South Dakota v. Wayfair: What this new precedent means for Canada?

October 2018

Online Tax Strategies

On June 21, 2018 the Supreme Court of the United States released its verdict on the landmark *South Dakota v. Wayfair* case, ruling that individual states have the ability to require that businesses collect sales taxes from consumers, should they meet a certain volume of sales in that state, regardless of whether the business itself has a physical presence in that state.

Background

This ruling overturns a previous case, *Quill Corp. v. North Dakota*, which ruled that a business would not be required to collect sales taxes on sales transactions in a particular state unless the business had a physical presence in that state. "Physical presence", in this case, would typically have required that business to maintain an office space, warehouse, inventory, or employees/contractors in that state.

This precedent was set in 1992 and it applied primarily to catalogue sales. In the years since *Quill Corp.*, the economic environment has changed significantly with the advent of e-commerce. As such, the argument made by South Dakota was that the previous ruling did not align with current consumer behaviours and local brick and mortar businesses were at a disadvantage by being required to collect sales taxes in cases where online retailers were not.

The Canadian perspective

Canadian businesses

While it may seem that this ruling will only affect businesses and residents of the United States, instituting reporting requirements that are based on volume of sales as opposed to physical presence will surely mean that Canadian businesses selling to the United States will also be impacted.

This becomes especially important due to the fact that more and more states are likely to draft similar legislation to South Dakota's in the future, to access this revenue source that has been largely unavailable to them in the past. Currently, Illinois, Indiana, Iowa, Kentucky, and Maine have implemented similar legislation and this number is likely to increase rapidly going forward.

Given that each individual state has the ability to create its own sales tax system (including thresholds for reporting as well as specific reporting requirements), a Canadian business selling to consumers in a wide range of states could be faced with a much larger compliance burden going forward.

As a result of these changing requirements, Canadian businesses will need to ensure they are aware of the specific compliance and reporting requirements of the state in which they are transacting and have accurate tracking systems to determine the volume of sales being made in each specific state.

For Canadian businesses transacting in North Dakota, we expect the State to begin enforcing this ruling later this year.

The Canadian system

While the federal and provincial sales tax systems in Canada do not adhere to the same physical presence standard as the United States, a supplier of goods and services in Canada will generally be required to register and remit for GST/HST if they are determined to have a permanent establishment in Canada or are considered to be carrying on business in Canada—a concept that is similar to physical presence.

Typically, in cases where a supplier is not required to be registered for Canadian sales tax (i.e. GST/HST or PST), the onus is on the purchaser to self-assess and remit for the relevant sales tax on a transaction—a process which is largely ignored by Canadian consumers.

From a Canadian perspective, it will be interesting to see whether the federal and provincial governments begin to move towards a system that would require more non-residents to register as a result of this change in the United States.

Recent changes in Quebec

One province that is leading the way in this regard is Quebec. In its recent provincial budget, the government of Quebec announced that it would be requiring non-resident suppliers (whether they be located in Canada or abroad) to register for the province's Quebec Sales Tax system beginning in 2019—a change that has been commonly referred to as the "Netflix tax".

Notably, this new registration requirement will apply to suppliers in the e-commerce sector as well as suppliers of certain digital property and service distribution platforms. The change makes Quebec the first Canadian province to impose such a requirement with regards to their provincial sales tax system.

It is anticipated that Quebec's success in implementing this change will determine the likelihood of more provinces following suit in imposing similar requirements on non-resident suppliers.

Do not hesitate to contact your Raymond Chabot Grant Thornton advisor who can help you determine which measures apply to your situation and assist you with the steps needed to benefit from these measures.

For further information, visit our website at rcgt.com.