



## COLORADO: SUPREME COURT CONSIDERS 2010 TAX NOTIFICATION LAW

Colorado subjects online purchases to sales and use tax. Taking this a few steps further in 2010, the state passed a law designed to facilitate collection of these taxes. The Direct Marketing Association (DMA) filed a lawsuit in response, and the case has made its way to the United States Supreme Court. Last week, in *Direct Marketing Association v. Brohl*, the Court heard oral arguments in that challenge.

### Background

The Colorado Department of Revenue's **FYI publication, General 10** informs readers that the state imposes a 2.9 percent use tax on Internet purchases, payable when tax is due but not collected by the retailer. The sales tax, which retailers collect at the time of a purchase, is also 2.9 percent.

Another **FYI publication, Sales 5**, states that a remote seller, defined as an out-of-state business with no physical presence in Colorado, is not required to actually collect and remit taxes. This is so because of a 1992 Supreme Court case, *Quill Corp. v North Dakota*, prohibiting such requirements. Instead, Colorado requires consumers, who purchase items from remote sellers that are subject to the tax, report and pay it with their income tax returns.

In an attempt to bolster compliance, the General Assembly passed the above-mentioned 2010 law that required out-of-state online retailers that do not collect Colorado state sales and use taxes to notify customers 1) of the amount of taxes they owe; and 2) that they are obligated to pay those taxes. In addition, the law requires remote sellers with sales of more than \$100,000 to report the amount of tax owed to the state.

Thus, between the requirements imposed on remote sellers and Colorado residents, the state attempted to mitigate lost sales tax revenues through legislative action. A Colorado Statesman **article** revealed that by one estimate, Colorado lost \$352.6 million in sales and use taxes that went uncollected from customers of online and catalog retailers in 2012.

### *Direct Marketing Association v. Brohl*

When the DMA sued the Executive Director of the Colorado Department of Revenue in federal court, claiming that the 2010 law was unconstitutional, the court agreed, and Colorado appealed to the 10th Circuit Court. **There**, the appellate court determined that it lacked the authority to hear the case. It reasoned that the **Tax Injunction Act (TIA)**, which prohibits the federal courts from enjoining, suspending or restraining "the assessment, levy or collection of any tax under state law where a remedy exists in a state court," bars the federal courts from prohibiting tax collection efforts in the first place.

The DMA appealed the 10th Circuit's conclusion to the United States Supreme Court. In its **petition for certiorari**, the DMA argued that it was not attempting to get in the way of tax collection, "but rather to prevent the imposition of discriminatory and burdensome regulatory obligations..."

### The oral argument

**Ronald Mann**, a contributor to SCOTUSBlog.com, characterized the **oral arguments** as "puzzling," because of the justices' skepticism of both sides' reasoning.

For example, one line of questioning concerned whether the 2010 law's notification and reporting requirement constitutes the "collection" of taxes. If it does, then the 2010 law falls under the purview of the TIA, which would then strip the federal court of jurisdiction. Justice Breyer indicated that he thought a better way to enforce the collection of taxes would be to ask citizens, politely, to "pay", and if they don't, send them to prison. Acknowledging that this is a "not perfect" way of handling it, he observed that the method "does tend to encourage people to pay the taxes that they believe that they owe."

On the other hand, Justices Ginsburg and Kagan wondered what was different about previous decisions allowing a state to facilitate its tax collection efforts via a reporting requirement. Counsel for the DMA suggested the difference was in whom the requirement was being imposed on: a citizen rather than, say, an employer.

Observers indicated that it was not easy to read the Justices, and it will likely be several months before we expect an opinion.

## STATES REMIND CONSUMERS OF THEIR TAX OBLIGATIONS FOR ONLINE PURCHASES

In a recent **Alert**, we wrote about Indiana's Department of Revenue reminder to consumers that online purchases are subject to sales and use taxes that should be reported on state tax returns. Other states, like Michigan, Idaho and Alabama are doing the same.

### Michigan

The Michigan Department of Treasury (DOT) **prompts** shoppers to keep receipts and report use tax on the Michigan 1040 tax return. The DOT confirms that purchases made online are not tax-free during holiday season, or at any other time of year.

In deciphering the tax, the DOT points out the following:

Michigan's 6 percent Use Tax generally applies to transactions in which the retailer does not collect sales tax. This happens most frequently

## multistate tax update december 18 2014

---

when an individual makes a purchase from online retailers, through mail-order outlets, or television shopping networks that do not have physical locations in Michigan. When out-of-state vendors do not collect sales tax on purchases, under Michigan law, the purchaser is responsible for reporting and paying the use tax.

Purchases subject to Michigan's use tax include appliances, books, clothing, computers, DVDs/CDs, electronics, furniture, pre-written computer software, and tobacco products.

### Idaho

Likewise, the Idaho State Tax Commission (Commission) issued a **news release** (release) informing consumers that they may owe use tax to the state if the seller doesn't charge them sales tax. The Commission explained that "[w]hen shoppers buy goods on the Internet, by telephone, or from a mail-order catalog, sellers won't charge sales tax if they're not Idaho retailers. In that case, the shoppers owe use tax if the goods are used, given away, stored, or consumed in Idaho. The shoppers are responsible for paying the tax directly to the Tax Commission."

Idaho's use tax rate is the same as the sales tax rate, 6 percent.

The release offers the perspective of Randy Tilley, the Tax Commission's Audit Division Administrator. He justifies the tax as "an important tool that helps Idaho retailers remain competitive with out-of-state sellers that do not charge tax." The funds help pay for state and local services, ensuring "that all consumers in the state contribute fairly to the funding of these services, whether they choose to make purchases in Idaho, online, or outside the state."

### Alabama

The Alabama Department of Revenue **reminds** its citizens to ring up the use tax on their online purchases this holiday season if the retailer does not do so. Not only does the 4 percent state use tax on out-of-state purchases apply when the seller does not collect it, local sales and taxes apply in cities and counties that levy one.

Alabama earmarks its sales and use taxes primarily for its Education Trust Fund.

## AMAZON.COM WILL OPEN ITS FIRST WAREHOUSE IN 2015, REQUIRING IT TO COLLECT SALES TAXES IN ILLINOIS

Amazon.com, Inc., Illinois Governor Pat Quinn, and U.S. Senator Dick Durbin recently **announced** Amazon.com's plans to build its first warehouse, in the state of Illinois. Amazon.com will invest \$75 million in the project, and plans to create more than 1,000 new, full-time jobs by 2017. Amazon already has a **physical presence** in certain parts of the country, including fulfillment centers in 14 states and customer service centers in three states.

Internetretailer.com **observed** that "[t]he new warehouse will mean Amazon will start charging sales tax to Illinois consumers. Law applying to web retailers ties in-state collection of sales taxes for web purchases with a merchant's presence in the state—that can include not only warehouses but offices or stores." Illinois' **Public Act 98-1089**, effective January 1, 2015, applies to all retailers with annual gross receipts of more than \$10,000 in sales to Illinois customers.

Though Amazon.com would be paying taxes in Illinois by virtue of the presence of the warehouse, it **supports** a national law, like the proposed federal Marketplace Fairness Act, requiring online sales tax collection regardless of a physical presence. In fact, according to **bankrate.com**, there are 23 states in which the online retailer already collects taxes. Some states collect the tax by virtue of Amazon.com's physical presence, while others have deals with Amazon.com, like the one in Indiana we **previously addressed**. Bankrate.com states that Minnesota and Maryland are the latest two as of October 1, 2014, and South Carolina will join the group on January 1, 2016.

Amazon.com views the taxing of online purchases as a leveling of the playing field. **Dailyfinance.com** points out that on-line retailers with no physical presence in a state are usually not subject to a use tax. But Amazon.com has a physical presence in enough states that it is at a disadvantage over competitors with less of physical presence, like eBay and Overstock.

Ebaymainstreet.com, a grassroots action network, explicitly **opposes** any such legislation, in part because of its purported "damage to the competitiveness and innovation of small businesses" who use the Internet.

Leading up to the midterms, lawmakers were too focused on elections to move forward on the proposed Marketplace Fairness Act (MFA). In a **taxanalysts.com** piece, Rep. Jason Chaffetz (R-Utah) hinted that post-midterm compromise efforts may be fruitful, which could lead to his introduction of a separate bill to replace the MFA after the New Year that addresses concerns from conservative members of Congress.

For additional information regarding these subjects, or any other multistate tax issues, please contact:

#### David M. Kall

216.348.5812

dkall@mcdonaldhopkins.com

#### David H. Godenswager, II

216.348.5444

dgodenswager@mcdonaldhopkins.com

#### Susan Millrad McGlone

216.430.2022

smcglone@mcdonaldhopkins.com

### MULTISTATE TAX SERVICES

Businesses must be vigilant and careful in managing their state and local tax liabilities and exposures. We understand this can be a daunting task. McDonald Hopkins Multistate Tax Services provides a broad range of state and local tax services including tax controversy, tax evaluation, tax planning, and tax policy. With professionals who have worked both inside and outside government agencies, our multistate tax team leverages its knowledge and experience to help clients control their complex multistate taxes.