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WITH THE MARKETPLACE FAIRNESS ACT

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Quill v. North Dakota[2] unbalanced the American retail market with its preference for out-of-state over in-state sellers. The preference under *Quill* is that sellers without *physical presence* in a state cannot be compelled to collect the sales tax. If the buyer does not voluntarily remit the complementary use tax, the purchase is effectively tax-free. As a result, *Quill* is seen as facilitating tax avoidance and driving business to sellers who have no in-state *nexus*, notably e-businesses. Revenue losses are estimated in excess of $10 billion per year.[3]

The reach of the *Quill* decision is international. Preferred sellers can reside just as easily in another country as they can in another State. The international dimension of the *Quill* decision means that legislative efforts to correct *Quill's* preference for out-of-state sellers, like the Marketplace Fairness Act (MFA),[4] also have international implications. This paper provides a rough analytical and quantitative measure of the impact of the MFA on the largest block of foreign businesses selling into the US, businesses selling from the EU.[5]

Analytically, the MFA offers a compliance regime similar to that advanced by the EU Commission for collecting VAT on difficult cross-border transactions. This administrative replication allows outcomes to be compared. Quantitative measures can be extrapolated from trade statistics, and will allow some rough estimate of where the MFA will have its greatest international impact.

Just like the American retail sales tax, the EU VAT has struggled with distance sales. The EU VAT has adopted a solution that is remarkably similar to that found in the MFA. It is a one-stop-shop (OSS) – a single administrative vehicle for multi-jurisdictional compliance. The major difference between the American and European OSSs is that the MFA requires states to certify *private sector* software to perform OSS

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[2] *Quill v. North Dakota*, 504 U.S. 298 (1992) (requiring the *physical presence* of a business within a jurisdiction before a state can require the business to collect a local sales or use tax on local sales).

[3] Donald Bruce, William F. Fox & LeAnn Luna, *State and Local Sales Tax Revenue Losses from E-Commerce*, 52 STATE TAX NOTES 537 (May 18, 2009) (indicating that losses were projected to be $11.4 billion per year by 2012 with a six-year total of $52 billon).

[4] S. 743 (113th) Marketplace Fairness Act of 2013 (also introduced as H.R. 684 and S336).

[5] The transatlantic economy is the largest and wealthiest market in the world, accounting for over 54% of world GDP in terms of value and 40% in terms of purchasing power. *See*: Daniel S. Hamilton & Joseph P. Quinlan, *The Transatlantic Economy 2011 – Annual Survey of Jobs, Trade and Investment between the United States and Europe*, Center for Transatlantic Relations, Johns Hopkins University, Paul H. Nitz School of Advanced International Studies.

functions, whereas the EU requires each Member State to maintain a *government operated* OSS through an Internet portal.

The EU uses its OSS to level the playing field between Community Member States and third countries in a limited market segment – electronically provided services from non-EU suppliers to EU final consumers. It has recently extended its OSS to another limited market segment involving – radio and television broadcasting, telecommunications and electronic services from EU businesses to EU final consumers in other Member States. The MFA is similarly concerned with sales to final consumers, but in the American case the problematical supplies are commonly goods not services. The RST taxes relatively few services.

There are proposals in the EU to extend the OSS throughout the VAT. There are also concerns that (as currently constituted) the EU OSSs over-correct; that is, they provide a *superior* compliance regime for non-EU sellers (in one case), and selective EU suppliers (in another instance), but *deny* the regime to other similarly situated EU sellers. The MFA has the same issue.

This paper is comparative. It considers the OSS solution in the MFA and compares it with the similar OSSs in Articles 359 through 369 of the VAT Directive. Both US and EU systems struggle when their respective destination-based consumption taxes tilt in favor of distant sellers. The playing field is not level – the marketplace is not fair. The MFA takes a slice of the US playing field and levels it. It levels it (a) in States that meet the MFA's conditions – these States are allowed to compel *domestic remote sellers* to collect the retail sales tax. But in the case of (b) States that do not meet the MFA's conditions – the MFA allows *Quill's* dictates to remain in place, and as a result this part of the playing field remains unlevel.

International remote sellers similarly fall into these same two categories, but the ability of a State to compel a foreign remote seller to comply with state tax laws (even after MFA passage) is difficult. This is another slice of the US playing field that remains unbalanced. This aspect of the MFA echoes a problematical area of VAT enforcement. Both the MFA and the EU see the OSS addressing *international remote sellers* through the OSS simplification because the OSS *encourages* remote sellers (who cannot be *forced* to comply) to collect and remit taxes on their remote sales.

If the MFA is enacted, we may find out if the EU's *government-centric* OSS provides more or less *encouragement* than the US's *private sector* OSS. Significant US and EU revenue is at stake. If there is a "better way," it is important to know what it is.

MARKETPLACE FAIRNESS ACT of 2013

On May 6 the Marketplace Fairness Act of 2013 (MFA)[6] passed the US Senate on a vote of 69 to 27. The MFA is one of three "remote seller" bills currently in Congress attempting to correct *Quill*. It is the only one to pass any chamber of Congress. The

[6] S. 743; also S. 336 and H.R. 684.

others are the Main Street Fairness Act (MSFA),[7] and the Marketplace Equity Act (MEA).[8] Each bill builds on the *private sector OSS* in the Streamlined Sales and Use Tax Act (SSUTA).[9] The reason the MFA has drawn the most support is because it is simpler (than the MEA),[10] and because it imposes fewer burdens on the State (than the MSFA).[11]

Each bill overturns *Quill* by conditionally permitting States to require "remote sellers" to collect sales and use tax. The MSFA's condition is SSUTA membership; the MEA's conditions are set out in "minimum simplification requirements" (many of which are drawn from SSUTA);[12] the MFA sets out alternative conditions of either SSUTA membership or adoption of "minimum simplifications" that are similar to those under the MEA. Each of these acts has unique software provisions drawn largely from the SSUTA. They establish *private sector OSSs* with certified software.

SSUTA – voluntary compliance facilitated by an OSS

The genesis of the *private sector OSS* is in the SSUTA. Unable to overturn *Quill*, the states began a project through the National Tax Association in 1997 that led to the adoption of the SSUTA in 2002.[13] SSUTA's approach to *Quill* was to *induce* traders to *voluntarily* collect and remit sales and use taxes that *Quill* held they were not legally obligated to collect.

The inducement was certified software and third party tax collection agents. The agents, certified service providers (CSPs), literally assumed all of the vendor's sales and use tax functions and did so at no cost to the vendor.[14] A variation on the CSP was also advanced. Where certified automated software (CAS) is deployed by the vendor (not a

[7] S. 1452 and H.R. 2701.
[8] H.R. 3179.
[9] The Streamlined Sales and Use Tax Agreement is available at: http://www.streamlinedsalestax.org/uploads/downloads/Archive/SSUTA/SSUTA%20As%20Amended%205-24-12.pdf. The SSUTA requires its members to harmonize tax base definitions, standardize electronic reporting, move local reporting to the state level, and to streamline audit and collection processes. The SSUTA was adopted on November 12, 2002, and became effective on October 1, 2005. There are twenty-four member states. They are: Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Vermont, Washington, West Virginia, Wisconsin and Wyoming.
[10] For example the MEA does not require a single audit for all jurisdictions in the State (so the audit burden remains high), and the MEA allows three different rates to be used (so the rate simplification is not robust). It also has a lower threshold for exemption ($500,000 of US sales as opposed to $1,000,000 in the MFA, §2(c)), and this will bring more remote sellers into the sweep of the law.
[11] For example, the MSFA mandates SSUTA membership. There have always been difficulties reaching consensus on some issues in the SSUTA and this has kept some of the larger states, like California and New York, out of the agreement. SSUTA membership is only an option under the MFA. Some States may want this option, or may already be a member.
[12] Those standards are: (1) identification of a single revenue authority within the state for the filing of sales and use tax returns; (2) creation of a single sales and use tax return; (3) establishment of a uniform tax base applicable at state and local levels; (4) the provision of adequate software for remote sellers that will substantially reduce the burden on business of collecting tax at multiple rates within the State; and (5) providing relief of liability for any remote seller whose tax determination is in error because of reliance on information provided by the State. MEA, §§ 2(b)(2) and 2(b)(3).
[13] NTA, *Communications and Electronic Commerce Tax Project Final Report* (September 7, 1999).
[14] SSUTA §§ 201, 203, 205.

third-party service provider), and where this software is used properly the vendor is again insulated from liability for errors in determining the proper tax. The SSUTA Governing Board is charged with certifying CSPs and software.[15]

The CSP (and the certified software alone) function as a *private sector OSSs* for the vendor. It determines and reports all sales and use taxes due in all SSUTA member states. What the SSUTA cannot do however is to *compel* the vendor to use the OSS mechanism. *Quill's* physical presence test allows any vendor without presence in a state to refuse to volunteer to collect the tax.

MFA – mandatory compliance facilitated by an OSS

As federal legislation the MFA can do what SSUTA's aggregation of state legislation cannot. The MFA will allow States to exercise jurisdiction over remote sellers making sales into their state.[16] It does so only if the vendor made more than $1 million in remote sales in the US the previous year.[17] The MFA allows states to make compliance mandatory, not voluntary.

If a vendor exceeds the $1 million threshold, then there are two alternate paths that the state can take to bypass the *Quill* mandate. Both involve certified software (certified software providers), and both effectively establish OSSs. The alternatives are:

1. The State is a member of the SSUTA;[18] or
2. The State must "enact [and] … implement" the minimum simplification requirements, which are:
    - A single state-level agency will administer all State and local sales and use taxes, returns processing, and audits for remote sales.[19]
    - A single audit of a remote seller for all sales and use taxes;[20]
    - A single sales and use tax return will be used for all taxes, and will be filed with the state administrative agency. The return for remote sellers cannot be required to be filed any more frequently than the returns of non-remote sellers.[21]
    - A uniform sales and use tax base for all taxes in the state.[22]
    - Information on taxable products and services, the exemptions, rates, and the boundary database.[23]

[15] SSUTA § 501.
[16] MFA, §4(5). Remote sales are sales "… into a State, as determined under the sourcing rules under paragraph (7), in which the seller would not legally be required to pay, collect, or remit State or local sales and use taxes unless provided by this Act."
See also SSUTA § 605(A) "… sales into a state in which the seller would not legally be required to collect sales or use tax, but for the ability of that state to require such "remote seller" to collect sales or use tax under federal authority."
[17] MFA,§2(c).
[18] MFA,§2(a).
[19] MFA, §2(b)(2)(A)(i).
[20] MFA, §2(b)(2)(A)(ii).
[21] MFA, §2(b)(2)(A)(iii).
[22] MFA, §2(b)(2)(B).
[23] MFA, §2(b)(2)(D)(i).

- Provision of "software free of charge for remote sellers that calculates sales and use taxes due on each transaction at the time the transaction is completed, that files sales and use tax returns, and that is updated to reflect rate changes … [and] capable of calculating and filing sales and use tax returns in all States qualified under this Act."[24]
- Provision of certification procedures for the software.[25]
- The State will hold the remote seller harmless for errors or omission in the rate information provided by the State,[26] and do the same for certified software providers."[27]
- 30 days notice will be given of any rate changes by any locality in the State.[28]

These options are not identical. The "minimum simplification" option may not only be easier for the States to implement, it may also be more favorable to both merchants and the technology companies (CSPs) who provide the software solutions. The MFA shifts the cost of compliance and the balance of responsibility for software errors from the seller (or the seller's software provider under the SSUTA) to the State.

The MFA is very clear. The minimum simplification alternative is met "only if" the State provides "software free of charge," just as under the SSUTA. In addition, if that software is "provided by certified software providers [it] shall be capable of calculating and filing sales and use tax returns in all States qualified under this Act."[29] This is very clearly the establishment of an OSS – a single compliance portal available free of charge to receive taxes for multiple jurisdictions.

With the MFA there is a substantial compliance-cost reduction for businesses, and substantial risk reduction for businesses and certified software providers. In terms of compliance costs, both tax calculation and return filing functionality are provided free of charge. In terms of compliance risk the MFA shifts these risks back to the State, and does so in a manner that is perfectly in tune with *Quill.*

At its core the Supreme Court's *Quill* decision rests on a perception of unfairness. It is unfair if a State creates an extremely complex retail sales tax regime, and then penalizes businesses if they cannot comply with the law. Under the MFA this will change. If a State wishes to participate in the MFA and require remote sellers to collect the local sales and use tax, and if complexities remain in its sales tax regime that leads to software errors or omissions in tax calculation and reporting, then it is only fair that the State (not the taxpayer or the software provider) be held at fault.

If the MFA becomes law, and if the forty-five states with a sales tax opt either for SSUTA or minimum simplification, then only remote sellers who make less than $1m of

[24] MFA, §2(b)(1)(D)(ii).
[25] MFA, §2(b)(1)(D)(iii)
[26] MFA, §2(b)(1)(E)
[27] MFA, §§2(b)(1)(F) & (G).
[28] MFA, §2(b)(1)(H)
[29] MFA, §2(b)(2)(D).

remote sales in the US will be protected by *Quill*. This will leave *international remote sellers* as the major enforcement area for the States.

With respect to these remote sellers the US States will be in exactly the same position as the EU Member States when they try to collect VAT on electronically provided services from non-EU suppliers to EU final consumers. Collection and remission of the RST will technically be required under the MFA, but enforcement of this obligation will be nearly impossible. The US States and the EU Member States will be in exactly the same position. Compliance will depend on *moral authority* and the *persuasive power* of the OSS.

OSSs IN THE EU

There are two OSSs in the EU, and an active proposal to open up the OSS procedure to all taxpayers. Only the two limited OSSs have been adopted. In both of the adopted OSSs the goal has been to level the playing field for a defined slice of the marketplace.

EU – a limited OSS only for non-EU businesses (B2C)

In the late 1990's the EU became concerned with the large volume of digital products sold to EU customers by non-EU businesses. The issue was sourcing. The *Sixth Directive*[30] sourced these supplies outside the EU, making them not subject to VAT. However, consumption (use and enjoyment) was occurring within the EU.[31] EU sellers of the same services were at a considerable disadvantage with VAT rates ranging from 15% (Luxembourg) to 25% (Denmark).

The playing field was not level. Because the marketplace was tilted in favor of the non-EU seller, sourcing rules were changed and an OSS adopted.

Sourcing rules. Electronically supplied services from non-EU businesses were added to the list of exceptions in the earlier version of Article 56, and a special rule dealing with similar B2C transactions was added to the earlier version of Article 57(1). Tax now became due in the EU because the place of supply was within the EU.

Working out the practical aspects of this change was more complicated. Business-to-business (B2B) transactions from non-EU suppliers, by far the largest part of e-commerce in monetary terms, were handled through a reverse charge procedure. Business-to-consumer (B2C) transactions were more difficult. Consumers do not file

[30] The SIXTH COUNCIL DIRECTIVE of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover tax – Common system of value added tax: uniform basis of assessment (77/388/EEC) 1977 O.J. (L 145) 1 was repealed and replaced on November 28, 2006 with the RECAST VAT DIRECTIVE. Council Directive 2006/112/EC on the Common system of value added tax, O.J. (L 347) 1. Citations throughout this document will be to both versions. The most updated version will be referenced as the VAT DIRECTIVE.

[31] Specifically, the sourcing issue was that the fall back rule of Article 9(1) [VAT DIRECTIVE, Article 43]. This rule provided that any service not covered in the series of exceptions that make up the rest of the former Article 9 were to be taxed where the supplier was located. In the case of digital services this was frequently outside the EU, and commonly in the US.

VAT returns, thus a reverse charge was not possible. Non-EU businesses were simply required to collect and remit the VAT. However, there was no way to enforce this requirement.

At this juncture, the EU VAT and the RST under the MFA are in exactly the same position. Both *require* overseas businesses to collect and remit a destination-based consumption tax, but neither can *enforce* the requirement.[32] The EU sought to *induce* compliance with its first OSS.

The one-stop-shop (OSS). Articles 359 through 369 (formerly Article 26c) were adopted. Together they provide for an OSS that allows non-EU established businesses to select a single "Member State of identification" where they will register (but are not considered established). VAT from sales made throughout the EU is charged on a destination-basis, and the full sum is paid over to the Member State of identification on a single electronic return. The member state of identification then redistributes the VAT to the appropriate jurisdictions. Everything is required to be digital.

Although the compliance costs and risk of errors are born by the business, filing and payment is streamlined through a dedicated web portal established by the Member State.

EU – a second limited OSS only for EU radio and television broadcasting, telecommunications and electronic services businesses (B2C)

In 2008 the place of supply for services was changed generally from the seller's to the buyer's location. For radio and television broadcasting, telecommunications and electronic services, this was a very significant change. Under the previous sourcing rules it had been common for EU broadcasters to establish themselves in a low tax jurisdiction (Luxembourg was favored at 15%) when broadcasting into high tax jurisdictions (Denmark's 25% rate was avoided).[33]

This sourcing adjustment was so difficult for this industry segment that an agreement to make overall changes could not be reached without selectively delaying the effective date for this industry until January 1, 2015, and then further allowing use of the OSS procedure by these firms.[34]

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[32] If a business was willing to comply with the requirement to collect the VAT on B2C sales, there were essentially two options: they could either (1) establish themselves in a Member State, or (2) register in each Member State where they made taxable supplies. Neither choice was optimal. Although under the first option all digital sales would be sourced to the one EU jurisdiction where the business was established, the establishment process itself led to direct tax obligations. The formerly non-EU business would become a real EU business for tax and regulatory purposes. The second option also had disadvantages. Under this option a business could conceivably be required to register in what was then 25 Member States (now 27), file 25 sets of VAT returns, and do so in as many as 20 different languages. Sourcing of sales under this option would be destination-based.

[33] Council Directive 2008/8/EC of 12 February 2008 amending Directive 2006/112/EC as regards the place of supply of services, O.J. (L 144) 1 (February 20, 2008).

[34] Commission implementing Regulation (EU) No. 815/2012 of 13 September 2012 laying down detailed rules for the application of Council Regulation (EU) No 904/2010 as regards special schemes for non-established taxable persons supplying telecommunications, broadcasting or electronic services to non-

The implementing regulation now distinguishes between two OSSs: (1) the new "Union Scheme" (the special scheme for taxable persons that are established within the Community, but not established within the Member State where the services are supplied) and (2) the older "Non-Union Scheme" (for taxable persons not established within the Community). The regulation structures the OSS process as follows:[35]

- Statement – the taxable person must submit a statement to the Member State where he would like to be *identified* (the Member State of Identification);[36]
    - The Member State cannot refuse the request.
- Updates – the statement must be updated to reflect commencement and cessation of activity;[37]
- Details – the statement must indicate:[38]
    - Name
    - Postal address
    - Electronic address & web site
    - National tax number (if any);
- In the case of a non-EU business a statement that the person is not identified for VAT purposes within the EU.[39]
- Return – a single return is required each quarter which must show:[40]
    - VAT identification number;
    - Total value of supplies made in each Member State;
    - Total amount of VAT due in each Member State;
    - The applicable VAT rate in each Member State.
- Euros – the VAT return must be in euros (unless the Member State of Identification has not adopted the euro).[41]
- Payment – one payment will be made into the bank account designated by the Member State of Identification.[42]
- Record keeping – records must be kept for 10 years.[43]

The VAT paid to the Member State of Identification is reallocated to the appropriate Member State of Consumption. The taxpayer's calculation and allocation is followed. There is no unitary audit, each Member State will audit on its own.

TWO LESSONS FROM THE COMPARTIVE STUDY:

taxable persons. On October 9, 2012 the Council adopted Regulation (EU) No 967/2012 amending implementing Regulation (EU) No 282/2011 as regards the special scheme for non-established taxable persons supplying telecommunications services, broadcasting services or electronic services to non-taxable persons.

35 All taxpayer/government communications are required to be electronic.

36 VAT DIRECTIVE, Articles 359 & 369b.

37 VAT DIRECTIVE, Article 360 & 369c.

38 VAT DIRECTIVE, Article 361 & 369e.

39 VAT DIRECTIVE, Article 364.

40 VAT DIRECTIVE, Article 365 & 369f.

41 VAT DIRECTIVE, Article 366 & 369h.

42 VAT DIRECTIVE, Article 367 &369i.

43 VAT DIRECTIVE, Article 369 & 369k.

(1) The Over-correction (or under-inclusiveness) Problem of the OSS
(2) Don't forget the International Slice of the Marketplace

There are two lessons to be learned from a comparison of the OSSs in the MFA and the EU VAT. The first has to do with the domestic dynamic that arises when an OSS is implemented and is found to be successful. Businesses that were excluded from the OSS in the beginning seek admission later to capture efficiencies and reduce compliance risks.

Secondly, because the entire area of remote sellers and destination consumption taxes has a strong international component, the quest to level the domestic playing field eventually leads overseas. States should anticipate that foreign cooperation would be forthcoming, and may want to prepare the way for further federal involvement in the US sales tax. The first step in this analysis is to measure the potential revenue flows.

LESSON (1):
The Over-correction (or under-inclusiveness) Problem of the OSS

The EU's OSSs are not open to all taxpayers. Only non-EU businesses selling to EU final consumers, or EU radio and television broadcasting, telecommunications and electronic service firms can use it. However, the efficiency of filing a single pan-EU return through a single web portal has not gone unnoticed by similarly situated businesses established in the EU.

The same situation will (most likely) arise under the MFA. Neither the SSUTA's nor the MFA's OSSs are open to all taxpayers. If the MFA's OSS is a success, it would be reasonable to expect a dynamic similar to that found in the EU to arise in the US.

In March 2004 the EU Commission suggested in a *Consultation Paper* that any EU businesses making supplies (digital or otherwise) directly to EU end users in a Member State other than the state where they were established should be allowed to file under an OSS procedure.[44]

The business response to the *Consultation Paper* was overwhelmingly positive.[45] European businesses urged the expansion of the OSS system. Intra-community B2C, domestic B2C, and even B2B transactions should be allowed to use the OSS, they said. The OSS was seen as a simplification that worked, but had been unfairly open only to foreigners (it was later opened to EU radio and television broadcasting,

[44] Although not clearly stated in the *Consultation Paper* it appears that non-EU established persons would have to become established to participate. European Commission, *Consultation Paper: Simplifying VAT Obligations, The One-Stop System* (March, 2004) TAXUD/590/2004-EN, page 3.
[45] See for example the response of Eurochambres, *Position Paper 2004: Simplifying VAT Obligations: the One-Stop System.* Eurochambres is a 17 million-member business organization that is the sole European body serving the interests of every sector and every size of European business. Available at: http://www.eurochambres.be/PDF/pdf_position_2004/VAT%20One-Stop-Shop.pdf

telecommunications and electronic service providers). Nevertheless, for political reasons, the proposal in the *Consultation Paper* was not adopted.[46]

The EU Commission's short hand expression for the current situation is that there is a *mini-one-stop-shop.* This expression leaves open an expectation that a comprehensive OSS could be right around the corner. In fact, the Commission proposes that after 2015 there should be a "… managed broadening of the One Stop Shop over time. [But that] … it's a good idea to wait to see the success of the mini One Stop Shop before embarking on an expansion; and this we will do."[47]

Provided that the MFA passes and the States comply with its conditions, and if they then demand that remote sellers collect the sales and use tax, it may only be a matter of time before in-state businesses request an extension of the MFA's OSS to all taxpayers (whether or not they are making remote sales). The argument will be: Why should an out-of-state seller be provided tax software free of charge, and be held harmless for errors when in-state sellers are not accorded the same benefits?

This is a difficult argument to rebut in the context of a tax reform that is based on fairness. Thus, apart from aiming to level the playing field between e-commerce and brick-and-mortar businesses, as a side-effect, the MFA could facilitate tax collection and compliance in the whole economy: Although the bill's, measures target specific companies, they could potentially benefit all.

LESSON (2):
Don't forget the International Slice of the Marketplace

In terms of US imports, the second largest piece of the American cross-border trade is European. In 2011, trade with the EU27 accounted for 16.9% of the total value of US imports, exceeded only by China at 18.8%.[48] In order to arrive at an estimate of the volume of international trade likely to be affected by the MFA (remote sales by

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[46] The main reason this expanded OSS was not adopted had to do with the clearinghouse mechanism that would need to be established. In the Commission's mind the main problem was a matter of trust. Algirdas Semeta, the European Commissioner for Taxation, Customs, Anti-fraud and Audit indicated:

> The One Stop Shop has many merits. It can bring substantial simplification and cost reductions for businesses and member states. But for it to work in practice, *member states must trust each other* to collect the VAT on their behalf. It needs to be asked whether that degree of confidence between the member states currently exists.

Algirdas Semeta, *The mini-One Stop Shop for VAT – the start of something big!* WORLD COMMERCE REVIEW (June 2012) 29 (emphasis added). See also: Sijbren Cnossen, (Commentary on Ian Crawford, Michael Keen & Stephen Smith, *Value Added Tax and Excises*, Ch 4 in Institute for Fiscal Studies, DIMENSIONS OF TAX DESIGN: THE MIRRLEES REVIEW) at subheading *Exporter Rating System Proposed by the European Commission* at 377-382 *available at*: http://www.ifs.org.uk/mirrleesreview/dimensions/ch4.pdf (discussing the political discord arising with the proposal of a clearing house).

[47] Algirdas Semeta, *supra* note **Error! Bookmark not defined.**~~9~~, at 29.

[48] *United States: EU Bilateral Trade and Trade with the World* (May, 2013) European Commission. Available at: http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113465.pdf

businesses that exceed the MFA's $1,000,000 threshold) we need to start with aggregate EU-US trade data.[49]

Table 1 shows the number of European enterprises exporting to the US in 2010, with the exception of Belgian and Irish data (this data is not available in the OECD Trading Partners Database). The upper estimate of the number of EU firms that could potentially be required to charge sales tax under the MFA is, therefore, approximately 146,000. These firms generated $253 billion of EU-US trade value in 2010.

Under *Quill* most of these firms would never have had an obligation to collect sales or use tax. The vast majority of these firms have *no physical presence* in the US. In 2009, 16 EU Member States with 141,331 US-exporting businesses reported only 15,920 US based affiliates.

There are several reasons why not all 146,000 EU exporters will want to access the *private sector OSS* of the MFA.

First, some firms' remote sales will not surpass $1 million. The majority of these will likely be micro-enterprises, usually defined as enterprises with fewer than 10 employees and turnover below EUR 2 million. While we cannot control for turnover, OECD Trade by Size Classes Database, Rev.4 provides information on the size class of all European firms involved in external EU-trade. By identifying the fraction of micro-enterprises in the total population of exporting firms we can get a rough idea of their number in the subsample of EU-US exporters (only).

Thus, we find that 44% of all EU companies trading with partners outside the EU have between 1 and 9 employees. Assuming that the percent of micro-enterprises is similar for the sample of US-exporting firms, then roughly 64,800 of these firms are likely to be too small to exceed the $1 million small seller threshold.[50]

Even though almost half of all firms involved in external EU-trade are micro-enterprises, they account for only 8% of the value of external trade. In contrast, 3% of companies with more than 250 employees generate 53% of the value of external EU trade. These larger firms and SMEs, or roughly 80,000 firms are in all likelihood above the MFA threshold. Yet, for reasons explained below, this does not mean that they will

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[49] It is important to note that the MFA states that, "… the remote sales of 2 or more persons shall be aggregated if:

> 1. such persons are related to the remote seller within the meaning of subsections (b) and (c) of section 267 or section 707(b)(1) of the Internal Revenue Code of 1986; or
> 2. such persons have 1 or more ownership relationships and such relationships were designed with a principal purpose of avoiding the application of these rules."

MFA, §2(c) (1) & (2).

These conditions eliminate incentives for the establishment of multiple sister companies without physical presence by the parent or other subsidiaries, whose goal would be to maintain sales below the threshold and thus, avoid the collection of sales tax.

[50] This assumption is rather strong as it is possible that micro-enterprises are mostly trading with partners in close geographical proximity to the EU, whereas big exporters are engaged in overseas trade.

all be subject to state efforts to compel sales and use tax collection as a remote seller under the MFA. Nor does it mean that the sales and use tax on US imported products is fully lost.

Second, many SMEs and large corporations active in the US market already use the services of giant resellers like Digital River ($22 billion revenue) for the sale of their digital products. In fact, such resellers typically provide comprehensive services – they are a payment platform, offering both digital and physical product fulfillment as well as marketing of the product. What this means is that the obligation to collect the sales tax will not rest with the remote foreign seller but with the American reseller. The burden of compliance would be shifted from the international party onto the domestic player in the American market. Some of the sales and use tax would already have been captured in states in which a reseller is physically located.

Third, on B2B sales the American buyer will most likely remit the use tax, but on B2C sales the tax is most likely not reported. This is the same pattern that plays out in the EU where the reverse charge collects the VAT on B2B cross-border transactions, but there is low compliance in a comparable B2C transaction.

It is useful therefore, to look at the composition of European imports into the US. The OECD Statistics on Measuring Globalization contain a dataset on bilateral trade in intermediate goods and services with the latest recorded year being 2005 (Table 1, Column 5). In 2005, European exports of intermediate goods/services to the US were $198 billion or 63% of the value of total exports to the US in 2006.[51] As mentioned above, a large portion of the use tax on these B2B sales may already be collected. Nevertheless, the remaining 37% of trade value is likely generated by B2C transactions, which implies significant foregone sales tax revenue.

Apart from intermediate goods, we can disaggregate EU exports to the US by sector, the most interesting being wholesale, retail trade and repair (Table 1, Columns (2) and (4)). In 2010, 30% of all European exporters conducted wholesale and/or retail trade with the US amounting to $27 billion, or 10% of total value.

To summarize, *Quill* is not dead. Currently, international traders without a physical presence in the US have no obligation to collect the sales and use tax barring:

(a) passage of the MFA (or another similar federal statute),

(b) state membership in SSUTA or satisfaction of "minimum simplifications" requirements, and

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[51] The earliest available year with data for the value of European exports to the US is 2006 in OECD Trading Partners, Rev. 3. The calculation of the percent excludes data for Bulgaria, Germany, Greece, Malta, the Netherlands, Spain and the UK, all of which have missing observations for the value of trade with the US for 2006.

(c) a State statute requiring remote sellers to collect the sales and use tax on in-state sales.

Table 1 Number of EU Enterprises Exporting to the US and Value of Exports, 2010

Country	(1) Total number of enterprises exporting to the US	(2) Wholesale, retail trade and repair, number of enterprises	(3) Value of trade in mil USD (total number of enterprises)	(4) Value of trade in mil USD (wholesale, retail trade and repair	(5) Value of intermediate goods and services, mil USD, 2005
Austria	2,694	893	6,225.79	631.063	4,074.169
Bulgaria	725	197	277.733	41.149	228.8975
Cyprus	143	51	15.733	1.66	305.0888
Czech Republic	2,166	578	1,813.47	201.9	1,689.441
Denmark	3,175	1,213	5,944.5	1208.34	4,963.871
Estonia	251	54	431.341	7.475	198.8327
Finland	1,758	427	4,633.74	63.611	2,367.472
France	19,251	6,478	28,533	4398.48	20,037.14
Germany	20,795	5,705	77,481.1	3085.18	45,526.91
Greece	2,422	770	1,533.11	78.682	5,155.519
Hungary	1,243	328	1,986.17	651.78	1,380.397
Italy	29,129	7,075	25,457.3	2473.95	18,274.61
Latvia	274	70	120.671	13.079	177.363
Lithuania	384	106	558.691	19.153	196.442
Luxembourg	157	82	376.932	11.3	631.1612
Malta	147	37	258.335	23.483	246.5662
Netherlands	5,617	2,101	18,523.5	5640.39	8,649.117
Poland	3,625	911	2,549.36	292.132	1,548.474
Portugal	2,236	544	1,723.08	94.134	1,534.645
Romania	792	155	652.963	17.317	943.69
Slovakia	481	98	899.616	11.849	334.3952
Slovenia	493	86	360.418	6.669	229.232
Spain	11,360	3,393	8,269.75	1301.47	7,666.638
Sweden	6,351	2,126	11,268.9	471.939	7,825.544
United Kingdom	29,554	10,217	53,417	6,337.45	40,226.83
Total	145,178	43,695	253,312.2	27,083.64	198,177.5

Source: OECD Trading Partners Database, Rev.4; OECD Bilateral Trade in Intermediate Goods and Services

If the MFA becomes law, and if the use tax on imported intermediate and B2C goods is partially collected, it is reasonable to assume that the international slice of US trade will contribute significantly to rising sales tax revenue. It is, however likely, that many international firms would outsource the service of sales tax collection to US resellers, so the obligation to comply with state tax laws may ultimately reside with US businesses. Nevertheless, if approximately 80,000 EU businesses exceed the $1 million remote sale threshold, and if these firms are making more than $200 billion in US sales, it is likely that a significant amount of recovered sales and use tax revenue will come from the international slice of the unbalanced American marketplace.

CONCLUSION

The EU and the US Sates are looking at much the same problem when they endeavor to have remote sellers collect and remit destination-based consumption taxes. Both systems recognize that simply having a law in place requiring collection is not sufficient. Both systems have adopted OSSs and compliance simplifications to induce or persuade remote sellers to comply. The EU's preference for a *government-centric OSS* and the US preference for OSSs that involve *third-parties and certified software* may have very different success profiles. This is an important assessment that is yet to come, but it suggests that the US may want to borrow a solution from the EU, or the EU may want to borrow a solution from the US States. Both sides need to be open to the possibility.

At the present time, it is clear that there is room for considerable international cooperation. Algirdas Semeta, the European Commissioner for taxation indicated that the EU Commission is anxious to cooperate. He observes:

> There is no effective way of ensuring compliance if a business located in California, for example, provides e-services to a private individual in Slovakia and does not register for the e-commerce scheme and pay Slovak VAT what can the national tax authorities do realistically? *The Commission is addressing this issue and has asked member states for a mandate to negotiate with third countries on this issue from a collective position of power*. For the time being, though, compliance depends on the willingness of suppliers in third countries to assume their legal obligations.[52]

If the EU is concerned about a remote seller in California making sales into Slovakia, then the California Board of Equalization is most likely equally concerned about a remote seller in France making sales into Los Angles.

[52] Algirdas Semeta, *The mini-One Stop Shop for VAT – the start of something big!* WORLD COMMERCE REVIEW (June 2012) 28 (emphasis added).

Cooperation could be government-to-government, but it could also be through software certification. If the EU adopted the March 2004 *Consultation Paper* proposal and moved generally to OSS compliance, and if the EU decided to adopt the *private sector* software model advanced by SSUTA and the MFA, then it would be a relatively easy matter to jointly certify global software platforms that would comply with all US and EU transaction taxes.

There are already a number of certified software packages in the US that are fully compliant with the thousands of US RST jurisdictions. Some of these packages are also fully compliant with the EU VAT. Joint EU-SSUTA certification may be just ahead if the MFA proves to be a success at persuading remote sellers to comply with collection obligations. It would certainly be a software solution that would be in high commercial demand for the businesses engaged in transatlantic trade – the largest and wealthiest market in the world that accounts for over 54% of world GDP in terms of value and 40% in terms of purchasing power.