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SC Court of Appeals

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT
Ralph King Anderson, III, Chief Administrative Law Judge

Appellate Case No. 2019-001706

Trial Court Case No. 17-ALJ-17-0238-CC

Amazon Services, LLC, Appellant,

v.

South Carolina Department of Revenue, Respondent.

CORRECTED BRIEF OF *AMICUS CURIAE* NATIONAL RETAIL FEDERATION

Jennifer B. Routh (SC Bar No. 101349)
McDermott Will & Emery
500 North Capitol St., N.W.
Washington, D.C. 20001
(202) 756-8165

Attorney for National Retail Federation

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I. INTEREST OF AMICUS CURIAE

The National Retail Federation (NRF), conditionally submits, upon motion to this Court, this brief as *amicus curiae* in support of Appellant, Amazon Services, LLC, to address and ultimately reverse the ruling of the Administrative Law Court (ALC) in *Amazon Services, LLC v. South Carolina Department of Revenue*. As an organization dedicated to representing the retail industry, the NRF is able to offer unique perspectives and insights regarding the adverse impact of the ALC’s decision on the broader retail community. This brief addresses matters of fact or law that might otherwise escape the Court’s attention and *amicus* has a substantial, legitimate interest in the outcome of the case.

The NRF is the world’s largest retail trade association, representing discount and department stores, home goods and specialty stores, Main Street merchants, grocers, wholesalers, chain restaurants, and internet retailers from the United States and more than 45 countries. Retail is the largest private-sector employer in the United States, supporting one in four U.S. jobs—approximately 52 million American workers—and contributing \$3.9 trillion to the annual GDP. Most retailers are small businesses – 90.8% of retail firms have fewer than 10 employees.

The retail industry directly employs 519,000 workers in South Carolina, a workforce that is double the next largest industry. The jobs supported by retail comprise 27.9% of the total jobs in the State. 20% of South Carolina’s labor income is supported by the retail industry and 20.2% of South Carolina’s GDP is supported by the retail industry. The NRF periodically submits *amicus curiae* briefs in cases raising significant legal issues impacting the retail community, and advocates for issues that affect retailers and their customers.

II. INTRODUCTION AND SUMMARY OF ARGUMENT

As the Appellant has explained to this Court, this case addresses whether South Carolina could, prior to passage of new legislation in 2019, deem Appellant Amazon Services LLC

(“Amazon Services”) the seller of products offered and sold in the Amazon.com marketplace by independent third parties resulting in a sales tax collection obligation and liability. The NRF herein explains the inevitable disruption, cost, and uncertainty the industry will experience should this Court uphold the Department of Revenue’s aggressive and retroactive application of a new and novel sales tax collection obligation. The NRF and its members’ concern is not just the application of the specific tax collection issue in this case; the issue of concern is that if aggressive and retroactive application is allowed in this instance, it will be imposed in other sales tax issues as well. Upholding the Department’s aggressive and retroactive application of a new and novel sales tax collection obligation means retailers, both large and small, will never have certainty over their financial obligations. It means retailers must spend time attempting to read a future Tax Director’s mind as to what additional obligations might be retroactively imposed. It means a liability that economically belongs to the customer becomes the liability of the retailer through the malleable nature of the South Carolina tax code. All of these results are financially untenable for any retailer, and perhaps risk bankrupting some.

III. ARGUMENT

A. Summary Of The Aggressive And Retroactive Tax Obligation Approved By The Administrative Law Court

South Carolina historically imposed sales and use tax¹ liability through a collection obligation on the retailer or seller making a sale to a customer. S.C. Code Ann. §§ 12-36-70(1)(a); 12-36-910(A); 12-36-1310; 12-36-1350(A). This was true even if the retailer made sales through a marketplace because the concept of a marketplace was not found anywhere in the sales tax statutes until 2019. As Appellant notes, there was ample evidence from both the

¹ For simplicity purposes, this brief will use the term “sales tax” hereafter to refer to both the sales tax and the use tax.

Legislature and the Department itself that the pre-2019 statute did not include a marketplace tax collection obligation.² A retailer selling on a marketplace was required to collect (if it had sufficient nexus) and the consumer retained the ultimate use tax liability for any unpaid sales tax. But in 2016³ the Department decided, with no change in the underlying statutes, to impose the tax collection obligation – and liability – also on a marketplace. To be clear – the Department decided that Appellant was not **just** subject to sales tax liability for sales beginning in 2016 when the Department first decided to create this interpretation; Appellant was subject to sales tax collection liability on sales that had already occurred. The Department reached this new position by re-interpreting the sales tax statutes, including the statute that defines “seller.” The ALC upheld the Department’s position by creating new concepts not found in the statute, such as the focus on the “point of sale” concept.⁴ The problems with the Department’s new interpretation are legion but for the retail industry as a whole, the aggressiveness of the interpretation of the law and the retroactive application of a new tax collection rule can be devastating.

B. Aggressive And Retroactive Interpretations Of Sales Tax Liability Are Financially Disruptive To The Industry.

At issue in the case is whether the Department can aggressively reinterpret a long-standing sales tax law and then apply the new interpretation retroactively to commercial activity that happened in the past. Prior to the Department’s audit and assessment of Appellant, the third-party sellers and their customers were the persons subject to the sales tax liability. The apparent impetus for the Department’s imposition of the tax liability on the Appellant is the Department’s inability to impose the tax collection obligation on third-party sellers without nexus with the

² Initial Brief of Appellant, Amazon Services LLC, pp. 2-3; 17 – 20; 39-44.

³ The marketplace fact pattern existed for 15 years prior to the Department’s change in opinion and may be one of the most written about developments in retail.

⁴ *Amazon Servs., LLC v. South Carolina Department of Revenue*, No. ALJ-17-0238-CC, 2019 WL 4391561, at pp 24 - 27 (S.C. Admin. L. Ct. Sept. 10, 2019).

State and the impracticality of directly auditing and assessing individual purchasers. The NRF has been at the forefront of advocating for solutions to the sales tax collection challenges states encountered as a result of historic constitutional nexus restrictions. Amicus’ members have long argued for a level sales tax collection playing field as between traditional brick and mortar retailers and online sellers because, if a state has the authority to require traditional retailers to collect and remit sales taxes, that authority should extend to all retailers – regardless of whether those retailers have a physical presence in the state. However, any changes in sales tax authority should be communicated clearly and uniformly in a way that provides adequate notice of any new collection and remittance responsibilities. *See* Jerome R. Hellerstein & Walter Swain, *State Taxation*, ¶ 19A.07[3] (Thomson Reuters/Tax & Accounting, 3rd ed. 2001, with updates through November 2020) (online version accessed on Checkpoint (www.checkpoint.riag.com) January 21, 2021) (“Sellers need advance notice of changes in tax base, tax rate, and boundaries of local taxing jurisdictions in order to adjust their tax collection systems and procedures”).

If this Court allows the Department to bypass the state legislature and impose new interpretations of settled terms in this case, the Department will have judicial authority to retroactively reinterpret other statutory terms related to retailers’ sales tax collection obligations. Amicus’ members believe – as apparently do the South Carolina legislators⁵ – that the proper approach to implementing sales tax liability and collection requirements is for the legislature to adopt clear, comprehensive, uniform, and prospective legislation, as outlined in *Wayfair* and as other states have done. *See S. Dakota v. Wayfair, Inc.*, 585 U.S. ___, 138 S.Ct. 2080 (2018); *see, e.g.*, Ga. Code Ann. § 48-8-30(c.2) (enacted by 2020 Georgia Laws Act 322 (H.B. 276), effective April 1, 2020 and applicable to all sales occurring on or after April 1, 2020); Miss. Code. Ann.

⁵ 2019 South Carolina Laws Act 21 (S.214) (eff. April 26, 2019) (amending S.C. Code Ann. §§ 12-36-70, 90, 130 and 1340 and creating S.C. Code Ann. § 12-36-71).

§§ 27-65-7, 9 (amended by 2020 Miss. Laws H.B. 379, effective and in force from and after July 1, 2020); N.C. Gen. Stat. Ann. § 105-164.4J (enacted by 2019 North Carolina Laws S.L. 2019-246 (S.B. 557), Sec. 4, effective February 1, 2020 and applicable to sales occurring on or after that date); Tenn. Code Ann. § 67-6-501(f) (enacted by 2020 Tennessee Laws Pub. Ch. 646 (S.B. 2182), effective October 1, 2020); Va. Code Ann. § 58.1-612.1 (enacted by 2019 Virginia Laws Ch. 815 (H.B. 1722), which is not applicable to any retail sales transactions occurring before July 1, 2019); *see also* National Conference of State Legislatures Executive Committee Task Force on State and Local Taxation, *Marketplace Facilitator Sales Tax Collection Model Legislation*, § 3 (“No obligation to collect the sales and use tax required by this Act may be applied retroactively”) (unanimously approved Nov. 22, 2019), available at https://www.ncsl.org/Portals/1/Documents/Taskforces/SALT_Model_Marketplace_Facilitator_Legislation.pdf?ver=2020-01-30-122035-320×tamp=1580412048938. All jurisdictions that are enforcing marketplace collection obligations are doing so through specific marketplace legislative authority. The few jurisdictions that initially attempted to enforce a marketplace collection obligation in the absence of specific legislative authority either quietly gave up or lost in a judicial challenge. *See Normand v. Wal-Mart.com USA, LLC*, No. 2019-C-00263, 2020 WL 499760 (La. Jan. 29, 2020).

At its heart, this case is not just a marketplace issue – every retailer subject to South Carolina sales tax liability and tax collection obligations could suffer if this Court upholds the type of aggressive and retroactive rulemaking by audit underlying this case. The Department could target any element of the sales tax statutes, such as an exemption or the tax base calculation, and reinterpret the statute to expand liability. As a result, any retailer, whether selling taxable or non-taxable items, could be in the same position as Appellant with a surprise,

retroactive liability. This result is particularly destructive because a retroactive change deprives such retailers of the opportunity to collect the tax from consumers.

The risk to the retail industry can be demonstrated by a postulated example of a retailer selling an innovative service that is not an enumerated service subject to sales tax. The service is popular and it receives significant press coverage. The press coverage and public policy consultants routinely suggest the Legislature should impose a tax on the service because the state is losing revenue as customers shift from consuming historically taxable services to purchasing the new, nontaxable service. Nevertheless, the Legislature fails to act for years after the service was first offered for sale, keeping in place the existing legislation omitting the service from the list of taxable. Consistent with the statutory exclusion of the service from the inventory of taxable services and the Department's apparent acceptance of this omission, the retailer sells these services and does not collect a tax as none is lawfully imposed. Years after the service is created and begins to be sold, the Department determines this service is taxable and has always been taxable by reimagining the words of the statute. With no change in the underlying statute, the Department assesses the retailer for tax on its historic sales based on the new, retroactive interpretation. If the law clearly taxed the services at the time the sales were made, the retailer would have collected tax from its customers. But collection from customers is not possible when the Department decides years later the service should have been taxed. As a result, the retailer shoulders the financial burden of a tax that should have been paid by others. Given the slim operating margins in the retail industry, this retroactive imposition of tax could put retailers selling the service at issue out of business.

The retroactive application of aggressive interpretations of sales tax liability laws is particularly insidious because of the risk of double or triple taxation. For example, a small

business may buy a non-taxable item from a third-party retailer on an online marketplace. Subsequent to that sale, the State re-characterizes the product as subject to tax. The small business buying the product is audited and pays the tax. The retailer selling the product is separately audited and pays the tax. The marketplace providing the forum for selling and purchasing the product is also separately audited and pays the tax. Thus, the State has received the tax three times for the same transaction solely because it created a new interpretation that could not have been anticipated by any of the parties and applied that interpretation retroactively. While this may not be a common result, the fact that this is a plausible example demonstrates the inappropriateness of aggressively reinterpreting tax collection obligations retroactively.

Another problem with the Department's and the ALC's approach is that the Department not only retroactively re-characterized the law, it also retroactively re-characterized the facts of transaction. The Department and the ALC concluded that Amazon Services made sales to consumers purchasing the products from the third-party sellers. But the evidence clearly shows the transaction was Amazon Services selling services to the third-party sellers.⁶ Thus, if this Court upholds the ALC's decision and the Department's actions, retailers are not just at risk of a change of interpretation of statute imposed retroactively; retailers are also faced with the daunting proposition that the Department may disregard taxpayers' valid contractual relationships. This is an impossible environment in which to run a business.

The solution to this problem is not to suggest that retailers accept and comply with the broadest sales tax imposition possible. First, retailers will not be able to anticipate just how broad an interpretation could possibly be applied by the Department. Second, broad interpretations risk angry customers who do not understand why tax is due (and discuss this in internet forums,

⁶*Amazon Servs., LLC v. South Carolina Dep't of Revenue*, 2019 WL 4391561, at pp 2 - 9.

spreading the resentment against the innocent retailer). Finally, sales tax laws are too complex to find an optimum point at which retailers can apply some hypothetical broad interpretation of taxability to every product, every transaction, every potential use and every customer to anticipate potential retroactive expansion of the law by the Department. There should be clear statutes and timely administrative guidance so retailers can collect the tax due from the customer at the time the transaction occurs. Thus, the solution is for this Court to corral aggressive interpretations applied by the Department retroactively to relieve retailers of this Odyssean predicament.

C. Both Small And Large Businesses Are At Risk Of Financial Disruption If The ALC's Decision Is Upheld.

As stated previously, the vast majority of retail firms, who have the responsibility of *collecting* sales tax under South Carolina's statutes and the statutes of other states imposing sales taxes, are small businesses. These small retail firms rarely have an experienced tax professional on staff to assist with implementing tax rules. Smaller businesses often rely on tax preparation software, especially with respect to sales taxes. These software products cannot possibly anticipate a retroactive interpretation of the tax law. Yet based on the Department's and the ALC's approach here, even these small retailers must find the means to read the minds of future Tax Directors and if they fail to do this, absorb the retroactive tax.

Most retailers operate on slim operating margins. For smaller retailers that cannot take advantage of economies of scale, the margins are even slimmer.⁷ These businesses do not have the financial wherewithal to pay a tax liability that they had no idea existed at the time that they sold an item because of a retroactive interpretation of sales tax laws.

⁷ While there is no specific data regarding the margins of small retailers, general retail firms average a net margin of 2.79%. New York Univ. Stern School of Business, *Margins by Sector*, http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/margin.html (last visited 1/29/2021).

To be clear, the retroactivity issue is not just a small business issue. Larger retailers frequently have a more complex product mix and varied customer base, thus providing more opportunities for a retroactive application of a taxability or exemption change to disrupt their businesses. Furthermore, many large retailers have the same slim margin issues as small companies.

The implications of a decision of this Court to uphold the Department's authority to aggressively reinterpret and retroactively change sales tax collection rules imposes a financial burden on the retail industry that could not have been anticipated. While it is unfair to impose a retroactive tax burden at any time, it is particularly devastating to impose this burden on the retail industry at this time. Retailers are at particular risk of economic devastation today as a result of the pandemic.⁸ These businesses should not also be subject to the fear and risk that the Department will seek to raise money by reinterpreting some element of sales tax obligations retroactively. The Department could do this by narrowing exemptions or by expanding the definition of taxable services. While all taxpayers are presumed to know their tax obligations, retailers tasked with the responsibility should not be expected to anticipate an interpretation for which there is no clear statutory or administrative guidance. It may seem fanciful to suggest the Department would just reinterpret a statute to retroactively require a tax collection obligation when there was none originally, but since this is what happened to Appellant, it could happen again unless this Court prevents it.

⁸ Due to the pandemic and other systemic factors, almost 6000 more stores closed in 2020 than in 2019. Walter Loeb, *More Than 15,500 Stores Are Closing In 2020 So Far – A Number That Will Surely Rise*, Forbes.com (July 6, 2020) <https://www.forbes.com/sites/walterloeb/2020/07/06/9274-stores-are-closing-in-2020--its-the-pandemic-and-high-debt--more-will-close/?sh=b5a2821729fd>.

D. Retroactive Application Unfairly Shifts The Economic Burden From The Consumer To The Seller In Contravention Of South Carolina's Tax System.

A final important and fundamental element of the sales tax collection liability rules that magnifies the harshness of the Department's aggressive and retroactive reinterpretation of the statutes relates to where the economic obligation for sales tax lies. The sales tax is not, primarily, an economic obligation of the retailer. While the retailer has the legal obligation to remit the tax to the State, the retailer collects this tax from the consumer. Thus, in a properly functioning sales tax system, the retailer does not have an economic tax liability from the transaction. It is only if the retailer fails to collect a lawfully owed sales tax from the customer that the State can hold the retailer liable for the tax. But, if the retailer does not have sufficient information to know that the tax is due and that it must collect it, the retailer will obviously not collect the tax. Any retroactive creation of an aggressive sales tax interpretation creates liability for the retailer where there should have been none. Thus, allowing aggressive retroactive interpretation of sales tax statutes not only creates new tax liability, it also shifts the person on which the economic liability is imposed. This result is contrary to the South Carolina statutes, which clearly intend the economic cost of the tax to be on the ultimate consumer.

IV. CONCLUSION

For the reasons stated, and for the reasons stated by Petitioner, this Court should reverse the judgment of the Administrative Law Court.

Respectfully submitted,



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Jennifer B. Routh (SC Bar No. 101349)
McDermott Will & Emery
500 North Capitol St., N.W.
Washington, D.C. 20001
(202) 756-8165

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