



Legislative Fiscal Bureau

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Joint Committee on Finance

Paper #345

Require Marketplace Providers to Collect Sales Tax (General Fund Taxes -- Sales and Use Taxes)

[LFB 2019-21 Budget Summary: Page 150, #1]

CURRENT LAW

Prior to the 2018 U.S. Supreme Court decision in *Wayfair vs. South Dakota*, out-of-state sellers that lacked a physical presence in Wisconsin (sellers that had no property or employees physically located in the state) were not required to collect state sales and use tax. The *Wayfair* decision overturned this physical presence requirement and held that states can require these remote sellers to collect and remit sales tax, provided the imposition of the tax meets certain other conditions.

In response to *Wayfair*, DOR issued an emergency rule that required remote sellers to collect and remit sales tax on their sales of taxable goods and services into Wisconsin beginning October 1, 2018, except that a seller with fewer than 200 annual transactions in Wisconsin or \$100,000 or less in annual gross sales in the state was not required to collect and remit the tax. This collection threshold, also known as the small seller exception, was codified in 2017 Act 368.

Most sellers that make taxable sales of goods and services must collect and remit sales tax on such sales, unless they are otherwise exempted in statute. Under current law, a seller who makes total taxable sales of less than \$2,000 in a calendar year is generally not required to collect and remit sales tax under the occasional sales exemption. However, the occasional sales exemption only applies to the transfer, sale, or rental of motor vehicles if: (a) the vehicle is transferred to certain relatives; (b) the vehicles has been registered or titled in the name of the transferor; and (c) the transferor is not engaged in the business of selling motor vehicles.

Also under current law, a person is not required to collect and remit sales tax on sales made on behalf of third-party sellers if the person, or the person's affiliate: (a) operates a distribution facility

where no retail sales take place; (b) discloses to the customer that the third-party is the seller and the third-party seller owns the goods being sold; and (c) makes no sales of goods for which the customer takes possession of the goods at a location operated by the person or any of the person's affiliates. This provision is known as the distribution facility exception.

GOVERNOR

Define a marketplace provider and a marketplace seller as described below. In addition, require a marketplace provider to collect and remit state sales and use tax, and other applicable taxes and fees, on sales the marketplace provider makes on behalf of a seller.

Definition of a Marketplace Provider. A marketplace provider would be defined as a person who contracts with a seller to facilitate for consideration, regardless of whether deducted as fees from the transaction, the sale of the seller's products through a physical or electronic marketplace operated by the person, and who engages, either directly or through one or more affiliated persons, in any of the following:

- a. transmitting or communicating the offer or acceptance between the seller and a buyer.
- b. owning or operating the technology or electronic or physical infrastructure that brings the buyer and seller together.
- c. providing a virtual currency that a buyer is allowed or required to use to purchase a product from the seller.
- d. developing software or conducting research and development for activities described in "b" that are directly related to a physical or electronic marketplace operated by the person or an affiliated person.

In addition to meeting one of the conditions described above, to be considered a marketplace provider, the person also would have to engage in any of the following with respect to the seller's products: (a) providing payment processing services; (b) providing fulfillment or storage services; (c) listing products for sale; (d) setting prices; (e) branding sales as those of the marketplace provider; (f) taking orders; (g) advertising or promotion; or (h) accepting or assisting with returns or exchanges or providing other types of customer service.

An affiliated person would mean a person who, with respect to another person: (a) has an ownership interest of more than five percent, whether direct or indirect, in the other person; or (b) is related to the other person because a third person, or group of third persons who are affiliated persons with respect to each other, holds an ownership interest of more than five percent, whether direct or indirect, in the related person.

Definition of a Marketplace Seller and Expanded Definition of a Retailer. Under the bill, a marketplace seller would mean a seller who sells products through a physical or electronic marketplace operated by a marketplace provider, regardless of whether the seller is required to be registered with DOR. In addition, the bill would add to the definition of a retailer a marketplace

provider who facilitates, on behalf of a marketplace seller, taxable sales of goods and services that are sourced to Wisconsin. The bill would expand the definition of a retailer for purposes of sales tax collection to mean every seller who makes any sale of tangible personal property or services, regardless of whether the sale is made on the seller's own behalf or on behalf of another person (the bill would similarly modify the definitions of sale and seller under current law to clarify that the definitions apply regardless of whether the sale is made on the seller's own behalf or on behalf of another person). As a result, both marketplace providers and marketplace sellers could be regarded as retailers for purposes of the sales tax.

Liability of Marketplace Providers and Marketplace Sellers. The bill would stipulate that a marketplace provider is liable to collect and remit the sales and use tax on sales made on behalf of a marketplace seller. In addition, for each sale facilitated on behalf of a marketplace seller, the marketplace provider would be required to obtain and maintain each exemption certificate provided by a purchaser claiming an exemption from the tax. The sales price subject to tax would include the price charged to a purchaser, including any charges for facilitating the sale on the seller's behalf.

The bill would require a marketplace provider to notify the marketplace seller that it will collect and remit the applicable taxes on the seller's behalf. Upon notification, only the provider could be audited and held liable for the taxes due on the sale. The seller could claim a deduction on their sales tax return for the sales price of each sale on which the seller received such notification. However, if the seller does not receive such notification, both the provider and seller could be audited and held liable for the taxes.

Deductions. The bill would specify that a marketplace provider who collects and remits sales or use tax on behalf of a marketplace seller could claim a deduction for bad debts against their sales tax liability if either the marketplace provider or marketplace seller could claim a deduction for bad debt under federal income tax law. A marketplace seller would not be allowed to claim such a deduction for the same transaction.

Repeal the Distribution Facility Exception. As described above, current law provides an exception from sales tax collection and remittance for distribution facilities that meet certain conditions. The bill would repeal this exception.

Other Provisions. The bill would modify laws governing the room tax, the local rental car tax, the local food and beverage tax, and the state rental vehicle fee to conform to this provision, so that the responsibility for tax collection and remittance is with the same person for each tax or fee.

The provision would take effect on the first day of the calendar quarter that is at least three months after publication of the bill, or, for a marketplace provider, the day on which the provider is notified by DOR to collect sales and use tax on sales made on behalf of third-party sellers, whichever is earlier. The administration estimates that the provision would increase state tax revenues by \$26,800,000 in 2019-20 and \$67,100,000 in 2020-21 and annually thereafter.

DISCUSSION POINTS

Background

1. Every retailer engaged in business in Wisconsin that makes sales of taxable goods and services that are sourced to this state must collect sales and use tax from their purchasers and remit payment to DOR. Current law defines all vendors as retailers engaged in business within the state for use tax purposes if they sell tangible personal property or other taxable items or services for storage, use, or other consumption in Wisconsin "unless otherwise limited by federal law." Prior to the *Wayfair* decision, federal law prohibited states from requiring out-of-state sellers without a physical presence in the state to collect and remit the tax.

2. In 2016, South Dakota enacted an economic nexus threshold to establish tax jurisdiction over remote sellers without any requirement for physical presence in the state. South Dakota extends nexus to remote sellers if: (a) they conduct 200 or more annual transactions with consumers in the state; or (b) their annual sales into the state exceed \$100,000. The state argued that remote sellers meeting the "small seller exception" were required to collect and remit sales tax. This position became the impetus for the *Wayfair* decision by the U.S. Supreme Court.

3. The *Wayfair* decision was upheld, in part, because South Dakota's law was found not to constitute an undue burden on interstate commerce. Specifically, South Dakota's economic threshold provides a safe harbor for retailers with limited sales in the state. Secondly, the law does not apply retroactively to sales that have already occurred. Moreover, South Dakota is a member of the Streamlined Sales and Use Tax Agreement (SSUTA), which requires a single state level tax administration, uniform definitions of products and services, and simplified tax rate structures.

4. In the wake of *Wayfair*, DOR issued an emergency rule adopting similar provisions to those of South Dakota to ensure its imposition of collection and remittance responsibility on remote sellers was in line with the decision. As stated above, Wisconsin implemented a small seller exception (codified in 2017 Act 368) to negate sales tax collection responsibilities for those remote sellers under a specific sales or transaction threshold. In addition, the state did not require remote sellers to retroactively collect sales tax on their sales made prior to the *Wayfair* decision. Further, Wisconsin is a member of SSUTA and adheres to its simplification and uniformity requirements.

5. DOR began requiring remote sellers to collect and remit sales tax following *Wayfair* on October 1, 2018. It was originally estimated this would result in additional state tax collections of \$90 million in 2018-19 and \$120 million annually thereafter. However, these estimates were subsequently reduced to \$45 million in 2018-19 and \$60 million annually thereafter.

6. The original estimates for *Wayfair*-related sales tax collections were reduced primarily because of lower observed compliance than originally expected. This lower compliance served as a primary impetus for the Governor's recommendation to include the provisions described in this paper, which are designed to further address sales tax collection and remittance following *Wayfair*. Together with this provision, total *Wayfair*-related sales tax collections would be estimated at \$86,800,000 in 2019-20 and \$127,100,000 in 2020-21 and annually thereafter.

7. According to industry representatives, current law is unclear as to whether marketplace providers are authorized or required to collect sales tax on sales made on behalf of remote sellers. The marketplace provider industry has conveyed the need for a legislative grant of authority to collect on behalf of such sellers. Based on information provided by the Sales Tax Institute, as of May, 2019, 28 states and the District of Columbia have enacted rules or legislation similar to the marketplace provider provisions recommended by the Governor.

Marketplace Providers and Marketplace Sellers

8. On May 1, 2019, the administration submitted an erratum seeking to clarify the intent of the marketplace provider provisions. According to the administration, the intent of the legislation is to regard as marketplace providers all persons engaging, either directly, indirectly, or through affiliated persons, in the associated activities described under the bill. A marketplace provider could subcontract with an unaffiliated person who could perform certain activities of a provider, and the marketplace provider could subsequently claim they do not have a responsibility to collect and remit the tax because they are not directly engaging in all the necessary activities to be considered a provider under the bill. Alternative 1 includes this technical clarification.

9. In general, the bill would not change the underlying taxability of goods and services. If an item is taxable or exempt under current law, that item is taxable or exempt under the bill. As stated, the bill would specify that a marketplace provider is liable to collect and remit state sales and use tax, and any other applicable taxes and fees, on sales it facilitates on behalf of a marketplace seller. This treatment would apply to all marketplaces where the structure of marketplace provider and marketplace seller exists, regardless of the taxable product or service being sold.

10. For purposes of determining whether a marketplace provider qualifies for the small seller exception, the annual gross sales and transaction amounts would be derived from sales the provider makes on its own behalf and those it makes on behalf of other sellers.

11. Similarly, a marketplace seller's sales that are facilitated by a marketplace provider and those that are made outside the marketplace are both included in determining whether the seller meets the small seller exception. If a seller who would otherwise qualify for the small seller exception makes sales through a provider, those sales are only eligible for the exception if the provider is also eligible for the exception.

12. This same approach applies in determining whether a marketplace provider or marketplace seller meets the occasional sales exemption. Under the bill, a marketplace seller's sales facilitated by a marketplace provider would qualify for the occasional sales exemption only if the provider also qualifies for the exemption (namely, if the provider's total taxable sales price from sales it makes on its own behalf and on behalf of marketplace sellers is less than \$2,000 in a calendar year).

13. A marketplace seller is still eligible for the occasional sales exemption under the bill, provided the total taxable sales price from sales it makes within and outside the marketplace is less than \$2,000 in a calendar year. However, a marketplace seller's sales made through most marketplace providers would generally be subject to tax.

14. In addition, several legislators have asked for clarification regarding how the bill would treat peer-to-peer car sharing services in which an individual rents their car to another individual through a marketplace provider. As with other marketplaces, the onus would be on the marketplace provider to collect and remit sales tax on such a transaction.

15. Under the bill, as under current law, the occasional sales exemption would not apply to the rental, including peer-to-peer rental, of motor vehicles, except in the limited circumstances described above (transfer to certain relatives). The bill would clarify that the marketplace provider would be liable to collect and remit all applicable taxes on such sales, rather than the onus being on either the marketplace seller or the marketplace provider as under current law.

Lodging Marketplaces

16. Lodging marketplaces facilitate the sale of lodging to travelers on behalf of lodging companies. These marketplaces charge travelers a fee in addition to the base price of the room, but are required to collect and remit sales tax only on the base price, not on the markup.

17. The Tax Appeals Commission made this determination in *Wisconsin Department of Revenue v. Orbitz, LLC*. In so determining, the Commission cited the ambiguity of the statute that provides for the imposition of sales tax on the *furnishing* of rooms or lodging. The meaning of "furnishing" in this context was found to be ambiguous, and the Commission noted that when such ambiguity arises in a taxing statute, it must be resolved in favor of the taxpayer. In addition, the Commission held that the relevant statute does not specifically provide for the imposition of tax on those who provide the service of reserving lodging on behalf of members of the public. DOR estimates that this decision has resulted in foregone sales tax collections of \$7.1 million on an annual basis.

18. DOR appealed this decision to the Dane County Circuit Court, which found that the interpretation of the Tax Appeals Commission was reasonable. The Department appealed once more to the Wisconsin Court of Appeals, District 4, which found that the Commission's interpretation is not contrary to the clear meaning of the statute and that another, more reasonable interpretation of the statutory language does not exist. For these reasons, lodging marketplaces are not required to collect and remit tax on the markup they charge for their services under current law.

19. It could be argued that this tax treatment presents an issue of tax equity between different types of business organization. In the aforementioned scenario, if a hotel rents a room directly to a traveler, the traveler pays sales tax on the full price of the room. However, if the same traveler rents the room through a lodging marketplace, the traveler pays sales tax only on the price of the room, not on the markup included in the final price charged to the purchaser. Some would contend this gives certain businesses an unfair advantage over others.

20. Under the bill, a marketplace provider would be liable to collect and remit sales tax on the total sales price the provider charges to the purchaser, including any charges for facilitating the sale on behalf of the marketplace seller. As a result, lodging marketplaces would be required to collect and remit sales tax on the total sales price of the lodging, including any markup the marketplace imposes on such a sale. Absent such a provision, it is possible that other marketplace providers could structure their contracts in such a way so as to assert that the service fees they charge are not taxable.

Over time, this could erode the value of the additional sales tax revenues estimated under this provision, as well as sales taxes collected under current law. The Committee could separately address whether sales tax should apply to the markup for the service of facilitating the sale of lodging (Alternative 2).

Liability Relief

21. Under the bill, if a marketplace provider is audited by DOR for sales occurring prior to January 1, 2021, the marketplace provider may obtain relief from liability determined in the audit, not to exceed five percent of the total tax due for each sale, if it could demonstrate to DOR's satisfaction that: (a) the sale was made solely on behalf of a marketplace seller; (b) the marketplace provider properly notified the marketplace seller as described above; and (c) the retail sale was properly sourced to Wisconsin (the sale took place in Wisconsin). This liability relief would not apply to sales in which the marketplace provider improperly determined where the sale took place.

22. The administration indicates that a primary goal of this provision is to relieve the underlying seller from the responsibility to collect and remit the relevant taxes on sales it makes through a marketplace. According to DOR, the purpose of the liability relief described above is to acknowledge the administrative burden some providers may experience in order to comply with the law, and to incent those providers to collect on behalf of marketplace sellers. Nothing in the bill would remove a purchaser's obligation to remit use tax for any transaction on which a marketplace provider or marketplace seller did not collect and remit the tax.

23. The fiscal impact of the liability relief given to marketplace providers would likely be minimal. Because the liability relief only applies to sales made by marketplace providers under audit for which the providers complied with the provisions listed above, the administration indicates this relief would likely only apply to a small subset of providers. In addition, any marketplace provider who qualifies for liability relief but did not collect sales tax on a sale made on behalf of a seller would still be required to pay the applicable interest and penalties on its tax amounts owed DOR.

Repeal of Distribution Facility Exception

24. As explained above, current law provides an exception from sales tax collection and remittance for persons who meet certain conditions related to the operation of a distribution facility. DOR is not aware of any persons currently operating in Wisconsin that are eligible for this distribution facility exception. Thus, the Committee could consider deleting this obsolete provision to simplify the relevant tax statutes (Alternative 3).

Maintain Current Law

25. The Committee could choose to take no action on the Governor's request and maintain current law (Alternative 4). As stated previously, current law requires all retailers engaged in business in Wisconsin to collect and remit sales and use tax on sales of taxable goods and services, unless otherwise limited by federal law. In addition, current law allows DOR to regard any salesperson as the agent of an entity from whom the salesperson obtains taxable goods and services sold by the salesperson, and as such to regard both salesperson and entity as retailers for purposes of the sales

tax. The Department states that this provision already requires most marketplace providers to collect and remit sales tax on sales made on behalf of a marketplace seller.

26. However, as noted above, the marketplace provider industry has communicated the need for a clear legislative grant of authority to require providers to collect on behalf of marketplace sellers. It is possible that certain marketplace providers would not comply with current law absent the clarification of current law that this provision is intended to create. If the Committee decided to take no action on this provision, the Committee could also choose to require DOR to provide a report detailing the additional auditors that may be necessary to pursue those marketplace providers who are not collecting and remitting sales tax as required under current law. It should be noted that the Governor is requesting that additional auditors be provided to DOR in separate provisions of the budget bill, some of which would conduct auditing activities related to sales tax collection and remittance by out-of-state sellers (some of these sellers would meet the definition of a marketplace provider or a marketplace seller under this provision). The report could also include a summary of the costs that would be incurred in the event the relevant statutes are litigated in court between the Department and the relevant marketplace providers. The report could also detail any additional administrative rules that DOR believes are necessary to effectively administer current law as it relates to the collection and remittance of sales tax by marketplace providers.

27. The Committee could also elect to adopt some combination of Alternatives 2, 3, and 4.

ALTERNATIVES

1. Adopt the Governor's recommendation, and clarify that a marketplace provider would include a person that indirectly engages as a provider. Estimate increased sales tax collections at \$26,800,000 in 2019-20 and \$67,100,000 in 2020-21.

ALT 1	Change to	
	Base	Bill
GPR- Tax	\$93,900,000	\$0

2. Take no action on the Governor's request. However, require any entity that facilitates the sale of taxable goods and services, including a marketplace provider, lodging marketplace, or retailer, to collect and remit sales tax on any fee or charge the entity charges to the purchaser, including any charges for facilitating such a sale. If the entity that facilitates the sale is not required to collect tax on the underlying taxable good or service under current law, specify that any charge or other fee the entity charges to the purchaser for facilitating the sale is subject to sales tax, and the associated tax must be collected and remitted by the entity facilitating the sale. Estimate increased sales tax collections of \$2,800,000 in 2019-20 and \$7,100,000 in 2020-21.

ALT 2	Change to	
	Base	Bill
GPR- Tax	\$9,900,000	-\$84,000,000

3. Take no action on the Governor's request. However, repeal the distribution facility exception as an obsolete provision. Estimate reduced sales tax collections under the bill of \$26,800,000 in 2019-20 and \$67,100,000 in 2020-21.

ALT 3	Change to	
	Base	Bill
GPR-Tax	\$0	- \$93,900,000

4. Take no action on the Governor's request. Instead, require DOR to submit a report to the Joint Committee on Finance, no later than the first day of the third month beginning after publication of the bill, detailing any additional auditors and/or administrative rules that may be necessary, as well as the estimated costs that would be incurred in the event the current laws governing sales tax collection and remittance by marketplace providers are litigated in court. Estimate reduced sales tax collections under the bill of \$26,800,000 in 2019-20 and \$67,100,000 in 2020-21.

ALT 4	Change to	
	Base	Bill
GPR-Tax	\$0	- \$93,900,000

5. Take no action.

ALT 5	Change to	
	Base	Bill
GPR-Tax	\$0	- \$93,900,000

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