

South Carolina Law Review

Volume 65
Issue 4 *SURVEY OF SOUTH CAROLINA LAW*
and *FOURTH CIRCUIT SURVEY*

Article 9

Summer 2014

Remote Seller Sales and Use Tax Law: How Proposed Law Will Impact South Carolina

James Bull Sterling

Follow this and additional works at: <https://scholarcommons.sc.edu/sclr>



Part of the [Law Commons](#)

Recommended Citation

Sterling, James Bull (2014) "Remote Seller Sales and Use Tax Law: How Proposed Law Will Impact South Carolina," *South Carolina Law Review*. Vol. 65 : Iss. 4 , Article 9.
Available at: <https://scholarcommons.sc.edu/sclr/vol65/iss4/9>

This Article is brought to you by the Law Reviews and Journals at Scholar Commons. It has been accepted for inclusion in South Carolina Law Review by an authorized editor of Scholar Commons. For more information, please contact digres@mailbox.sc.edu.

**REMOTE SELLER SALES AND USE TAX LAW: HOW PROPOSED LAW WILL
IMPACT SOUTH CAROLINA**

I. INTRODUCTION827

II. THE CURRENT STATE OF REMOTE SELLER SALES AND USE TAX LAW830

III. AN OVERVIEW OF THE MARKETPLACE FAIRNESS ACT.....835

 A. *Key Provisions of the Act and How They Might Be Amended to Accommodate Representative Bob Goodlatte’s “Seven Principles”*...835

 1. *The Senate’s Version of the Marketplace Fairness Act*835

 2. *U.S. Representative Bob Goodlatte’s Seven Basic Principles*836

IV. ANALYZING THE MARKETPLACE FAIRNESS ACT: HOW SOUTH CAROLINA CAN COMPLY AND HOW PROPOSED AMENDMENTS AFFECT THE STATE837

 A. *Complying with the Act in South Carolina: The Streamlined Agreement*.....838

 B. *Applying the Act’s Simplification Requirements in South Carolina: The Single Audit Rule*839

 1. *Simplifying the Simplification Requirements: The Auditing Problem*.....840

 C. *Applying the Simplification Requirements in South Carolina: A Uniform Tax Base*.....842

 1. *Simplifying the Simplification Requirements: Uniform Definitions*.....843

 D. *Applying the Simplification Requirements in South Carolina: The Destination Sourcing Rule*.....844

 E. *Applying the Minimum Simplification Requirements in South Carolina: The Small Seller Exception*845

 1. *Simplifying the Simplification Requirements: The Small Seller Exception*845

 F. *Applying the Simplification Requirements in South Carolina: Clarifications and Ambiguities*847

 G. *Considering the Costs of Compliance*849

 H. *A Constitutional Challenge to the Marketplace Fairness Act*850

V. CONCLUSION.....851

I. INTRODUCTION

Somewhere in South Carolina is a student named Jim who spends all of his time studying and eating junk food. Jim wants to get in better shape, so he decides to start running. First, Jim must purchase a pair of running shoes, so he researches various styles until he finds the right pair. Now Jim has two choices: (1) he can go to the local store to purchase those shoes or (2) he can purchase

them online. The difference between these sellers is that, while the product is identical, Jim will be required to pay a sales tax if he purchases the shoes locally. If, however, he purchases the same shoes from a “remote seller,”¹ he likely will not pay a sales tax and almost certainly will not pay his use tax obligation.² Given these tax circumstances, Jim will likely purchase his shoes online from the remote seller.³ That remote seller will not be required to charge Jim a use tax on his purchase, unless it has a “physical presence” in South Carolina.⁴ Jim’s decision to ignore his use tax obligation, while technically against the law, is a common occurrence in South Carolina—in 2009 only half of one percent of South Carolina residents reported their use tax obligations on their state income tax returns.⁵

Due to the low rates of compliance, the states would like to require remote sellers to collect use taxes from their customers and pay those taxes to the respective states where the customers use the product.⁶ However, the remote seller from whom Jim intends to purchase his shoes likely services customers like Jim located all over the country. The remote seller would prefer to avoid the compliance costs⁷ related to calculating which of the roughly 9,600 tax

1. A *remote seller* makes sales to consumers in a state in which the remote seller is not legally “required to pay, collect, or remit [s]tate or local sales and use taxes.” Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 4(5)–(6) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

2. Use taxes are often confused with sales taxes. The seller is responsible for collecting a sales tax when it makes a sale to the customer. The seller then pays that sales tax to the state. Use taxes are akin to sales taxes, except the taxable sale occurs outside the state where the customer “uses” the product. The purpose of the use tax is to allow states to realize revenue from taxable sales “that would have been subject to the sales tax” had they occurred in the state. Richard D. Pomp, *State and Local Taxation: Vol. II*, 9-1 (7th ed. 2011).

3. Even though Jim is legally obligated to calculate and pay his use tax when he fills out his state income tax return, the odds of the state auditing his personal expenses is small enough that he, like most South Carolinians, will take the risk. See Alan D. Viard, *Use Tax Collection on Interstate Sales: The Need for Federal Legislation*, 66 ST. TAX NOTES 657, 657–58, (Nov. 26, 2012) (citing John Buhl, *California BOE Survey: Some Choose Not to Pay Use Taxes*, 62 ST. TAX NOTES 141, 141 (Oct. 17, 2011); Amy Hamilton, *BOE Analysis: Use Tax at 1.4 Percent*, 60 ST. TAX NOTES 463, 463 (May 16, 2011); *Two-Thirds of Consumers are Confused by Online Sales-Tax Compliance*, OFFICIAL ICSC BLOG (July 29, 2011), <http://blog.icsc.org/?p=928>) (noting the low rate of compliance with use tax laws among individual consumers of different states). The 2012 individual income tax return form has a line for the taxpayer to put his or her “use tax” obligation. S.C. DEP’T OF REVENUE, SC1040, at 3 (2012), available at http://www.sctax.org/NR/rdonlyres/32BC8DAF-B34A-4D31-9640-2FA4013192CA/0/IIT_PACKET_WEB_10312012.pdf. The phrase *use tax* is capitalized and emboldened on the form, which is likely an indicator that the Department of Revenue wants to emphasize to taxpayers that they have a duty to report their use taxes on their income tax returns. *Id.*

4. See *Quill Corp. v. North Dakota*, 504 U.S. 298, 311, 312 (1992).

5. Nina Manzi, *Use Tax Collection on Income Tax Returns*, 65 ST. TAX NOTES 23, 26 tbl. 1 (July 2, 2012).

6. See Viard, *supra* note 3, at 657.

7. *Id.* at 659 (stating that compliance costs are the “only valid argument” for restricting a state’s authority to tax remote sellers on their Internet sales).

jurisdictions nationwide applies to a particular customer.⁸ From state to state, there may be a myriad of different exemptions, definitions, and even short “tax holidays” on specific goods.⁹ For instance, South Carolina provides a sales tax holiday for school supplies and clothing during the first weekend of August.¹⁰ Consequently, if Jim buys his shoes during that weekend, he will not pay a sales tax.¹¹ If the remote seller is required to collect use taxes but does not know about South Carolina’s sales tax holiday in August, the remote seller will cause Jim to overpay for his shoes and will overpay its tax obligation.¹² On the other hand, the remote seller could mix up the date of South Carolina’s tax holiday and get penalized for failure to pay its full tax obligation.¹³

While the remote seller enjoys the competitive advantage it gets by setting a price point that in-state sellers cannot match, it also feels justified in doing so because the remote seller does not realize the protections and benefits in-state sellers enjoy.¹⁴ The remote seller argues that physical presence is necessary for a seller to benefit from basic state services like roads and police protection.¹⁵ Instead of requiring that the remote seller collect and pay a use tax, the remote seller would prefer that states enforce the use tax laws they already have in place, which puts the burden of paying use taxes on the customer.¹⁶

The other two parties that care about the type of seller Jim buys his new shoes from are the state of South Carolina and sellers with a physical presence in the state. South Carolina, like any state with sales and use taxes, loses tax revenue it would otherwise recognize when Jim purchases his shoes from a remote seller instead of an in-state seller and does not pay his use tax obligation.¹⁷ Additionally, sellers with a physical presence in South Carolina lose sales they would have made before Jim had the option to purchase his shoes

8. *Hearing on Marketplace Fairness: Leveling the Playing Field for Small Businesses Before the S. Comm. on Commerce, Sci., and Transp.*, 112th Cong. 4 (2012) (statement of Joseph Henchman, Vice President, Legal & State Projects, Tax Foundation), available at <http://taxfoundation.org/sites/taxfoundation.org/files/docs/Henchman%20Statement%20Senate%20Commerce%20Aug%201%202012.pdf>.

9. *See, e.g.*, S.C. CODE ANN. § 12-36-2120 (2014) (providing numerous South Carolina sales tax exemptions); *id.* § 12-36-2130 (providing numerous South Carolina use tax exemptions).

10. *Id.* § 12-36-2120(57).

11. *See id.*

12. *Cf. id.* § 12-36-2550 (stating that overpayments can be used to offset penalties due).

13. *See id.* § 12-49-10, -90.

14. *See* Peter G. Stathopoulos, *State Taxation of Remote Sellers: Has the Physical Presence Nexus Test Been Rendered Obsolete?*, 23 J. OF MULTISTATE TAX’N & INCENTIVES, August 2013, at 22, 27, 46.

15. *Id.*

16. *Id.* at 46; *see* Manzi, *supra* note 5, at 26 tbl.1 (noting low compliance rates with state use tax laws).

17. Five states do not have sales and use taxes at the state level. SCOTT DRENKARD, TAX FOUND., FISCAL FACT NO. 392: STATE AND LOCAL SALES TAX RATES MIDYEAR 2013, at 1 (2013), available at http://taxfoundation.org/sites/taxfoundation.org/files/docs/ff392_0.pdf (noting that those states are Alaska, Delaware, Montana, Oregon, and New Hampshire).

online.¹⁸ Both parties see the playing field as skewed in favor of remote sellers who otherwise provide the same products and services, but are not required to pay the same amount of taxes.¹⁹

This Note examines the Marketplace Fairness Act of 2013 (the Act), which the federal government may enact to resolve the gap in the sales and use tax obligations described above. To exercise authority under the Act, states will have to abide by certain compliance rules; however, those rules would be relatively easy for South Carolina to adopt. Thus, this Note concludes that South Carolina should make the necessary changes to its tax code to comply with the Act—if it becomes law. Part II analyzes current sales and use tax law. Part III gives an overview of the Act, and it also introduces the Goodlatte Principles—the U.S. House Judiciary Committee Chairman’s response to the Senate’s bill. Part IV explores the compliance requirements laid out in Part III with greater detail. It examines the compliance requirements while considering South Carolina’s interests, the Goodlatte Principles, and how the Act could be amended.

II. THE CURRENT STATE OF REMOTE SELLER SALES AND USE TAX LAW

The 1992 U.S. Supreme Court case of *Quill Corp. v. North Dakota*²⁰ defines the benchmark a state must satisfy to require a remote seller to collect and pay use taxes to that state.²¹ In *Quill*, the Supreme Court overturned the North Dakota Supreme Court and held that a state law requiring remote sellers to collect and pay use taxes to the state is unconstitutional under the Commerce Clause, unless the remote seller has a physical presence in that state.²² The remote seller in *Quill* ran a mail order business, an industry that saw substantial growth in the years leading up to the case.²³ On an annual basis, the remote seller sent twenty-four tons of goods into North Dakota.²⁴ The North Dakota Supreme Court attempted to uphold its state law by distinguishing *Quill* from *Bellas Hess*,²⁵ an earlier U.S. Supreme Court case based on facts similar to *Quill*.²⁶ In *Bellas Hess*, Illinois also tried to use a state law to require a mail

18. Donald Bruce, William F. Fox & LeAnn Luna, *State and Local Sales Tax Revenue Losses From E-Commerce*, 52 ST. TAX NOTES 537, 546 tbl. 6 (May 18, 2009).

19. See Stathopoulos, *supra* note 14, at 27.

20. 504 U.S. 298 (1992).

21. See generally *id.* at 301 (citing Nat’l Bellas Hess, Inc. v. Dep’t of Revenue, 386 U.S. 753, 753–54 (1967), *overruled by Quill*, 504 U.S. 298) (stating that the case involved the state’s attempt to require a remote seller to pay the state use tax).

22. *Id.* at 311–12.

23. *Id.* at 302, 303 (quoting *State v. Quill Corp.*, 470 N.W.2d 203, 209 (N.D. 1991), *rev’d*, 504 U.S. 298.).

24. *Id.* at 304 (citing *State v. Quill*, 470 N.W.2d at 218–19).

25. *Id.* at 301 (citing *Bellas Hess*, 386 U.S. at 758).

26. See *id.* at 302; *Bellas Hess*, 386 U.S. at 753–54.

order seller to collect use taxes.²⁷ The North Dakota Supreme Court reasoned that, since *Bellas Hess*, improvements in technology and growth in the mail order business rendered the physical presence requirement obsolete.²⁸ The *Quill* Court disagreed, however, holding that the physical presence requirement from *Bellas Hess* remains good law.²⁹ Despite the seller's substantial activity in North Dakota, the Court reasoned that a "bright-line" test benefits businesses and individuals and "encourages settled expectations."³⁰ Additionally, the Court suggested that Congress, with its power to regulate interstate commerce, is in a better position to resolve the physical presence issue.³¹ Congress, however, has not acted on the Court's suggestion.

As a consequence of *Quill*, the states can only require remote sellers to collect and pay use taxes if they have a physical presence in the state where the final sale is made.³² A group of states tried to mitigate *Quill*'s impact by creating the Streamlined Sales and Use Tax Agreement in 2002 (the Streamlined Agreement),³³ but it never gained nationwide support.³⁴ Member states of the Streamlined Agreement consented to simplify their sales and use tax codes by implementing uniform definitions, sourcing rules, and auditing procedures.³⁵ Remote sellers could choose to participate in the Streamlined Agreement, whereby, using the member state's simplified tax code, they collected and paid the customer's use tax obligation back to that state.³⁶ Critics of the Streamlined Agreement argued that the compliance requirements were too burdensome for member states.³⁷ Furthermore, the Streamlined Agreement did nothing to overrule *Quill*'s physical presence standard and, ultimately, the remote sellers could decide to stop complying at any time.³⁸

27. *Bellas Hess*, 386 U.S. at 754 (citing Dep't of Revenue v. Nat'l Bellas Hess, Inc., 214 N.E.2d 755, 760 (Ill. 1966), *rev'd*, 386 U.S. 753).

28. *Quill*, 504 U.S. at 303 (citing *State v. Quill* 470 N.W.2d at 213).

29. *Id.* at 311–12.

30. *Id.* at 316.

31. *Id.* at 318 n.10 ("The precise allocation of such burdens is better resolved by Congress rather than this Court.").

32. *See id.* at 312.

33. *Streamlined Sales and Use Tax Agreement*, STREAMLINED SALES TAX GOVERNING BOARD, INC. (Oct. 30, 2013), http://www.streamlinedsalestax.org/uploads/downloads/Archive/SSUTA/SSUTA_As_Amended_10-30-13.pdf.

34. *State Info*, STREAMLINED SALES TAX GOVERNING BOARD, INC., <http://www.streamlinedsalestax.org/index.php?page=state-info> (last visited Mar. 30, 2014) (noting that only twenty-three states are full members and only one qualifies as an associate member). South Carolina never became a member of the Streamlined Agreement. *Id.*

35. Pomp, *supra* note 2, at 6-58.

36. Pomp, *supra* note 2, at 6-54 to 6-55.

37. Joseph Henchman, *Nearly 8,000 Sales Taxes and 2 Fur Taxes: Reasons Why the Streamlined Sales Tax Project Shouldn't Be Quick to Declare Victory*, TAX FOUND. (July 28, 2008), <http://taxfoundation.org/blog/nearly-8000-sales-taxes-and-2-fur-taxes-reasons-why-streamlined-sales-tax-project-shouldnt-be-quick>.

38. *See* Stathopoulos, *supra* note 14, at 25.

According to a study led by Professor William Fox of the University of Tennessee, South Carolina lost approximately 138 million dollars of tax revenue in 2012 because of its inability to require remote sellers to collect and remit use taxes.³⁹ Critics of Fox's predictions argue that states with "affiliate nexus legislation"⁴⁰ have not recognized increased revenue.⁴¹ Remote sellers have an affiliate relationship with an in-state seller when a customer can buy products from the remote seller through the in-state seller's website.⁴² The in-state seller receives a percentage of the profits made on each sale.⁴³ To avoid any potential tax liability under affiliate nexus legislation, most remote sellers have terminated their affiliate relationships with the in-state sellers.⁴⁴ South Carolina Senator Marlon Kimpson introduced a bill similar to New York's affiliate nexus law that would create a rebuttable presumption of physical presence for a remote seller that "enters into an agreement" with a South Carolina resident.⁴⁵ It remains to be seen whether Senator Kimpson's bill can gain momentum in the General Assembly and, if enacted, what sort of revenue impact South Carolina will recognize.

The combination of *Quill* and *Bellas Hess*, the nation's broader financial problems, and the growing number of purchases made online from remote sellers has created a unique environment incentivizing federal legislation.⁴⁶ States forced to balance their budgets on reduced revenue and increased expenses are

39. Bruce et al., *supra* note 18, at 556 app. A tbl. 3.

40. While affiliate nexus legislation cannot extend a state's power beyond the physical presence standard in *Quill*, it does encourage a remote sellers to remit use taxes on behalf of their customers. *See generally* *Quill Corp. v. North Dakota*, 504 U.S. 298, 311–312, 317–318 (1992) (discussing the physical presence standard). These laws test the limits of *Quill*, and some remote sellers have challenged their constitutional validity. *See, e.g.,* *Amazon.com, LLC v. N.Y. State Dep't of Taxation & Fin.*, 913 N.Y.S.2d 129, 133 (N.Y. App. Div. 2010) (discussing Amazon's challenge to a New York law that created a rebuttable presumption that, if a remote seller had an affiliate in New York, it was doing business in New York and was obligated to pay use taxes), *cert. denied*, 134 S. Ct. 682 (2013).

41. *Disappointing Returns*, STATE NET CAPITOL J. (Mar. 11, 2013), http://www.statenet.com/capitol_journal/03-11-2013/html#sncj_spotlight (urging remote sellers with in-state affiliates to collect and remit use taxes to the state as New York passed an affiliate nexus law and recognized 360 million dollars in new revenue). Fox defended his study by noting that many states with affiliate nexus legislation provide exemptions for small remote sellers, and remote sellers have terminated their affiliate relationships with in-state sellers instead of paying the use tax. *Id.*

42. *See* Doug Sheppard, *An Interview with George Isaacson*, 70 ST. TAX NOTES 169, 172 (Oct. 21, 2013).

43. *See id.*

44. *Id.*

45. S. 870, 120th Gen. Assemb., 1st Reg. Sess. (S.C. 2013). The bill was introduced fifteen days after the U.S. Supreme Court denied certiorari to hear a challenge to the New York state law. *See Amazon.com*, 134 S. Ct. 682.

46. *See* Yi Feng & Matthew Wade, *An Analysis of Business to Consumer Electronic Commerce Sales and Use Tax Compliance on Revenue Collections*, 23 MULTISTATE TAX COMM'N REV., no. 1, Winter 2013, at 7, 7–8, available at http://www.mtc.gov/uploadedFiles/Multistate_Tax_Commission/Resources/Publications/MTC_Review/Winter%202013.pdf.

struggling to provide basic services to their residents.⁴⁷ It looks like Congress might finally be inspired to do what the *Quill* Court asked it to do: pass federal legislation.⁴⁸

The U.S. Senate addressed the remote seller issue in May of 2013 when it passed, with relatively broad support,⁴⁹ the Marketplace Fairness Act.⁵⁰ The Act responds to the *Quill* Court by “level[ing] the playing field” between sellers with and sellers without physical presence in a given state.⁵¹

Due to the growing volume of sales made online,⁵² many influential groups and individuals have expressed their respective opinions of the Act. For instance, the National Governors Association and the National Conference of State Legislatures both support the Act.⁵³ As representatives for state interests, the two organizations have a logical interest in a federal law that would authorize the states to require remote sellers to collect use taxes.⁵⁴ The South Carolina Retail Merchants Association, which represents local retailers, also supports the Act.⁵⁵ Critics of the Act include the eMainstreet Alliance, which represents the interests of over one hundred Internet-based businesses,⁵⁶ and the Heritage Foundation, an organization run by former U.S. Senator Jim DeMint of South

47. *See id.* at 8.

48. *See Online Taxes About Fairness, Not State Revenue*, 21 HARTFORD BUS. J., June 3, 2013, at 5, 5 (containing an interview with Richard Pomp, Alva P. Loisel Professor of Law at the University of Connecticut School of Law, regarding online taxes).

49. S. 743: *Marketplace Fairness Act of 2013*, GOVTRACK.US, <http://www.govtrack.us/congress/bills/113/s743#overview> (last visited Mar. 30, 2014) (showing the Senate passed the Act with a 69-27 vote).

50. Marketplace Fairness Act of 2013, S. 743, 113th Cong. (as referred to the H. Comm. on the Judiciary, May 20, 2013). U.S. Senator Lindsey Graham of South Carolina voted for the Act, but fellow U.S. Senator Tim Scott did not. *U.S. Senate Roll Call Votes 113rd Congress – 1st Session*, U.S. SENATE, http://www.senate.gov/legislative/LIS/roll_call_lists/roll_call_vote_cfm.cfm?congress=113&session=1&vote=00113 (last visited Mar. 30, 2014).

51. Henry J. Reske, *Marketplace Fairness Act Clears Another Procedural Hurdle in U.S. Senate*, ST. TAX TODAY, Apr. 25, 2013, available at LEXIS, 2013 STT 80-1 (quoting U.S. Senator Johnny Isakson).

52. Bruce et al., *supra* note 18, at 537 (stating that, between 1999 and 2006, E-commerce sales grew from 995 billion dollars to 2.385 trillion dollars).

53. *NCSL Thanks Senators for Passing Marketplace Fairness Act: Next Step, House of Representatives*, NAT'L CONF. OF ST. LEGISLATURES (May 6, 2013) (quoting NGA Executive Director Dan Crippen), <http://www.ncsl.org/press-room/ncsl-thanks-senators-for-passing-marketplace-fairn.aspx>; *State Leaders Call for Passage of Marketplace Fairness Legislation: Technology Companies Demonstrate Ease of Sales Collection Software*, NAT'L GOVERNORS ASS'N (June 19, 2013), <http://www.nga.org/cms/home/news-room/news-releases/2013-news-releases/col2-content/state-leaders-call-for-passage-o.html>.

54. *See State Leaders Call for Passage*, *supra* note 53 (quoting NGA Executive Director Dan Crippen).

55. *Who Supports the Marketplace Fairness Act?*, MARKETPLACE FAIRNESS ACT, <http://marketplacefairness.org/support/> (last visited Mar. 30, 2014).

56. *See Letter from eMainStreet Alliance to Representative Bob Goodlatte*, U.S. House of Representatives and Representative John Conyers Jr., U.S. House of Representatives (June 25, 2013), available at <http://emainstreet.org/wp-content/uploads/2013/06/eMainStreet-Alliance-Letter-June-2013.pdf>.

Carolina.⁵⁷ While Republicans tend to oppose the Act and Democrats tend to support it, plenty of exceptions exist,⁵⁸ and the Act has enough bipartisan support overall to suggest that the debate is not strictly partisan.⁵⁹ Even some members of Congress who signed the “Taxpayer Protection Pledge,” a pledge not to raise or create new taxes, expressed their support for the Act’s general principles.⁶⁰

Supporters of the Act argue that, instead of creating a new tax, it actually closes a loophole in the national marketplace that remote sellers have been able to successfully exploit.⁶¹ Passing the Act would inject stability into an area of the law currently marked by uncertainty.⁶² Along with a lack of federal legislation, uncertainty comes from state sponsored laws that challenge the boundaries of *Quill*.⁶³ Ordinarily, states that lose the most revenue from sales to remote sellers are the same ones passing laws that stretch *Quill*’s physical presence rule.⁶⁴ Conversely, critics argue that, rather than passing new legislation burdening remote sellers, the states should start actually enforcing on

57. *Who Supports the Marketplace Fairness Act?*, *supra* note 55; see Senior Management, THE HERITAGE FOUND., <http://www.heritage.org/about/staff?positions=%22Senior+Management%22> (last visited Mar. 30, 2014) (listing Jim DeMint as President).

58. See *U.S. Senate Roll Call Votes 113th Congress – 1st Session*, *supra* note 50 (listing the Yeas and Nays). For instance, Arthur Laffer, a former economic advisor of President Reagan—and a man who distastes taxes so much that he moved from California to Tennessee and calls federal legislation that helps states do business “rare”—supports the Act. See Arthur Laffer, *E-Fairness Good for TN Economy, Budget*, THE TENNESSEAN (Oct. 8, 2013). He estimates the Act would increase Tennessee’s gross state product by four percent, add nearly fifty thousand jobs in the state, and add fifteen billion dollars to the economy over ten years. See *id.*; see also Paul Solman & Arthur Laffer, *How Low Can They Go? Arthur Laffer Defends Slashing State Income Taxes*, PBS NEWSHOUR (Aug. 1, 2013, 10:50 AM), <http://www.pbs.org/newshour/making-sense/how-low-can-they-go-arthur-laf/>. But see *infra* note 178 for a brief discussion of the lobbyist influence on studies.

59. *S. 743: Marketplace Fairness Act of 2013: Senate Vote #113*, GOVTRACK.US, <https://www.govtrack.us/congress/votes/113-2013/s113> (last visited Mar. 30, 2014) (listing the forty-six Democrats, twenty-six Republicans, and two Independents who support the Act); *Who Supports the Marketplace Fairness Act?*, *supra* note 55 (listing the thirteen Republicans, twelve Democrats, and one Independent who support the Act).

60. John Buhl, *Sales Tax Streamlining Proponents Unmoved by Norquist’s Tax Pledge*, 62 ST. TAX NOTES 717, 717 (Dec. 12, 2011). The supporters, all Republicans, include five Senators and six members of the House of Representatives. *Id.* The Act contains a clause that says it will impose “No New Taxes” and will not affect intrastate sales. Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 3(e)–(f) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

61. See Viard, *supra* note 3, at 658.

62. See Stathopoulos, *supra* note 14, at 27.

63. See, e.g., *Amazon.com, LLC v. N.Y. State Dep’t of Taxation and Fin.*, 913 N.Y.S.2d 129, 132 (N.Y. App. Div. 2010) (noting the significant “ramifications” relating to the issue of the new tax law), *cert. denied*, 134 S. Ct. 682 (2013).

64. See Feng & Wade, *supra* note 45, at 11 (discussing how over half of the revenue lost due to Internet sales to remote sellers is estimated to be concentrated in six states, including New York and California); see, e.g., *Amazon.com, LLC*, 913 N.Y.S.2d at 133 (discussing Amazon’s challenge to New York’s new state law regarding physical presence); *Borders Online, LLC v. State Bd. of Equalization*, 29 Cal. Rptr. 3d 176, 180 (Cal. Ct. App. 2005) (challenging the state laws that push the physical presence requirement under *Quill*).

their residents the use tax laws that are already in place.⁶⁵ Even if the Act's opponents may stall its present version in the House Judiciary Committee,⁶⁶ it remains likely that something similar to the Act will eventually become law.⁶⁷ Determining how that law will affect South Carolina can be accomplished by analyzing the core principles of the Act, with consideration for how its opponents may influence the ultimate law.

III. AN OVERVIEW OF THE MARKETPLACE FAIRNESS ACT

A. Key Provisions of the Act and How They Might Be Amended to Accommodate Representative Bob Goodlatte's "Seven Principles"

The Marketplace Fairness Act represents the latest in a recent trend of congressional efforts to clarify the states' authority to require remote sellers to collect use taxes on the products that are shipped into a state when the remote seller lacks a physical presence in that state.⁶⁸ The Act's stated purpose is "[t]o restore States' sovereign rights to enforce State and local sales and use tax laws."⁶⁹ It would help states currently struggling to meet their budgetary obligations by allowing them to enforce their use tax laws more effectively.⁷⁰ One of the Act's selling points is that none of the additional revenue collected would go to the federal government.⁷¹ In exchange for the increased revenue, states are required to meet certain compliance requirements before exercising their authority under the Act.⁷²

1. The Senate's Version of the Marketplace Fairness Act

The following bullet points present a brief, nonexhaustive summary of the Senate's version of the Marketplace Fairness Act:

- Under the Act, a state may require a remote seller to collect and remit

65. See Stathopoulos, *supra* note 14, at 46.

66. See Henry J. Reske, *Goodlatte's Marketplace Fairness Principles Don't Remove Uncertainty Over Fate of Bill*, ST. TAX TODAY, Sept. 19, 2013, available at LEXIS, 2013 TNT 182-8 [hereinafter Reske, *Uncertainty*] (stating that the gap between groups that support and oppose the Act is too large to bridge, requiring more than "tweaks"); Henry J. Reske, *House Judiciary Committee May Hold February Hearing on Marketplace Fairness Act*, ST. TAX TODAY, Jan. 21, 2014, available at LEXIS, 2014 STT 13-2 (noting a potential hearing in February of 2014).

67. See Reske, *Uncertainty*, *supra* note 66.

68. See Viard, *supra* note 3, at 665-66 (discussing prior bills introduced in 2011, including the Main Street Fairness Act and the Marketplace Equity Act).

69. Marketplace Fairness Act of 2013, S. 743, 113th Cong. (as referred to the H. Comm. on the Judiciary, May 20, 2013).

70. See *Online Taxes About Fairness, Not State Revenue*, *supra* note 48, at 5 (noting that increased collections will help, but will not lead to "a pot of gold").

71. *Id.*

72. S. 743 § 2(b)(2).

use taxes for products sold into that state in one of two ways. First, a state can become a member of the Streamlined Agreement.⁷³ Alternatively, a state can comply with the minimum simplification requirements described in the Act.⁷⁴

- To comply with the Act's minimum simplification requirements, each state must:
 - Provide the remote seller with a single entity, a single audit, and a single sales and use tax return;⁷⁵
 - Provide a uniform statewide "sales and use tax base";⁷⁶
 - Provide the remote seller with software free of charge,⁷⁷ and relieve both the remote seller and the software provider of any liability for mistakes in tax collection if they rely on incorrect information provided by the state;⁷⁸
 - Additionally, if either the remote seller or certified software provider provides incorrect information to the other party, the party not at fault must be relieved of liability for relying on the incorrect information;⁷⁹
 - "Provide [the] remote seller[] and certified software provider[] with 90 days notice of a rate change";⁸⁰ and
 - Provide a "small seller exception" if the remote seller's aggregate "gross annual receipts in total remote sales" are not more than \$1 million.⁸¹
- The Act states that it imposes "no new taxes" and that it "shall not apply to intrastate sales."⁸²
- Under the Act, the proper rate to be applied to each purchase will be the sales and use tax rate at the customer's address.⁸³

2. *U.S. Representative Bob Goodlatte's Seven Basic Principles*

U.S. Representative Bob Goodlatte is the Chairman of the House Judiciary Committee, which is considering the Senate's Marketplace Fairness Act.⁸⁴ In

73. *See id.* § 2(a).

74. *See id.* § 2(b).

75. *See id.* § 2(b)(2)(A)(i)–(iii).

76. *Id.* § 2(b)(2)(B).

77. *Id.* § 2(b)(2)(D)(ii).

78. *Id.* § 2(b)(2)(G).

79. *See id.* § 2(b)(2)(E)–(F).

80. *Id.* § 2(b)(2)(H).

81. *Id.* § 2(c).

82. *Id.* § 3(e)–(f).

83. *See id.* § 4(7).

84. *See* Press Release, U.S. House of Representatives Judiciary Committee, House of Judiciary Committee Releases Principles on Internet Sales Tax (Sept. 18, 2013), <http://judiciary>.

response to the Senate's Act, Representative Goodlatte put forth seven principles (the Goodlatte Principles) that he wants represented in the law.⁸⁵ The Act will likely need to be amended to accommodate the Goodlatte Principles in a manner that will receive enough bipartisan support to pass both chambers.⁸⁶ Thus, it is important to compare where the Act satisfies the Goodlatte Principles, where it falls short, where things could be changed, and where fundamental differences may persist. The Goodlatte Principles are as follows:

1. Tax Relief: The new law should not create any new taxes, or otherwise affect interstate commerce;
2. Tech Neutrality: The new law should not unequally burden any type of businesses, whether Internet or brick and mortar;
3. No Regulation Without Representation: The new law should provide remote sellers with a means of challenging the taxes imposed on them by a state;
4. Simplicity: The new law should simplify the tax code, making it easy for businesses to comply;
5. Tax Competition: The new law should encourage competition, and not disadvantage any businesses;
6. States' Rights: The new law should respect states' sovereignty; and
7. Privacy Rights: The new law should protect customer data.⁸⁷

IV. ANALYZING THE MARKETPLACE FAIRNESS ACT: HOW SOUTH CAROLINA CAN COMPLY AND HOW PROPOSED AMENDMENTS AFFECT THE STATE

The Senate's version of the Act gives individual states two alternatives for compliance purposes.⁸⁸ The first alternative, discussed below in Part IV.A, allows a state to comply by becoming a member state under the Streamlined Agreement.⁸⁹ Under the second alternative discussed below, the Act gives a state the option to comply by "implement[ing] the minimum simplification requirements" in the Act.⁹⁰

house.gov/index.cfm/2013/9/house-judiciary-committee-releases-principles-on-internet-sales-tax [hereinafter *Goodlatte Principles*].

85. *Id.*

86. See Reske, *Uncertainty*, *supra* note 66 (quoting conflicting opinions on the overall value of the Goodlatte Principles).

87. See *Goodlatte Principles*, *supra* note 84 (listing the seven Goodlatte Principles).

88. Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 2(a)–(b) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

89. *Id.* § 2(a).

90. *Id.* § 2(b).

A. Complying with the Act in South Carolina: The Streamlined Agreement

South Carolina should not join the Streamlined Agreement for two reasons. First, the Streamlined Agreement's compliance requirements are more burdensome than the Act's minimum simplification requirements.⁹¹ Second, the compliance requirements for the Streamlined Agreement might eventually conflict with the Act's compliance requirements, which would automatically negate South Carolina's authority to require remote sellers to pay use taxes to the state.⁹²

To become a member and maintain membership under the Streamlined Agreement, South Carolina would have to amend its tax code to adopt the bylaws of the Streamlined Agreement's governing board.⁹³ The governing board is made up of no more than four representatives from each Streamlined Agreement member state.⁹⁴ It has the power to make changes to the Streamlined Agreement, and while those changes may benefit the majority of its member states, they may not align with South Carolina's interests.⁹⁵ Additionally, to remain a member state under the Streamlined Agreement, South Carolina would have to pay annual dues⁹⁶ and "annually re-certify that [South Carolina] is in compliance with all terms of the Agreement"⁹⁷

Furthermore, South Carolina should not join the Streamlined Agreement because the Act says that "any changes to the Streamlined Sales and Use Tax Agreement made after the date of the enactment of this Act [cannot] conflict" with the Act's minimum simplification requirements.⁹⁸ Consequently, if the governing board passes an amendment to the Streamlined Agreement that conflicts with the Act, South Carolina would immediately lose its authority under the Act by complying with the Streamlined Agreement.⁹⁹ A more likely scenario would be that, due to how frequently the Streamlined Agreement is

91. Compare *Streamlined Agreement*, *supra* note 33, at art. III § 327 (providing that, to attain membership status under the SSUTA, a state must adopt the Agreement's uniform definitions), with S. 743 § 2(b) (not requiring states to adopt uniform definitions).

92. See S. 743 § 2(a) (stating that amendments to the Streamlined Agreement must not conflict with the Act); *Streamlined Agreement*, *supra* note 33 (noting that the Streamlined Agreement has been amended thirty times since its creation).

93. See *Bylaws of the Streamlined Sales Tax Governing Board, Inc.*, STREAMLINED SALES TAX GOVERNING BOARD, INC. art. 3 (May 24, 2012), http://www.streamlinedsalestax.org/uploads/downloads/Bylaws/SST%20Bylaws%20%20Updated%20through%2010_30_13%20-%20Revised%2012_26_13.pdf.

94. *Id.* art. 3 § 8.

95. See *id.* art. 4 § 6, art. 9 § 2 (providing that each state only gets one vote and a three-fourths vote is needed to amend the agreement).

96. See *id.* art. 3 § 7.

97. *Id.* art. 3 § 6.

98. Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 2(a) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

99. See *id.* § 2(a).

amended,¹⁰⁰ South Carolina would lose its authority under the Act by neglecting to comply with an amendment.¹⁰¹ The ongoing uncertainty of the Streamlined Agreement makes it more burdensome for compliance purposes, particularly when compared to the Act's simplification requirements.¹⁰²

B. Applying the Act's Simplification Requirements in South Carolina: The Single Audit Rule

Under the Act's second method of compliance, South Carolina will need to create a single entity "responsible for all State and local sales and use tax administration, return processing, and audits for remote sales sourced to the State"¹⁰³ This entity will be responsible for conducting "a single audit of a remote seller for all State and local taxing jurisdictions"¹⁰⁴ Remote sellers will be responsible for filing "a single sales and use tax return" with that entity.¹⁰⁵ The purpose of the single audit and single tax return provisions is to ensure that South Carolina offers equal tax treatment for all sellers, whether remote or located in-state.¹⁰⁶

In South Carolina, it is unclear how the Act will change the procedures that the state already has in place for auditing remote sellers.¹⁰⁷ For instance, state law authorizes South Carolina to hire a collection agency in another state to collect from a delinquent taxpayer.¹⁰⁸ The state can also "enter into agreements with other states . . . or their authorized representatives for the mutual exchange of tax returns, information thereon, and related information."¹⁰⁹ Therefore, in practice, South Carolina already appears ready and able to collect information from companies located in other states.¹¹⁰

100. See *supra* note 92 and accompanying text.

101. See *Streamlined Bylaws*, *supra* note 93 (noting that the bylaws have been amended seven times since being adopted in 2005).

102. Compare *Streamlined Agreement*, *supra* note 33 (noting that the Streamlined Agreement has been amended twenty-nine times since 2003), and S. 743 § 2(a) (providing that amendments to the Streamlined Agreement must not conflict with the Act), with S. 743 § 2(b) (providing the Act's minimum simplification requirements).

103. S. 743 § 2(b)(2)(A)(i).

104. *Id.* § 2(b)(2)(A)(ii).

105. *Id.* § 2(b)(2)(A)(iii).

106. See *id.* § 2(b)(2)(A).

107. See generally S.C. CODE ANN. § 12-54-227 (2014) (explaining the out of state collections procedure).

108. *Id.* § 12-54-227(A)(1).

109. *Id.* § 12-54-225.

110. See *id.* § 12-49-90 (stating that "[t]he South Carolina Department of Revenue . . . is hereby empowered to bring suit in the courts of other states to collect taxes legally due this State").

1. *Simplifying the Simplification Requirements: The Auditing Problem*

Some are still worried by the single-audit-per-state rule because they believe it is not adequately simplified and creates sovereignty issues.¹¹¹ For remote sellers, the fear is that they will be subject to “perpetual audit[s].”¹¹² While the sixth Goodlatte Principle—which provides that “States should be sovereign within their physical boundaries”—alludes to the auditing concern, the Act may need to be amended to clarify the extent of a state’s authority to audit a remote seller.¹¹³

In an effort to reduce concerns over the auditing provision, Goodlatte has been studying alternatives to the single-audit-per-state rule.¹¹⁴ Two suggestions include “requiring multiple states to coordinate a single audit or allowing a remote seller to elect a multistate joint audit.”¹¹⁵ The first option is also known as a *base state* model.¹¹⁶ Under a base state model, one state conducts a single audit of a remote seller on behalf of a group of states, collects the appropriate use taxes, and distributes the revenue to the participating states.¹¹⁷

The second option Goodlatte is considering would allow a remote seller to select a multistate joint audit company.¹¹⁸ That option, however, is problematic because remote sellers cannot reach an agreement as to the organization that should conduct those audits.¹¹⁹ Although the Multistate Tax Commission (the MTC)¹²⁰ says it “could start [auditing] tomorrow,” businesses already objected to the MTC’s involvement when the same auditing issue came up in the Streamlined Agreement.¹²¹ Therefore, businesses would probably object to the MTC’s involvement under the Act as well. The MTC was designed to be a collaborative effort by the states to proactively simplify and unify their sales and use taxes without involving the federal government.¹²² Using the MTC seemingly satisfies the sixth Goodlatte Principle—regarding states’ rights—

111. See Amy Hamilton, *Goodlatte Considering New Audit Framework for Marketplace Fairness Act*, ST. TAX TODAY, Oct. 10, 2013, available at LEXIS, 2013 STT 197-1.

112. *Id.*

113. See *Goodlatte Principles*, *supra* note 87.

114. Hamilton, *supra* note 111.

115. *Id.*

116. See Sheppard, *supra* note 42, at 170.

117. *Id.*

118. Hamilton, *supra* note 111.

119. See *id.*

120. The Multistate Tax Commission, created in 1967, is an intergovernmental state tax agency that provides multistate taxpayers with an impartial forum for settling their tax obligations. *About the Multistate Tax Commission*, MULTISTATE TAX COMMISSION, <http://www.mtc.gov/About.aspx?id=40> (last visited Mar. 31, 2014).

121. Hamilton, *supra* note 111 (quoting MTC Executive Director Joe Huddleston). The MTC was rejected as an auditor under the Streamlined Agreement. *Id.*

122. MULTISTATE TAX COMM’N, MULTISTATE TAX COMPACT (1968), reprinted in 66 ST. TAX NOTES 600 (Nov. 19, 2012).

because the MTC is a creation of the states, not the federal government.¹²³ However, businesses have concerns that the MTC auditors would use the information they gather auditing the businesses' use tax obligations against those businesses when auditing their income taxes.¹²⁴ Therefore, even if an amendment to the Act would simplify the auditing issue, other conflicts would still need to be resolved.¹²⁵

According to Scott Peterson, the former executive director of the Streamlined Agreement's governing board and former director of the South Dakota Department of Revenue's Business Tax Division,¹²⁶ neither remote sellers nor Goodlatte ought to fear the Act's current single-audit-per-state rule.¹²⁷ Peterson says that, absent evidence of fraud—which would result in a very specific audit of a remote seller—a state like South Carolina has no reason to enter another state to collect use taxes, and remote sellers will not be faced with multiple audits from various states.¹²⁸ Rather than audit the remote seller, some of the member states under the Streamlined Agreement would choose to audit the company that provided the certified software procured by the remote seller for purposes of calculating use tax obligations.¹²⁹ That software provider might be responsible for calculating use taxes on behalf of thousands of remote sellers.¹³⁰ Then, under a theory of agency law, the state could hold the software provider liable for mistakenly calculating a remote seller's use tax obligations.¹³¹ Peterson's statements are supported by the statistics, which show that, nationwide, states rarely audit more than two percent of their retailers annually.¹³²

Given that the Act will expand the authority that states like South Carolina have to require remote sellers to collect use taxes and audit remote sellers to ensure their compliance, the third Goodlatte Principle—"No Regulation Without Representation"—warrants special consideration.¹³³ This principle speaks to a remote seller's right to have a fair forum for challenging a tax levied against

123. See Hamilton, *supra* note 111; see also *Goodlatte Principles*, *supra* note 84 (referring to the specific "States' Rights" Goodlatte Principle).

124. Hamilton, *supra* note 111.

125. See *id.*

126. *Id.*

127. See *id.*

128. See *id.*

129. *Id.*

130. *Id.*

131. See *id.* (explaining that Streamlined Agreement member states have laws that hold software providers liable for failing to correctly calculate a participating remote seller's use tax obligation).

132. *Id.*

133. See generally *Goodlatte Principles*, *supra* note 84 ("Those who would bear state taxation, regulation and compliance burdens should have direct recourse to protest unfair, unwise or discriminatory rates and enforcement.").

it.¹³⁴ The Act could be amended to satisfy this principle by either requiring that disputes be litigated in federal court or requiring mediation.¹³⁵ Providing federal jurisdiction to resolve disputes over tax liabilities might lessen the remote seller's fear that it will be treated prejudicially by a state agency.¹³⁶ Alternatively, allowing the remote seller to mediate the disputed tax liability could be a quick and inexpensive substitute to litigation.¹³⁷ If the parties are unable to settle their dispute through mediation, they could reserve the right to take their claims to court.¹³⁸ Thus, South Carolina should not worry if either proposed amendment is adopted into the Act's final version because neither will have a substantial negative effect on the state's interests.

C. Applying the Simplification Requirements in South Carolina: A Uniform Tax Base

The Act requires individual states to provide "a uniform sales and use tax base among the State and the local taxing jurisdictions within the State."¹³⁹ A *tax base* refers to the aggregate products and services the state elects to tax.¹⁴⁰ A state broadens its tax base by taxing additional products and services.¹⁴¹ For instance, a state might broaden its tax base by taxing groceries when it did not tax groceries beforehand.¹⁴² On the other hand, a state might narrow its tax base temporarily by providing a tax holiday for certain products and services, or by permanently excluding a product—like groceries—that it once taxed.¹⁴³ The Act's statewide uniform tax base requirement means that South Carolina could not tax certain products and services in one local jurisdiction while not taxing them in another jurisdiction.¹⁴⁴

In South Carolina, county governments are authorized to impose up to a 3% tax on "accommodations."¹⁴⁵ The accommodations tax is intended to fund

134. See Sheppard, *supra* note 42, at 170; *Goodlatte Principles*, *supra* note 84 (referring to the third Goodlatte Principle on "No Regulation Without Representation").

135. Sheppard, *supra* note 42, at 170.

136. *See id.*

137. *Id.*

138. *Id.*

139. Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 2(b)(2)(B) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

140. BLACK'S LAW DICTIONARY 1599 (9th ed. 2009).

141. *See Tax Policy Nuts and Bolts: Understanding the Tax Base and Tax Rate*, INST. ON TAX'N & ECON. POL'Y (Aug. 2011), <http://www.itepnet.org/pdf/pb50bolts.pdf> (explaining the purpose for a state to have a narrow or a broad tax base).

142. *See generally id.* (explaining potential tax base versus actual tax base).

143. *See generally id.* (explaining the difference between narrow and broad tax base).

144. *See* Joseph Henchman, *Marketplace Fairness Act Introduced: Expands State Internet Sales Tax Authority with Some Simplifications*, TAX FOUND. (Feb. 28, 2013), <http://taxfoundation.org/blog/marketplace-fairness-act-introduced-expands-state-internet-sales-tax-authority-some-simplifications> (referring to the effects of the Act on tax base).

145. S.C. CODE ANN. § 6-1-540 (2004) (providing that the local accommodations tax cannot exceed 3%); *see also id.* § 6-1-720(A) (imposing a local hospitality tax).

tourism-related projects.¹⁴⁶ Statewide, during the fiscal year 2010–2011, the local accommodations tax generated \$23.9 million in revenue.¹⁴⁷ The state Department of Revenue does not collect the accommodations tax; rather, local counties have the sole collection responsibility.¹⁴⁸ While counties welcome the revenue from accommodations taxes, state law requires that revenue be spent for narrow purposes related to tourism.¹⁴⁹ To create a statewide uniform base for sales and use taxes, South Carolina will need to decide whether to get rid of the accommodations tax or require that each county adopt an accommodations tax.¹⁵⁰ Either way, the new law will force local jurisdictions to comply with state-level policy, and some jurisdictions will be impacted adversely.

1. *Simplifying the Simplification Requirements: Uniform Definitions*

While a statewide uniform tax base will simplify tax administration for remote sellers, opponents of the Act argue that uniform definitions are also needed to ease the burden on remote sellers.¹⁵¹ In its current form, the Act only mandates that states “specify[] the tax or taxes” and “specify[] the products and services” included in their respective tax bases.¹⁵² The definition of a specific product or service, however, might vary from state to state.¹⁵³ For instance, one state might classify a granola bar as non-taxable food, while another classifies it as taxable candy; or the remote seller might classify the same granola bar without any regard for whether it is or is not candy.¹⁵⁴ The result would be a disconnect among the states, or between a state and a remote seller, whereas uniform definitions would provide greater certainty for remote sellers and states

146. *Id.* § 6-1-530(A) (imposing a local accommodations tax); S.C. CODE ANN. § 12-36-2630(3) (2014); see also Robert Behre, *Back to the Table: Boosting Tourism? S.C. Meal Taxes Get Closer Look*, POST & COURIER (Charleston, SC), Aug. 29, 2013, at B1, available at <http://www.postandcourier.com/article/20130828/PC1610/130829295> (reporting controversy over whether revenue generated by the accommodations tax is actually being spent towards tourism-related projects).

147. Behre, *supra* note 146.

148. S.C. DEP'T OF REVENUE, ACCOMMODATIONS AND ADMISSIONS TAX MANUAL 2010, at 2 n.1 (2010), available at <http://www.sctax.org/NR/rdonlyres/6E5845F4-4E12-48D4-931C-BEF9DC467405/0/2010AccandAdmissionsManual.pdf>.

149. S.C. CODE ANN. § 6-1-530(A).

150. See S.C. CODE ANN. § 12-36-2630(3) (stating that “the [local accommodations] tax may be decreased or repealed”).

151. See Sheppard, *supra* note 42, at 170, 171–72.

152. Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 2(b)(1) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

153. See *id.* § 2(b)(1)(B).

154. LARRY KAVANAGH & AL BESSIN, THE REAL-WORLD CHALLENGES IN COLLECTING MULTI-STATE SALES TAX: FOR MID-MARKET ONLINE AND CATALOG RETAILERS 5 (2013), available at http://truesimplification.org/wp-content/uploads/Final_Embargoed-TruST-COI-Paper-.pdf.

because neither would be left wondering what the other meant by a simple term like *granola bar*.¹⁵⁵

Requiring uniform definitions would also help fix the uniform tax base problem discussed in Part IV.C. The Act currently allows products to be defined in such a way that they might fall outside of one state's uniform tax base, but remain within another state's uniform tax base.¹⁵⁶

On the other hand, amending the Act to require uniform definitions is problematic because the states might perceive it to be as burdensome as the Streamlined Agreement.¹⁵⁷ In the ten years since the Streamlined Agreement was created, Congress likely did not create an analogous federal law because state representatives would not support legislation that included the Streamlined Agreement's compliance requirements.¹⁵⁸ Even though every state wants to protect its right to define its own terms, the failure to require uniform definitions contradicts the Act's purpose of simplifying sales and use tax administration.¹⁵⁹ Balanced against the Act's revenue benefits and the compliance burdens felt by remote sellers, it would not be overly burdensome to require South Carolina to provide remote sellers with uniform definitions.¹⁶⁰ In light of the fourth Goodlatte Principle—regarding simplicity¹⁶¹—South Carolina should be prepared for an amendment to the Act requiring the state to adopt uniform definitions.¹⁶²

D. Applying the Simplification Requirements in South Carolina: The Destination Sourcing Rule

To comply with the Act, states must tax remote sales using the “destination-based sourc[e]” rule.¹⁶³ Under the destination-based source rule, use tax rates are computed utilizing the applicable rate in the customer's jurisdiction and

155. See *FAQs: How do Uniform Definitions Reduce Business Administrative Expenses?*, STREAMLINED SALES TAX GOVERNING BOARD, INC., http://www.streamlinedsalestax.org/index.php?page=gen_9 (last visited Mar. 31, 2014).

156. See KAVANAGH & BESSIN, *supra* note 154, at 5.

157. See *Hearing on Marketplace Fairness*, *supra* note 8, at 6.

158. See *supra* Part IV.A (discussing why South Carolina should not join the Streamlined Agreement).

159. *What is the Marketplace Fairness Act of 2013?*, MARKETPLACE FAIRNESS ACT, <http://www.marketplacefairness.org/what-is-the-marketplace-fairness-act/> (last visited Mar. 31, 2014); see generally *Marketplace Fairness Act*, S. 743, 113th Cong. (as referred by S. Comm. on the Judiciary, May 20, 2013) (providing how the state tax law should be simplified).

160. See generally Henchman, *supra* note 144 (criticizing the bill's requirements for state legislation, one of which involves providing a list of taxable products and services).

161. *Goodlatte Principles*, *supra* note 84.

162. See Sheppard, *supra* note 42, at 170 (noting that states are resisting uniform definitions because “states want to have their cake (more tax revenue) and eat it too (not be forced to simplify, and make more administratively uniform, their tax systems)”).

163. See Joseph Henchman, *New York Times Columnist Misstates Marketplace Fairness Act*, TAX FOUND. (May 13, 2013), <http://taxfoundation.org/blog/new-york-times-columnist-misstates-marketplace-fairness-act>.

remitting the tax revenue to that jurisdiction.¹⁶⁴ Fortunately, South Carolina already calculates use tax rates at the destination rate, so the state would not have to change its code to comply with the Act.¹⁶⁵ In the event that a customer's home address cannot be established, the Act provides a hierarchy of alternative addresses that can be used.¹⁶⁶ South Carolina should not expect any change to the sourcing rule, which would also appear to satisfy the second Goodlatte Principle—that “businesses should all be on equal footing.”¹⁶⁷

E. Applying the Minimum Simplification Requirements in South Carolina: The Small Seller Exception

Due to fears that—notwithstanding the Act's simplification requirements—compliance would still be overly burdensome on small businesses, the Senate included a “small seller exception” in the Act.¹⁶⁸ Under the small seller exception, South Carolina would only be able to require remote sellers with “gross annual receipts in total remote sales in the United States in the preceding calendar year exceeding \$1,000,000” to collect and remit use taxes to the state.¹⁶⁹ While it is unclear how Congress decided to draw the line for qualified remote sellers at \$1 million, over 99% of small businesses do not make enough annual remote sales to actually qualify under the Act.¹⁷⁰

1. Simplifying the Simplification Requirements: The Small Seller Exception

Challenges to the small seller exception have come from all sides: some argue it should be higher;¹⁷¹ others want to eliminate it;¹⁷² others argue it should

164. See S. 743 §§ 2(a)–(b), 4(7) (proscribing the remittance of remote sales tax and defining the location to which remote sale is sourced).

165. See S.C. CODE ANN. § 12-36-1310 (2014).

166. S. 743 § 4(7). For determining use tax rates, the Act uses the purchaser's delivery address; the address known to the remote seller or, if the seller does not know the address, the address the remote seller obtained during the transaction's consummation; and then the remote seller's address. *Id.*

167. *Goodlatte Principles*, *supra* note 87.

168. See generally S. 743 § 2(c) (noting that a remote seller must have gross annual receipts over one million dollars for the state to require the remote seller to collect sales and use taxes).

169. *Id.*

170. Hamilton, *supra* note 111 (stating that some estimates indicate no more than 1,000 remote sellers nationwide make enough sales to be affected by the Act); Letter from The Marketplace Fairness Coalition to Grover Norquist, Ams. for Tax Reform 3 (May 13, 2013), available at <http://www.marketplacefairnessnow.org/download/mfc-letter-to-grover-norquist-5-13-13.pdf>.

171. See Stathopoulos, *supra* note 14, at 47 (stating that some argue for as high as a \$50 million exception); Letter from Jeffrey A. Porter, Chair, AICPA Tax Executive Committee, to Members of Congress at 7 (Sept. 10, 2013), reprinted in TAX NOTES, Sept. 13, 2013, available at LEXIS, 2013 TNT 178-30 (recommending that the \$1 million exemption threshold be “substantially larger”).

vary depending on the particular business sector;¹⁷³ and still others want supplementary rules for small sellers.¹⁷⁴

Raising the small seller exception will ease the burden of tax administration on many remote sellers, but it will also undercut the Act's purpose.¹⁷⁵ A potential compromise would raise the small seller exception initially and then allow it to be phased out over time.¹⁷⁶ Even though advances in technology continue to ease the burdens of tax administration, holding large and small sellers to the same standards seems unfair, especially when some large sellers dedicate "entire teams of employees" to their tax obligations.¹⁷⁷

Another proposed amendment would vary the small seller exception depending on the type of business the remote seller operates.¹⁷⁸ Under this proposal, the Small Business Administration's (the SBA) definition of a *small business* would control the revenue threshold necessary to qualify under the Act's small seller exception.¹⁷⁹ In some instances, it would be lower than the present \$1 million mark, while it would be much higher in others.¹⁸⁰ Just as it is unclear how the drafters of the Act decided to use a \$1 million threshold, it is unclear how the SBA came up with its definition of a *small business*. Additionally, offering a different small seller exception based on the particular industry might invite confusion and litigation, which all parties affected by the Act would certainly prefer avoiding.

Another way to reduce the burden on small remote sellers would be to amend the Act to require that individual states allow small remote sellers to elect to calculate their use tax obligations based on a state's blended sales and use tax

172. See Goodlatte *Principles*, *supra* note 87 ("Governments should not stifle businesses by shifting onerous compliance requirements onto them; laws should be so simple and compliance so inexpensive and reliable as to render a small business exemption unnecessary." (emphasis added)).

173. JONATHAN ORSZAG, THE DEFINITION OF SMALL BUSINESS IN THE MARKETPLACE FAIRNESS ACT OF 2013, at 3-4 (2013).

174. See Henchman, *supra* note 144 ("Offering this option [of a single blended sales tax rate for each state], even if just for small sellers, would greatly reduce the complexity of compliance down to a more manageable 44 tax rates." (emphasis added)).

175. See Marketplace Fairness Act of 2013, S. 743, 113th Cong. (as referred to the H. Comm. on the Judiciary, May 20, 2013) (stating that the purpose of the Act is "[t]o restore States' sovereign rights to enforce State and local sales and use tax laws").

176. Henry Reske & Amy Hamilton, *U.S. House Judiciary Committee May Draft Its Own Remote Sales Tax Bill*, ST. TAX TODAY, May 17, 2013, available at LEXIS, 2013 TNT 96-9.

177. Stathopoulos, *supra* note 14, at 47.

178. See ORSZAG, *supra* note 173, at 3. Note that the persuasiveness of Orszag's study—as is the case with many other studies on the Act—suffers because its conclusion aligns with the views of the company that funded the report, which in this case was eBay. *Id.* at n.1. The Marketplace Fairness Coalition, which supports the Act, recently paid Arthur Laffer to conduct an economic study that focused on the Act's benefits. Henry Reske, *eBay-Funded Study Faults Small Business Definition in Marketplace Fairness Act*, TAX NOTES TODAY, Oct. 9, 2013, available at LEXIS, 2013 TNT 196-7. Mr. Laffer's study is briefly mentioned *supra* note 57.

179. See ORSZAG, *supra* note 173, at 3.

180. *Id.* at 1-2 (noting that certain types of farms would be exempt up to \$750,000, while dry cleaners would be exempt up to \$5 million).

rate, effectively reducing the number of tax jurisdictions from 9,600 to forty-four.¹⁸¹ Blended sales and use tax rates are calculated using a combination of zip codes and population weights.¹⁸² One problem with the blended rate method, however, is that population numbers for each zip code are only calculated once every ten years.¹⁸³ Accordingly, changes in local population numbers might skew the applicable blended sales tax rate.¹⁸⁴ Another problem is that the blended sales tax rate method negatively impacts local jurisdictions with higher sales and use taxes because they will recognize less than their usual share of sales and use tax revenue under the model.¹⁸⁵ In South Carolina, the sales and use tax rates vary from a low of six percent to a high of nine percent, depending on the local jurisdiction.¹⁸⁶ Using a blended rate would adversely affect some counties, while others would enjoy a windfall.¹⁸⁷ Although South Carolina could figure out how to distribute the taxes among the counties, that process would undoubtedly generate intrastate tension.

F. Applying the Simplification Requirements in South Carolina: Clarifications and Ambiguities

The Act fails to clearly define certain key terms, which creates some curious consequences. For example, the Act defines a *remote sale* as “a sale into a State” where the seller would not otherwise be obligated to pay.¹⁸⁸ The Act provides a generic definition of a *state*, including territories like Puerto Rico and tribal organizations.¹⁸⁹ However, commingling the definition of a *state* and a *remote sale* with the small seller exception creates a scenario in which a very large remote seller may, nonetheless, qualify for the small remote seller

181. See Henchman, *supra* note 144. This number is forty-four because some states do not have local sales and use taxes. *Id.*

182. *Id.*

183. See SCOTT DRENKARD, TAX FOUND., FISCAL FACT NO. 357: STATE AND LOCAL TAX RATES IN 2013, at 4 (2013), available at <http://taxfoundation.org/sites/taxfoundation.org/files/docs/ff357.pdf>.

184. See Henchman, *supra* note 144 (noting that the calculation of the blended tax rates is dependent upon population).

185. Basically, a blended sales tax rate combines the rates from local jurisdictions with the statewide rate into a single blended rate, or a blended average. Thus, the counties currently employing the highest sales tax rates would be required to lower their respective rates to the blended rate. See S.C. DEP'T OF REVENUE, FORM ST-439: SALES AND USE TAX RATES OF SC MUNICIPALITIES (BY ZIP CODE) (2013), available at http://www.sctax.org/NR/rdonlyres/F79AAE8-A168-427A-92CB-0BB67427FE9E/0/ST439_12022013.pdf (listing county and municipality sales and use tax rates in South Carolina, which range from six to nine percent).

186. See *id.*

187. If the blended tax rate is used, some counties would be forced to decrease their respective tax rates, while others would experience an increase. See *id.*

188. See Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 4(5) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

189. See *id.* § 4(8).

exception and not be required to collect sales taxes from certain customers.¹⁹⁰ The small seller exception only applies to remote sellers with “gross annual receipts in total *remote sales* in the United States” over the prior year of less than \$1 million.¹⁹¹ Because sellers with a physical presence are already subject to sales and use taxes under *Quill*,¹⁹² the sales they make in areas where they have a physical presence are not *remote sales* as defined under the Act.¹⁹³ Therefore, if a remote seller sends products into a tribal organization—which the Act defines as a state¹⁹⁴—it might not be obligated to collect and remit a use tax due to the low number of qualified remote sales.¹⁹⁵ Further, this loophole could arise in the case of a large seller that has a physical presence in most areas and does most of its business in person, but makes the occasional remote sale to a tribal organization where the seller lacks physical presence.¹⁹⁶ The Senate could not have intended to retain this loophole in its bill, and an amendment would be helpful to clarify how remote sales would be treated under these facts.

Congress may also need to amend the Act to fix an advantage that non-Streamlined Agreement states currently have over the Streamlined Agreement member states.¹⁹⁷ As noted in Part II, South Carolina is not a member of the Streamlined Agreement.¹⁹⁸ However, states that do opt to comply under the Act via their Streamlined Agreement membership could begin requiring remote sellers to collect use taxes 180 days after notifying remote sellers of their intent to exercise their authority under the Act.¹⁹⁹ The 180-day requirement can be satisfied “no earlier than the first day of the calendar quarter that is at least 180 days” from when the Act becomes law.²⁰⁰ On the other hand, non-Streamlined Agreement states may begin exercising their power under the Act after six months from the time they implement the simplification requirements.²⁰¹ Some states are already simplifying their tax codes to comply, effectively getting a head start on Streamlined Agreement states.²⁰²

190. See *id.* §§ 2(c), 4(5), 4(8).

191. *Id.* § 2(c) (emphasis added).

192. See *Quill Corp. v. North Dakota*, 504 U.S. 298, 311, 312 (1992).

193. See S. 743 § 3(f) (“The provisions of this Act shall apply only to remote sales and shall not apply to intrastate sales or intrastate sourcing rules.”).

194. *Id.* § 4(8).

195. See *id.* §§ 2(c), 4(5).

196. See *id.* §§ 2(c), 4(5), 4(8).

197. See Porter Letter, *supra* note 171, at 6 (describing how Streamlined Agreement states would be allowed to impose a collection and remittance requirement upon remote sellers starting at least 180 days after the enactment of the Marketplace Fairness Act of 2013, whereas non-Streamlined Agreement states could impose the same requirements starting at least six months after the state enacts legislation implementing the Act’s sales tax simplification requirements).

198. See *supra* note 34.

199. See Porter Letter, *supra* note 171, at 6.

200. *Id.*

201. *Id.*

202. See Amy Hamilton, *MTC Launches Project on State Implementation of Marketplace Fairness Act*, ST. TAX TODAY, July 29, 2013, available at LEXIS, 2013 STT 145-1 (describing how

G. *Considering the Costs of Compliance*

Any forecast of exactly how much the Act will cost South Carolina is nothing but an estimated figure.²⁰³ The Act's opponents argue that compliance will be costly for remote sellers,²⁰⁴ and they question whether the revenue will be realized as predicted.²⁰⁵ The Act expressly states some of the expenses: the duty to provide information about products that will be taxed or exempted;²⁰⁶ the duty to provide a database of the state's rates and boundaries;²⁰⁷ the duty to provide free software for calculating sales and use taxes, which must be updated when rates change;²⁰⁸ and the duty to provide "certification procedures for persons to be approved as certified software providers."²⁰⁹ However, some of the costs associated with compliance—such as maintaining a state entity to administer remote seller use tax compliance²¹⁰—should also help the state economy by creating new jobs because employees will be needed to run that entity. Supplementing those express costs are constructive expenditures. For example, if South Carolina provides the wrong information to a remote seller or its certified software provider, and either party relies on the state-provided information to its detriment, the state may not hold the relying party liable for failure to comply with the Act.²¹¹ Relieving a party of liability for filing deficient tax returns amounts to a constructive expenditure because South Carolina would recognize less revenue than it would if the state required that the tax obligation be paid in full after the mistake was recognized.²¹²

Most of the costs remote sellers are worried they will be required to cover are related to modifying their tax software to comply with the certified software

Colorado and the District of Columbia have already taken steps to meet the requirements of the Act).

203. Compare Bruce et al., *supra* note 18, at 540 tbl.1 (estimating a total state and local revenue loss of up to \$12.65 billion by 2012 from E-commerce sales), with KAVANAGH & BESSIN, *supra* note 139, at 2 (estimating the cost impact to mid market online and catalog retailers of \$80,000–\$290,000 in initial setup costs and \$57,500–\$260,000 annually for maintenance and service fees). See also Clark, *supra* note 41 (describing how early estimates of the revenue to be gained from online sales taxes were largely overestimated).

204. See KAVANAGH & BESSIN, *supra* note 154, at 2 (asserting that sellers with \$5–50 million in annual sales will spend between \$80,000–290,000 initially to set up the Act's software and an additional \$57,000–260,000 in annual expenses and hidden costs).

205. See Clark, *supra* note 41.

206. Marketplace Fairness Act of 2013, S. 743, 113th Cong. § 2(b)(2)(D)(i) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

207. *Id.*

208. *Id.* § 2(b)(2)(D)(ii).

209. *Id.* § 2(b)(2)(D)(iii).

210. *Id.* § 2(b)(2)(A)(i).

211. See *id.* § 2(b)(2)(E)–(H).

212. See *id.* Incorrect information provided by the state would relieve both the certified software provider and the remote seller of liability. *Id.* § 2(b)(2)(G). The state would also have to provide both parties ninety days' notice of any rate change, or else relieve them of liability. *Id.* § 2(b)(2)(H).

providers.²¹³ The Act will require South Carolina to provide remote sellers with the software necessary for filing their use tax obligations, and the state also will have to provide certification procedures for approving certified software providers.²¹⁴ Nevertheless, remote sellers are worried about how much it will cost to comply with the state-provided software services.²¹⁵ Online retailers regularly change their inventory, and those new products will have to be matched with a corresponding code in the certified software to determine whether the product is taxable.²¹⁶ Although integrating the new software with the remote seller's existing software may cost money at first, most sellers already overhaul their websites every three to five years²¹⁷ and should become acclimated to the new software systems.

Considering the glitches that could occur in implementing the new procedures, advocates for remote sellers are pushing for a brief transition period after the Act takes effect, in which a state-provided amnesty would relieve a remote seller who "reasonably tries" to comply with the law but makes a mistake in filing its use tax returns.²¹⁸ Relieving a remote seller of tax liability for merely trying to conform under the law would be another constructive cost for the state because current state law provides no such leniency.²¹⁹ Under current law, South Carolina considers the noncollection of use taxes owed to the state as a tax deficiency,²²⁰ and the state will hold the seller liable for the deficiency plus collection costs.²²¹ The temporary amnesty, however, might be a necessary compromise to get the Act passed and, in the long term, South Carolina would definitely be better off compared to the status quo.

H. A Constitutional Challenge to the Marketplace Fairness Act

After the Act becomes law, it may be subject to a constitutional challenge under the Due Process Clause. In *Quill*, the Court stated that the test of a law's constitutional validity under the Commerce Clause differs from a Due Process Clause test.²²² Still, any law Congress enacts has a favorable chance of overcoming a Commerce Clause challenge because the Constitution states that Congress has the power to "regulate Commerce with foreign Nations, and among

213. See KAVANAGH & BESSIN, *supra* note 154, at 2.

214. S. 743 § 2(b)(2)(D)(ii)–(iii).

215. See generally KAVANAGH & BESSIN, *supra* note 139, at 2 (noting that most states will likely offer compensation to some software providers "to fulfill their obligation to provide 'free' software to retailers," but that using these software providers will hardly be free).

216. *Id.*

217. See *id.* at 7.

218. Porter Letter, *supra* note 171, at 9.

219. See S.C. CODE ANN. § 12-36-1350 (2014).

220. *Id.*

221. *Id.* § 12-55-40.

222. *Quill Corp. v. North Dakota*, 504 U.S. 298, 305, 312 (1992).

the several States, and with the Indian Tribes.”²²³ On the other hand, the Supreme Court is not required to give such deference to Congress when considering a law challenged under the Due Process Clause.²²⁴ In *Quill*, the Court was satisfied that the challenged state law did not violate the remote seller’s due process rights, but held that the state law did violate the Commerce Clause.²²⁵ A remote seller could argue that the Act violates its individual due process rights because even though the remote seller has aggregate sales over the \$1 million mark, it only makes a few sales into a particular state.²²⁶ The remote seller would have to show that its due process rights were violated when it had to collect and remit use taxes to that state.²²⁷ While a successful challenge under this scenario would only negate the Act’s authority as applied to that remote seller, it might also undermine the Act’s effectiveness and inspire more challenges by other remote sellers.²²⁸

V. CONCLUSION

The Senate’s version of the Marketplace Fairness Act is not perfect. Greater clarification would help states like South Carolina, as well as the remote sellers they hope to tax, better understand what changes they must make to comply with the law. The challenge in drafting the final law will be finding a compromise between simplifying the tax administration process for remote sellers and respecting each state’s right to regulate its own tax code. Given that the

223. U.S. CONST. art. I, § 8, cl. 3.

224. See *Quill*, 504 U.S. at 305 (“[W]hile Congress has plenary power to regulate commerce among the States and thus may authorize state actions that burden interstate commerce . . . it does not similarly have the power to authorize violations of the Due Process Clause.” (citations omitted)).

225. See *id.* at 308, 317–18 (upholding the North Dakota Supreme Court’s holding that the proposed use tax did not violate the Due Process Clause, but reversing the holding that physical presence is not required to establish a “substantial nexus” under the Commerce Clause). In that case, the state did not violate the Due Process Clause because the remote seller “purposefully directed its activities at North Dakota residents, . . . the magnitude of those contacts [was] more than sufficient for due process purposes, and . . . the use tax [was] related to the benefits [the company] receive[d] from access to the State.” *Id.* at 308.

226. Nearly 50% of revenue losses can be attributed to six states. Feng & Wade, *supra* note 46, at 10. Across the nation, revenue loss ranges from as high as \$3.1 billion in California to a low of \$1.6 million in Arkansas. *Id.* at 9–10. While a remote seller would not likely challenge hundreds of thousands of dollars in sales sourced to California, what about fifty dollars in sales to Arkansas? See *id.* at 12–13 tbl.1.

227. See, e.g., *Quill*, 504 U.S. at 298, 301 (challenging a North Dakota law that required soliciting mail order companies to collect and remit sales tax from customers on due process grounds).

228. See Steven Roll, *State Tax Snapshot: Does the Marketplace Fairness Act Satisfy Due Process Requirements?*, BLOOMBERG BNA (Oct. 7, 2013), <http://www.bna.com/state-tax-snapshot-b17179877671/> (describing how “it is unclear if the Marketplace Fairness Act would withstand scrutiny under the Due Process Clause” based on recent Supreme Court precedent requiring purposefully directed actions within a state before a company is subject to that state’s jurisdiction).

Marketplace Fairness Act would require South Carolina to make only modest changes to its tax code, the state should adopt the Act when it becomes law. The way that the national economy continues to evolve—where a person can purchase a new pair of shoes online and receive them within a few days—has presented problems for states that rely on their sales and use taxes to generate needed revenue. For remote sellers who have been able to avoid creating a physical presence in most states, it has been quite a run. Congress, however, is now poised to pass legislation that it expects will put all sellers back on level footing.

James Bull Sterling