

# Massachusetts to Require Remote Retailers to Collect and Remit Sales Tax

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By



Out-of-state internet vendors will be required to collect and remit state sales and use taxes on sales into Massachusetts beginning July 1, according to the state Department of Revenue.

The sales tax collection requirement under DOR [Directive 17-1](#) would apply to remote retailers with more than \$500,000 in sales into Massachusetts and 100 or more transactional sales delivered into the state within the past 12 months.

The department explained that, unlike other states with similar remote sales tax collection requirements like South Dakota and Alabama, the directive was not designed to challenge the U.S. Supreme Court's decision in *Quill Corp. v. North Dakota*. The DOR said its directive meets the due process and commerce clause requirements the *Quill* Court said are needed for sales tax collection duties to be valid as imposed on remote retailers.

Under the directive, internet vendors' use of in-state software and "cookies," as well as content distribution networks and online marketplaces, constitutes a physical presence in Massachusetts.

"*Quill* recognized that 'title to a few floppy diskettes present in a state might constitute some minimal nexus' but concluded that 'the existence in [a state] of a few floppy diskettes to which [the vendor] holds title' does not result in nexus because it would represent a mere de minimis or 'slightest presence,'" according to the directive. "In contrast, large internet vendors own software that exists on the computers or other devices of all or substantially all of their in-state customers — software that is instrumental in the creation of the vendor's in-state sales. A vendor's in-state software is often the means itself of significant in-state business activity on the part of the vendor, which is also a stark difference from the facts of *Quill*."

The DOR used a similar argument for cookies, saying that "vendors own the proprietary cookies that they place on their customers' computers and devices" and that "ownership and use of these in-state cookies result in in-state business activity by such vendor that distinguishes such vendors from the mail order vendors that were evaluated by *Quill*."

The directive also explained that large internet vendors typically use content distribution network servers, which are "housed in geographically distributed data centers" that are usually close to or within the state. The content distribution networks "perform local activities 'on behalf of the [vendor

that] are significantly associated with the [vendor's] ability to establish and maintain a market' for its sales," according to the directive. "When that activity takes place in Massachusetts it establishes an in-state physical presence on behalf of such vendor."

According to the directive, large internet vendors commonly sell goods through third-party agreements with companies, referred to as online marketplaces, and those agreements include a set of services. "Although the website maintained by the online marketplace on which the vendor's products are sold is 'virtual,' some of the various services provided by the online marketplace in connection with the sale of the vendor's products will be physical in nature," the directive said. And because the "physical services operate to establish and maintain the internet vendor's market, these services, when performed in the state, will result in an in-state physical presence on the part of such vendor," it added.

Those agreements could also provide additional services by the online marketplace, including logistics, order fulfillment, storage, return processing, and order management — and those services, when performed in the state, will result in an in-state physical presence for the retailer, the directive said.

The remote sales tax collection directive is estimated to generate \$30 million for the state in fiscal 2018. That number does not include revenue generated from sales through Amazon.com, which began collecting and remitting the state's 6.25 percent sales and use tax in November 2013, after the online giant [reached](#) an agreement with the state in December 2012.

A DOR spokeswoman told Tax Analysts that the directive will prioritize highly active online retailers that are not already collecting and remitting sales tax in Massachusetts, adding that the move is in line with similar actions taken by other states, including Tennessee, South Dakota, and Alabama, in response to a changing legal landscape.

### Practitioners React

Some tax practitioners found the Massachusetts DOR directive to be surprising, given its interpretation of physical presence, while others labeled it an attack on *Quill*, although different in nature from other states'.

Richard Jones of Sullivan & Worcester told Tax Analysts that while other states have pursued regulations and legislation to generate litigation challenging *Quill*, the Massachusetts DOR justified it through "an extremely broad and creative reinterpretation of what constitutes as physical presence."

"This creativity cannot hide the simple fact that, at the end of the day, the [DOR] is trying to extend its reach to remote sellers, in violation of *Quill*," Jon Maddison of Reed Smith LLP said.

In an emailed statement, Matt Hedstrom of Alston & Bird LLP said the directive “does go to great lengths to explain that it is not directly challenging *Quill*,” but that “the intention is clearly to attack the bright-line physical nexus standard by establishing a bright-line economic nexus rule.”

Whether Directive 17-1 will trigger litigation remains to be seen. Robert Weyman, also of Reed Smith, said that it “depends on how aggressive the department will be with this directive.” Unlike with other states, the Massachusetts directive doesn’t have the “procedural avenues to proactively bring action,” he said, adding that if anything, “many taxpayers [will be] waiting for the department to knock on the door before they challenge this.”

Joseph Henchman of the Tax Foundation said he’d be surprised if the directive didn’t trigger litigation. In an emailed statement, he said the directive gives “Massachusetts the authority to tax every website on the planet and every business associated with it. . . . It was precisely the fear of such a bold and aggressive state claim that led to the Supreme Court ruling as they did in *Quill* in the first place.”

Max Behlke of the National Conference of State Legislatures said it was not surprising to see the DOR’s directive. “In fact, I would find it surprising if no other state Department of Revenue takes similar steps this year,” he told Tax Analysts. “*Quill*’s days are numbered.”

The DOR directive also provides that software is “generally considered to be tangible personal property,” which several tax practitioners said could affect other taxes, including income and personal property taxes.

Jones said he found that to be a “unique argument,” given that the common law definition of tangible personal property is that which can be “seen, weighed, measured, felt, or touched or is in any other way perceptible to the senses.” Jones noted that the statement might have applied years ago when software was transmitted via a tangible medium like floppy disks or CDs, but not today, when most software is electronically transmitted.

“If you added up all the software for Massachusetts customers that came from an out-of-state internet vendor website and combined it all, could you see it? Could you hold it? Could you feel it? I’m thinking the answer is no,” Jones said.

Weyman said the DOR’s “reasoning that tangible personal property is generally understood to include software could create an opportunity for corporate excise tax purposes.”

“In its apportionment regulations, the Department excluded electronically delivered software from the definition of TPP [tangible personal property],” Weyman said. “That interpretation reversed the treatment of software as TPP under the previous version of the regulation and, at least according to this directive, is contrary to the general common law understanding of software as TPP.”

## DOCUMENT ATTRIBUTES

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JURISDICTIONS	MASSACHUSETTS
SUBJECT AREAS	ONLINE SALES TAXATION SALES AND USE TAXATION TAX SYSTEM ADMINISTRATION
AUTHORS	PAIGE JONES
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