

## Click Here for Nexus?: What You Need to Know about Pennsylvania's New Click-Through and Affiliate Nexus Guidance

Author: [Lee A. Zoeller](#), Partner, Philadelphia

Author: [Michael A. Jacobs](#), Partner, Philadelphia

Author: [Kelley C. Miller](#), Associate, Philadelphia

Author: [Kaitlin A. McKenzie-Fiumara](#), Associate, Philadelphia

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On December 1, 2011, the Department of Revenue issued Sales and Use Tax Bulletin 2011-01 to remind remote sellers of their sales tax collection obligations. For a link to the Bulletin, please visit [www.reedsmith.com/patax](http://www.reedsmith.com/patax). This Bulletin makes it clear that going forward, the Department's policy will be to apply Pennsylvania's sales and use tax statute<sup>1</sup> to remote sellers "maintaining a place of business in the Commonwealth" to the full extent allowed by existing law.<sup>2</sup>

If you are a remote seller who is not collecting Pennsylvania sales tax, there are three things you need to know about Bulletin 2011-01:

1. If you are making sales into Pennsylvania through use of a web-based affiliate or agent located in Pennsylvania-or if you are using affiliates or agents to provide services (e.g. storage, repair or delivery services) to support your sales in Pennsylvania-the Department believes that you have nexus in Pennsylvania for sales and use tax purposes;
2. If you have nexus with Pennsylvania based on the foregoing, you have the opportunity to register to collect and remit sales tax to Pennsylvania by February 1, 2012, and avoid potential exposure for periods prior to February 1, 2012<sup>3</sup>; and
3. Even under Pennsylvania's expansive statutory definition of "maintaining a place of business in the Commonwealth," some remote sellers may not have nexus with Pennsylvania. All remote sellers should carefully consider their particular facts and circumstances (and audit and assessment risks) before taking the steps to register.

### The Department's New Nexus Position

Sales and Use Tax Bulletin 2011-01, which the Department characterizes as a "reminder" to remote sellers regarding Pennsylvania's existing sales and use tax statute, contains seven examples of activities whereby a remote seller may have nexus for Pennsylvania sales and use tax. The examples include:

- Regular solicitation of orders from Pennsylvania customers through the website of an entity or individual physically located in Pennsylvania (e.g., clicking-through one website of a Pennsylvania-based entity to get to another remote seller's website);
- Maintaining a contractual relationship with an entity or individual physically located in Pennsylvania whose website has a link that encourages purchasers to place orders with the remote seller; and

- Use of affiliates or agents within Pennsylvania to provide services within Pennsylvania (including, but not limited to storage, delivery, marketing or soliciting sales) that benefit, support and/or complement the remote seller's business activity through its affiliates, agents and/or independent contractors.<sup>4</sup>

The Department concludes that these activities establish sales tax nexus in Pennsylvania based on its interpretation of existing Pennsylvania law and U.S. Supreme Court jurisprudence. According to the Department, under the U.S. Supreme Court's nexus cases-namely, *Scripto v. Carson*<sup>5</sup> and *Quill v. North Dakota*<sup>6</sup> -a remote seller may have nexus with Pennsylvania based on its relationship with a third party, when that third party has physical presence in the Commonwealth, and acts as an agent or representative of the remote seller.<sup>7</sup>

So, what's "new"? As far as the Bulletin's restatement of the current sales and use tax statute in Pennsylvania-nothing. Significant, however, and in direct contrast to the canon of previous case law<sup>8</sup>, rulings, and other Department-issued guidance, the Bulletin expands and clarifies the Department's latest interpretation of the existing sales tax statute to recognize affiliate and click-through nexus. In essence, the Bulletin makes click-through and affiliate nexus the policy of the Department of Revenue in Pennsylvania.

The Bulletin leaves a number of key questions unanswered. For example: (i) what level of activity will be required before the Department deems a remote seller to be "regularly soliciting" orders from Pennsylvania customers?; and (ii) will a remote seller whose only connection with Pennsylvania is the placement of advertising on the websites of individuals and businesses located in Pennsylvania be deemed to be "maintaining a place of business in the Commonwealth"?

### **What Does This Guidance Mean for Taxpayers and Pennsylvania?**

The new guidance is likely to be a revenue win for the Commonwealth but also an opportunity for taxpayers whose activities may fall within those described in the statute (and reiterated in the Bulletin) to consider their options and, specifically, to bring themselves into compliance with the Department's new position with respect to remote sellers.

The Department's approach to applying this shift in application of Pennsylvania sales tax nexus statute prospectively clearly reflects Governor Corbett's pledge, that his Administration would be more business friendly.

For Pennsylvania, whose fiscal year-to-date General Fund revenue collections are \$345.3 million (or 3.6 percent<sup>9</sup>) below estimate, the potential impact is an obvious one: A cash-strapped state stands to reap sales tax receipts from online purchases, creating a significant, new revenue source for the Commonwealth. In fact, the Department of Revenue estimates that online purchases will result in about \$380 million in unpaid sales tax this year in Pennsylvania, up from \$350 million in 2010.<sup>10</sup>

### **What Are Your Options?**

If you are a remote seller that has nexus with Pennsylvania (and you are not presently collecting sales tax on your sales into Pennsylvania) based on any of the activities described in Sales and Use Tax Bulletin 2011-01, you have two options:

1. Register with the Commonwealth to collect and remit Pennsylvania sales tax for online sales arising from the activities described in the Bulletin by February 1, 2012; or
2. Review your particular facts and circumstances under Pennsylvania law and decide not to register with the Commonwealth and be prepared to challenge the Department if you receive an assessment.

Remote sellers should carefully consider the examples contained in the Bulletin in light of their online activities in deciding whether to immediately register with the Commonwealth. Although the Bulletin and its accompanying press release are silent on whether remote sellers will face any potential liability for failure to collect and remit tax for prior periods, we understand that the Department will be willing to agree to allow most remote sellers with possible nexus exposure in light of the Bulletin to begin collecting and remitting sales and use tax on a prospective basis if they register and begin collecting and remitting tax by February 1, 2012.

It may be prudent to obtain written confirmation from the Department that registering to collect tax and collecting tax beginning on February 1, 2012, will absolve all potential tax collection responsibilities for all prior periods.

### **Who Should Consider Not Registering?**

After a careful consideration of the facts and circumstances of their activities in the Commonwealth, some remote sellers may choose to forego registering (either immediately or before February 1, 2012) at the risk of receiving an assessment later on. One example of a situation in which a remote seller might choose not to register with Pennsylvania, notwithstanding the Bulletin, would be if the seller's only connection with Pennsylvania is a contractual relationship with a Commonwealth entity whereby the seller pays a flat, monthly fee for banner advertisements placed on that entity's website. Arguably, in this scenario the remote seller is contracting with the Commonwealth entity for a service more akin to traditional advertising than active sales solicitation. Another example of a situation in which a remote seller might choose not to register with Pennsylvania would be if the seller makes a de minimis (e.g., less than \$10,000 annually) amount of Pennsylvania sales attributable to any click-through/affiliate marketing arrangement with a Pennsylvania entity.

Arriving at a decision to register-or not-will require remote sellers to thoughtfully consider their connections with Pennsylvania in light of the Department's guidance. Notably, in addition to the Bulletin and the Department's press releases, the Department has issued an updated nexus questionnaire, a copy of which may be found here: [www.reedsmith.com/patax](http://www.reedsmith.com/patax).

Remote sellers with Pennsylvania nexus, as interpreted by the Department, who fail to begin collecting tax could be assessed tax on sales into Pennsylvania for prior periods. The Department has indicated that it may look back at least three years for audit and assessment purposes.

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1. 72 P.S. § 7202(a). In conjunction with the Bulletin, the Department issued a press release characterizing the guidance as "[an explanation of] existing sales tax nexus law for remote sellers, clarifying the law and the department's authority to require e-commerce and other out-of-state sellers with physical presence in Pennsylvania to collect sales tax."



Department of Revenue Press Release: Revenue Department Clarifies Existing Sales Tax Nexus Law for Remote Sellers (December 1, 2011).

2. 72 P.S. § 7201(b).
3. Although the Bulletin is silent as to the necessary deadline to register and collect tax in Pennsylvania, we have been advised that the deadline to register in Pennsylvania is February 1, 2012.
4. Sales and Use Tax Bulletin 2011-01 (December 1, 2011).
5. 362 U.S. 201 (1960).
6. 504 U.S. 298 (1992).
7. Id.
8. See, e.g., *Bloomington's By Mail, Ltd v. Commonwealth*, 567 A.2d 773 (Pa. Commw. 1989)(held that in-state affiliates do not create nexus for out-of-state affiliates selling into Pennsylvania).
9. "Revenue Department Releases November Collections," Pennsylvania Department of Revenue Press Release (December 1, 2011).
10. "Cyber Monday Puts State Online Sales Tax Laws Under Spotlight," AP News (Nov. 28, 2011).

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