

The background is a complex, abstract digital composition. It features a dark blue base with vibrant, multi-colored lines (red, orange, yellow, green, and purple) that create a sense of depth and movement, resembling a digital cityscape or data visualization. Numerous small, glowing dots in various colors are scattered throughout, adding to the high-tech, futuristic aesthetic.

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# **THE NEW NORMAL: LIVING IN THE TIME AFTER WAYFAIR (A DISCUSSION ON ECONOMIC NEXUS)**

Adam P. Beckerink, Matthew S. Mock, Cosimo A. Zavaglia,  
Justin D. Cupples, and Laura Grace Mezher  
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<b>COVID-19</b>	<b>Global Commerce</b>	<b>Regulating Tech</b>

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# TODAY'S PRESENTERS:



Adam P. Beckerink  
Partner  
Chicago



Cosimo A. Zavaglia  
Partner  
New York



Laura Grace Mezher  
Associate  
Chicago



Matthew S. Mock  
Partner  
Chicago



Justin D. Cupples  
Of Counsel  
Philadelphia

# Agenda

- Recap *Wayfair* Decision
- State of States – Trends & Issues
- COVID-19 State Tax Issues & Implications
- Takeaways



# RECAP *WAYFAIR* DECISION

The background of the slide is a vibrant, abstract digital cityscape. It features several tall, rectangular structures resembling skyscrapers, each composed of a grid of glowing dots in various colors including orange, yellow, pink, and blue. These structures are set against a dark blue background. A network of thin, intersecting lines in similar colors crisscrosses the scene, creating a sense of depth and connectivity. In the foreground, two prominent lines of glowing dots, one pink and one blue, lead the viewer's eye towards the center of the image. The overall aesthetic is high-tech and digital, evoking a sense of data and innovation.

# Recap *Wayfair* Decision

- *South Dakota v. Wayfair* (2018) was a **sales tax** case about physical presence vs economic nexus.
- The US Supreme Court held that physical presence is **not** necessary for sales tax nexus.
- South Dakota's (SD) law defines sales tax nexus as having at least \$100k in annual sales or 200 annual transactions in the state.
- The Court found SD's law to be reasonable, in part, because the thresholds reflected substantial virtual economic contacts with the state.
- "Rejecting the physical presence rule is necessary to ensure that artificial competitive advantages are not created by this Court's precedents."
- "The basic principles of the Court's Commerce Clause jurisprudence are grounded in functional, marketplace dynamics; and States can and should consider those realities in enacting and enforcing their tax laws."

# Recap *Wayfair* Decision – Reading Between the Lines

- The Court spoke broadly about the rationale for affirming an economic nexus statute. Why would its rationale apply any differently to state income tax or gross receipts tax?
- If the Court took a state income tax or gross receipts tax economic nexus case following *Wayfair*, would the Court not use this same rationale?
- The Court said that *Wayfair* satisfied the first prong of the nexus test under *Complete Auto*, which asks whether the tax applies to an activity with a substantial nexus with the taxing state. Taxpayers have always argued that *Complete Auto* applies to the nexus analysis of income and gross receipts taxes too.
- The Court uses examples to illustrate how distortive physical presence nexus is for companies with no physical presence but significant virtual/economic presence. These examples are equally applicable to other tax types.



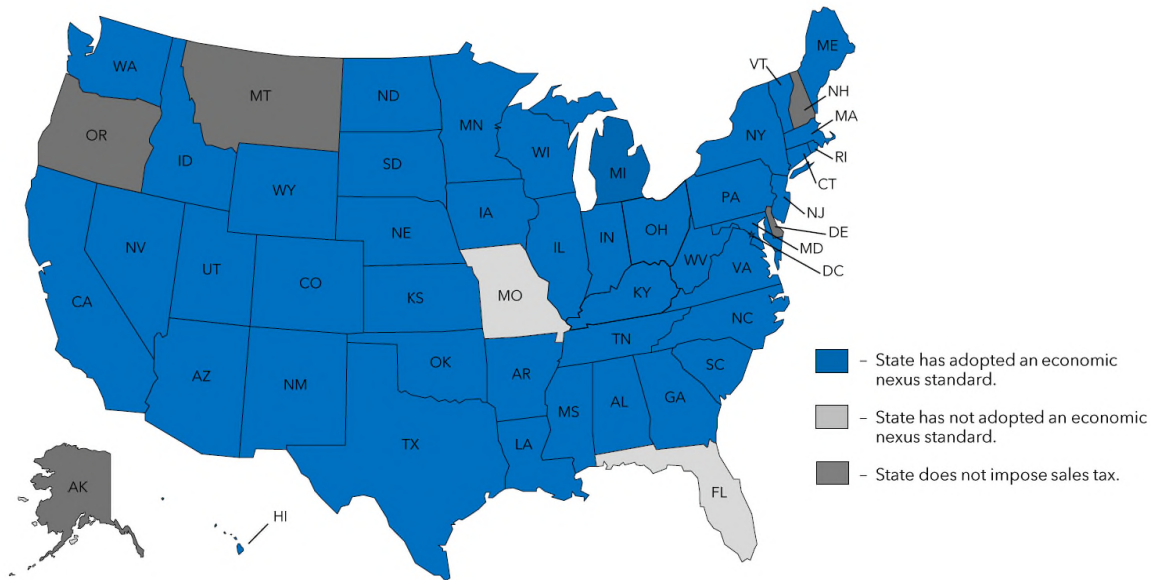
# STATE OF THE STATES – TRENDS & ISSUES





# Sales and Use Tax Economic Nexus Standards & Trends

- Almost every state has adopted economic nexus for its sales and use taxes.
- Common threshold for most states – \$100,000 or 200 transactions.
- Seeing a trend for lower nexus thresholds – e.g., the Kansas DOR has taken the position that there is no minimum sales or transaction threshold. Under this theory, one sale could create nexus. See Kansas Notice 19-04 (Aug. 1, 2019).
- Outlier states like California, Tennessee and Texas have adopted a higher threshold – \$500,000.



Source: Bloomberg Tax, 2019

# Sales and Use Tax Economic Nexus

## Recap: Transition Issues

- Review nexus footprint
  - Physical presence
  - Economic nexus thresholds
- Make taxability determinations
  - Tangible personal property, enumerated services, manufacturing, SaaS, sale for resale, etc.
- Addressing historical exposure
  - Amnesty programs, voluntary disclosure programs
- Filing compliance and initial registration
  - Software solutions, internal controls, etc.
- Consider overall business implications

# Marketplace Facilitator Laws - Intricacies and Pitfalls

- The large majority of states have also enacted marketplace facilitator laws based on new economic nexus thresholds.
- Implementation
  - Retroactivity
  - Start Date
- Definition of Marketplace facilitator – “facilitates sale by ...”
  - 1 prong test
    - Listing or advertising property, ...
  - 2 prong test
    - Listing or advertising property, ..., and
    - Either directly or indirectly through an agreement with a third party ... collecting payment from a purchaser of property
  - Marketplace facilitator “has all the obligations and rights of a vendor”
    - Is a “retailer” for purposes of Sales and Use Tax Act?



# Marketplace Facilitator Laws - Intricacies and Pitfalls

- Sale of the marketplace facilitator or marketplace seller?
  - Nexus Determination/Calculation
  - Collection Obligation
- Contractual Workaround?
- Sales and Use Tax? Local Taxes?
- Notice and Reporting Requirements?
- Registration and Reporting?

# Marketplace Facilitator Laws - Intricacies and Pitfalls

- Tax Base: Marketplace fees taxed?
  - Definition of “gross income” or “gross proceeds of sale”
- Exemption from Collection
- Resale and exemption certificates
- Two Audits
- Sales price?
  - Was tax included – “tax on tax”?

# Corporate Income Tax Economic Nexus Standards & Trends

- In addition to *Wayfair*, during the last decade, several state courts have decided that physical presence is not necessary for a taxpayer to have income tax nexus in the state (e.g. Louisiana – *Geoffrey*; Oklahoma – *Geoffrey*; New Jersey – *Lanco*; North Carolina – *A&F Trademark*; South Carolina – *Geoffrey*).
- Today, many states impose some form of economic nexus for income taxes.
  - Often, a state's economic nexus threshold for income tax purposes is the same or close to the economic nexus threshold for sales/use tax purposes.
  - Trend towards more states adopting economic nexus thresholds for income tax purposes
- Issues
  - Interplay between a state's economic nexus law for income tax purposes and the application of the state's throw out rule (e.g., Illinois)



# COVID-19 STATE TAX ISSUES AND IMPLICATIONS

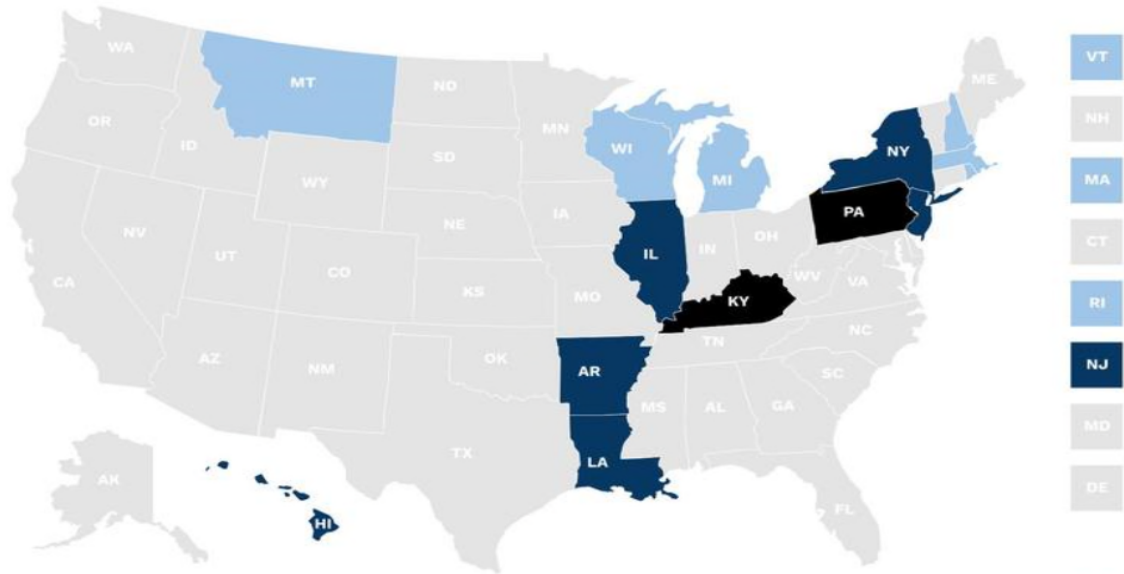


# States Will Be Cash-Strapped due to COVID-19

- All States, without question, will face significant fiscal challenges as a result of the COVID-19 pandemic.
- Multistate Associates predicts that Kentucky and Pennsylvania will be the states most likely to face immediate budget problems. Six states fall in the next highest risk tier: Arkansas, Hawaii, Illinois, Louisiana, New Jersey, and New York.

How likely is each state to have immediate budget issues as a result of COVID-19?

More likely to face immediate budget issues Less likely to face immediate budget issues



Source: MultiState Associates.

# COVID-19: State Payroll Tax Observations

- State Payroll Tax Registration and Filing Concerns
  - State “Work-from-Home” orders inadvertently trigger state payroll tax issues
    - Thresholds requiring state payroll tax registration and filing requirements vary significantly amongst states, and include no specific threshold at all, or specific wage and day thresholds.
      - Many states are easing threshold requirements.
  - Reciprocal Agreements amongst states must be considered – confirm compliance with documentation requirements.
  - Determine “convenience of employer” state implications in CT, DE, NE, NY, and PA.
- Local Wage Tax Implications (e.g., Philadelphia, etc.).
- Action Item: Determine proper telecommuting policies are in place, including documentation, employee work location, and telecommuting policies are in place.



# COVID-19: Non-Payroll State Tax Observations

- Nexus Concerns
  - State “Work-from-Home” orders inadvertently trigger “nexus” with a state for corporate income/franchise tax purposes.
    - Several jurisdictions, including DC, MI, NJ, OR, and PA, have announced via express guidance, or informal statements, that they will ease nexus requirements impacted by employees working from home as a result of COVID-19.
- State Tax Conformity to IRC Changes
- Local Gross Receipts Tax Implications (e.g., San Francisco, Los Angeles, etc.)
- Receipts Factor Sourcing Concerns
  - If employee resides or works in a state that differs from employer’s state, the shifting of employee’s responsibilities to remote locations can impact sourcing of revenues in both states that adopt cost-of-performance and market-based sourcing type regimes.

# Presentation Takeaways

1. Takeaway 1 – Evaluate changing income and sales tax nexus footprint in light of states' economic nexus laws.
2. Takeaway 2 – Understand marketplace facilitator laws.
3. Takeaway 3 – Consider how employees working remotely due to COVID-19 will impact your company's corporate income tax nexus and withholding tax positions, as well as apportionment calculation.
4. Takeaway 4 – Be prepared for states to become more and more aggressive post-pandemic due to fiscal shortages.

# Morgan Lewis Coronavirus/COVID-19 Resources

We have formed a multidisciplinary **Coronavirus/COVID-19 Task Force** to help guide clients through the broad scope of legal issues brought on by this public health challenge.

To help keep you on top of developments as they unfold, we also have launched a resource page on our website at

[www.morganlewis.com/topics/coronavirus-covid-19](http://www.morganlewis.com/topics/coronavirus-covid-19)

If you would like to receive a daily digest of all new updates to the page, please visit the resource page to [subscribe](#) using the purple “Stay Up to Date” button.

# Adam P. Beckerink



**Adam P. Beckerink**

Chicago

T +1.312.324.1495

F +1.312.324.1001

Adam Beckerink represents clients, including multinational corporations and high net-worth individuals, in tax disputes, controversies, and litigation with revenue authorities throughout the United States. His practice spans all aspects of the tax planning and dispute resolution process, including audit, litigation, and appeals in matters including state False Claims Act tax defense, state tax refund class action defense, individual residency, telecommunications excise tax, and sales and income tax.

Connect with me on LinkedIn: [Adam P. Beckerink](#)

# Matthew S. Mock



**Matthew S. Mock**

Chicago

T +1.312.324.1701

F +1.312.324.1001

Matthew S. Mock advises clients on state and local tax litigation and planning, regularly representing them in all stages of state and local tax controversies, including sales tax, income tax, and unclaimed property disputes. Matt is often called on to counsel on audits, protests before state administrative agencies, and appeals to state courts. He also advises multinational companies on the state and local tax aspects of corporate restructurings and transactions.

Connect with me on LinkedIn: [Matthew S. Mock](#)



# Cosimo A. Zavaglia



**Cosimo A. Zavaglia**

New York

T +1.212.309.6646

F +1.212.309.6001

Cosimo A. Zavaglia advises corporations, partnerships, and individuals on state and local tax controversy, planning, and transactional matters. Cosimo routinely represents clients in high-stakes state and local tax audits, appeals, and litigations in matters throughout the United States, including defending clients in state False Claims Act cases and sales and use tax, individual residency, withholding tax, corporate income tax, and real estate transfer tax audits and disputes. He also advises clients on developing state and local tax planning strategies for corporate acquisitions, dispositions, restructurings, and mergers.

Connect with me on LinkedIn: [Cosimo A. Zavaglia](#)

# Justin D. Cupples



**Justin D. Cupples**

Philadelphia

T +1.215.963.4911

F +1.215.963.5001

Justin D. Cupples focuses his practice on providing the highest quality State and Local Tax (SALT) counsel and advocacy to Fortune 500 companies and large multistate organizations. Justin obtains significant state tax savings for his clients by developing and implementing state tax return positions, defending state tax audits, and advocacy through administrative appeals and litigation.

Connect with me on LinkedIn: [Justin D. Cupples](#)

# Laura Grace Mezher



**Laura Grace Mezher**

Chicago

T +1.312.324.1713

F +1.312.324.1001

Laura Grace Mezher advises multinational companies in a wide range of tax planning and controversy issues. In particular, Laura Grace focuses on issues concerning income tax, gross receipts tax, sales and use tax, franchise tax, excise tax, property tax, and unclaimed property matters. Before joining Morgan Lewis, she was an associate in the tax practice group of another global law firm.

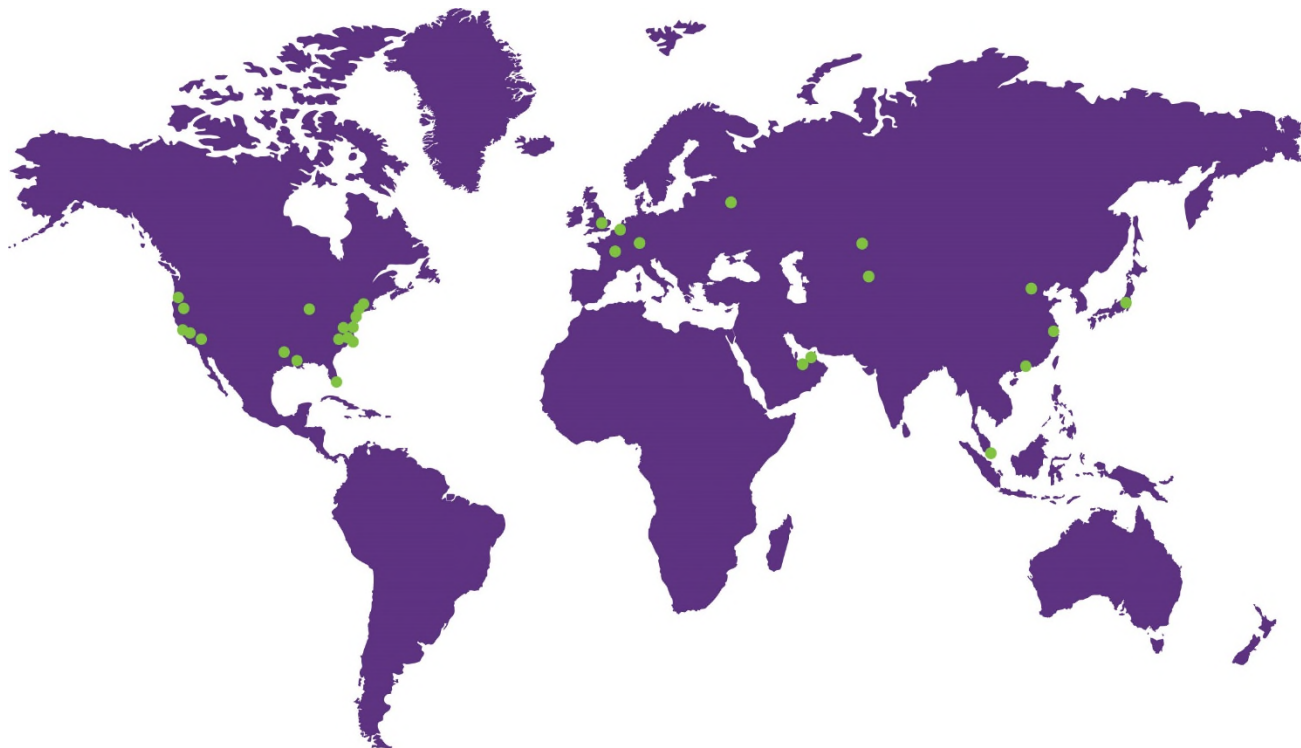
Connect with me on LinkedIn: [Laura Grace Mezher](#)

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