

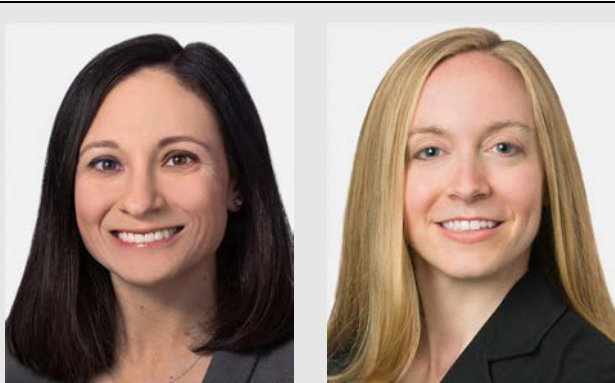
Good Idea Gone Wrong? Evaluating Marketplace Facilitator Laws

by Lauren A. Ferrante and Stefi N. George

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In this inaugural installment of SALT Insights, Ferrante and George examine the value and effectiveness of state marketplace facilitator laws five years after *Wayfair*.

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When the U.S. Supreme Court rocked the state and local tax world in 2018 with *Wayfair*,¹ most states moved quickly to adopt legislation on economic nexus and marketplace facilitators. Almost five years later, economic nexus laws have become commonplace, and most remote sellers have devised methods of complying with varying state thresholds and statutes.

Marketplace facilitator laws, however, continue to pose significant challenges for facilitators, sellers, and state and local

governmental authorities. Are these rules truly necessary? Are they achieving their intended purpose? Or are they merely inappropriately and inefficiently shifting the burden away from the party in the best position to comply? And perhaps the most important question: Who meets the definition of a marketplace facilitator in the first place?

I. What Is a Marketplace Facilitator?

Unfortunately, there is no single definition of a marketplace facilitator because each state has adopted its own rules. Generally, states with a sales or use tax have enacted legislation requiring entities operating a marketplace platform (marketplace facilitators) to collect taxes due on the sales made through their platform by third-party sellers (marketplace sellers) if the marketplace facilitator has nexus in the state. In other words, when a marketplace seller sells through an e-commerce platform, marketplace facilitator rules may shift the burden for sales tax compliance from the marketplace seller to the marketplace facilitator running the platform.²

As a threshold question, though, when does a platform become a marketplace facilitator subject to these laws? While a particular forum may possess some marketplace-like characteristics, not every website offering products for sale constitutes a marketplace facilitator under these statutes.

² In lieu of a tax collection obligation imposed on marketplace facilitators (and because nexus standards were more stringent), states that enacted marketplace platform laws pre-*Wayfair* imposed a notification and reporting obligation requiring marketplaces to report third-party sales to tax authorities and notify customers of their use tax obligation on their purchases. Also, this article focuses on sales made by marketplace sellers through the marketplace facilitator's platform, and not on customer sales directly made by the facilitator.

¹ *South Dakota v. Wayfair Inc.*, 585 U.S. ___, 138 S. Ct. 2080 (2018).

Of course, SALT authorities have sought to broaden the definition of a marketplace, in some cases arguing that even a website merely providing contact information for a seller or a link to purchase products should be required to register as a marketplace facilitator. However, the broader the definition, the less equipped the marketplace facilitator will be to comply with the requirements. As states become more aggressive in defining marketplace facilitators, businesses need to carefully review the details of the sales transaction, including contracts and parties' roles, to determine whether the definition is met in a given state.

This problem is exacerbated in some instances because transactions can have multiple layers of marketplace facilitators. For example, if a business that serves as a marketplace facilitator in some capacity enters into an agreement with another marketplace facilitator to provide customers a product or service that is ancillary to its primary offerings, who bears the burden for sales tax collection? Similar circumstances commonly arise in the travel industry when online travel companies contract with one another to facilitate the same accommodations.³

Marketplace facilitator laws, as constructed, do not address these issues and do not clearly define what falls within these definitions. How is a company expected to manage these ambiguous and overbroad definitions? It is time to reevaluate these definitions and provide more certainty to the marketplace.

II. Are Marketplace Facilitator Rules Necessary?

Another important question to ask is whether these laws are necessary. One of the primary drivers of the enactment of marketplace platform legislation, like that of many tax laws, was, from the tax authority's perspective, to close a tax "loophole" by increasing tax compliance (and, accordingly, collection) with

³ See Niki Ford, "Lodging Intermediary Platforms: Tips for Parsing Their Sales Tax Duties Across the States," Thomson Reuters, Checkpoint Catalyst, Oct. 20, 2022.

administrative efficiency.⁴ At the onset, it was believed that this goal was achievable by targeting the big, popular marketplace facilitators that sell third-party sellers' (in many instances) tangible products.⁵ Pre-*Wayfair*, marketplace platform legislation purportedly would plug the "loophole" by requiring these facilitators — which often had a physical presence in many jurisdictions because of their size — to collect state sales and use tax on sales they facilitated for third-party sellers that lacked sufficient physical presence-type nexus to obligate them to collect tax.

For tax authorities, imposing a tax collection obligation on a new group of actors, especially one that results in a relatively light administrative burden for governments, looked like a winning, straightforward scenario. However, marketplace facilitator laws were introduced at the same time new economic nexus laws swept across the country. With economic nexus rules in place, do we really need to shift the burden to marketplace facilitators? Are marketplace facilitator laws truly and materially aiding in compliance and increasing sales tax collection? The answer remains unclear.

III. Are These Laws Merely Serving to Expand the Base?

Of course, even before the enactment of marketplace facilitator laws and without statutory authority, tax authorities have consistently attempted to expand the tax base to include the value added by facilitators.⁶ Facilitators' value-add is not the object of the customer's desire (e.g., hotel room, food, a ride),

⁴ See, e.g., Charles E. McLure Jr., "Use Tax After *Wayfair*, Part 3: Marketplace Facilitator Legislation," *Tax Notes State*, Feb. 24, 2020, p. 655 ("The marketplace facilitator/provider sales/use tax collection model offers states a highly effective, efficient way to achieve enhanced tax compliance in the rapidly expanding area of marketplace sales. The state registers one marketplace facilitator/provider that will collect and remit sales/use tax on the sales of its many marketplace sellers — without the state needing to deal directly with each marketplace seller." (quoting MTC Uniformity Committee, *Wayfair* Implementation and Marketplace Facilitator Work Group, 2019 White Paper, Dec. 2, 2019, at 9)).

⁵ *Id.* at 657.

⁶ See Jerome R. Hellerstein, Walter Hellerstein, and Andrew Appleby, *State Taxation*, at Part V, Ch. 19, paras. 19.08[6] (updated through Dec. 2022) (analyzing the plethora of online travel company litigation, much of which commenced pre-*Wayfair* and resulted in taxpayer victories, in which taxing agencies argued OTCs should be remitting transaction tax on fees paid by customers, including OTCs' service facilitation fee).

but rather the ease of obtainment and presentation of choices when the customer purchases the item. Is the fee earned for a marketplace facilitator's facilitation of the customer-desired product legally taxable, or does this amount to an impermissible tax on services (which, in most states, are not taxable unless specifically enumerated)? Because many transaction taxes do not explicitly tax these services, a common argument raised by tax authorities is that these services are inseparable from and inextricably linked to what clearly is taxable.

Thus, instead of merely shifting the tax burden and purportedly easing tax administration, marketplace platform laws have been used to grow the tax base, with or without statutory authority.⁷ In this way, the marketplace facilitator laws may be serving a different purpose from the stated intent of tax collection efficiency and instead be stealthily expanding the scope of what is subject to tax.

IV. Are These Laws Shifting the Burden Away From Those in the Best Position to Comply?

What about marketplace platforms that facilitate transactions on behalf of sellers with a physical presence or facilitate the sale of something other than tangible property? Regarding the former, these sellers independently have a tax collection obligation and presumably have long-standing mechanisms in place to continue collecting tax. Regarding the latter, the taxability of sales other than tangible property generally is a more complex and nuanced inquiry than the taxation of a tangible product. Also, if a sale is subject to tax in addition to or other than state sales and use tax, which party has the collection obligation?

One of the principal issues with marketplace facilitators is "information disconnect" — when a marketplace facilitator is deemed to essentially step into the shoes of the true retailer (marketplace seller) but lacks key information in the sole possession of the marketplace seller. For instance, even the taxability of tangible personal

property can be speculative, depending on the purchaser, anticipated use, and other key information. The marketplace seller may possess this information, but often, the marketplace facilitator does not. In addition to unconditional tax exemptions, many exemptions depend on a purchaser's identity (charity) or use (resale). When the product sold is something other than tangible property, the challenges become even more complex.

For nuanced taxability issues, with which marketplace sellers are intimately familiar, the sellers may be in the best position to be the sole decision-maker for reasons of efficiency, and any attempt by marketplace facilitator laws to drive a wedge between the appropriate decision-maker and ultimate decision may risk "leakage" in the form of incorrect tax determinations. Relatedly, for sales of products when taxability is legally ambiguous or questionable (sales of software-related products in some states), while states generally may not hold marketplace facilitators liable on audit if they rely on "incorrect" product information provided by the marketplace sellers, how can information be "incorrect" if the answer to the taxability question is "uncertain" or "it depends"? Some states have workarounds under which the parties can agree to shift the burden back to the marketplace seller, but many states do not.

Another example of "information disconnect" can arise in jurisdictions with destination-based sourcing for local taxes, when the marketplace seller is a local business with a physical location that itself has never before offered delivery service that contracts with a marketplace facilitator to facilitate the delivery of product (e.g., restaurant meals, groceries). Depending on the agreement between the marketplace seller and facilitator, perhaps the seller does not even have access to the delivery location and is unable to calculate the correct tax rate. Or, on the other hand, in origin-sourcing jurisdictions, marketplace facilitators may be obligated to collect tax, even though the marketplace seller has a long-established practice of doing so (in some instances, some facilitators are carved out of the law).

While the above scenarios vary because of the variety of business models and the nonuniformity

⁷ See, e.g., Lauren A. Ferrante, David C. Blum, and Stefi N. George, "Wayfair's Stealthy Creep Continues to Peer-to-Peer Car Sharing," *Tax Notes State*, Jan. 2, 2023, p. 55.

of marketplace platform laws, they all demonstrate the need for businesses, lawmakers, and taxing agencies to embrace flexibility as the inevitable legal and practical kinks are ironed out.

V. Conclusion

Five years after the enactment of marketplace facilitator laws, it is time to review these provisions and consider how they can be improved. Small changes, such as uniformly allowing the parties to shift the burden back to the marketplace seller where appropriate and refining the definitions to clarify exactly who falls within the statutes, would go a long way towards improving the sales tax landscape for e-commerce transactions. ■

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