

Illinois Independent

Tax Tribunal

Wayfair LLC)
Petitioner)
)
v.)
)
Illinois Department of Revenue,)
Respondent)

BRIEF OF THE PETITIONER

The Petitioner, Wayfair LLC (“Wayfair”), moves for summary judgment pursuant to 735 ILCS 5/2–1005 and submits this brief in support of its Petition to review and reverse and/or modify the Notice of Tax Liability (“Notice”) issued by the Illinois Department of Revenue (“Department”) for the reasons stated below.

PROCEDURAL STATUS OF THE CASE AND LEGAL ISSUE TO BE DECIDED

On August 19, 2020, following an audit, the Department issued its Sales Tax Audit Summary Analysis to Wayfair, LLC, disclosing the total proposed additional Retailer’s Occupation Tax in the amount of \$380,399.59. Ex. A. Wayfair protested the proposed assessment, and concentrated its dispute on the portion of the proposed assessment that related to Wayfair’s online sales that occurred (i.e., that Wayfair accepted and approved) prior to February 1, 2016 that resulted in Retailers’ Occupation Tax in the amount of \$164,643.46. Stip. ¶ 5. After the ICB upheld the proposed assessment, the Department issued a Notice of Tax Liability to Wayfair, assessing Retailers’ Occupation Tax in the amount of \$334,242.00, plus \$58,106.17 in accrued interest for taxable periods February 19, 2016 through March 31, 2019. Stip. ¶ 9.

The parties agree there is not a dispute as to the facts, and therefore entered into the Stipulation of Agreed Facts on July 26, 2022. In addition, the parties agree the only legal issue in dispute is:

[W]hether sales that were accepted and approved before Wayfair established nexus in Illinois on February 1, 2016, are nonetheless subject to Illinois tax in the amount of \$164,643.46 (plus interest thereon) because payment was processed and items were shipped after nexus was established per 86 Ill. Adm. Code 130.101(a)(1).

Stip. ¶ 1.

STATEMENT OF FACTS

Launched in 2011, Wayfair is an online merchant of home goods, furniture, and décor. Stip. ¶ 11. Since its founding, Wayfair has expanded its logistics and infrastructure network beyond New England, opening distribution centers throughout the United States, the United Kingdom, and Germany. Stip. ¶ 12.

On February 19, 2016 Wayfair opened a facility located at 815 Kimberly Drive, Carol Stream, Illinois. Stip. ¶¶ 13, 15. This was not a distribution center and Wayfair did not store inventory there or fulfill orders from inventory located at the facility after it was opened on February 19. Instead, the facility was a last-mile location used only to facilitate delivery of orders fulfilled from inventory located outside of Illinois. Wayfair executed the lease for the facility on February 1, 2016. Stip. ¶ 14. Prior to February 1, 2016, Wayfair did not maintain a place of business in Illinois and did not have nexus with the state of Illinois. Stip. ¶¶ 16, 17. Beginning with sales that occurred on or after February 19, 2016, Wayfair filed the Illinois Form ST-1, a combined ROT and Use Tax return, reporting and remitting any applicable taxes collected from its Illinois customers. Stip. ¶ 23.

At all times, both before and after February 1, 2016, orders submitted through Wayfair's website have been accepted and approved at Wayfair's headquarters in Boston. Stip. ¶ 19. All orders were processed by Wayfair outside of Illinois. Stip. ¶ 24. Even after Wayfair opened the Carol Stream facility, Wayfair fulfilled sales to Illinois residents from inventory stored outside of Illinois. Stip. ¶¶ 25, 26. Prior to (and after) February 19, 2016, Wayfair delivered sales to Illinois residents by common carrier from points outside of Illinois. Stip. ¶ 26.

At all times, the sales price (including an estimate of any applicable taxes in states in which Wayfair has nexus), as well as payment information, on the order the customer submitted was accepted and approved by Wayfair at the time the order was submitted on the Wayfair website. Stip. ¶ 20. In the case of the sales at issue, all such customer orders were accepted and approved prior to February 1, 2016. Stip. ¶ 18. Payment was processed at the time the orders were shipped out. Stip. ¶ 21. Wayfair was permitted only to process payment on the credit card in the amount of the sales price accepted and approved at the time the order was submitted on the Wayfair website, and was not authorized to process payment in an amount that exceeded the sales price accepted and approved by both the customer and Wayfair when the order was submitted on the Wayfair website. Stip. ¶ 22. For all sales that were accepted and approved after February 19, 2016, Wayfair reported these sales to the Department once it processed payment and shipped out orders for those sales, in a manner consistent with Wayfair's reporting practice in all states in which it has nexus. Stip. ¶ 23.

Wayfair objects to the portion of the assessment that proposes to assess the Retailers' Occupation Tax on Wayfair's online sales that occurred prior to February 1, 2016, in the amount of \$164,643.46, plus interest thereon. Stip. ¶ 19. The Department based this portion of the assessment on its conclusion that the sale did not occur until the moment of delivery, and since delivery occurred after Wayfair established nexus with Illinois—on or after February 19, 2016—Wayfair was obligated to collect tax on the sale and remit the tax to the Department.

SUMMARY OF ARGUMENT

The Department's position is fatally flawed for two reasons.

First, the Department assessed the Retailers' Occupation Tax (the ROT). Stip. ¶ 9. The ROT is imposed only on those retailers that have nexus with Illinois and are also engaged in the "occupation of selling" in Illinois, which in turn is based on where the taxable business of selling takes place. 86 Ill. Adm. Code 220.115(b)(2) (citing *ExCello Corp. v. McKibbin*, 383 Ill. 316 (1943)). Wayfair is not liable for the Retailers' Occupation Tax because neither at the time Wayfair accepted and approved the orders at issue nor when the goods were delivered was Wayfair a retailer that conducted selling operations in Illinois within the meaning of 86 Ill. Adm. Code 220.115.

Second, even if the assessment of the Retailers' Occupation Tax can be revised after-the-fact to be deemed an assessment of Use Taxes, Wayfair cannot be held liable for Use Taxes because it did not have nexus with Illinois at the time its obligation to collect any applicable Use Tax from its customers arose. Under Illinois law, although a retailer that does not engage in the business of selling in Illinois is subject to the Use Tax, the retailer is liable for collection and remittance of the Use Tax only when it has nexus—i.e. maintains a place of business in Illinois—at the time of the sale. Once the retailer maintains a place of business in Illinois, the obligation to collect the use tax occurs when the retailer accepts and approves the order submitted by its customer. All of the sales resulting in the assessed tax of \$164,643.46 were accepted and approved before Wayfair maintained a place of business in Illinois.

ARGUMENT

Summary judgment is proper when "the pleadings, depositions, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." 735 ILCS 5/2–1005(c). The interpretation of a statute is a matter of law and is thus appropriate for summary judgment." *Performance Mktg. Ass'n, Inc. v. Hamer*, 2013 IL 114496, ¶ 12, 998 N.E.2d 54, 57 (citing *Village of Chatham, Illinois v. County of Sangamon, Illinois*, 216 Ill.2d 402, 433 (2005)). Summary judgment is appropriate in this case, as there is no dispute of fact and the parties are in agreement that there remains only a single question of the proper interpretation of Illinois statute at issue.

Illinois has two types of taxes that can be imposed on the basis of a retailer's sales: the Retailers' Occupation Tax or the Use Tax. For different reasons, the Department lacked the authority to assess either tax on Wayfair for orders accepted and approved before February 1, 2016 (but for which the products sold were not delivered until after Wayfair had nexus).

The Retailers' Occupation Tax is a sales tax on the retailer on the activities of conducting the business or occupation of selling in Illinois. As such, the Department of Revenue's authority to impose the ROT extends only to those retailers who are in fact conducting the business of selling within Illinois. In other words, while a business may have a physical presence (i.e., nexus) to permit the imposition by the Department of the duty to collect the Use Tax, the Department is authorized to impose the ROT only when the retailer's nexus consists of engaging in selling activities in the State. At the time it processed payment and delivered the products that were part of the orders on which the auditor assessed the ROT, Wayfair was not engaged in the business of

selling in Illinois. Indeed, during the entire audit period, Wayfair did not engage in business of selling in Illinois at all, even though it established nexus in Illinois as of February 1, 2016.

As to the Department's authority to assess the Use Tax, we note the old adage in retail that the customer is always right. While that may not be directly the case here, the customer lies at the core of the dispute between the Department and Wayfair regarding when the Use Tax collection obligation of Wayfair is triggered. In other words, is Wayfair obligated to collect the Use Tax (if it does not become liable for the tax itself) when the sale is accepted and approved? Or does that obligation arise when the products are delivered? Unlike the Retailers' Occupation Tax, the Illinois Use Tax is a tax *on the customer*, not on the retailer. Retailers who have nexus (i.e., maintain a place of business in Illinois within the meaning of 35 ILCS 105/2) are required to collect the Use Tax and facilitate their customer's compliance with the Use Tax by collecting the tax. Retailers who do so *must* notify their customers that they are collecting the tax on the sales invoice. The invoice – the sales contract – binds the retailer and its customer not just to the items sold, but also to the price at which they are sold. It is the customer who approves of the sales price, just as it is the customer who owes the Use Tax in the first place.

The retailer is not the true taxpayer. Unless the retailer has nexus with the state, the retailer does not have the obligation to collect the Illinois Use Tax and its failure to collect the tax does not give rise to any liability of the retailer for not doing so. 35 ILCS 105/3-45. This stands in stark contrast to the ROT, which *can and is* imposed directly on the retailer, regardless of whether the retailer collects the tax from its customers. 86 Ill. Adm. Code 130.101(d) (the ROT “is an occupation tax whose legal incidence is on the seller, rather than on the purchaser.”). A retailer may or may not have nexus with the state at the time of delivery of the products to the customer if the delivery occurs after the sale is accepted and approved. But by then it is too late for the retailer to charge the customer the Use Tax because the customer did not approve charging the customer's credit card for the tax. That is why the Illinois law determines Use Tax collection obligations based on the nexus of the retailer on the date the sale is accepted and approved, or, said another way, when the retailer has the opportunity to collect the tax and the authority of the customer to charge the customer's credit card for the tax.

In contrast to the Use Tax, since the ROT is a tax on the seller for the occupation of selling, and the business of selling can include the processing of payment for orders in Illinois and the delivery of merchandise from inventory in Illinois, 86 Ill. Adm. Code 220.115, then the time for measurement of when the ROT is due is based on when delivery of the merchandise to the customer occurs. *See e.g.*, 86 Ill. Adm. Code 130.101(a)(1) (tax becomes due as of the date the seller receives the receipts for the sale from the purchaser); 86 Ill. Adm. Code 130.201.

A common misconception is that the ROT (Illinois' equivalent of a sales tax) and the Use Tax are interchangeable – complementary taxes names of which are ‘distinctions without differences.’ They are not. Indeed, Illinois' statutes and regulations under the ROT and the Use Tax make these distinctions plain: the ROT is a tax on the seller, and the Use Tax a tax on the purchaser. And yet, the Department relies heavily on this “distinction without a difference” misconception as it performs Cirque du Soleil-like contortions to justify the assessment of tax of \$164,643.46. Although Wayfair processed payment and delivered merchandise when Wayfair had nexus, Wayfair is not liable for the Retailers' Occupation Tax because it was not engaged in selling activities in Illinois. And while Wayfair did have nexus at the time of delivery of products to the customer, the determination of when an obligation to collect the Use Tax arises is based on when

the sale is accepted and approved, which, as stipulated, occurred prior to the time that Wayfair had nexus.

A. Wayfair cannot be held liable for the Retailers' Occupation Tax because it did not engage in the business of selling in Illinois.

The parties stipulated that the Department assessed a Retailers' Occupation Tax. Stip. ¶¶ 4, 5, 8, 9, 18; Ex A. Thus, whether the assessment should be sustained turns on whether Wayfair owed the Retailers' Occupation Tax. Under the law in effect during the assessment period, Wayfair's activities in Illinois did not create any liability for the Retailers' Occupation Tax.

During the taxable periods, Illinois imposed the Retailers' Occupation Tax on "persons engaged in the business of selling at retail tangible personal property" 35 ILCS 120/2. "[T]he business that forms the basis for the tax must be one carried on within [Illinois]." *Ex-Cell-O Corp*, 383 Ill. at 321. 86 Ill. Adm. Code 220.115(b)(1) makes clear that the ROT is due only if the location of the selling activity takes place in Illinois. It provides: "Because the statute imposes a tax on the retail business of selling and not on specific sales, the jurisdiction in which the sale takes place is not necessarily the jurisdiction where the retailers' occupation tax is owed. Rather, it is the jurisdiction where the seller is engaged in the business of selling that can impose the tax." *Id.*

A retailer is deemed to engage in the business of selling "in the taxing jurisdiction where its predominant and most important selling activities take place." 86 Ill. Adm. Code 220.115(b)(7). Selling activities that are considered "primary" include:

- The location from which sales personnel exercise discretion and authority to solicit customers;
- The location from which the seller takes action that binds it to the sale;
- The location where payment is tendered and received;
- The location of inventory, if that inventory is in the retailer's inventory at the time of sale or delivery; and
- The location of the retailer's headquarters.

86 Ill. Adm. Code 220.115(c)(1).

Establishing where a retailer carries on the taxable occupation of selling requires an inquiry into the activities that comprise the business of being a retailer. 86 Ill. Adm. Code 220.115(d)(2); *Hartney Fuel Oil Co. Hamer*, 2013 Ill. 115130 ¶ 32. Where a retailer engages in three or more of the primary selling activities for a particular sale outside of Illinois, the retailer is not subject to the Retailer's Occupation Tax for that sale. 86 Ill. Adm. Code 220.115(c)(2). In this case, Wayfair did not engage in *any* of the selling activities listed in Section 220.115(c)(1), let alone three. Stip. ¶¶ 16, 17.

Wayfair's headquarters are located in Boston, Massachusetts. Stip. ¶ 10. Orders are received and approved, and payment processed, in Massachusetts. Wayfair did not employ sales personnel in Illinois during the taxable periods. Stip. ¶ 34. Wayfair's Illinois customers placed orders for the purchase of tangible personal property over Wayfair's website. Upon approval and fulfillment of the order, Wayfair shipped the sold items to its Illinois customers. Stip. ¶ 25. Wayfair's customers did not pick up items they purchased from Wayfair in Illinois, or otherwise

take possession of the items purchased at places of business owned or leased by Wayfair in Illinois. Wayfair did not fulfill orders from inventory out of its Carol Spring facility or any other location in Illinois.

The icing on the cake of why Wayfair did not engage in retail selling activities in Illinois is the Department's own regulations regarding sales over the Internet. The regulations provide that "[w]hen a customer places an order for the purchase of tangible personal property through a consumer-based retailer website available without limitation on the world wide web and the retailer ships the property to the customer in this State, the Department will presume that the retailer's predominant selling activities take place outside of this State." 86 Ill. Adm. Code 220.115(d)(3). The only conclusion to be reached is that where the company is an eCommerce retailer (as is Wayfair) operating, fulfilling, and shipping purchased items from outside of Illinois, the seller's "selling activity occurs outside of Illinois" and its "sales are not subject to the [Retailers Occupation Tax]." Ill. Dept. Rev. ST-21-0035 (Sept. 9, 2021).

Wayfair's sales to Illinois residents are "Sales over the Internet." 86 Ill. Adm. Code 220.115(d)(3); Stip. ¶ 27. Both parties agree that all orders were processed and fulfilled outside of Illinois, from inventory stored outside of Illinois. Stip. ¶ 24, 25. As a sale over the Internet, Wayfair's predominate selling activities are presumed to take place – and in fact did take place – outside of Illinois.

Wayfair was not engaged in the business of selling *in Illinois* and for that reason is not subject to the Retailers' Occupation Tax. Because the assessment was of Retailers' Occupation Tax (Stip. ¶ 9), the assessment must be abated.

B. Wayfair is not liable for any Use Tax assessment of \$164,641.46 because it did not maintain a place of business in Illinois at the time the customers submitted their orders and Wayfair accepted and approved of the orders.

In effect, the Department seeks to rewrite the assessment to convert it from an assessment of Retailers' Occupation Tax to that of a Use Tax. It is too late in the day to do so, particularly in light of the extensive delays the Department has caused in obtaining resolution of the case. Yet, even if the Department is allowed, in effect, to reassess the Use Tax rather than the Retailers' Occupation Tax for the sales accepted and approved prior to February 1, 2016, Wayfair is not liable for the Use Tax because it did not have nexus with Illinois at the time any obligation to collect the tax arose.

The Use Tax is imposed on the customer for "the privilege of using ... tangible personal property purchased at retail from a retailer". 35 ILCS 105/3-3. Only retailers who maintain a place of business in Illinois at the time of the taxable transaction are obligated to collect the Use Tax from Illinois customers. A "Retailer maintaining a place of business in this State" consists of a retailer maintaining an office, a subsidiary, an office, a distribution house, a sales house, a warehouse, or another place of business; an agent or representative; or entering into a contract with a person located in Illinois to which the retailer pays a commission or other consideration. 35 ILCS 105/2.

Retailers who maintain a place of business in Illinois are obligated to "collect the [use] tax from users by *adding the tax to the selling price* of the tangible personal property...." 35 ILCS 105/3-45 (emphasis added). For Internet sales, such as those at issue in this case, the customer

places an order through the retailer's (in this case Wayfair's) website. The customer's willingness to make a purchase – to enter into a sales contract with Wayfair—is based in part on Wayfair's full disclosure of the selling price for the products that the customer seeks to purchase. Wayfair issues – and indeed every ecommerce retailer issues – an invoice to its customers at the time the customer commits to the sale. Retailers responsible for collecting the Use Tax are required to disclose to the customer *on the invoice* the tax, if any, that is due and obtaining the customer's agreement to the terms of the sale, including the products to be sold and the total selling price for the products. 86 Ill. Admin. Code 150.601; Ill. Dept. Rev. GIL 2002-0213 (Sept. 25, 2002) (“Retailers should not be cavalier about this obligation, as retailers are generally required to state the selling price and the tax *on the invoice* as a separate item and to collect the tax exactly at the applicable rate.” (emphasis added)). The only time that the seller can add the tax to the selling price to be disclosed to the customer is when the customer submits the order. *When* a retailer performs on the sale—delivery of the merchandise—occurs is immaterial to when the sale is accepted and the tax can be added to the sales price. Thus, under the Use Tax Act, a retailer's obligation to collect Use Tax is triggered at the point the purchaser's order is accepted and approved because that is the point at which both the seller and the customer bind themselves to the sale terms, including the selling price and the Use Taxes thereon.

The Department's own regulations support the conclusion that the time for sale, and therefore the time the retailer becomes obligated to collect the use tax if it has nexus, is the date for determination of whether the retailer maintains a place of business in Illinois. The regulations provide that a retailer is obligated to report the Use Tax as a separate line item *on the receipt* issued to its customer in order to notify the customer that tax has been collected. 86 Ill. Admin. Code 150.1305(b). The receipt is issued when the order is submitted and accepted and approved, and not the later time of when delivery occurred. A retailer may or may not have nexus on the date of delivery. The event that gives rise to the nexus may occur before or after delivery. A retailer cannot magically redo the sales transaction—the submission of the order and the acceptance of the order—if delivery occurs. And if the retailer collected the Use Tax based on the prediction that the retailer would establish a place of business in Illinois, assuming delivery would occur after that date, but delivery in fact occurs before the retailer established nexus, the retailer would have collected the tax without the state's authorization to do so.

When Wayfair accepted and approved the orders from its customer and obtained the customer's payment information, it informed the customer of the sales price that the customer would be charged. Stip. ¶20. In states where Wayfair has nexus at the time it accepts and approves the order, Wayfair includes applicable sales or use taxes. *Id.* For the transactions at issue, the sales price did not include tax because Wayfair did not have nexus at the time it accepted and approved the orders. It neither had the obligation to collect to tax on behalf of the state where it did not have nexus at the time the orders were received, accepted and approved, nor the authority from the customer to charge the customer for the tax if it had nexus when delivery occurred. Stip. ¶22. It simply did not know whether it would have nexus at the point of delivery.

Unlike the sales tax, the Use Tax is not an obligation of the seller. It is the customer's obligation, and Wayfair simply acts as an agent to make payment of the tax. As discussed above, Wayfair is unable to recover the tax from the true taxpayer—its customer—because it wasn't authorized to do so at the time it accepted and approved the customer's order and issued its invoice to the customer. Indeed, if it had indicated Use Tax prior to February 1, 2016, when it did not

have nexus, it would have been acting contrary to the law, which requires registration as a basis for tax collection.

Only such retailers who maintain a place of business in Illinois must collect the Use Tax from the purchaser. 35 ILCS 105/3-6, 105/3-45. As stipulated by the parties, Wayfair did not maintain a place of business in Illinois prior to February 1, 2016, when the sales in dispute were accepted and approved. Thus, even if the Assessment can be reissued, in effect, as an assessment of Use Taxes, it is invalid because Wayfair did not maintain a place of business in Illinois at the time of the acceptance and approval of the sale.

Finally, we should note that the assessment cannot be reconceived as an assessment of a different tax type than the one stated on the notice without violating Wayfair's rights under the Taxpayer Bill of Rights. The Taxpayer Bill of Rights guarantees that the state will identify the tax type being assessed, with an explanation of the tax, penalties, and interest, to any and all taxpayers. 20 ILCS 2520/4(b). Thus, upholding this assessment, on the after-the-fact basis that what was assessed was a Use Tax would be to deprive Wayfair of the notice Wayfair was entitled to receive.

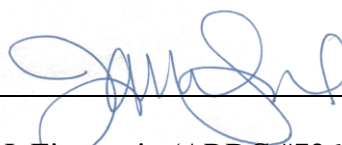
CONCLUSION AND RELIEF REQUESTED

Because Wayfair's primary selling activities did not occur in Illinois, Wayfair is not liable for the assessment of the Retailers' Occupation Tax of \$164,643.46. Likewise, because Wayfair did not maintain a place of business in Illinois at the time the sales were accepted and approved, the assessment of \$164,643.46 is not justified as an assessment of Use Tax.

For all the reasons addressed above, Wayfair requests that this Tribunal abate the portion of the assessment that relates to sales accepted and approved prior to February 1, 2016, in the amount of \$164,643.46, plus interest thereon. Pursuant to 20 ILCS 2520/7, Wayfair also requests recovery of attorneys' fees and costs incurred to pursue this appeal, especially in light of the delays on the part of the Department in litigating this case.

WAYFAIR LLC

By: _____



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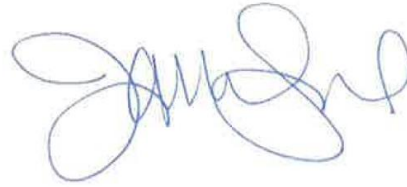
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CERTIFICATE OF SERVICE

On October 6, 2022 a copy of the foregoing *Brief of the Petitioner* was served via electronic mail on the following counsel of record in this matter:

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