailers must collect sales tax from out-of-state customers only if they have a physical presence (such as a store, warehouse or office) in the customer's state. Yet that was in the dark ages of technology, and

Internet purchases are now a large and growing percentage of all retail sales.

Many states including New York and California passed modifications to their sales and use tax law to expand sales tax. Since traditionally the best way to collect is at the point of sale, the idea was to require merchants to collect taxes even if they did not have a retail store presence in the state. It would be enough if they merely have in-state affiliates they contract with and link to.

More than a few consumers, businesses and lawyers have wondered whether this is constitutional under *Quill*, the case about stores and warehouses. Clicks and links are hardly the same, but the New York Court of Appeals upheld New York's Amazon law and says it passes muster under *Quill*.

Amazon was fighting a similar court battle in California but dropped its litigation when it agreed with the Franchise Tax Board that it would begin collecting the tax Oct. 15, 2012. That was a controversial move at the time, representing an about-face from Amazon's adamant no-tax policy.

Eventually, some hope that a U.S. Supreme Court case will consider whether the kind of new breed of nexus many Amazon tax statutes apply is constitutional under *Quill*. For now, however, it is safe to assume that it is constitutional. In fact, Amazon's and Overstock's loss in a 4-to-1 *decision* by the New York Court of Appeals is likely to be followed.

The appellate court found Internet and mail order sales to be similar. To the court, the key was the affiliations and links that gear sites to local audiences including radio stations, religious institutions and schools. Many websites urge local constituents to support them by making purchases through Amazon links. Essentially, through these types of affiliation agreements, a vendor can be considered to have established an in-state sales force.

So said the court. This is more than mere advertising, which would not create nexus under *Quill*. Yet many disagree and this last chapter in this saga clearly hasn't yet been written. Interestingly, though Amazon has mostly now reversed course on its no-tax mantra, it does say it wants a nationwide solution, not state-by-state answers.

That brings us to the pending battleground that is federal law. Even as far back as 1992, there was discussion of enacting a federal sales and use tax law that would not impose a new tax but implement the myriad state laws and impose some uniformity. There have recently been three competing bills for the last few years, though now the recently reintroduced bill called the Marketplace Fairness Act (S.336/H.R.684) is the vehicle of choice.

In the current climate of Washington, there are bigger problems than state sales tax. Still, the Senate passed it in a symbolic vote demonstrating support for the Marketplace Fairness Act. But it really wasn't the act itself, but rather a budget amendment, and only in the Senate.

So will it pass? Not necessarily, and not necessarily soon. But regardless, the days of tax-free clicks are numbered. And as California ramps up its use tax collection techniques, pay it or keep some money handy. You just may need it.



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