HB 726

Department of Legislative Services

Maryland General Assembly
2015 Session

FISCAL AND POLICY NOTE

House Bill 726 (Delegate Pena-Melnyk, *et al.*)
Ways and Means

Sales and Use Tax - Online Sales Presumption

This bill specifies that, for purposes of determining whether a person is engaged in the business of an out-of-state vendor under provisions of the State sales and use tax law, a seller is presumed to have an agent, canvasser, representative, salesman, independent contractor, or solicitor operating in the State for the purpose of selling or taking orders, under certain circumstances. As a result, these sellers must collect the State sales and use tax from sales made to Maryland consumers.

The bill takes effect July 1, 2015.

Fiscal Summary

State Effect: General fund revenues may increase significantly beginning in FY 2016. The amount of the increase depends on the number of sellers impacted and the amount of sales made in Maryland. Any expenditures associated with licensing can be handled with existing budgeted resources.

Local Effect: None.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: A seller is defined as a person making sales of tangible personal property or a taxable service. For the purpose of a person engaged in the business of an out-of-state vendor, a seller is presumed to have an agent, canvasser, representative, salesman, independent contractor, or solicitor operating in the State for the purpose of selling or taking orders for tangible personal property or a taxable service if (1) the seller enters into an agreement with a resident of the State under which the resident, for a commission or other consideration, directly or indirectly refers potential customers to the seller, whether by a link on an Internet website or otherwise and (2) the cumulative gross receipts from sales by the seller to customers in the State who are referred to the seller by all residents having an agreement with the seller is greater than $10,000 during the preceding four quarterly periods ending on the last day of February, May, August, and November.

The presumption under the bill may be rebutted by proof that the resident with whom the seller has an agreement did not engage in any solicitation in the State on behalf of the seller that would satisfy the nexus requirement of the U.S. Constitution during the four quarterly periods in question.

The bill may not be construed to narrow the scope of the terms of agent, canvasser, representative, salesman, independent contractor, or solicitor for purposes of any other provision of law.

Current Law: Engaging in the business of an out-of-state vendor means to sell or deliver tangible personal property or a taxable service for use in the State. This includes (1) permanently or temporarily maintaining, occupying, or using any office; sales or sample room; or distribution, storage, warehouse, or other place for the sale of tangible personal property or a taxable service directly or indirectly through an agent or subsidiary; (2) having an agent, canvasser, representative, salesman, or solicitor operating in the State for the purpose of delivering, selling, or taking orders for tangible personal property or a taxable service; or (3) entering the State on a regular basis to provide service or repair for tangible personal property.

Background: Pursuant to a 1992 U.S. Supreme Court ruling (*Quill Corp. v. North Dakota*), Internet and mail-order retailers are only required to collect sales and use tax from out-of-state customers if the retailer maintained a physical presence (*e.g.*, a store, office, or warehouse) in the customer's home state. In an effort to ensure parity with bricks-and-mortar booksellers, New York passed a law in 2008 providing that affiliate sellers (*e.g.*, independent websites that link to an online retailer's products in return for a commission) were included within the definition of "physical presence," thus requiring out-of-state web retailers to collect sales taxes from buyers in the state if the retailers have New York-based representatives referring businesses to them. This law has been upheld by the Appellate Division of the New York Supreme Court. The U.S. Supreme Court denied a review of the New York court decision in December 2013.

In 2011, California also enacted a law creating nexus through affiliate sales. As a result, Amazon.com ended its affiliate relationships in the state and undertook a campaign to repeal the law by voter referendum. A compromise was later reached under which Amazon.com agreed to build a number of warehouses in the state and begin collecting sales tax on sales in California in September 2012, unless federal legislation addressing the taxation of remote sales was enacted before that point.

A number of other states, including Arkansas, Connecticut, Georgia, Illinois, Minnesota, Missouri, North Carolina, and Rhode Island, have passed legislation similar to legislation passed in New York and California. As a result, Amazon.com and Overstock.com, generally the largest companies affected, have, in some instances, ended their relationships with affiliates in those states in order to avoid a determination that nexus exists.

In 2010, Colorado took a different approach to the online sales tax collection issue. Rather than attempting to define nexus through affiliate relationships, Colorado passed legislation intended to improve enforcement of the state's use tax. The Colorado law requires all vendors who do not collect the sales tax and who have over $100,000 of sales into Colorado in the prior calendar year to provide an annual report to the state listing all customers and purchases for the year. In addition, these remote sellers are obligated to notify their customers that the customers are required to remit use tax on their purchases. The Colorado law is currently under review by the U.S. Supreme Court.

Beginning October 1, 2014, Amazon.com began collecting sales taxes on sales made to Maryland residents. The company is opening a 1.0 million square foot distribution center in Baltimore. The Comptroller's Office estimates that approximately $34.0 million in sales taxes will be collected for sales made by Amazon.com to Maryland residents in fiscal 2015 and $55.0 million in fiscal 2016.

The Comptroller's Office advises that of the 50 largest online retailers in the United States, 38 currently have nexus in the State.

State Fiscal Effect: The bill requires out-of-state retailers making online sales to be licensed by the Comptroller and to collect sales taxes from buyers in the State if the retailers have Maryland-based representatives referring businesses to them. Under an affiliate program, website owners can provide links to products of larger retailers, such as Amazon.com and Overstock.com, in exchange for a commission based on sales produced by customers who "click through" using a link from the affiliates' website.

As a result, sales and use tax revenues may increase significantly beginning in fiscal 2016. The amount of the increase depends on the amount of sales made by online retailers who have affiliate agreements with Maryland businesses. However, to the extent that sellers eliminate relationships with Maryland affiliates, the increase in State revenues will be less. In addition, to the extent the provisions of the bill are challenged in court (as was done in New York), the timing of when revenues begin to be collected will be affected.

Small Business Effect: Some small businesses could be negatively affected if the change in the law results in Internet sellers altering or terminating affiliate agreements with Maryland retailers. Small Maryland retailers that are not affiliated with large Internet sellers may realize increased sales if consumers are not able to avoid the State sales tax by shopping online and therefore have less incentive to make online purchases.

The 2012 Statistics of U.S. Businesses reports that there are 10,447 retail firms in Maryland with 49 or fewer employees. These firms employed approximately 60,800 people and had a total annual payroll of $1.7 billion.

Additional Information

Prior Introductions: As introduced, the Budget Reconciliation and Financing Act of 2012 (SB 152/HB 87) contained provisions similar to the provisions in this bill. The provisions were amended out of the bill for third reading. SB 824 of 2010 and SB 1071 of 2009 received hearings in the Senate Budget and Taxation Committee, but no further action was taken on either bill.

Cross File: None.

Information Source(s): Maryland Chamber of Commerce, Comptroller's Office, Department of Legislative Services

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