

Mass. ATB Rejects Pre-Wayfair Application of Taxation of Out-of-State Seller Under Massachusetts' Internet Vendor Rule

Until the U.S. Supreme Court's June 2018 decision in *South Dakota v. Wayfair*, states could not require out-of-state sellers to collect and remit sales or use tax unless the seller had a physical presence in that state.¹ The *Wayfair* court examined a South Dakota statute that did not require physical presence to establish sales tax nexus and overruled its previous decision in *Quill Corp. v. North Dakota*² that required in-state physical presence for states to require out-of-state vendors to collect and remit sales or use tax.³ The question remained, however, whether states could retroactively tax out-of-state sellers under these regulations for the time between the regulations' implementation and the *Wayfair* decision.

Massachusetts passed and implemented regulations prior to *Wayfair* allowing it to require internet vendors to collect and remit sales tax if their annual internet sales exceeded \$500,000 or 100 or more transactions, so long as the vendor's contacts with Massachusetts included the placement of "cookies" (data files a website transfers to a customer's computer) or mobile applications ("apps") on Massachusetts devices, or the use of third-party content delivery networks ("CDNs") ("the Internet Vendor Rule" or "the Regulation").⁴ On December 7, 2021, the Massachusetts Appellate Tax Board (the "board") issued its findings of fact and report in *U.S. Auto Parts Network Inc. v. Commissioner of Revenue*⁵ that made clear that *Wayfair* cannot be retroactively applied in Massachusetts. Additionally, the board ruled that electronic tools that an out-of-state seller may use do not satisfy the pre-*Wayfair* physical presence requirement for a state to require a remote vendor to collect and remit sales or use.

Background

U.S. Auto Parts Network, Inc. ("U.S. Auto Parts") is a California-based online retailer of automobile parts and accessories with no locations or representatives in Massachusetts.⁶ Its annual Massachusetts sales exceeded the Regulation's thresholds, so the Commissioner of Revenue ("Commissioner") notified U.S. Auto Parts that it was required to collect and remit tax for Massachusetts sales on or after October 1, 2017 under the Regulation and assessed \$60,139.81, including penalties and interest, for its failure to do so.⁷ U.S. Auto Parts' application for abatement was denied.⁸

U.S. Auto Parts appealed to the board and moved for summary judgment.⁹ It asserted that it had no physical presence in Massachusetts under *Quill* and could not be taxed.¹⁰ The Commissioner also moved for summary judgment, arguing that *Wayfair* must be applied retroactively.¹¹ Even if *Wayfair* did not apply and *Quill*

¹ 138 S. Ct. 2080 (2018).

² 504 U.S. 298 (1992).

³ 138 S. Ct. at 2099.

⁴ 830 CMR § 64H.1.7(3).

⁵ *U.S. Auto Parts Network Inc. v. Commissioner of Revenue*, No. C339523, 2021 WL 5930709 (Mass. App. Tax Bd., Dec. 7, 2021).

⁶ *Id.* at *2-3.

⁷ *Id.* at *2.

⁸ *Id.*

⁹ *Id.* at *1.

¹⁰ *Id.*

¹¹ *Id.*

governed, the Commissioner argued that U.S. Auto Parts' electronic contacts with Massachusetts through cookies, apps, or CDNs were sufficient to establish physical presence.¹²

Retroactive Application of *Wayfair*.

The board ruled that *Wayfair* did not retroactively apply in this appeal for three reasons.¹³

First, the board noted that *Wayfair* emphasized the non-retroactivity of the South Dakota statute at issue as a reason it may be constitutional.¹⁴ The Commissioner nevertheless argued for retroactivity by relying on cases where retroactive application of cases was applied to afford relief to taxpayers who had been taxed under unconstitutional schemes.¹⁵ But unlike in those cases, where an unconstitutional tax was avoided through retroactive application, a retroactive application here would expand the state's power to tax out-of-state vendors.¹⁶ The board stressed that “[n]othing” in those cases “supports the notion that a taxing authority may apply a court ruling retroactively against taxpayers who were acting consistently with then-current law.”¹⁷

The board also highlighted that retroactive application would expand the scope of the Regulation beyond what was publicly promulgated and implemented, noting that its text refers to enforcement “to the extent allowed by the ‘physical presence’ ... standard as set forth in *Quill*.”¹⁸

Finally, retroactive application would require U.S. Auto Parts to pay the tax itself instead of collecting it from customers during transactions and remitting it to the state. The board rejected the “fundamental unfairness” that would result.¹⁹

Physical Presence Under *Quill*.

Because *Wayfair* did not retroactively apply, the cookies, mobile apps, and CDNs used by U.S. Auto Parts would have to constitute “physical presence” under *Quill* for the Commissioner to justify its assessment.²⁰ The board, however, pointed to *Wayfair*'s recognition that websites accessible on in-state customers' computers, cookies saved to their hard drives, and mobile apps on their phones did not satisfy *Quill*'s physical presence requirement.²¹ The board concluded that *Wayfair* “leaves no doubt that” these electronic tools do not satisfy *Quill*'s physical presence rule.²²

The board therefore granted U.S. Auto Parts summary judgment and an abatement of the assessed tax.²³

¹² *Id.* at *1, *3-4.

¹³ *Id.* at *4.

¹⁴ *Id.* at *8.

¹⁵ *Id.* at *8-10 (citing *Harper v. Va. Dep't of Taxation*, 509 U.S. 86, 97 (1993); *James B. Beam Distilling Co. v. Georgia*, 501 U.S. 529 (1991)).

¹⁶ *Id.* at *10.

¹⁷ *Id.*

¹⁸ *Id.* at *11 (quoting 830 CMR § 64H.1.7(1)(b)(2)).

¹⁹ *Id.* at *11.

²⁰ *Id.*

²¹ *Id.* at *12 (citing *Wayfair*, 138 S. Ct. 2080, 2094 (2018)).

²² *Id.* at *13.

²³ *Id.*

Conclusion

The Commissioner may appeal this ruling, but no appeal has been filed to date. If this ruling stands, it is unlikely that the Commissioner can apply the current Internet Vendor Rule to require out-of-state companies whose only contacts with Massachusetts are electronic tools like cookies or mobile apps to collect and remit sales or use tax for the periods before the *Wayfair* decision.

Outstanding assessments of tax for this time period likely will not be enforceable. Additionally, some out-of-state companies with only electronic contacts to Massachusetts may be able to claim refunds for tax already collected and remitted for this time period, although it would be required to repay any customer who incurred sales tax on the charges at issue, which may be practically difficult or impossible.²⁴

²⁴ G.L. c. 62C, § 37; 830 CMR 62C.37.1.