

WAYFAIR IS APPLICABLE TO CANADIAN VENDORS

Business Tax & International Tax Alert
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On June 21, 2018, the U.S. Supreme Court (the “Court”) sent a shockwave through the Internet—and the state and local tax (SALT) community—by issuing its long-awaited decision in the *South Dakota v. Wayfair* case which resoundingly overturned the *Quill* physical-presence nexus standard that had been the law of the land for sales tax purposes for the past several decades.

Even though the case focused on South Dakota retailers, the ruling is huge news for **anyone** buying or selling **anything** on-line. The decision even impacts Canadian vendors selling into the U.S. market in states where the specific thresholds are met. More about the thresholds later. First, some details regarding the sweeping effect of the *Wayfair* decision.

Setting a New Precedent

Before last month, it was unconstitutional for a state to require an out-of-state vendor to collect and remit the state’s sales tax if the vendor didn’t have a *physical presence* within the state. In a 5-4 decision written by Justice Anthony Kennedy, the Court ruled that the “physical presence rule [has] become further removed from economic reality” with every passing year. In the view of the Court’s majority, the growth of e-commerce and Internet sales has made *Quill* unworkable and unreliable as precedent. Because of this, the Court took the somewhat unusual step of overturning *not one, but two*, of its prior decisions on the issue (*Quill* and a 1967 case called *Bellas Hess*). And once it disposed of *Quill*, the Court remanded the case back to the lower courts for a determination on whether South Dakota’s new nexus standard discriminates against or unduly burdens interstate commerce in violation of the dormant Commerce Clause.

And what would South Dakota’s new law provide? The law sets forth **two alternative thresholds** requiring a vendor to collect and remit the South Dakota sales tax if during the prior twelve months it: (i) delivered more than \$100,000 of goods and services into South Dakota, **or** (ii) engaged in 200 or more transactions for the delivery of goods and services into South Dakota. The Supreme Court held that the above thresholds—along with prospective-only applicability and South Dakota’s participation in the multistate Streamlined Sales and Use Tax Agreement—appear to have been “designed to prevent discrimination against or undue burdens upon interstate commerce.”

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Federal and State Legislation

So, even though the case was remanded to the lower courts, a majority of the Supreme Court is sending signals that South Dakota's new law seems OK. While the *Wayfair* case was pending, many tax lawyers and accountants predicted that Congress might step in once the dust settles on the decision, to set up "dollar and transaction threshold" legislation for the states. The House Judiciary Committee held a hearing on July 24 to examine the impact of *Wayfair* on business and consumers. Andrew Moylan, executive vice president of the National Taxpayers Union Foundation called for legislation and noted that he has "always said that ultimately Congress needs to legislate on this issue because it is a genuine matter of national importance." Meanwhile, many states have already jumped on the bandwagon and proposed or passed provisions similar to South Dakota's. We expect to see most states craft new laws based on the South Dakota model. We note that some states (e.g. Pennsylvania) have adopted laws with thresholds lower than that of South Dakota! So a state-by-state analysis may be necessary.

Canadian Vendors Selling in the U.S. Market—It Happens with a Simple Press of a Key

Many Canadian vendors may have *Wayfair* exposure. Here's an example of how this concept works between the U.S. and Canada. Suppose a 17-year-old teen from Buffalo ("Hockey Girl") prefers a particular brand and style of hockey stick. She is in a summer league, and her local sporting goods store inventories the sticks only during the fall and winter. Fortunately Hockey Girl has identified an on-line vendor in Moose Jaw, Saskatchewan that has exactly what she needs. A few clicks, \$500, and two weeks later she has three new sticks.

If New York adopts *Wayfair*-style sales tax legislation, the Canadian hockey stick vendor will be required to collect and remit New York State and local sales tax on the sale of the hockey sticks to Hockey Girl if the vendor had more than 200 sales into New York in the prior twelve months or had more than \$100,000 of sales shipped to New York in the prior twelve months.

The "Take Away" for Canadian Vendors—No Treaty Protection

Canadian vendors should understand that they cannot hide behind the Canada/U.S. Tax Treaty which provides protection to Canadian vendors *only for federal income taxes*. That means the treaty is not binding with respect to state and local taxes which are now collectable. Not wanting to comply is not an option for Canadian vendors since states within the U.S. can issue tax warrants against them affecting their credit-worthiness. What's more, U.S. tax officials can actually seize Canadian assets that are included in Canadian accounts if the Canadian Bank has a branch located in the particular American state that is seeking to seize the Canadian vendor's assets. And many of the larger Canadian Banks have branches in the U.S.'s money-center cities.

Affecting Potential Acquisitions

Sooner or later, the online transactions will likely show up not only in a Canadian vendor's creditworthiness but also in the "due diligence" phase of the sale of the business. And, if the information is "material" in nature, it could scuttle the sale or reduce the business' value.

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Final Analysis

In the final analysis, the most daunting issue maybe that most unreported tax liabilities never go away. In most states, if a sales tax return is not filed by the vendor, the statute of limitations on assessment *never* begins to run. This can be gnawing at the financial health of your Canadian business forever!

The remote sales tax landscape is changing. If you think your business may be at risk as the result of these new developments, we encourage you to talk to one of our U.S. tax lawyers to address compliance and risk mitigation strategies.