ECONOMIC NEXUS: WHAT'S NEW AND WHAT'S COMING

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With You Today

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Agenda

- Sales Tax Economic Nexus Developments
  - Economic Nexus Updates
  - Updates on Home Rule States
  - Notable Court Cases

- State Income Tax Economic Nexus Developments
  - Various State Approaches to Economic Nexus
  - PL 86-272 Developments

ECONOMIC NEXUS UPDATES

Nexus Changes, Remote Sellers, and Marketplace Facilitators

Multitstate Developments

State of *Wayfair* – Developments

- All states imposing a sales and use tax have enacted economic nexus provisions in some form applying to remote sellers, marketplace providers
  - Missouri: effective Jan. 1, 2023
- Post-*Wayfair* litigation challenging complex decentralized state sales tax regimes with self-administered home-rule local jurisdictions
  - *Halstead Bead v. Lewis*: AZ-based online business filed lawsuit in LA federal court alleging that Louisiana's decentralized sales tax system presents undue compliance burdens for remote sellers under *Wayfair*
  - *Online Merchants Guild v. Hassell: PA Online sellers notified of in-state filing requirements due to Amazon FBA inventory*
- Audit cycle starts to ramp up
  - 5 years in and states are starting to audit post-Wayfair periods
  - Tracking nexus
- Tweaks to state marketplace facilitator laws:
  - Rapid adoption of marketplace provisions resulted in sales tax compliance difficulties for marketplace facilitators navigating sales tax collection obligations and responsibilities

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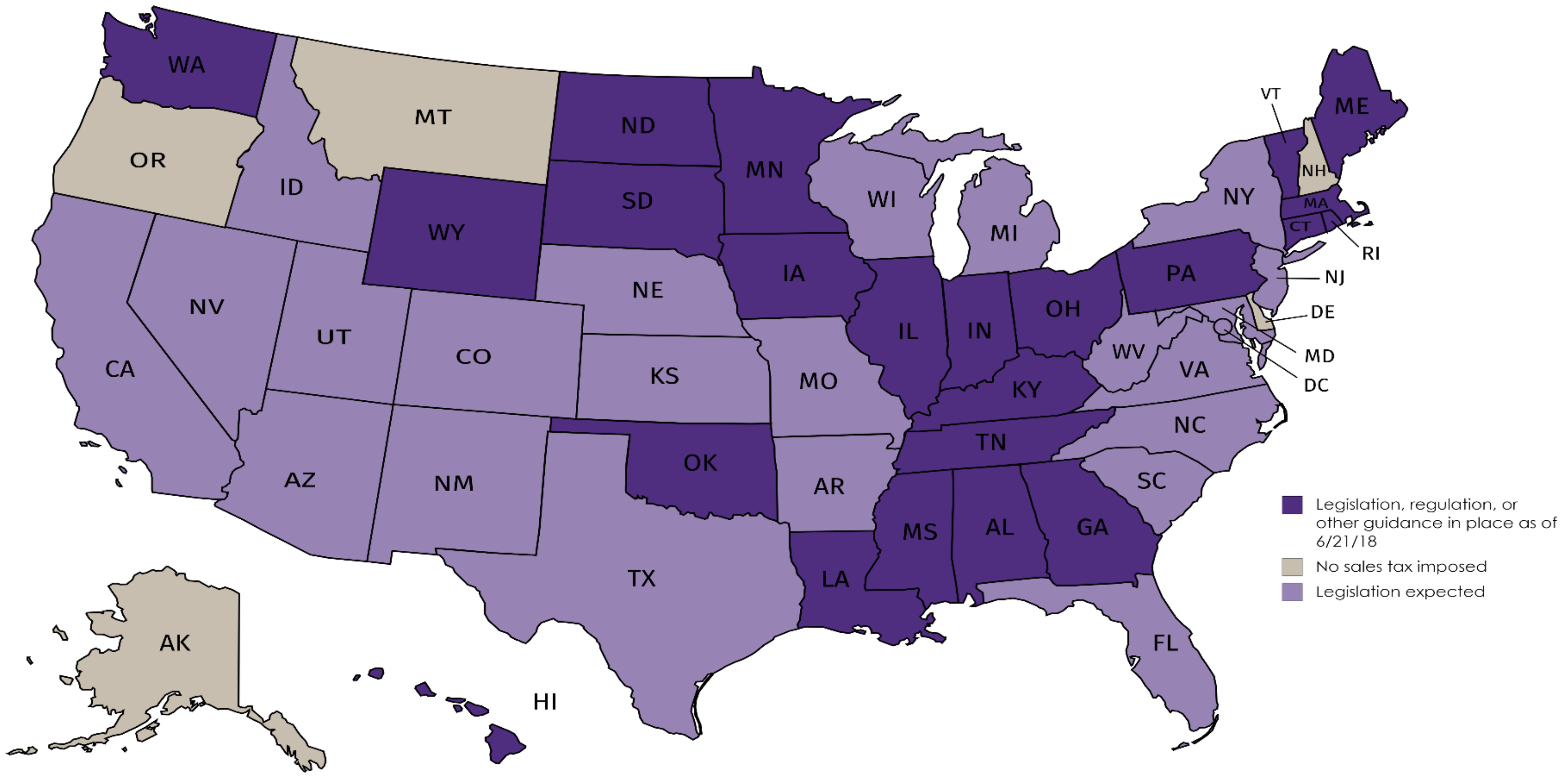
Sales Tax Economic Nexus Footprint As of 6/21/18



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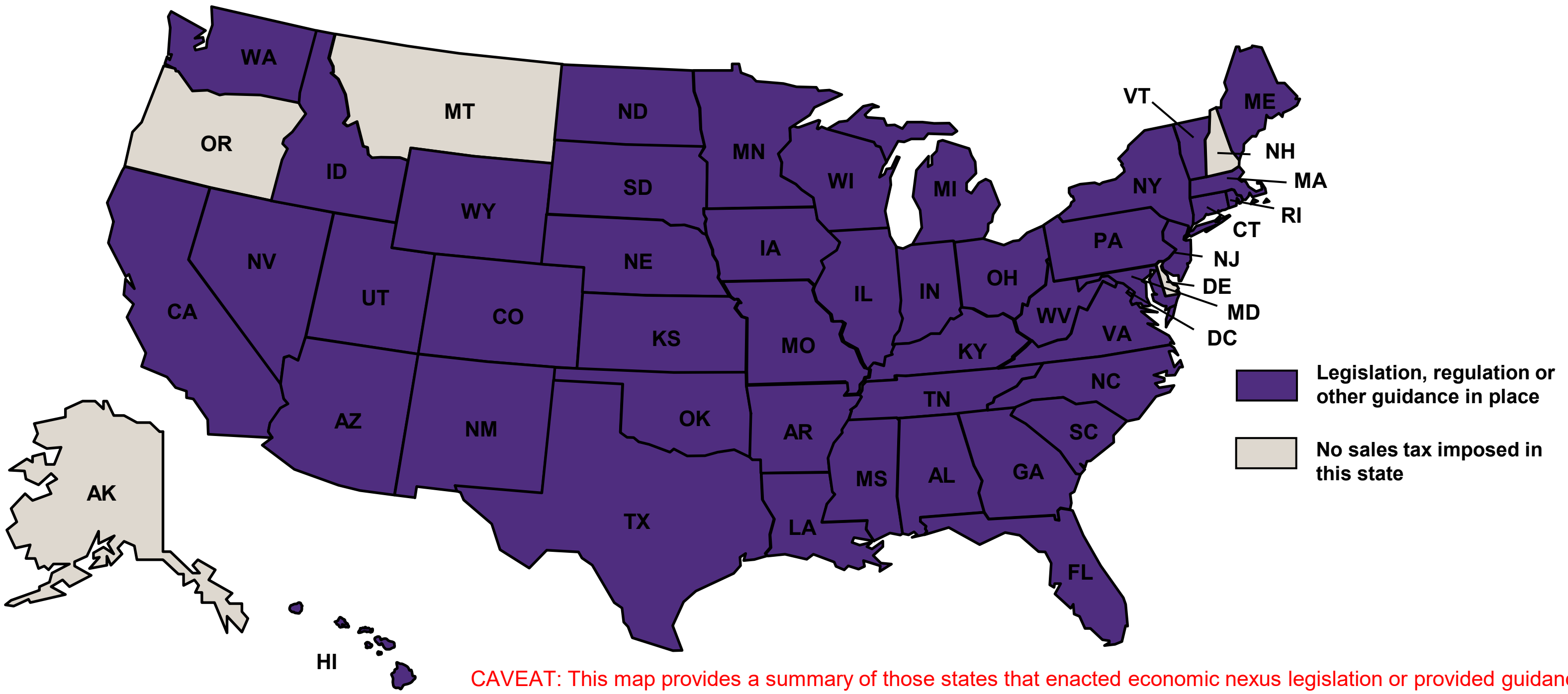
Sales Tax Economic Nexus Footprint As of 1/1/23



CAVEAT: This map provides a summary of those states that enacted economic nexus legislation or provided guidance as of January 1, 2023, and where we anticipate laws to be passed in the future. Due to amount of activity by the states around economic nexus, it is important that company activities are reviewed on a state-by-state basis to determine the potential sales tax nexus implications as the rules are continually changing.

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Challenges for Businesses

Managing Nexus

- Sales Thresholds
  - Gross sales, Retail Sales, Taxable sales
  - Amounts range from $100k*- $500k

- Transaction thresholds
  - Some states removing the transaction requirement
  - Generally, 200 transactions

- Annual vs. Rolling period

*OK $10,000 sales threshold to collect or comply with notice and reporting requirements remains in effect

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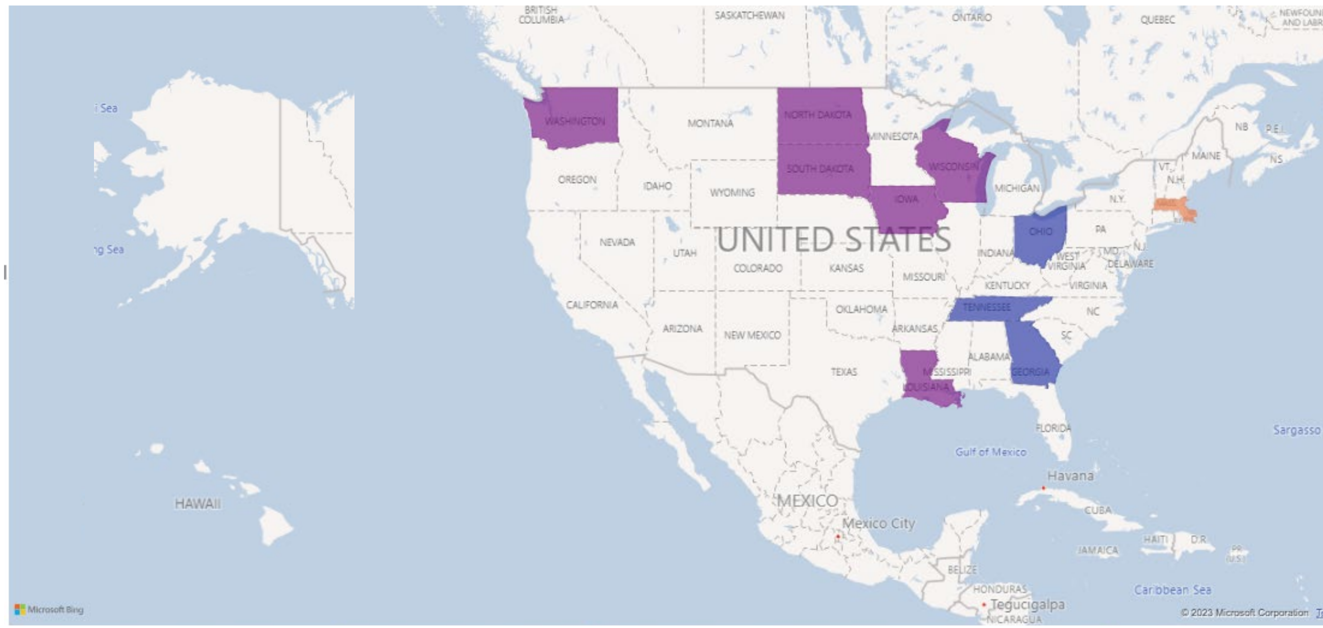
Changes in Economic Nexus Threshold Requirements

- 6 states have eliminated transaction thresholds
- 3 states have reduced the sales threshold to $100,000
- MA reduced the sales threshold to $100,000 AND eliminated the transaction threshold



Changes to Economic Nexus Thresholds: ● Sales Threshold Reduced to $100,000 ● Sales Threshold Reduced to $100,000 AND Transaction Threshold Eliminiated ● Transaction Threshold Eliminated

UPDATES ON HOME RULE STATES

Alabama, Louisiana, and Colorado

Locally Administered Jurisdictions

Remote Seller Challenges

- Volume of returns
  - Lodging, Food & Beverage, Bottled Water, Alcohol, etc.
- Volume of audits
- Misinformation
  - Local jurisdictions can't keep up with changes
- Varying Laws
  - Local jurisdiction tax base, non-uniform exemptions, rates and types of taxes

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Locally Administered Jurisdictions

Marketplace Facilitator Challenges

- Responsible for local taxes
  - AL – Simplified return; TX must collect local tax
- Multiple tax types- occupation taxes, food and beverage, plastic bag fee's, bottled water, etc.
  - May be administered locally requiring additional returns
  - Origin vs. destination
- Information Reporting – Requests to include seller information, state tax returns
- Local B&O taxes

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Alabama

Reporting Options

- Traditional City & County Tax Return
  - Centralized reporting, single payment method available
  - Administered locally, requires separate registrations, audits, etc.

- Simplified Sellers Use Tax program
  - Flat 8% rate on remote sales made into Alabama.
  - Formal application
  - Available to marketplace facilitators

Louisiana

Reporting Options

- Physical presence = traditional registrations with each Parish
  - No central registration and reporting available
  - Parish E-file website available for local returns
- Remote Sellers – >$100k or 200 transactions effective July 1, 2020 may register on the Louisiana Sales and Use Tax Commission for Remote Sellers
- Remote Retailers - >$50k; reporting requirement unless voluntarily registers to collect and remit sales tax
- Direct Marketers – sellers with no physical or economic presence may voluntarily collect at 8.45%
- Marketplace facilitators are also eligible remote sellers
- Sales and Use Tax Commission For Remote Sellers (SUTCRS?)- allows both state and local tax remittance from a single portal
  - Single registration number
  - Parishes receive a list of who is registered
  - Audits handled by SUTCRS

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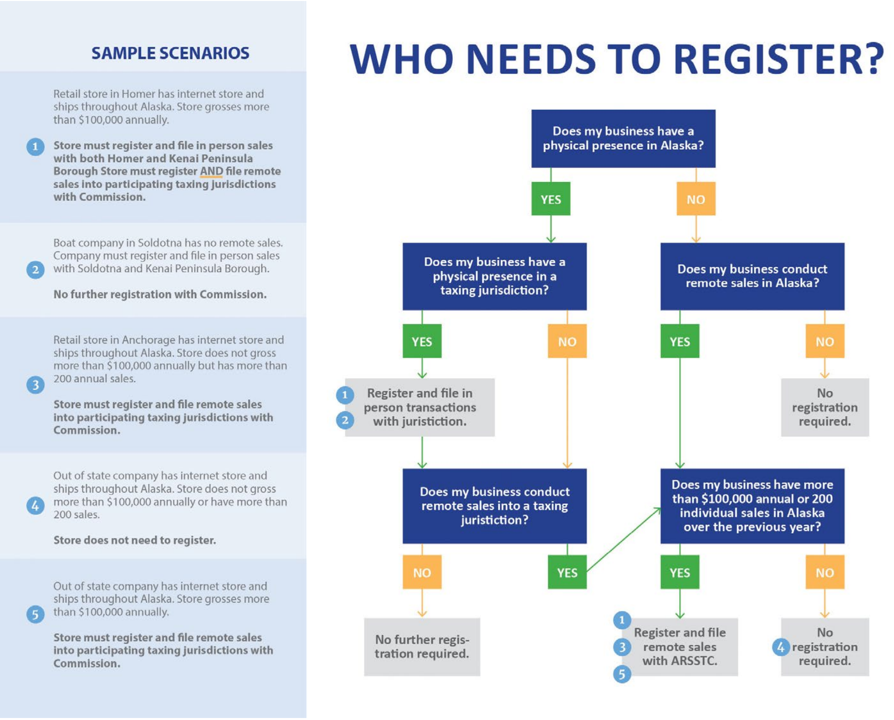
Colorado

- Colorado Model Ordinance- provides a standard model for local jurisdictions
  - $100k sales into the state
  - Intended to reduce complexity
  - Does not address tax base or uniform exemptions

- Sales & Use Tax System (SUTS) – Designed to allow taxpayers a single return to remit sales and use taxes for state and local taxes.
  - Voluntary
  - Participating jurisdictions- 51 full, 5 MPF only and 1 economic nexus only
  - Sales tax only
  - Administration, registration and tax base are local
  - State highly recommends jurisdictions to sign up to avoid potential litigation

Alaska

- Alaska Remote Sellers Sales Tax Commission
  - Local tax only
  - Only available to remote sellers
  - $100k sales or 200 transactions in state
    - Gross sales, including marketplace facilitator sales (exception if 100% of sales are through MPF. Affidavit required)
  - 57 participating jurisdictions*



*As of 6/31/2023

LEGISLATIVE UPDATES

Online Merchants Guild v. Hassell, Pa. Commw. Ct. Sept. 9, 2022

- Commonwealth Court ruled that PA Dept. of Revenue could not collect sales tax from out-of-state retailers with inventory in the state through participation in Amazon FBA program – insufficient contact with the state to create nexus for due process purposes

- Mar. 2021: Department mails notices to remote FBA sellers, informing them of potential sales tax collection/remittance obligations due to storage of inventory in-state
  - Launches voluntary compliance program offering limited lookback to Jan. 1, 2019 and penalty relief for participating remote sellers
  - Registration demand letters suggest that failure to participate in VCP may result in additional enforcement action, forfeiture of penalty relief, limited lookback

- Online Merchants Guild brings lawsuit in state court on behalf of FBA sellers

- Commonwealth Court finds FBA sellers lack minimal connection with PA for due process nexus – under FBA arrangement, sellers do not have knowledge their inventory is located in PA. “Purposeful availment” of the state’s market requires more than a prediction that the taxpayer’s goods reach the taxing state.

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Halstead Bead v. Lewis

- *Halstead Bead v. Lewis*, U.S. District Court, E.D. La., filed Nov. 15, 2021
  - AZ-based online business filed lawsuit in LA federal court alleging that Louisiana's decentralized sales tax system presents undue compliance burdens for remote sellers under *Wayfair*
    - Argued lack of uniformity in administration between state sales tax and local sales taxes administered by Louisiana's 64 parishes
  - Case dismissed in federal district court, holding lawsuit was barred by the federal Tax Injunction Act (TIA) –remedy available in state court
  - On appeal to Fifth Circuit U.S. Court of Appeals, taxpayer argued case was moot after enactment of two LA bills:
    - H.B. 171: drops 200-transaction threshold from state's economic nexus threshold;
    - H.B. 558: creates a single system for remitting state and local sales tax beginning 2024
  - July 2023: Fifth Circuit affirmed district court, dismissing the case on TIA grounds

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VARIOUS STATE APPROACHES TO STATE INCOME TAX ECONOMIC NEXUS

Economic Nexus States – Different Approaches

1. States With Factor-Based Economic Nexus Threshold

2. States With Economic Nexus Based on Statute/Rule, But Without Thresholds

3. States That Impose Tax “To Fullest Extent Under the US Constitution”

4. States With No Guidance on Economic Nexus

Factor-Based Economic Nexus States

COLORADO

39-22-301.1(2)(a)(ii)

Business entities organized outside the State are doing business in this State, have substantial nexus, and are subject to Colorado filing requirements and, if applicable, Colorado income tax imposed by Article 22 of Title 39 when in any tax period the property, payroll or sales of the business in the State, as such property, payroll, and sales are defined below in Subsection (c), exceeds the thresholds set forth in Subsection (b).

39-22-301.1(2)(b) Substantial nexus is established if any of the following thresholds is exceeded during the tax period:

39-22-301.1(2)(b)(i) a dollar amount of $50,000 of property; or

39-22-301.1(2)(b)(ii) a dollar amount of $50,000 of payroll; or

39-22-301.1(2)(b)(iii) a dollar amount of $500,000 of sales; or

39-22-301.1(2)(b)(iv) twenty-five percent of total property, total payroll or total sales.

STATES WITH FACTOR-BASED ECONOMIC NEXUS PROVISIONS

Alabama	Maine	New York City	Texas
California	Massachusetts	Ohio (CAT)	Washington (B&O)
Colorado	Michigan	Oregon (CAT)	
Connecticut	New Jersey	Pennsylvania	
Hawaii	New York	Tennessee	

States With Economic Nexus Statutes/Rules, But Without Thresholds

WISCONSIN

71.22(1r)

"Doing business in this state" includes, except as prohibited under P.L. 86-272, issuing credit, debit, or travel and entertainment cards to customers in this state; regularly selling products or services of any kind or nature to customers in this state that receive the product or service in this state; regularly soliciting business from potential customers in this state; regularly performing services outside this state for which the benefits are received in this state; regularly engaging in transactions with customers in this state that involve intangible property and result in receipts flowing to the taxpayer from within this state; holding loans secured by real or tangible personal property located in this state; owning, directly or indirectly, a general or limited partnership interest in a partnership that does business in this state, regardless of the percentage of ownership; and owning, directly or indirectly, an interest in a limited liability company that does business in this state, regardless of the percentage of ownership, if the limited liability company is treated as a partnership for federal income tax purposes.

STATES WITH ECONOMIC NEXUS STATUTES/RULES, BUT WITHOUT THRESHOLDS

Indiana	New Hampshire	Rhode Island
Minnesota	Oregon (Income Tax)	Wisconsin

States That Impose Tax "To Fullest Extent Under the US Constitution"

GEORGIA

48-7-31(a)

The tax imposed by this chapter shall apply to the entire net income, as defined in this article, received by every foreign or domestic corporation owning property within this state, doing business within this state, or deriving income from sources within this state to the extent permitted by the United States Constitution. A corporation shall be deemed to be doing business within this state if it engages within this state in any activities or transactions for the purpose of financial profit or gain whether or not:

> **48-7-31(a)(1)**
>
> The corporation qualifies to do business in this state;
>
> **48-7-31(a)(2)**
>
> The corporation maintains an office or place of doing business within this state; or
>
> **48-7-31(a)(3)**
>
> Any such activity or transaction is connected with interstate or foreign commerce.

STATES THAT IMPOSE TAX "TO FULLEST EXTENT UNDER THE US CONSTITUTION"

Georgia	Maryland

States That Impose Economic Nexus In Other Situations

- States That Impose Economic Nexus Upon Financial Organizations

Indiana	Minnesota	Tennessee	West Virginia

The above states all have factor-based economic nexus provisions for financial organizations.

- States That Have Statutes Or Case Law That Impose Economic Nexus Upon Royalty/Intangibles Companies

Arkansas	Louisiana	New Mexico	Oklahoma
Iowa	Maryland	North Carolina	South Carolina

INCOME/FRANCHISE/ GROSS RECEIPTS TAXES: Factor-Based Presence Thresholds and Economic Nexus Rules

This chart summarizes "factor-based presence" nexus thresholds for income, franchise and gross receipts taxes. A state with a "factor-based presence" nexus standard provides that an out-of-state entity has "substantial nexus" and a filing requirement in a state if the company's sales, property and/or payroll exceed the thresholds established by the state. The chart summarizes the "sales" threshold in each state with "factor-based presence" nexus standards that would subject an out-of-state company to tax even without a physical presence.

In addition, there are numerous states that impose "economic" nexus on out-of-state companies but have not established factor-based thresholds (i.e., Indiana, New Hampshire, Wisconsin). These states create economic nexus standards by statute or case law.

State	Tax Type	Thresholds/ Other
Alabama	Income	$596,000 (1)
Alaska	Income	Statute/Rule (2)
Arizona	Income	Case Law (2)
Arkansas	Income	Statute/Rule (2)
California	Income	$690,144 (1)
Colorado	Income	$500,000 (1)
Connecticut	Income	$500,000
Delaware	Income	
District of Columbia	Income	
Florida	Income	Statute/Rule (2)
Georgia	Income	
Hawaii	Income	$100,000
Idaho	Income	
Illinois	Income	
Indiana	Income	Statute/Rule (3)
Iowa	Income	Statute/Rule (2)
Kansas	Income	
Kentucky	Income	Statute/Rule (2)
Louisiana	Income	Case Law (2)
Maine	Income	$500,000 (1)
Maryland	Income	Case Law (2)
Massachusetts	Income	$500,000
Michigan	Income	$350,000
Minnesota	Income	Statute/Rule (3)
Montana	Income	
Mississippi	Income	

State	Tax Type	Thresholds / Other
Missouri	Income	
Nebraska	Income	
Nevada	Gross Receipts	
New Hampshire	Income	Statute/Rule
New Jersey	Income	$100,000
New Mexico	Income	Case Law (2)
New York	Income	$1,138,000
New York City	Income	$1,000,000
North Carolina	Income	Statute/Rule (2)
North Dakota	Income	
Ohio	Gross Receipts	$500,000 (1)
Oklahoma	Income	Case Law (2)
Oregon	Income	Statute/Rule
Oregon	Gross Receipts	$750,000
Pennsylvania	Income	$500,000
Rhode Island	Income	Statute/Rule
South Carolina	Income	Case Law (2)
South Dakota	No Tax	
Tennessee	Income/Franchise	$500,000 (1) (3)
Texas	Franchise	$500,000
Utah	Income	
Vermont	Income	Statute/Rule
Virginia	Income	Statute/Rule
Washington	Gross Receipts	$100,000 (1)
West Virginia	Income	Statute/Rule (3)
Wisconsin	Income	Statute/Rule
Wyoming	No Tax	

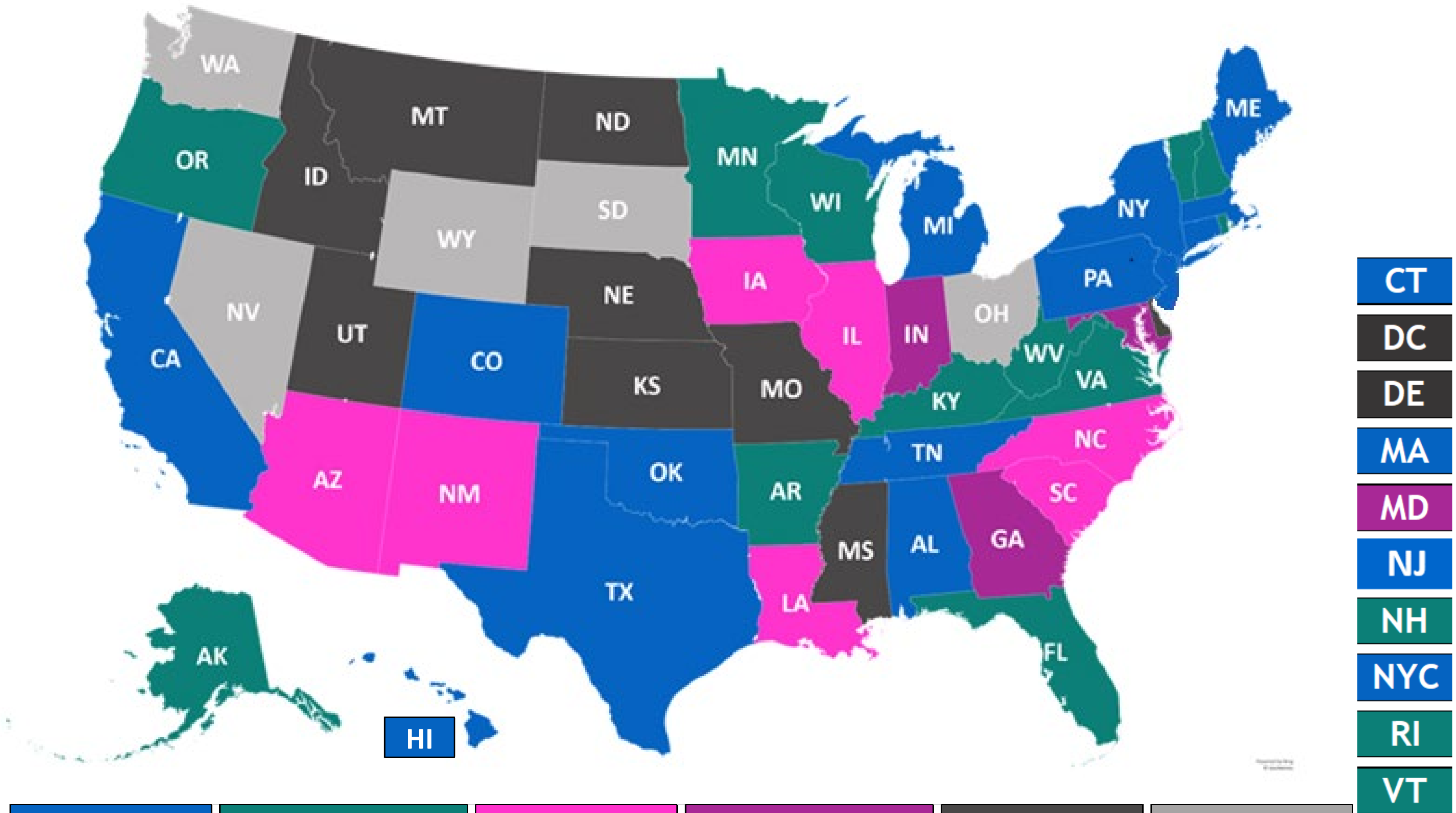
(1)States that also have factor-based nexus thresholds for property and payroll. Even if a company does not meet the "sales" factor-based threshold, it would still have nexus if it exceeds the state's payroll or property standards. In certain states with factor-based presence thresholds, a company will have nexus if 25% or more of its total sales (or more than 25% of its total property or payroll, for states with property and payroll thresholds) are from the state, even if the company does not exceed the factor-based thresholds.

(2)States that impose economic nexus on out-of-state companies based on statutory, regulations or other administrative decisions, and/or court decisions involving financial services, out-of-state licensors of trademarks, tradenames and other intangibles (e.g., franchises).

(3)States that impose factor-based nexus thresholds on out-of-state financial institutions.

States with Corporate Income Tax Economic Nexus Thresholds

(AS OF 8/31/2023)



Factor-Presence Nexus

Other economic nexus statute or rule

Economic nexus case law

Fullest extent under US Constitution

No Guidance

No CIT

PL 86-272 DEVELOPMENTS

PL 86-272: MTC's New Interpretation for Internet-Based Activities

- On August 4, 2021, MTC issued its 4th revision of the "*Statement of Information Concerning Practices of Multistate Tax Commission and Supporting States Under Public Law 86-272*"

- MTC's revised interpretation of PL 86-272 includes a new section for unprotected (and a few protected) "internet-based activities". If followed by states, the protections of PL 86-272 will largely be eliminated for most multistate businesses with a website.

- MTC's revised interpretation provides as follows:

  - The Supreme Court recently opined, in South Dakota v. Wayfair, Inc., construing the Commerce Clause, that an Internet seller *"may be present in a State in a meaningful way without the presence being physical in the traditional sense of the term."*

  - "As a general rule, when a business interacts with a customer via the business's website or app, the business engages in a business activity within the customer's state."

State Responses to MTC's Revised Statement - California

- Even though not a MTC "compact member," CA became the first state to formally adopt the MTC's revised interpretation to PL 86-272 in CA Technical Advice Memorandum (TAM) 2022-01 issued February 14, 2022.

- Adopts all of the provisions from the MTC's new "Internet Based Activity" section

BDO Alert – California 86-272
CA TAM 2022-01

State Responses to MTC's Revised Statement

California
TAM 2022-01 (Feb. 14, 2022)

- CA became the first state to formally adopt a revised interpretation of P.L. 86-272 in response to the MTC's new "Internet-Based Activity".
- CA's guidance indicates that having an employee who telecommutes on a regular basis performing non-sales activities is not protected.
- The TAM acknowledges that CA sellers engaged in internet-based activities in other states considered unprotected by P.L. 86-272 will not be subject to CA's throwback rule.
  - Note: CA's TAM does not specify whether the state will attempt to enforce the revised interpretation of P.L. 86-272 retroactively or prospectively.

BDO Alert – California 86-272
CA TAM 2022-01

PL 86-272: New MTC and CA Interpretation for Internet-based Activities

According to the MTC and CA, the following internet-based activities are NOT protected:

1. Providing post-sale assistance through an electronic chat or email that customers access through the company's website.
2. Soliciting or receiving online credit card applications.
3. Inviting and/or accepting applications for employment through a web-based platform.
4. Placing internet "cookies" on computers of customers that are designed to gather market or product research.

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5. Transmitting code or electronic instructions via the internet to fix or upgrade products.
6. Offering or selling extended warranty services over the internet.
7. Contracting with a marketplace facilitator to house products or inventory or to fulfill orders.
8. Contracting with in-state customers to stream videos and music to electronic devices.

PL 86-272: New MTC and CA Interpretation for Internet-Based Activities

- According to the MTC and CA, the following are examples of internet activities that, if performed alone, continue to fall under the protection PL 86-272
  1. Posting a static FAQ to assist customers.
  2. Placing internet "cookies" that are used ancillary to the solicitation of orders such as to remember items in a shopping cart.
  3. Offering only TPP for sale on a website.

- CA TAM acknowledges that CA sellers engaged in internet-based activities in other states considered unprotected by PL 86-272 will not be subject to CA's throwback rule

State Responses to MTC's Revised Statement

California

American Catalog Mailers Association v Franchise Tax Board (August 19, 2022)

- On August 19, 2022, the American Catalog Mailers Association filed, what appears to be, the first complaint to challenge the MTC's revised interpretation of P.L. 86-272 against California.
- The case will undoubtedly be appealed by the losing party, so stay tuned for further updates.

Open Questions on MTC's Revised Interpretation for Internet-Based Activities

- Will other states adopt the MTC's revised interpretation?
  - Adopted: NJ (TB-108, Issued 9/5/2023)
  - Proposed: NY, MN. OR proposed but is now delaying implementation
  - More states likely to formally adopt or <u>take the new position on audit</u>

- Will states attempt to apply the MTC's Revised Statement retroactively?
  - We are already seeing some states take the MTC's internet-based activities position on audit

- How much deference will courts give to the MTC's revised interpretation?

- Will Congress update PL 86-272, which was always intended to be a temporary stop-gap back in 1959, by extending its protections to sales of services or repeal the federal law altogether?

- Will the MTC's Revised Statement operate as a double-edge sword for some taxpayers?

State Responses to MTC's Revised Statement

Arkansas

Office of Hearings & Appeals, Administrative Decision Nos. 22-154, 22-155, 22-156 (March 24, 2022)

- Arkansas is an MTC member state, and the case arose out of an MTC "joint audit" (the MTC also has an audit function ("Joint Audit Program"), and it will audit a taxpayer on behalf of multiple states at one time).

- The audit involved tax years 2014-2016.

- Based on case law, the opinion states that Arkansas applies the "substantial economic presence" standard for income tax.

- The case appears (the facts are heavily redacted) to apply the MTC's new P.L. 86-272 position on internet-based activities. Although an MTC state, Arkansas has not formally adopted the revised MTC statement. Regardless, the revised MTC statement appears to have been applied on audit by the MTC.

State Responses to MTC’s Revised Statement

Arkansas (cont’d)

Office of Hearings & Appeals, Administrative Decision Nos. 22-154, 22-155, 22-156 (March 24, 2022)

- A state has to approve the MTC audit. The MTC has the authority to audit, but the state still has to issue the assessment.

- *Takeaway*: P.L. 86-272 is a federal law that pre-empts state laws. As this decision demonstrates, a state may not have to formally adopt the MTC’s guidance, or even issue their own guidance (like California recently did). However, it is likely that we will see more states taking the MTC position on internet-based activities under P.L. 86-272 on audit, especially in “joint audits” handled by the MTC.

- At this time, it is unclear whether states will attempt to apply the revised interpretations of P.L. 86-272 retroactively, but this audit involved tax years prior to the 2018 Wayfair decision.

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Mariano focuses on performing state tax diagnostic reviews designed to provide businesses with an assessment of their state tax position, including the identification of refund and prospective filing opportunities and the reduction of exposure in multiple jurisdictions. In addition, Mariano assists businesses in designing and implementing structural enhancements in order to generate long-term state tax reductions.

Mariano consults on all aspects of state income tax, including participating in mergers and acquisition transactions, due diligence reviews, representation on state tax controversy matters, and assisting companies with state tax compliance and state tax accrual reviews. He has worked with Fortune 1000 and mid-size companies in industries such as manufacturing, retail, consumer services, financial services, real estate, technology, and transportation.

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Jeff leads Grant Thornton's Central Region Sales and Use Tax Compliance practice. He also helps clients to secure significant tax savings by representing them during audits and administrative appeals and helping to secure refunds for overpaid taxes.

Jeff focuses his efforts on creating automated solutions for clients to not only accelerate compliance, but also ensuring improved audit outcomes and enhanced data accessibility. Jeff is an Illinois licensed CPA.

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Questions?