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A Bridge Too Far: Could NC's "Amazon" Sales Tax Nexus Legislation Collapse Under Its Own Weight (And Bring Other Tax Nexus Principles Down With It)?

North Carolina's new budget bill enacted several broad tax measures, including a version of the "Amazon" sales tax nexus approach. Similar measures were considered by several state legislatures this year, but were ultimately passed only in New York and Rhode Island. The new measures are subject to a laundry list of legal and constitutional criticisms, the details of which are beyond the scope of this Client Alert. However, of the three states that passed such legislation, North Carolina's statutes may be the most vulnerable to attack. Additionally, North Carolina Department of Revenue audit officials have recently taken the surprising stance that *the law will be imposed retroactively*.

Traditional Sales Tax Nexus, and Retroactive Audits. "Nexus" refers to a state's jurisdictional ability to tax an out-of-state business. "Amazon-style" nexus has been so-called because the jurisdiction to tax an out-of-state company, such as an e-commerce company, is not based upon what the remote *e-tailer* is doing within the taxing state. Instead, it is based upon sales "solicitation" activities conducted by its in-state, *independent sales referral sources* within the taxing state; this has also been called "attributional nexus." This nexus approach threatens "affiliate," "agent," "representative," and similar programs across all retail industry categories. **The state is already auditing businesses – even businesses that discontinued their local referral programs prior to the effective date of the new law.** The Department reasons that the "new" law is merely a "clarification" of older state statutory and constitutional authority that has long been "on the books"; this reasoning may ultimately wind up jeopardizing the Department's assertion of sales tax nexus.

The "New" Nexus Test. Under North Carolina's new legislation, a "remote" (non-North Carolina) business is presumed to have sales tax nexus with North Carolina – and therefore to be responsible for North Carolina sales taxes on its sales to North Carolina customers – if it:

- Has any representatives – including true third party independent contractors, as well as affiliates, that:
 - are located within North Carolina; and
 - solicit sales leads for the "remote" business (including merely by website); and
 - are compensated by the "remote" business for the referrals; AND

- Has total sales to North Carolina purchasers arising from these referrals which exceed \$10,000 for the preceding four quarters. (Though the law is ambiguous as to whether this means \$10,000 for *each* quarter, so far state tax officials are interpreting it as requiring only \$10,000 in total for the prior four quarters).

Attempting to Counter the New Nexus Presumption. The presumption is particularly daunting for two reasons. First, once it attaches, it risks subjecting the “remote” business to sales tax liability for a potentially unlimited number of prior years, because (at least in theory), non-filers are not protected by any statute of limitations. Second, taxpayers may find themselves at a loss on how to rebut (that is, counter) the presumption. The law “clarifies” that the nexus presumption may be rebutted by proving that the in-state representative(s) “did not engage in any solicitation” in North Carolina “that would satisfy the nexus requirement of the U.S. Constitution during the four quarterly periods in question.” The law suggests that mere advertising will not be enough to trigger sales tax nexus, but offers no additional guidance.

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