

## PA Revenue Dept. Pursuing Use Tax on Purchases from Online Retailers and Other Out-of-State Vendors

by Sharon R. Paxton

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The PA Department of Revenue continues to contact businesses with no recent Use Tax reporting history, to encourage participation in the Department's Use Tax Voluntary Compliance program by conducting a self-audit of their books and records. This initiative is intended to recover tax owed by Pennsylvania businesses on taxable items, such as office equipment and supplies, purchased from out-of-state retailers who do not collect Pennsylvania Sales Tax.

The benefits to participation in the Voluntary Compliance Program include a limited look-back period and a waiver of penalties. Voluntary Compliance is available to businesses that are not registered with the Department for Sales and Use Tax purposes and for which no investigations or collection actions have begun. A business can elect to participate in the Voluntary Compliance Program, even if it has not received a notice from the Department of Revenue. Businesses that do not respond to a Use Tax Voluntary Compliance letter received from the Department may face additional tax enforcement measures.

Non-taxed online purchases are of particular concern to the Department and are part of the impetus behind its Voluntary Compliance Program. While estimates vary, Pennsylvania is missing out on hundreds of millions of dollars annually in Use Tax revenue. The Department recognizes, however, that its authority to force many online retailers to collect Pennsylvania tax is limited by court decisions.

Pennsylvania retailers have been frustrated by the Department of Revenue's failure to require various online retailers to collect Pennsylvania Sales Tax. However, in order for a state to impose a tax collection obligation on an out-of-state retailer, such imposition must be authorized by statute and must satisfy certain constitutional requirements. Pennsylvania's Sales and Use Tax statute contains very broad nexus provisions. Nevertheless, online retailers take the position that constitutional requirements prohibit Pennsylvania from imposing a Sales Tax collection obligation on out-of-state retailers with no physical presence in the state.

A detailed explanation of the applicable constitutional requirements is beyond the scope of this article, but the United States Supreme Court has ruled that the Commerce Clause of the U.S. Constitution requires a physical presence in, and a "substantial nexus" with, a state before that state can impose a tax collection obligation. See *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). The physical presence requirement can be satisfied through in-state activities conducted by another on a retailer's behalf, even if those activities are conducted by an independent contractor. See, e.g., *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960). However, a state may not impose a tax collection duty on a vendor whose only connection with customers in that state is by mail or common carrier. See *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967). Many online and mail order retailers have structured their businesses in a way that they maintain avoids the establishment of a physical presence in Pennsylvania and the concomitant obligation to collect tax on sales to Pennsylvania customers.

The McNees State and Local Tax Practice Group provides advice on Use Tax filing and payment obligations, including the identification of taxable and nontaxable purchases, and can assist businesses who would like to participate in the Department's Use Tax Voluntary Compliance Program. The Group also advises retailers concerning sales tax collection obligations and procedures.

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