Federal court delays ruling on controversial remote taxation law in Colorado

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In recent years, state lawmakers have passed laws to expand (or in attempt to expand) their respective department of revenue's authority to cause out-of-state or remote sellers to collect and remit sales taxes. In some cases, these laws have been deemed to be unconstitutional, as the statute exceeded the guidelines articulated in the seminal case of *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). In *Quill*, the U.S. Supreme Court held that it was unconstitutional under the dormant commerce clause of the Constitution for a state to require a retailer with no in-state physical presence to collect sales or use tax.

Most recently enacted statutes addressing this issue have (mostly successfully, thus far) attempted to get around the physical presence requirement by creating an affiliate nexus standard which creates sufficient nexus to subject businesses to sales and use tax in a particular state. For example, New York requires out-of-state retailers who only conduct their business over the internet to collect and remit sales tax despite not having any physical location or employees in the state under certain circumstances. A New York court, in ruling on the validity of this law, held that where these out-of-state retailers enter into arrangements whereby they use a third party New York resident's website to link to the out-of-state retailer's website for compensation to the resident, the out-of-state retailer is responsible to collect and remit sales tax (**click here** for a prior article where we discussed this New York case).

Colorado lawmakers took an entirely different tack. Instead of requiring out-of-state retailers to collect and remit state sales tax, an area fraught with constitutional traps, lawmakers require out-of-state retailers to simply provide information about the sales made to Colorado residents, a so-called "tattletale" law. The rationale of the Colorado lawmakers is that such a law does not *directly* conflict with the holding of *Quill*.

More specifically, the 2010 Colorado law (Colo. Rev. Stat. 39–21–112(3.5)(c) & (d)) requires non-collecting retailers whose gross sales in Colorado exceed $100,000 to: (1) provide transactional notices to Colorado purchasers; (2) send annual purchase summaries to Colorado customers; and (3) annually report Colorado purchaser information to the Colorado Department of Revenue (the "Department").

This law was most recently litigated in *Direct Marketing Ass'n v. Brohl*, 2013 WL 4419324 (10th Cir. 2013). In *Direct Marketing Ass'n*, the U.S. Court of Appeals declined to rule on the merits of the case and held that the lower federal court did not have the authority to make a ruling or grant an injunction to the taxpayer under the Tax Injunction Act ("TIA") – Colorado state courts retain jurisdiction for such a ruling. The TIA provides that "district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State." 28 U.S.C. § 1341. The *Direct Marketing Ass'n* holding remands the ultimate decision of whether the statute is constitutional to Colorado state courts for now.

Three aspects should be noted: (1) the Court of Appeals did not rule whether the Colorado law is constitutional; (2) if an out-of-state retailer does not collect and remit sales taxes, the state resident is required by state law to report and pay use taxes to the Department with their income tax returns; and (3) this Colorado "tattletale" law provides the Department with the information necessary to enforce use tax laws. Additionally, the failure to report and pay use tax is a criminal offense. However, as the court recognized in *Direct Marketing Ass'n*, "use tax collection is elusive. Most Colorado residents do not report or remit use tax despite the legal obligation to do so." As long as this is the case, state legislators will certainly continue to attempt to increase the requirement of mandating out-of-state retailers to collect and remit sales taxes.

Click here to read the 10th Circuit Court of Appeals' *Direct Marketing Ass'n v. Brohl* decision.

Click here to read the text Colorado Revised Statute 39–21–112.

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