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Weighing Wayfair for Nonprofits

By: Tiffany Gourley Carter

Legislative agendas across the country in 2019 are loaded with bills seeking to alter state sales taxes to take advantage of the U.S. Supreme Court's [*South Dakota v. Wayfair*](#) decision. Reversing decades of precedent, the decision makes clear that states have the power to impose taxes on entities beyond their borders, meaning that states that alter their tax laws can [collect sales taxes for online purchases](#) of goods and services from sellers without a physical presence in the state. About half of the states have taken legislative or regulatory action to tap into the billions of dollars in new revenue that the new taxing authority makes available, and new bills are under active consideration in more than a dozen states so far this year.



Analysis by
Tiffany Gourley Carter
Policy Counsel

Charitable nonprofits conducting sales activities out of state via event ticket sales, online marketplaces, online auctions, and more may now find themselves uncertain about whether their own state's sales tax exemptions control, or if they are facing a multitude of additional taxing jurisdictions with endless new registration, calculation, reporting, and payment requirements. These changes may mean that nonprofits, which in the past had to know their own state laws, may need to look beyond their borders lest they fall into the cracks that may form as tax laws develop among the approximately [12,000 taxing jurisdictions](#) in the United States. Conversely, as states craft new laws and systems, policy and advocacy opportunities may present themselves for streamlining processes and expanding exemptions in your state. Regardless, charitable, religious, and philanthropic organizations cannot afford to just sit on the policy sidelines and wait to see what politicians and lobbyists do.

The *Wayfair* decision arose from a [2016 South Dakota law](#) that imposed state sales taxes on internet sales of vendors that made at least 200 transactions with or \$100,000 in sales to residents in the state. South Dakota argued that an *economic* presence test, rather than a *physical* presence test, should be recognized as legally sufficient to extend sales tax liability. The Court, reversing longstanding precedent, ruled that South Dakota's law was a sufficient alternative to the previous- physical presence rule and found that the state statute "did not impose an undue burden on interstate commerce." However, the Court did not identify the factors states must show to establish enough economic presence - leaving states to determine appropriate alternative thresholds when crafting new tax policies. Nor did the Court differentiate between nonprofit corporations and for-profit corporations, sweeping charitable nonprofit organizations into the fray and leaving them subject to the rulings of tens of thousands of distant policymakers and bureaucrats.

Tapping into the *Wayfair* Windfall

More than half the states that have sales taxes have [already adopted or proposed laws](#) that mirror the one in South Dakota, and the remaining states are likely to open their laws this legislative session to tap into the potential [\\$23 billion dollars per year](#) windfall from the newly recognized taxing authority. The *Wayfair* windfall has

already come to fruition for some, as states saw a [\\$847.1 million net increase](#) in sales and use tax receipts according to a recent report by the National Conference of State Legislatures (NCSL). The increase, which was the largest net change among all tax revenues in the report, is “primarily a result of states being authorized to expand their tax bases to include remote sales, which several pursued following the *South Dakota v. Wayfair* decision,” according to NCSL.

Prior to the NCSL report, officials in **Illinois**, **Michigan**, and **New Jersey** estimated that each of their states will generate more than \$100 million in additional sales tax revenues next year and are [accounting for the increased revenues in budget](#) and spending plans. **Arkansas** Governor Hutchinson went so far as to [include projected increased sales tax revenues](#) of \$24 million into his spending plan for the next two years, along with calling for a complete state income tax overhaul that adjusts tax brackets and doubles the standard deduction. In December, lawmakers in [Wisconsin](#) took the opportunity to pass end-of-session legislation clarifying that the *Wayfair* decision triggers changes to the state income tax rate, while making additional tax cuts in the state.

By the end of 2018, [35 states adopted or proposed](#) laws to tax out-of-state sellers while an additional three had other statutes or rules that may have applied to require sellers to collect and remit sales taxes to the foreign state. Many states [have begun collecting taxes](#), claiming they have the authority without needed follow-up or enabling legislation. Several more ([Alabama](#), [Idaho](#), [Nevada](#), [New York](#), [North Carolina](#), [Pennsylvania](#), [South Carolina](#), [West Virginia](#), and [Wyoming](#)) are using regulatory authority in state agencies to start collecting taxes, sometimes despite dubious statutory authority to meet the standards set forth in *Wayfair*. Others states ([Maine](#) and [Texas](#)) issued other guidance for registration and collection procedures. [Colorado](#) officials attempted to [rush the collection without proper procedure](#), and ultimately decided to delay collection due to its [complex tax system and policy](#).

Predictions started early that [every state without a sales tax](#) would jump into the legislative fray in 2019. At least 26 bills in 13 states are currently pending in state legislatures this year to reconsider, officially adopt, or clarify standards further, and more are expected as sessions continue. The bills take numerous approaches: codifying the regulatory actions currently underway; adjusting thresholds for imposition of tax collection remittance; and clarifying definitions and terminology for what types of entities are subject to the new taxes.

Five states do not have sales taxes and their policymakers are proposing solutions to reduce the impact of the *Wayfair* decision on their taxpayers. Legislators in one of those five, **New Hampshire**, have introduced bills that would [shield residents from other states'](#) sales or use taxes unless mandated by an act in Congress and [prohibiting the state from enforcing](#) or agreeing to other state's collections. In Congress, New Hampshire Senators, along with Senators from **Montana** and **Oregon** – all states without a sales tax – have introduced legislation ([S. 128](#)) to essentially overturn the Supreme Court's *Wayfair* decision. Another recently introduced bill in the U.S. House of Representatives ([H.R. 379](#)) would limit states from collecting taxes or fees from sellers outside their states. The bill requires the collecting state to have a single tax rate and collection point as well as provides protections for purchaser information.

Some states authorize municipalities to set and impose various sales and use taxes, further complicating the matter as those [localities also look to grow their tax revenues](#). Colorado has [more than 300 taxing authorities](#), and Louisiana [has nearly 200](#). A commission in **Louisiana** [drafted a possible tax return](#) for retailers that, if adopted, would have alleviated some of these complex jurisdictional burdens for remote retailers by allowing them to collect and remit a combined state and local flat rate. However, the commission [postponed the rollout](#) of the return until a matrix of taxes was created. Similarly, localities in [Texas](#) may differ on sales and use taxes, and a newly introduced bill there would permit [remote sellers to pay a single use tax](#) based on an estimated average. Meanwhile, the Texas Comptroller is looking to [expand collections to the state franchise tax](#) as well.

State legislatures and executive agencies are not the only places where sales tax decisions are being made; there's also the ballot box. [Arizona](#) voters approved a ballot measure last year that restricts the state or any localities from imposing any new or increasing any existing fee, assessment, or tax on any service, thus limiting sales taxes to goods. A local ballot measure in **San Francisco** imposing a tax on gross receipts from cannabis business had an additional [less-publicized provision that expanded economic nexus](#) for the locality's gross receipts tax. Voters in the city passed [Proposition D](#) in November 2018 and applied the gross receipts tax to all sellers with more than \$500,000 in annual gross receipts in the city, regardless of physical presence. The approval of the measure removes ten conditions businesses previously had to meet to be taxed in the city.

Nine states have [no existing out-of-state tax on sellers](#). Seven states have [no personal income tax](#), which makes them heavily reliant on sales tax revenues, thus incentivizing them to impose sales tax collections from out-of-state sellers as soon as possible. See analysis by [National Conference of State Legislatures](#).

A federal fix was offered last year to address many of the conflicting tax implications of the *Wayfair* decision, but so far a federal approach faces opposition from the states. The [National Conference of State Legislatures](#) opposed the federal [Online Sales Simplicity and Small Business Relief Act](#), which would have required the states to develop, and Congress to approve, an interstate compact governing sales by small businesses with less than \$10 million in gross annual receipts and delay implementation of any tax on out-of-state sellers until January 1, 2019. NCSL claimed the bill was “an unwarranted intrusion on state authority, which, if enacted, would continue the competitive advantage online sellers enjoy over Main Street sellers.”

The governing board of the [Streamlined Sales and Use Tax Agreement](#) (SSUTA), of which 24 states are members, is [not advocating for federal legislation](#), but is urging that the states work it out. The SSUTA provides for a [central collection and registration agency](#), as well as free software for vendors to help with compliance.

The Multistate Tax Commission, an intergovernmental tax agency of states that works on tax administration, has been meeting to [discuss uniformity and consistency](#) among the states, particularly [among marketplace providers](#) like Amazon and eBay. The proposals may affect 501(c)(3) organizations that sell or purchase supplies online from out of state.

Nonprofits and Sales Taxes

States vary on laws exempting nonprofits from paying sales tax on purchases exclusively for charitable purposes. More than half of the states (26) give broad sales tax exemptions for purchases by nonprofits, and an additional 15 states allow limited exemptions by certain types of nonprofits or specific organizations. **South Carolina** and **Washington State** have no exemptions for nonprofits making purchases. In [Hawai'i](#), certain nonprofits are exempt from the general excise tax, but are still subject to the tax when it comes to fundraising revenues, even if the income is ultimately used in furtherance of exempt activities.

A different set of rules apply when nonprofits are the seller of goods or services. Twenty-eight states allow limited exemptions for certain nonprofits, types of items, price of items under a threshold amount, number of days per year, and proceeds from sales. Eight states have broad exemptions for nonprofit sales, and another eight states have no general exemptions.

Nonprofits may now be subject to additional registration requirements and compliance issues for each state in which they conduct business. This varies for nonprofits as sellers that may now need to collect and remit sales and use taxes if they meet the various thresholds in the state. Nonprofits as purchasers that have exemption certificates would generally remain exempt under post-*Wayfair* taxing mandates, but they need to track legislative and regulatory changes.

Risks for Nonprofits

The *Wayfair* decision provides a big incentive for states to open up their sales tax laws to reap the financial windfall, estimated at \$23 billion per year. Legislatures making changes to their tax codes can – whether intentionally or inadvertently – impose taxes on previously exempt nonprofits. In 2018, prior to the *Wayfair* decision, the **Kentucky** Legislature enacted a [comprehensive tax reform package](#) that extended the six-percent sales tax to fundraising special events, silent auction items, and some types of memberships, such as recreational memberships. The end-of-session policy change and unintended consequences resulted in “a great deal of anxiety and frustration from all levels” by nonprofits, according to Danielle Clore, Executive Director of the [Kentucky Nonprofit Network](#). KNN took the lead on [educating nonprofits on the issue](#) and immediately set to work correcting the problem with the Legislature.

Uncertainty and Unanswered Questions

The question remains of when collection and remittance of sales tax by a state is triggered. Many states have chosen to follow the thresholds set under the *Wayfair* decision; others have passed or are considering legislation with higher sales amounts or a lower number of transactions. The amount of \$100,000 in sales and 200 transactions may be reasonable thresholds in South Dakota, a low-population state. Remote sellers will likely find it much easier to avoid exceeding those thresholds there, but be [triggered in a more populous state](#) such as [California](#) and

[New York](#). Further, each state may define “transaction” differently, and the minutiae of what qualifies for a portion of a transaction as it pertains to nonprofit sales could differ.

In many and varied circumstances, charitable nonprofits may be at risk of wading into unknown collection and remittance challenges, as well as registration and compliance issues. Challenges can arise after *Wayfair* for nonprofits with ties to buyers of goods in a separate state. Situations like a founder who moves to another state or a state with a population that specifically benefits from the services of a nonprofit located in a different state both raise questions that must be analyzed. For example, purchases by remote buyers of admission tickets to an event or sales for a specific item can rack up quickly. Nonprofits must be aware of whether and how much of the price of a gala ticket may constitute a sale (when differentiated from the donation portion of the ticket) or how many auction items are sold in a single state to count as a transaction. The determinations are daunting and unknown at this stage. Charitable nonprofits should take the opportunity now to have some of this information clarified by state agencies and government officials. It would be to the benefit of all nonprofits to ask.

During a procedural hearing on rulemaking concerning *Wayfair*, the [Colorado Nonprofit Association](#) recently took advantage of the opportunity to position itself, other nonprofits in the state, and out-of-state nonprofits more favorably. It did so by recommending clarifications and changes to the application of Colorado’s sales tax exemption to out-of-state retailers with substantial nexus to the state. The state association of nonprofits also urged delaying implementation of new sales-tax rules; ensuring that charitable donations are exempt from sales tax; clarifying the definition of “transaction”; imposing minimal compliance costs; and finding ways to reduce the burdens caused by trying to comply with the hundreds of taxing jurisdictions within the state. The testimony reflects a concern on behalf of all nonprofits, both those inside or outside the state, that may be affected by the proposed regulations.

Stepping into the future, especially one fraught with change, can be frightening. But the opportunity of shaping that future when the change is expected should be welcomed. This time, however, charitable nonprofits must directly take on this challenge together to protect themselves and others across the nation now potentially subject to other states’ laws.