

Pennsylvania Possibly Joining the Click-Through Nexus Bandwagon

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On October 3, 2011, 26 Pennsylvania House of Representatives members, including two Democratic members of the House Finance Committee, introduced House Bill 14. The bill seeks to incorporate the gamut of recent sales tax nexus trends into Pennsylvania law, including both "click-through" nexus, and affiliate nexus. At the same time, there are some hints that New Jersey may also be considering click-through nexus legislation in the near future.

Pennsylvania Legislation Takes Kitchen Sink Approach

Pennsylvania House Bill 14 includes a number of proposed changes that would expand the scope of nexus with the commonwealth for sales and use tax purposes.

The first proposed change is what is commonly referred to as click-through nexus provision. The bill provides that any person soliciting orders for taxable products through a paid referral from a Pennsylvania independent contractor shall be presumed to have nexus with the state if sales, as a result of such referrals, exceed \$10,000 per year.¹ The referral may be through a link on an Internet website or otherwise.²

Similar to the click-through nexus provisions enacted by Arkansas, California, New York, North Carolina and Rhode Island, Pennsylvania's click-through nexus provision would create a rebuttable presumption of nexus. In other words, the presumption of nexus could be rebutted by proof that the Pennsylvania contractor that was paid for the referrals was not significantly associated with the potential taxpayer's ability to establish or maintain a market in Pennsylvania.³ For purposes of comparison, Connecticut and Illinois' click-through provisions do not include a similar rebuttable presumption.

In addition, House Bill 14 would establish affiliate nexus for all members of a group that are conducting an "integrated business enterprise," provided one member of that group either has a location in Pennsylvania or is soliciting sales of taxable goods or services in Pennsylvania.⁴ In addition, an affiliate, meaning a member of a controlled group of corporations as that term is defined by § 1563(a) of the Internal Revenue Code, could subject a potential taxpayer to nexus in Pennsylvania if the affiliate maintains a place of business in the state and the potential taxpayer: (1) is in a similar line of business as the affiliate, (2) uses the affiliate's Pennsylvania employees or location to promote sales, (3) uses the affiliate's Pennsylvania locations to facilitate delivery of its products or services, (4) uses substantially similar trademarks or trade names to the affiliate in Pennsylvania, or (5) uses the affiliate to deliver, install or provide maintenance in for its customers in Pennsylvania.⁵

Interestingly, this new affiliate nexus standard would be contrary to established Pennsylvania case law, which holds that in-state affiliates do not create nexus for out-of-state affiliates selling into Pennsylvania.⁶

Finally, House Bill 14 includes a use tax notice and reporting requirement similar to the one previously enacted by Colorado. Under this notice requirement, sellers that do not have nexus with Pennsylvania, but that make sales into the state, would be required to provide the purchasers with notice regarding their use tax obligations at the time of sale. At the end of the year, non-nexus sellers would be required to send a form to each Pennsylvania purchaser that made purchases totaling \$500 or more, detailing the items purchased and the amounts paid. A copy of this form would also be required to be submitted to the Pennsylvania Department of Revenue.⁷

House Bill 14 was referred to the House Finance Committee upon introduction, but there has been no further action on the Bill. However, we understand that there is some support for this proposed legislation among House members.

Will New Jersey Also Join the Click-Through Nexus Club?

New Jersey may soon follow Pennsylvania in considering click-through legislation. The New Jersey Retail Merchants Association recently commissioned a study from Rutgers University examining the potential revenue lost by the state as a result of its failure to collect sales and use taxes on Internet-based retail transactions.⁸ The study found that as much as \$171 million was lost in 2009 alone. No official stance has been announced by the New Jersey Division of Taxation; however, in light of the current economic climate and the promise of substantial revenues, some form of click-through nexus legislation proposal appears likely.

However, New Jersey may be able to accomplish a significant expansion in sales tax collection, simply by enacting an affiliate nexus provision. Amazon recently acquired Quidsi, Inc. Quidsi, Inc. is the parent company of a number of online retailers including Diapers.com, Soap.com, Wag.com and YoYo.com.⁹ Quidsi, Inc. is physically headquartered in New Jersey. Thus, enacting an affiliate nexus provision may provide a compromise of sorts for New Jersey, creating nexus for Amazon and its affiliates, without generating all of the controversy that has been associated with click-through nexus legislation.¹⁰ There is precedent for states taking such an approach. For instance, earlier this year, Texas had been considering click-through legislation, but ultimately chose only to enact an affiliate nexus provision.¹¹ The location of a distribution warehouse owned by an Amazon affiliate in Texas was a driving force in the Texas legislature's decision to "make do" with an affiliate nexus provision.

If you have questions about the proposed Pennsylvania legislation or the click-through rumblings in New Jersey, please contact the authors of this article, or the Reed Smith lawyer with whom you usually work. For more information on Reed Smith's Pennsylvania tax practice, visit www.reedsmith.com/patax; for more information on Reed Smith's New Jersey state tax practice, visit www.reedsmith.com/njtax.

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1. H.B. 14, Pa. Session 2011.
2. *Id.*
3. This proof may be in the form of written statements provided by the Pennsylvania residents establishing that they did not engage in any activity in Pennsylvania that was significantly associated with the potential taxpayer's ability to establish or maintain a market in Pennsylvania.
4. H.B. 14, Pa. Session 2011.
5. *Id.*
6. In *Bloomingtondale's By Mail, Ltd. v. Commonwealth*, 567 A.2d 773 (Pa. Commw. 1989) the Commonwealth Court held that Bloomingtondale's brick-and-mortar stores in Pennsylvania did not establish nexus for Bloomingtondale's By Mail, Bloomingtondale's mail-order affiliate.
7. H.B. 14, Pa. Session 2011.
8. Estimates of New Jersey Sales and Use Tax Losses Resulting from E-Commerce, Rutgers Edward J. Bloustein School of Planning and Public Policy, May 2011.
9. Amazon.com, Inc. Form 10-K for the fiscal year ended December 31, 2010. See also www.diapers.com/aboutus/aboutus.aspx.
10. Although Amazon is not the only game in town, with almost \$19 billion dollars in 2010 of net North America sales, it certainly would be an attractive target for New Jersey. Amazon.com, Inc. Form 10-K for the fiscal year ended December 31, 2010.
11. H.B. 1317 and S.B. 1, 82nd Leg., Special Session (Texas 2011).

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