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Taxing Remote Sales in the Digital Age: A Global Perspective

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TAXING REMOTE SALES IN THE DIGITAL AGE: A GLOBAL PERSPECTIVE

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TABLE OF CONTENTS

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INTRODUCTION

The challenges associated with the taxation of remote sales in the digital age are global.[1] Providing a global perspective on these

1. *See, e.g.*, ORG. FOR ECON. CO-OPERATION & DEV., ADDRESSING THE TAX CHALLENGES OF THE DIGITAL ECONOMY 121 (2015) [hereinafter OECD, FINAL REPORT] (discussing the challenges of collecting value added taxes (VATs) on "[r]emote digital supplies to consumers"). There is no universally accepted understanding of the term "remote sale" or "remote supply." In principle, one might view a food order from Fresh Direct as a remote sale, because a remote sale might be defined as a sale effectuated by any means other than at a physical store (for example, over the telephone or the Internet). For purposes of this Article, however, it makes more sense to consider a remote sale as a *cross-border* sale, effectuated by mail, telephone, computer, the Internet, etc., with respect to which the seller is *physically remote* from the purchaser's jurisdiction. *See* Remote Transactions Parity Act of 2015, H.R. 2775, 114th Cong. § 4(8)–(9) (2015) (defining "remote sale" to mean "a sale that originates in one [s]tate and is sourced to another [s]tate" and defining "remote

challenges is therefore appropriate, even for a symposium addressed primarily to such challenges under the U.S. subnational retail sales tax.[2] Although the challenges associated with the taxation of remote sales in the digital age are global, the regimes that tax such sales are not. Accordingly, insofar as one looks to the implications of the global perspective on taxing remote sales in the digital age for guidance on U.S. subnational taxation of such sales, one should never lose sight of the contextual differences between the global and subnational tax regimes to avoid "lost in translation" problems.[3]

This Article addresses three fundamental questions raised by the taxation of remote sales in the digital age from a global perspective, but focuses on the implications, if any, of the answers to these questions in the global context for the U.S. subnational retail sales tax. First, should remote sales be taxed under a consumption tax? Second, if the answer to the first question is "yes," where should such sales be taxed? Third, how can remote sales be taxed effectively under a consumption tax in the digital age?[4]

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seller" to mean "a person that makes remote sales in the [s]tate without a physical presence"); Marketplace Fairness Act of 2015, S. 698, 114th Cong. § 4(5) (2015) (defining "remote sale" as "a sale into a [s]tate . . . in which the seller would not legally be required to pay, collect, or remit [s]tate or local sales and use taxes unless provided by this Act").

2. Agenda, American University Law Review Symposium: Taxing Remote Sales in the Digital Age (Nov. 13, 2015), http://americanuniversitylawreview.org/images/Vol._65_Annual_Symposium_Agenda.pdf.

3. *Cf.* Walter Hellerstein & Charles E. McLure, Jr., *Lost in Translation: Contextual Considerations in Evaluating the Relevance of U.S. Experience for the European Commission's Company Taxation Proposals*, 58 BULL. FOR INT'L FISCAL DOCUMENTATION 86, 86 (2004) (discussing the contextual differences between the U.S. and EU experiences with devising a tax regime when addressing the determination of a tax base, the definition of the group whose income is to be taxed, the formula used to apportion income, and other administrative issues).

4. This Article draws freely from my (and, where pertinent, my co-author's or co-authors') work in this area, including ARTHUR COCKFIELD ET AL., TAXING GLOBAL DIGITAL COMMERCE (2013); JEROME R. HELLERSTEIN, WALTER HELLERSTEIN & JOHN A. SWAIN, STATE TAXATION (3d ed. 2013 & Supp. 2016); Walter Hellerstein, *A Hitchhiker's Guide to the OECD's International VAT/GST Guidelines*, 18 FLA. TAX REV. 589 (2016) [hereinafter Hellerstein, *Hitchhiker's Guide*]; Walter Hellerstein, *Consumption Taxation of Cross-border Trade in Services in an Age of Globalization*, *in* GLOBALIZATION AND ITS TAX DISCONTENTS: TAX POLICY AND INTERNATIONAL INVESTMENTS 305 (Arthur J. Cockfield ed., 2010); Walter Hellerstein, *Exploring the Potential Linkages Between Income Taxes and VAT in a Digital Global Economy*, *in* VAT/GST IN A GLOBAL DIGITAL ECONOMY 83, 87 (Michael Lang & Ine Lejeune eds., 2015); Walter Hellerstein, *Jurisdiction to Tax in the Digital Economy: Permanent and Other Establishments*, 68 BULL. FOR INT'L TAX'N 346 (2014) [hereinafter Hellerstein, *Permanent and Other Establishments*]; Walter Hellerstein & Timothy H. Gillis, *The VAT in the European Union*, 127 TAX NOTES 461

I. SHOULD REMOTE SALES BE TAXED UNDER A CONSUMPTION TAX?

A. *The Global Perspective*

As a theoretical matter, it is difficult to imagine how the answer to the question of whether remote sales should be taxed under a consumption tax could be anything other than "yes." This is so for the simple reason that a good consumption tax should tax consumption. A broad-based consumption tax[5] generally measures taxable consumption by reference to purchases of goods and services for consumption, that is, by sales to private consumers.[6] Whether goods and services are acquired through a local or cross-border sale has no relevance to the determination of whether the sale is for consumption to a private consumer. Moreover, failing to tax remote sales for consumption while taxing local sales for consumption would violate the fundamental principles of economic neutrality that "[t]axation should . . . be neutral . . . between conventional and electronic forms of commerce" and that "[t]axpayers in similar situations carrying out similar transactions should be subject to similar levels of taxation."[7]

(2010); Walter Hellerstein & Harley Duncan, *VAT Exemptions: Principles and Practice*, 128 TAX NOTES 989 (2010); Michael Keen & Walter Hellerstein, *Interjurisdictional Issues in the Design of a VAT*, 63 TAX L. REV. 359 (2010).

5. A broad-based consumption tax is distinguishable from an excise tax, which "target[s] . . . specific forms of consumption such as [taxes on] the purchase of gasoline or alcohol." ORG. FOR ECON. CO-OPERATION & DEV., INTERNATIONAL VAT/GST GUIDELINES 11 (2015) [hereinafter OECD, VAT/GST GUIDELINES].

6. In other words, no effort is made to measure consumption directly, as, for example, by tracking the actual use of goods and services. Rather, a broad-based consumption tax is based on "proxies" for consumption and may be more accurately characterized as a tax on "consumption expenditure" rather than on consumption itself. ARTHUR COCKFIELD ET AL., TAXING GLOBAL DIGITAL COMMERCE, *supra* note 4, at 79.

7. OECD, VAT/GST GUIDELINES, *supra* note 5, at 13–14 (quoting ORG. FOR ECON. CO-OPERATION & DEV., TAXATION AND ELECTRONIC COMMERCE: IMPLEMENTING THE OTTAWA TAXATION FRAMEWORK CONDITIONS 230 (2001) [hereinafter OECD, TAXATION AND ELECTRONIC COMMERCE]).

B. *Implications of the Global Perspective for the U.S. Subnational Retail Sales Tax*

1. *Can the U.S. retail sales tax reasonably be characterized as a broad-based consumption tax?*

The implications for the U.S. subnational retail sales tax[8] (the "U.S. RST") of any conclusions drawn in the global context about the appropriate design of a broad-based consumption tax depend, at least in part, on the answer to the threshold question of whether the U.S. RST reasonably can be characterized as a broad-based consumption tax. If one regards the U.S. RST as a feature of "American exceptionalism,"[9] and, accordingly, that the U.S. RST has no theoretical relationship to other broad-based taxes on consumption, then one can bring this inquiry to an abrupt—and, in this Author's judgment, premature—halt. If the U.S. RST cannot be considered, at least in principle, to be a broad-based consumption tax, then normative criteria, international or otherwise, informing the design of broad-based consumption taxes are simply beside the point.

The better view, however, is that the U.S. RST should be viewed as a broad-based consumption tax, albeit one that is deeply flawed from a normative perspective. In principle, a broad-based consumption tax should tax all final consumption by households and should not tax businesses.[10] Although no state has adopted a theoretically pure

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8. References to the U.S. retail sales tax ("U.S. RST") include both the retail "sales tax," which is imposed on sales that occur within the state, as well as the "use tax," which is imposed on the use within the state of taxable items that are sold outside the state. *See generally* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, at ch. 16 (providing an overview of use tax, its relationship to the sales tax, and addressing issues arising under use tax statutes).

9. This term refers to the notion that the United States is inherently different from other countries. *See American Exceptionalism*, NEW WORLD ENCYCLOPEDIA, http://www.newworldencyclopedia.org/entry/American_exceptionalism (last visited May 17, 2016) (defining American exceptionalism as "the belief that the United States differs qualitatively from other developed nations because of its national credo, historical evolution, or distinctive political and religious institutions" and providing a historical description, general overview, and critique of American exceptionalism).

10. OECD, VAT/GST GUIDELINES, *supra* note 5, at 11. By saying that a broad-based consumption tax "should not tax business," this Article means only that the final burden of the tax "should not rest on businesses . . . because businesses . . . are incapable of final or household consumption." *Id.* This is not the same thing as saying that businesses are not involved in the tax collection process. Indeed, under the staged-collection process that is the central feature of VATs, the most widely adopted form of broad-based consumption taxation in the global context, businesses in fact pay the tax but are, in principle, relieved of the tax burden because they are entitled to credit the tax they have paid on their inputs against the tax they collect on

RST, all states have provisions that are designed to tax private consumption and to limit the tax on business purchases.[11] Every state RST excludes sales for resale from the tax base.[12] Similarly, states commonly exclude sales of ingredients or components of property produced for sale from the RST.[13] These types of exclusions typically require that the business input retain its physical form as it moves through the production process. Other provisions, such as the exemption for purchases of machinery and equipment, reflect the broader view that all business inputs should be excluded from the RST base, even though such costs cannot be tied directly to the item ultimately sold or to some component of that item. These sorts of provisions include exclusions or exemptions for purchases of machinery and equipment used to produce tangible personal property for sale.[14]

U.S. RSTs also share a number of administrative features that reflect, and in some cases are intended to further, the underlying philosophy of the tax as a levy imposed on the purchaser's use or consumption of the item sold, with the tax burden resting on the consumer.[15] To make it more likely that the economic incidence of the tax is borne by the consumer, U.S. RSTs are usually separately stated, and most states prohibit vendors from advertising that they will absorb the tax.[16] Furthermore, the tax itself is excluded from the

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their outputs. The RST differs from the VAT in that it is a single-stage levy imposed in theory only at the point of final sale. *See id.* (illustrating the theoretical differences and similarities between VATs and RSTs); *see also infra* Appendix A (demonstrating the way in which businesses "credit" the tax paid on their inputs).

11. *See* John L. Mikesell, *A Quality Index for State Sales Tax Structure—Measuring the States Against an Ideal Standard*, 35 ST. TAX NOTES 129, 130–31 (2005) (performing a state-by-state analysis comparing each state's existing sales tax to a proposed normative standard).

12. 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 14.02.

13. *Id.* ¶ 14.03.

14. *Id.* ¶ 14.05[1] (explaining how exemptions and lower tax rates for manufacturing machinery and equipment help "avoid pyramiding of the tax" and encourage industrial expansion).

15. JOHN F. DUE & JOHN L. MIKESELL, SALES TAXATION: STATE AND LOCAL STRUCTURE AND ADMINISTRATION 16, 30 (2d ed. 1994).

16. *Id.* at 30. These provisions, of course, cannot repeal the law of supply and demand, which determines the economic incidence of a tax; they can only encourage the vendor to shift the tax to the consumer. *See* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 12.03 (explaining how supply and demand affects the burden of the "sales tax[] on consumer purchases"). A vendor can always undercut the purpose of these provisions by reducing the base price of an item to offset the amount of the sales tax. *Id.*

base of the tax. In addition, U.S. RSTs are collected from the purchaser by the seller and are imposed on a transaction-by-transaction basis. These features effectuate the understanding that the sales tax is a discrete charge, apart from the price of an item, that is paid by the consumer and collected by the vendor.

To be sure, the U.S. RST fails in two fundamental respects to conform to the normative ideal of a broad-based consumption tax. First, the U.S. RST base includes a substantial portion of business purchases in the tax base, generally estimated to comprise forty percent of the RST base.[17] Second, the U.S. RST generally fails to include services in the tax base, thus failing to capture an increasingly important component of household consumption.[18] That said, it is nevertheless appropriate to view the U.S. RST as a broad-based consumption tax, because such a view is consistent with the overall design of the tax, and most of the tax base is comprised of household consumption. Moreover, insofar as the U.S. RST's deviations from the norm of a sound consumption tax bear on the inquiry that lies at the heart of this Article—whether, where, and how remote sales should be taxed in the digital age—the ensuing analysis takes those deviations into consideration.

2. *Should remote sales be taxed under the U.S. RST?*

Once one determines that it is appropriate to view the U.S. RST as a broad-based consumption tax, the implications of the guidance provided by the global perspective are clear. Remote sales should be taxed under the U.S. RST. There is nothing surprising about this conclusion. As Charles McLure and this Author have observed elsewhere:

> An economically neutral tax system would not interfere with market choices—choices of what to consume and produce and how

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17. 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 12.03 & n.29 (citing Robert Cline et al., *Sales Taxation of Business Inputs: Existing Tax Distortions and the Consequences of Extending the Sales Tax to Business Services*, 35 ST. TAX NOTES 457 (2005); John L. Mikesell, *The Disappearing Retail Sales Tax*, 63 ST. TAX NOTES 777, 781 (2012) (estimating that the median share of total sales tax base represented by business purchases is 41.1%); Raymond J. Ring, Jr., *Consumers' Share and Producers' Share of the General Sales Tax*, 52 NAT'L TAX J. 79 (1999); Raymond J. Ring, Jr., *The Proportion of Consumers' and Producers' Goods in the General Sales Tax*, 42 NAT'L TAX J. 167, 175 (1989); Alan D. Viard, *Sales Taxation of Business Purchases: A Tax Policy Distortion*, 56 ST. TAX NOTES 967 (2010)).

18. *See* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 12.05 (explaining how failing to tax services violates basic normative principles of consumption tax design).

> to organize and finance production and distribution. A neutral system of sales taxation would follow these four tenets: (a) *all sales to consumers would be taxed uniformly*; (b) all sales to business would be exempt; (c) *these rules would apply whether sales were made by in-state vendors or by out-of-state vendors*; and (d) the system would be simple—or at least as simple as possible, consistent with other objectives.[19]

II. WHERE SHOULD REMOTE SALES BE TAXED UNDER A CONSUMPTION TAX?

A. *The Global Perspective*

The Organization for Economic Co-operation and Development's (OECD's) recently issued *International VAT/GST Guidelines*[20] ("Guidelines"), which are designed for "broad-based taxes on final consumption collected from, but in principle not borne by, businesses through a staged collection process,"[21] reflect the global standard for determining the appropriate place of taxation for cross-border sales (including remote sales) under a consumption tax. Equating global standards for consumption taxes with global standards for value added taxes (VATs) reflects political and economic reality because the overwhelming majority of countries in the world have adopted VATs as a national consumption tax.[22] The

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19. Charles E. McLure, Jr. & Walter Hellerstein, *Congressional Intervention in State Taxation: A Normative Analysis of Three Proposals*, 31 ST. TAX NOTES 721, 727 (2004) (emphasis added).

20. OECD, VAT/GST GUIDELINES, *supra* note 5. In November 2015, the Guidelines were released in their consolidated form at the OECD Global Forum on VAT in Paris, France. *Third Meeting of the OECD Global Forum on VAT*, OECD, http://www.oecd.org/ctp/consumption/vat-global-forum.htm (last visited May 17, 2016). A number of countries, including Australia, Canada, and New Zealand, refer to their VATs as goods and services taxes (GSTs). For ease of reading, throughout the ensuing discussion (as throughout the OECD's Guidelines), the term VAT is generally used to describe all value added taxes, however denominated. OECD, VAT/GST GUIDELINES, *supra* note 5, at 9 n.1. It is worth noting that the Guidelines comprise not only individual, numbered Guidelines, but also a discussion of general VAT principles, explanations of individual Guidelines, extensive commentary, and other guidance, which is referred to collectively throughout this Article as the "Guidelines." References to specific Guidelines are referred to by their individual number.

21. OECD, VAT/GST GUIDELINES, *supra* note 5, at 10.

22. ORG. FOR ECON. CO-OPERATION & DEV., CONSUMPTION TAX TRENDS 14 (2014), http://www.oecd.org/tax/consumption-tax-trends-19990979.htm. The OECD lists 164 countries with VATs. *Id.* at 171. Although sources disagree on the precise number of countries in the world, the United Nations system classifies 195 countries between 193 member states and two non-member observer states (the Holy See and the State of Palestine). *See How Many Countries Are in the World?*, WORLDATLAS,

ensuing "global perspective" on where remote sales should be taxed under a consumption tax therefore describes the broad guidance that the OECD Guidelines provide for the application of the VAT to cross-border sales. The principal focus of the Guidelines is trade in services and intangibles, as distinguished from trade in goods, because the need for guidance with respect to trade in services and intangibles was most pressing.[23] However, the Guidelines' broad principles, including core features of value added taxes[24] and neutrality in the context of cross-border trade,[25] apply to all cross-border trade, including trade in goods.

1. VATs and cross-border trade: The destination principle

The fundamental design question regarding the VAT and cross-border trade is whether the VAT should be imposed by the jurisdiction of origin or destination. The Guidelines explain that, "[u]nder the destination principle, tax is ultimately levied only on the final consumption that occurs within the taxing jurisdiction."[26] By contrast, "[u]nder the origin principle, the tax is levied in the various jurisdictions where the value was added."[27] There are theoretical economic arguments that can be advanced in favor of either the destination or the origin principle,[28] with the former placing all firms competing in a given jurisdiction on an even footing and the latter placing consumers in different jurisdictions on an even footing. When it comes to the question of the choice between these two principles, however, "economic theory . . . gives a reasonably clear answer," namely, that "the destination principle is noticeably the more attractive."[29] As the Guidelines observe:

> The application of the destination principle in VAT achieves neutrality in international trade. Under the destination principle, exports are not subject to tax with refund of input taxes (that is,

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http://www.worldatlas.com/nations.htm (last visited May 17, 2016) (explaining that the number of countries in the world ranges from 189 to 196 independent countries, depending on the source).

23. OECD, VAT/GST GUIDELINES, *supra* note 5, at 9.

24. *See id.* at 11–14 (providing an overview of the core features of a VAT, such as the staged-collection process and the destination principle).

25. *See id.* at 15 (explaining the importance of tax neutrality and how the VAT works to achieve this goal).

26. *Id.* at 12.

27. *Id.*

28. *See* Keen & Hellerstein, *supra* note 4, at 360–66 (describing arguments in favor of both the destination and origin principle for the VAT).

29. *Id.* at 362.

> "free of VAT" or "zero-rated") and imports are taxed on the same basis and at the same rates as domestic supplies. Accordingly, the total tax paid in relation to a supply is determined by the rules applicable in the jurisdiction of its consumption and all revenue accrues to the jurisdiction where the supply to the final consumer occurs.[30]

Moreover, the destination principle is the norm in international trade, is sanctioned by World Trade Organization Rules,[31] and reflects rules generally in force under most existing VATs. Accordingly, the Guidelines, in accord with the widespread international consensus, embrace the destination principle as the basic rule for application of the VAT to international trade.[32]

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30. OECD, VAT/GST GUIDELINES, *supra* note 5, at 12. VATs typically use the terms "supply" and "supplier" to designate, respectively, the transaction that is potentially subject to the tax and the person effecting the potentially taxable transaction, rather than the terms "sale" and "seller," which may be more familiar to the American reader. It may be worth observing that there is more than one way of implementing the destination principle. Although the Guidelines describe the "standard way" of doing so, "[o]ne could also envisage, for instance, the exporting country charging tax on exports just as it does on all domestic sales, with the importing country allowing this as a credit against its own tax charge." Keen & Hellerstein, *supra* note 4, at 360.

31. Agreement on Subsidies and Countervailing Measures art. 1, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 14 n.1 (providing "the exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy").

32. OECD, VAT/GST GUIDELINES, *supra* note 5, at 12–13. The Guidelines' broad embrace of the destination principle clearly applies to trade in both goods *and* services, *id.* at 13, even though the individual place-of-taxation rules are directed *only* at trade in services and intangibles. *See supra* note 23 and accompanying text (explaining the Guidelines' principal focus being on services and intangibles). The individual place-of-taxation rule embracing the destination principle provides: "For consumption tax purposes[,] internationally traded services and intangibles should be taxed according to the rules of the jurisdiction of consumption." OECD, VAT/GST GUIDELINES, *supra* note 5, at 27. The Guidelines' articulation of the destination principle in Guideline 3.1 contains a slight variation from the original, and more straightforward, statement of the principle in the OECD's seminal report that delineated the overarching principles that should inform the development of rules to govern consumption taxes in the electronic age. OECD, TAXATION AND ELECTRONIC COMMERCE, *supra* note 7, at 228–34. The original statement provided: "Rules for the consumption taxation of cross-border trade *should result in taxation* in the jurisdiction where consumption takes place." *Id.* at 231 (emphasis added). The change implicitly addresses the situation of the United States, the only OECD Member State without a VAT. According to U.S. national rules, consumption *should not* "result in taxation" in the jurisdiction where consumption takes place, because the United States has no national broad-based consumption tax.

B. *Implications of the Global Perspective for the U.S. Subnational Retail Sales Tax*

Based on our operating premise that the U.S. RST may be treated as a broad-based consumption tax,[33] the global principles regarding where cross-border sales (including remote sales[34]) should be taxed for consumption tax purposes would presumably provide instructive guidance for the U.S. RST as well. However, there is an additional issue that must be addressed before one can invoke the global perspective reflected in the OECD's *International VAT/GST Guidelines* as guidance for analogous issues arising under the U.S. RST. Because the Guidelines are designed for VATs, i.e., consumption taxes collected "through a staged collection process," they technically "do not apply to single-stage consumption taxes charged only once to the end user at the final point of sale, such as retail sales taxes."[35] These structural differences between VATs and RSTs arguably render the Guidelines' guidance as to where certain cross-border sales should be taxed for VAT purposes inapplicable to the U.S. RST.

Although there may be some merit to this point when it comes to individual place-of-taxation rules that implement the destination principle,[36] the Guidelines' broad endorsement of the destination principle as the fundamental standard for application of consumption taxes to cross-border trade is relevant to RSTs as well as to VATs, which, at least in their ideal form, are theoretically equivalent and produce identical outcomes.[37] Indeed, most U.S. RSTs, like most VATs, embrace the destination principle as the basic rule for applying the tax to cross-border trade, at least with respect to the sale of goods.[38] "Imports" shipped from outside the state to purchasers within the state are generally subject to sales or use tax in

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33. *See supra* Section I.B.1 (explaining that the U.S. RST should be viewed as a broad-based consumption tax).

34. Remote sales are a subset of cross-border sales (namely, cross-border sales with respect to which the seller has no physical presence in the jurisdiction of the purchaser). *See supra* note 1 and accompanying text (defining "remote sale" for purposes of this Article).

35. OECD, VAT/GST GUIDELINES, *supra* note 5, at 10.

36. *See infra* Section III.A.3 (describing the VAT/GST Guidelines' individual place-of-taxation rules implementing the destination principle).

37. *See infra* Appendix A (demonstrating the equivalence between theoretically ideal VATs and RSTs).

38. This generalization does not apply to the sale of services as explained in the next paragraph.

the state of destination,[39] and "exports" shipped from within the state to purchasers outside the state are generally exempt from sales or use tax in the state of origin.[40]

There are, however, several caveats to the foregoing generalization in light of the flaws in the U.S. RST[41] when viewed from the perspective of an ideal consumption tax. First, to the extent that the U.S. RST fails to tax services sold to private consumers, it obviously fails to tax consumption where it is presumed to occur, because it fails to tax it at all. Moreover, the U.S. RST's application of the

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39. If the sale occurs within the state, the sales tax will apply; if the sale occurs outside the state or in interstate commerce, the use tax will apply. *See* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶¶ 16.01[2], 18.02[2] (providing an overview of sales and use taxes as applied to cross-border trade in the United States); *supra* note 8 and accompanying text (describing the relationship between sales taxes and use taxes in the U.S. RST).

40. This Article uses the term "imports" and "exports" in this context to signify goods shipped from or to other states or countries. The U.S. Supreme Court has confined the meaning of the term "Imports" and "Exports" in the Import-Export Clause of the Constitution, which bars "Imposts" or "Duties" on "Imports" or "Exports," U.S. CONST. art. I, § 10, cl. 2, to foreign imports and exports. *See* 1 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 5.01 (discussing the Court's decision in Woodruff v. Parham, 75 U.S. (8 Wall.) 123 (1868)). This Article uses the term "exempt" in the American sense of being free from tax, not in the sense used under many VATs as meaning free from output tax, but nevertheless subject to input tax. In VAT parlance, "[a]n exemption occurs when output is untaxed but input tax is not recoverable." LIAM EBRILL ET AL., THE MODERN VAT 83 (2001). "By contrast, when output is untaxed and input tax *is* recoverable, the transaction would be characterized as 'zero-rated' or an 'exemption *with input tax credit*.'" Hellerstein & Duncan, *supra* note 4, at 990 n.7 (first emphasis added). For the American mindset, this is a significant difference that needs to be understood fully. In the context of the U.S. RST, tax professionals and taxpayers tend to think of exemptions from the purchaser's point of view, as the exempt purchaser enjoys an economic benefit, and there is no self-evident adverse impact on the seller. *Id.* at 990 n.8. *But see* Walter Hellerstein, *Comparing the Treatment of Charities Under Value Added Taxes and Retail Sales Taxes*, *in* VAT EXEMPTIONS: CONSEQUENCES AND DESIGN ALTERNATIVES 175, 178, 184 (Rita de la Feria ed., 2013) (noting that exemptions for charities in the U.S. RST stem from the idea that imposing a consumption tax on charities' sales would undermine the government's policy of encouraging charitable activities). In a VAT system, however, the supplier who makes exempt sales—as distinguished from making zero-rated sales—is saddled with the burden of the VAT, at least as a legal matter. As an economic matter, of course, the extent to which the exempt seller can pass the burden of the VAT on to its purchasers (or pass it back to its suppliers) is a different question that turns on the cross-elasticities of supply and demand in the relevant market for the supplies in question.

41. *See supra* Section I.B.1 (discussing the U.S. RST's failure conform to the norm of an ideal broad-based consumption tax because of its exclusion of many services and its substantial taxation of business purchases).

destination principle to the sale of services that it does tax is much less consistent than it is with respect to the sale of goods.[42] Second, insofar as the U.S. RST taxes business purchases (without any credit for or refund of taxes paid, as under a VAT[43]), the role, if any, of the destination principle with respect to such transactions raises a number of theoretical and practical questions that are explored in more detail below.[44]

III. IMPLEMENTING THE DESTINATION PRINCIPLE

Adoption of the destination principle as a theoretical norm for taxing consumption is just the starting point for applying consumption taxes to cross-border trade. *Implementing* that principle—specifically, adopting practical place-of-taxation rules that identify the jurisdiction where final consumption occurs—raises a host of additional questions because "in many (if not most) cases[,] consumption is not directly observable," and identification of the jurisdiction in which final consumption occurs can be effectuated only through proxies that reflect one's "best guess" as to where final consumption is likely to occur.[45]

A. The Global Perspective

1. Trade in goods: An overview

Implementing the destination principle with respect to cross-border trade in goods is relatively straightforward based on the assumption that the destination of goods, as determined by physical flows, is a reasonable proxy for where consumption of the goods is likely to occur. Accordingly, when the seller of goods is in one jurisdiction and the purchaser is in another, the goods are generally taxed where they are delivered.[46] To accomplish this goal, exported goods are commonly zero-rated, meaning that no tax is collected on

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42. *See* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 18.05 (explaining that some states tax the sale of services based on where the service is performed, as distinguished from where the services are delivered or consumed).

43. Under a VAT, if the tax collected by the business on its sales is less than the tax paid on its purchases, the business taxpayer can, in principle, recover the difference from the taxing authority in the form of a refund. OECD, VAT/GST GUIDELINES, *supra* note 5, at 11–12.

44. *See infra* Sections IV.A.3.b and IV.B (discussing the application of the destination principle to business-to-business ("B2B") transactions in the context of VATs and the U.S. RST, respectively).

45. Keen & Hellerstein, *supra* note 4, at 367.

46. OECD, VAT/GST GUIDELINES, *supra* note 5, at 12.

the sale,[47] and imported goods are taxed at the border.[48] For the most part, border controls provide an effective mechanism for ensuring collection of VATs on cross-border supplies of goods at their destination.[49] In addition, the implementation of the destination principle is often facilitated in the business-to-business ("B2B") context by "reverse charge" mechanisms pursuant to which registered business purchasers, who are subject to control and audit by taxing authorities at the goods' destination, self-assess the VAT.[50] This is currently the case for trade in goods between Member States in the European Union (EU). In the EU, goods are zero-rated in the exporting Member State, and importing registered traders then account for import VAT not at the border but in their first periodic return, at which point they both charge themselves tax and claim any credit due against sales.[51]

This is not to suggest that the destination principle as applied to goods creates no difficulties. Zero-rating of exports can lead to fraud,[52] causing a loss of revenue when goods that are purportedly exported are in fact sold locally and traders claim input tax refunds on the purported exports.[53] If border controls are not airtight, and sometimes even if they are, individual consumers can avoid the

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47. When goods are "zero-rated," the goods are taxed at a rate of zero, and therefore no tax is collected on the sale, Hellerstein & Duncan, *supra* note 4, at 991, but, in contrast to an "exempt" sale, the seller is entitled to input tax credits associated with the goods that are sold. *See supra* Section I.B.1.

48. *See* Walter Hellerstein, *Jurisdiction to Tax Income and Consumption in the New Economy: A Theoretical and Comparative Perspective*, 38 GA. L. REV. 1, 28–29 (2003) [hereinafter Hellerstein, *Jurisdiction to Tax Income and Consumption in the New Economy*] (noting the use of border controls as an effective mechanism for collecting taxes on the importation of goods).

49. OECD, TAXATION AND ELECTRONIC COMMERCE, *supra* note 7, at 20.

50. *Id.* at 30. The destination principle is technically associated only with the final consumption that is subject to tax under VAT. *See, e.g.*, OECD, VAT/GST GUIDELINES, *supra* note 5, at 12 ("Under the *destination principle*, [the] tax is ultimately levied only on the *final consumption* that occurs within the taxing jurisdiction" (emphasis added)). Accordingly, the destination "principle is therefore entirely silent on which jurisdiction should tax business-to-business (B2B) transactions," Keen & Hellerstein, *supra* note 4, at 367, because B2B transactions do not involve final consumption. However, as explained in more detail in Section III.A.3.b, the B2B place-of-taxation rules should be designed to facilitate implementation of the destination principle.

51. Keen & Hellerstein, *supra* note 4, at 369.

52. EBRILL ET AL., *supra* note 40, at 184.

53. *See* INT'L VAT ASS'N, COMBATING FRAUD IN THE EU: THE WAY FORWARD 7, 10 (2007) (describing the different types of VAT fraud and noting the fiscal impact they have had on the EU).

destination principle through cross-border shopping, particularly with respect to high value, easily transported goods, which they illegally (or legally) bring back across the border.[54] Despite these difficulties, the widely accepted, if imperfect, mechanisms for implementing the destination principle with respect to cross-border trade in goods are generally workable. Indeed, if international trade consisted solely of trade in goods, it is doubtful the OECD would have undertaken the task of developing the *International VAT/GST Guidelines*.

2. Trade in services and intangibles: An overview

Implementing the destination principle is more complicated with respect to the taxation of cross-border trade in services and intangibles[55] than with respect to cross-border trade in goods. Part of the problem, particularly with regard to services,[56] is simply historical. Until fairly recently, cross-border trade in services attracted relatively little attention because most services were consumed where they were performed. Consequently, there was not much cross-border trade with respect to which a "destination" needed to be identified. The general rule in many jurisdictions—that services should be taxed where the service provider is established[57]—although technically an

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54. EBRILL ET AL., *supra* note 40, at 184 ("It has been estimated, for instance, that in 1986 about one-quarter of all spirits drunk in the Republic of Ireland were bought in Northern Ireland.").

55. There are many ways in which one can divide or subdivide the world of trade for VAT and other purposes. The EU VAT, for example, divides the entire universe of trade into trade in "goods" and trade in "services," with a "supply of services" defined as "any transaction which does not constitute a supply of goods." Council Directive 06/112, art. 24(1), 2006 O.J. (L 347) 1, 14 (EC) [hereinafter EU VAT Directive]. Other jurisdictions have categories of supplies in addition to goods and services, such as intellectual property rights and other intangibles, which this Article, in accord with the usage in the Guidelines, refers to collectively as "intangibles." OECD, VAT/GST GUIDELINES, *supra* note 5, at 10 n.2.

56. For purposes of the immediately ensuing discussion, the term "services" is employed in its narrower sense to denote services that are "performed" by a "service provider," as distinguished from the broader concept of services that would include all trade, other than trade in goods, including the licensing of intangible property. *Cf. supra* note 55 and accompanying text (referring to the broader definition of "services" used by the EU VAT).

57. *See, e.g.*, EU VAT Directive, *supra* note 55, art. 43 (deeming the place of supply of services, with some notable exceptions, to be "the place where the supplier has established his business or has a fixed establishment from which the service is supplied, or, in the absence of such a place of business or fixed establishment, the place where he has his permanent address or usually resides"). These rules changed in important respects on January 1, 2010 with regard to B2B supplies of services and on January 1, 2015 with respect to business-to-consumer ("B2C") supplies of services.

origin-based rule, in fact functioned satisfactorily as a destination-based rule, because the supplier's location was also the customer's location, and customer location may be viewed as a reasonable proxy for the "destination" of services.

This state of affairs changed dramatically with the enormous growth in cross-border trade in services, driven by the forces of globalization and facilitated by technological innovation. With the increasing disconnect between performance and consumption or use of services in a territorial sense,[58] the traditional rule for determining the place of taxation of services by reference to the service provider's establishment becomes problematic. The problem was exacerbated by the growth of multinational corporations, which render services in myriad locations through complicated legal structures. But the problem of designing an appropriate regime for taxing cross-border trade in services involves more than recognizing that many contemporary services are performed in one jurisdiction and consumed or used in another and simply adopting a destination-based rule for the place of taxation of services akin to the rule for the place of taxation of goods.

The more fundamental problem is that the enormous growth in services involving suppliers in one jurisdiction and customers in another often involves services that are intangible in nature. It is more difficult both to determine the appropriate jurisdiction of "destination" of intangible services and to enforce the tax based on that determination because these services are not amenable to border controls in the same manner as goods.[59] Such intangible services, which may be somewhat circularly defined as services "where the place of consumption may be uncertain,"[60] or, perhaps a bit more precisely, as "services and intangible property that are capable of delivery from a remote location,"[61] include services such as

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See Hellerstein & Gillis, *supra* note 4, at 469 (noting that in 2010, the basic place-of-supply rule for B2B supplies of services changed from the supplier's location to the customer's location, and in 2015, the place-of-supply rule for all B2C cross-border supplies of services became the place where the nontaxable person is established). For a detailed history of the development of these rules, see COCKFIELD ET AL., TAXING GLOBAL DIGITAL COMMERCE, *supra* note 4, at 193–232.

58. Indeed, even the place of performance may be uncertain, as when the warranty of a U.S. resident's computer is fulfilled by a technician in Bangalore, India who takes electronic control of her laptop and resolves the problem through key strokes performed 8000 miles away.

59. OECD, VAT/GST GUIDELINES, *supra* note 5, at 13.

60. OECD, TAXATION AND ELECTRONIC COMMERCE, *supra* note 7, at 24.

61. *Id.* at 44.

"consultancy, accountancy, legal and other 'intellectual' services; banking and financial transactions; advertising; transfers of copyright; provision of information; data processing; broadcasting; and telecommunications services."[62] Indeed, the foregoing challenges raised by cross-border trade in services and intangibles were the *raison d'être* of the OECD's *International VAT/GST Guidelines*.[63]

3. *The OECD Guidelines' individual place-of-taxation rules implementing the destination principle for cross-border trade in services and intangibles*

As explained above,[64] the OECD's *International VAT/GST Guidelines*' individual place-of-taxation rules implementing the destination principle address only cross-border trade in services and intangibles even though the Guidelines generally and wholeheartedly endorse the destination principle for all cross-border trade, including goods. The ensuing discussion provides a brief summary of these individual place-of-taxation Guidelines and seeks to place them within the broader framework of the destination principle they are designed to implement.[65]

a. *Business-to-consumer supplies*

There are two general place-of-taxation rules for implementing the destination principle in the business-to-consumer ("B2C") context.[66] The first of the two rules—the rule for "on-the-spot" supplies—is a reminder that some supplies are still consumed in the same jurisdiction in which they are provided notwithstanding the growth of the global digital economy. The second general rule—the residual rule that attributes all other B2C supplies to the customer's usual residence—is a reminder that the place-of-taxation rules generally are *proxies* reflecting our "best guess" or reasonable approximation as to where consumption is likely to occur.

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62. *Id.* at 25.

63. *See* OECD, VAT/GST GUIDELINES, *supra* note 5, at 9 (explaining that the Guidelines were developed to address the problems of double taxation and unintended non-taxation created by the growth of international trade in services and intangibles).

64. *See supra* notes 23–25, 32 and accompanying text.

65. For a more detailed and systematic discussion of the Guidelines, see generally Hellerstein, *Hitchhiker's Guide*, *supra* note 4.

66. As distinguished from the single general place-of-taxation general rule in the B2B context, see *infra* Section III.A.3.b, and as further distinguished from the specific place-of-taxation rules in both the B2B and B2C contexts, see *infra* Section III.A.3.c.

i. On-the-spot supplies

The first general rule for B2C supplies is the closest the Guidelines get to proposing a place-of-taxation rule that embodies the destination principle itself—*taxing actual consumption where consumption occurs*—rather than a proxy for predicting where consumption is likely to occur. Guideline 3.5 provides:

> [T]he jurisdiction in which the supply is physically performed has the taxing rights over business-to-consumer supplies of services and intangibles that
>
> - are physically performed at a readily identifiable place, and
> - are ordinarily consumed at the same time as and at the same place where they are physically performed, and
> - ordinarily require the physical presence of the person performing the supply and the person consuming the service or intangible at the same time and place where the supply of such a service or intangible is physically performed.[67]

In many respects, Guideline 3.5 is an "old economy" place-of-taxation rule. Indeed, many jurisdictions once employed the rule that services should be taxed where the service provider is established, an origin-based place-of-taxation rule that nevertheless functioned satisfactorily as a destination-based place-of-taxation rule because many (if not most) services were consumed or used by the customers at the supplier's location where they were provided.[68] Some services, of course, particularly in the B2C context, still fall squarely within that description. Despite the ability of twenty-first century doctors in New York City to perform "telesurgery" on the gallbladder of a patient lying on an operating table in Strasbourg, France,[69] the fact remains that today many B2C services are consumed where they are performed just as they have been long before anyone had ever heard of a VAT. Among those identified by the Guidelines are "services physically performed on the person (*e.g.* hairdressing, massage, beauty therapy, physiotherapy); accommodation; restaurant and catering services; entry to cinema,

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67. OECD, VAT/GST GUIDELINES, *supra* note 5, at 47.

68. *See supra* notes 55–57 and accompanying text.

69. D.L. Parsell, *Surgeons in U.S. Perform Operation in France via Robot*, NAT'L GEOGRAPHIC NEWS (Sept. 19, 2001), http://news.nationalgeographic.com/news/2001/09/0919_robotsurgery.html. According to the report, "[t]hrough a high-quality telecommunications circuit, the doctors in New York guided the movements of a three-armed robot in Strasbourg—about 6,230 kilometers (3,870 miles) away—that removed the gallbladder of a 68-year-old woman." *Id.*

theatre performances, trade fairs, museums, exhibitions, and parks; attendance at sports competitions."[70]

Although the scope of the "on-the-spot" supply rule is narrow, it is virtually a "perfect" place-of-taxation rule in terms of the criteria for evaluating the merits of such a rule. First, the rule identifies, as well as one feasibly can, the place where the supply is "ordinarily consumed." Second, it identifies a place that is easy for a supplier to determine and at which it easily can comply with tax collection obligations. Third, the rule identifies a place over which the tax administration can easily exercise its authority to enforce compliance with the relevant tax obligations.[71]

ii. The residual "usual residence" rule

In contrast to on-the-spot supplies, for which the happy confluence of the existence of (1) actual consumption (2) at a readily identifiable location (3) where taxing obligations can effectively be enforced determines the appropriate place-of-taxation rule, most supplies do not lend themselves to such a finely calibrated place-of-taxation rule. Accordingly, for B2C supplies other than on-the-spot supplies (and supplies that may be amenable to a specific place-of-taxation rule[72]), the Guidelines adopt a second "residual" place-of-taxation rule for B2C supplies. Guideline 3.6 provides that "the jurisdiction in which the customer has its usual residence has the taxing rights over business-to-consumer supplies of services and intangibles other than [on-the-spot supplies]."[73]

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70. OECD, VAT/GST GUIDELINES, *supra* note 5, at 47.

71. Indeed, the rule is so good that the Guidelines recommend its use in the B2B context, discussed below. *See infra* Section III.A.3.c; *see also* OECD, VAT/GST GUIDELINES, *supra* note 5, at 48 (explaining that on-the-spot supplies may be acquired by businesses as well as private consumers, but under the rubric of a "specific rule"). In the B2B context, of course, the rule loses the virtue of identifying the place of actual consumption, although it does effectively identify the place of actual business use.

72. *See infra* Section III.A.3.c (discussing the B2C supplies that the Guidelines identify as candidates for a specific place-of-taxation rule).

73. OECD, VAT/GST GUIDELINES, *supra* note 5, at 48. A more natural, if somewhat more clumsy, articulation of the rule might have described the place of taxation as "the jurisdiction in which the customer . . . has . . . [*his or her*] residence" rather than "its . . . residence," because the rule applies to B2C transactions where the customer is ordinarily a private person. *See id.* (emphasis added). Indeed, it is difficult to imagine where an "it" (other than a "he" or a "she") "regularly lives or has established a home." *See id.* (describing the jurisdiction in which a customer of a B2C transaction has "its usual residence"). An even better description, at the risk of offending the grammar police, would have been "the jurisdiction in which the customer has their usual residence." In fact, the use of the singular "they," which has

The use of "usual residence" as a place-of-taxation rule for B2C supplies is a quintessential "proxy." It makes no pretense of identifying the place of actual consumption, but seeks only to make an educated guess about where private consumers are likely to consume the supplies they acquire, and their usual residence is as good a guess as any. Indeed, for the universe of B2C supplies other than on-the-spot supplies and those for which a special place-of-taxation rule might be appropriate, it is difficult to imagine a better general rule than "usual residence."

The Guidelines describe the services and intangibles covered by the residual "usual residence" rule as including supplies that are likely to be consumed at a time other than when they are performed or provided, or for which the consumption and/or performance are likely to be ongoing, or that can be provided and consumed remotely.[74] Specifically such supplies may include "consultancy, accountancy and legal services; financial and insurance services; telecommunication and broadcasting services; online supplies of software and software maintenance; online supplies of digital content (movies, TV shows, music, *etc.*); digital data storage; and online gaming."[75]

Once it is established that the general "usual residence" rule is applicable to a B2C supply, the "heavy lifting" begins. Initially, of course, one must determine the customer's "usual residence." In principle, this does not pose a serious problem because it requires only that one determine "where the customer regularly lives or has established a home," as distinguished from a jurisdiction where customers "are only temporary, transitory visitors."[76] Although there always can be circumstances in which this line is less than clear, in the overall context of the B2C Guidelines this does not appear to be an issue that should generate much concern. The more serious problem in this regard is the practical one of how suppliers can determine a customer's usual residence, particularly in connection with digital supplies (especially those involving high volume and low value) where the limited interaction and communication between the supplier and its customer may make it difficult for the supplier to determine the customer's usual residence.

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a storied history and has gained increasing acceptance, was voted the 2015 Word of the Year by the American Dialect Society. *See 2015 Word of the Year is Singular "They"*, AM. DIALECT SOC'Y (Jan. 8, 2016), http://www.americandialect.org/2015-word-of-the-year-is-singular-they.

74. OECD, VAT/GST GUIDELINES, *supra* note 5, at 48.

75. *Id.*

76. *Id.* at 48–49.

The Guidelines' essential response to this problem is to urge governments to be reasonable, pragmatic, and flexible in permitting suppliers "to rely, as much as possible, on information they routinely collect from their customers in the course of their normal business activity, as long as such information provides reasonably reliable evidence of the place of usual residence of their customers."[77] The Guidelines recognize that the available information may vary depending on the type of business or product involved and the supplier's relationship to the customer, but that indicia of the customer's usual residence could include information collected during the ordering process, such as the customer's country, address, bank details, credit card information, IP address, telephone number, trading history, and language.[78]

b. Business-to-business supplies

i. Implementation of the destination principle in the B2B context: An overview

Practical implementation of the destination principle in the B2C context through adoption of place-of-taxation rules that identify the destination of a B2C sale makes good theoretical sense on the reasonable assumption that the destination of a B2C sale, however identified, is generally a good proxy for determining where final consumption is likely to take place.[79] Taxation at destination in the B2C context therefore falls squarely within the overarching place-of-taxation rule for cross-border trade, namely, that "[r]ules for the consumption taxation of cross-border trade should result in taxation in the jurisdiction where consumption takes place."[80] B2B transactions, however, generally involve business use as distinguished from final consumption.[81] Consequently, under the normal assumption that B2B supplies "do not involve final consumption,"[82] implementation of the destination principle as a means for

77. *Id.* at 49.
78. *Id.*
79. *See supra* Section III.A.3.a (discussing the place-of-taxation rules for implementing the destination principle in the B2C context).
80. OECD, TAXATION AND ELECTRONIC COMMERCE, *supra* note 7, at 18.
81. The reason for the qualification of the sentence is that businesses sometimes acquire supplies for the personal use of their owners, in which case the B2B supply in substance is, in whole or in part, a B2C supply and would be treated as such under most VAT regimes. EBRILL ET AL., *supra* note 40, at 17.
82. OECD, VAT/GST GUIDELINES, *supra* note 5, at 27.

identifying (or approximating) the jurisdiction of final consumption would appear to lose its theoretical relevance as a basis for identifying the jurisdiction in which B2B supplies should be taxed under a VAT. Indeed, as this Article observes above, albeit in a characteristically forgettable footnote,[83] "the destination principle . . . is therefore entirely silent on which jurisdiction should tax business-to-business (B2B) transactions."[84]

The destination principle, even though it applies in theory only to B2C transactions, nevertheless plays an important role in the *International VAT/GST Guidelines* in connection with B2B transactions, and it is important to understand why this is so. Perhaps the first point to make—and it is one this Article makes at several points in the preceding discussion, but is important enough to repeat[85]—is that the destination principle, from the perspective of tax administration, "seeks to approximate the location of consumption in a sensible and administrable fashion, not . . . to identify the location where consumption actually occurs."[86] Once one views the destination principle as a pragmatic mechanism for identifying the appropriate place of taxation rather than a means of satisfying a theoretical norm for determining where consumption actually occurs, it becomes easier to understand why identifying the "destination" of a supply in the B2B context may function satisfactorily as a place-of-taxation rule, even if it does not reflect the destination principle viewed narrowly as the place where final consumption actually occurs. If identifying the "destination" of a supply in the B2B context pinpoints a jurisdiction where tax can effectively be collected—i.e., if it is "good enough for government work, which . . . is what taxation is all about"[87]—do we really need to answer the academics' question: "It works in practice, but does it work in theory?"

Moreover, even if we do, there is in fact a theoretically defensible rationale for employing a destination-based approach for identifying the appropriate place of taxation in the B2B context that is influenced by the destination principle for identifying the place of final consumption (and taxation in the B2C context). As the Guidelines declare: "In theory, place of taxation rules should aim to identify the actual place of business use for [B2B] supplies (on the

83. *See supra* note 50.
84. Keen & Hellerstein, *supra* note 4, at 367.
85. This point is relevant to B2C transactions as well as to B2B transactions.
86. Keen & Hellerstein, *supra* note 4, at 367.
87. *Id.* at 368.

assumption that this best facilitates implementation of the destination principle) and the actual place of final consumption for [B2C] supplies."[88] The use of a destination-based approach for place-of-taxation rules in the B2B context can therefore be justified theoretically as a means for "implementing the destination principle," the destination-based approach for place-of-taxation rules in the B2C context.

Although the destination-based approach to place-of-taxation rules in both the B2B and B2C contexts focuses on the location (or deemed location) of the purchaser (whether a business or a consumer), the important differences between the two contexts identified above inform the objectives and design of the destination-based approaches in the two contexts. The Guidelines explicitly recognize this difference, and this Article quotes the Guidelines' explanation at some length because of its significance to the Guidelines' approach to the B2B and B2C place-of-taxation rules:

> [T]axation of [B2C] supplies involves the imposition of a final tax burden, while taxation of [B2B] supplies is merely a means of achieving the ultimate objective of the tax, which is to tax final consumption. Thus, the *objective of place of taxation rules for [B2B] supplies is primarily to facilitate the imposition of a tax burden on the final consumer in the appropriate country* while maintaining neutrality within the VAT system. *The place of taxation rules for [B2B] supplies should therefore focus* not only on where the business customer will use its purchases to create the goods, services or intangibles that final consumers will acquire, but also *on facilitating the flow-through of the tax burden to the final consumer* while maintaining neutrality within the VAT system.[89]

By contrast, as the Guidelines also recognize that "[t]he overriding objective of place of taxation rules for [B2C] supplies . . . is to predict, subject to practical constraints, the place where the final consumer is likely to consume the services or intangibles supplied."[90] In addition, because of the different characteristics of supplies to businesses and supplies to households, VAT systems often employ different mechanisms to collect the tax in connection with B2B and B2C supplies, and these different mechanisms in turn "often influence the design of place of taxation rules and of the compliance obligations for suppliers and customers involved in cross-border supplies."[91]

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88. OECD, VAT/GST GUIDELINES, *supra* note 5, at 28.
89. *Id.* (emphasis added).
90. *Id.*
91. *Id.*

Finally, whatever may be the theoretical case for B2B place-of-taxation rules that "identify the actual place of business use for [B2B] supplies,"[92] the Guidelines recognize that "place of taxation rules are in practice rarely aimed at identifying where business use . . . actually takes place."[93] Because the place of actual business use is generally not known at the time of the supply, "VAT systems . . . generally use proxies for the place of business use . . . to determine the jurisdiction of taxation, based on features of the supply that are known or knowable at the time that the tax treatment of the supply must be determined."[94] In short, the place-of-taxation rules "for border-crossing B2B transactions ultimately must be pragmatic."[95] What is needed, and what the Guidelines seek to provide, are "sensible and practicable rule[s] that facilitate[] implementation of the destination principle—the taxation of final consumption by real people."[96]

ii. The general B2B place-of-taxation rule: Customer location

To facilitate implementation of the destination principle, Guideline 3.2 provides the following general[97] place-of-taxation rule: "[F]or business-to-business supplies, the jurisdiction in which the customer is located has the taxing rights over internationally traded services or intangibles."[98] On the assumption that implementation of the destination principle can best be facilitated by taxing cross-border B2B supplies at the location of business use,[99] the rule is justified by the fact that "the jurisdiction of the customer's location can stand as the appropriate proxy for the jurisdiction of business use."[100] The question then becomes: "How does one determine the jurisdiction in which the customer is located?"

The answer to the question depends on the answer to two subsidiary questions: "Who is the customer?" and "Where is the customer located?" The answer to the first question, according to the Guidelines, "is normally determined by reference to the

92. *Id.*
93. *Id.*
94. *Id.* at 28–29.
95. Keen & Hellerstein, *supra* note 4, at 367.
96. *Id.*
97. *See infra* Section III.A.3.c (discussing how the general place-of-taxation rules, in both the B2B and B2C contexts, are distinguished from the specific place-of-taxation rules for particular types of supplies).
98. OECD, VAT/GST GUIDELINES, *supra* note 5, at 29.
99. *See id.* at 28–29.
100. *Id.* at 29.

business agreement."[101] A "business agreement" is not a formal legal concept, but simply embodies the elements that permit one to "identify the parties to a supply and the rights and obligations with respect to that supply."[102] Once the customer is determined, the customer's location is also determined for an entity with a single location (a "single location entity" or "SLE"), because of the truism that an SLE can have a customer location in only one jurisdiction.[103] A customer with "establishments in more than one jurisdiction"[104] is a "multiple location entity" or "MLE."[105]

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101. *Id.* at 30.

102. *Id.*

103. There can be uncertainty as to whether a customer is a single location entity ("SLE") or a multiple location entity ("MLE"), because the resolution of that question depends on whether the customer has an "establishment" in more than one jurisdiction, and therefore, on whether the customer has "a fixed place of business with a sufficient level of infrastructure in terms of people, systems[,] and assets to be able to receive and/or make supplies." *Id.* at 31. The answer may not be self-evident in all cases, particularly when it depends on laws of different countries that might provide different answers to this question based on the same set of facts. However, these are the types of questions that are endemic to any system of law, particularly in a global context, and one cannot expect (or reasonably demand) that a set of international "soft law" guidelines address them explicitly.

104. *Id.* at 31 & n.24 (explaining that, for the purpose of the Guidelines, "it is assumed that an establishment comprises a fixed place of business with a sufficient level of infrastructure in terms of people, systems[,] and assets to be able to receive and/or make supplies"). For American (and perhaps other) readers, who may be more familiar with "permanent establishments" for income tax purposes than with "fixed" or other establishments for VAT purposes, it should be kept in mind that the word "establishment" does not have the same meaning in both contexts. *Compare, e.g.*, ORG. ECON. CO-OPERATION & DEV., MODEL CONVENTION WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL art. 5 (2014) (defining "permanent establishment" for income tax purposes), *with* Hellerstein, *Permanent and Other Establishments*, *supra* note 4, at 348–49 (discussing the virtual permanent establishment and potential changes to the definition of a permanent establishment), *and* Rasa Mikutiene, *The Preferred Treatment of the Fixed Establishment in the European VAT*, 3 WORLD J. VAT/GST L. 166, 167–68 (2014) (defining "fixed establishment" for VAT purposes).

105. It is important to keep in mind that a MLE is a *single legal entity*, albeit one with multiple locations or branches, and the Guidelines' suggested place-of-taxation rules for MLEs are addressed only to what might be characterized as intra-entity or branch-to-branch supplies. When supplies are purchased by one *legal entity* for the benefit of a related *legal entity* or *entities* (for example, when a centralized purchasing company acquires auditing services for a multinational enterprise with subsidiaries around the world), the place-of-taxation rule for each supply to each legal entity is determined in accordance with the business agreement applicable to the supply to such legal entity. *See supra* Section III.A.3.b.ii (providing an overview of the implementation of the destination principle in the B2B context and observing that the customer is determined by reference to the business agreement); *see also* OECD, VAT/GST GUIDELINES, *supra* note 5, at 62–64, 67, 69 (furnishing examples of B2B

Determining which of the multiple jurisdictions has taxing rights over the services or intangibles becomes more complicated, and the Guidelines provide further detailed guidance on how to address these complications.[106]

The Guidelines identify three approaches to determining the establishment of a MLE that uses a service or intangible and to determining where the establishment is located: (1) the "direct use approach, which focuses directly on the establishment that uses the service or intangible;" (2) the "direct delivery approach, which focuses on the establishment to which the service or intangible is delivered;" and (3) the "[r]echarge method, which focuses on the establishment that uses the service or intangible as determined on the basis of internal recharge arrangements within the MLE, made in accordance with corporate tax, accounting or other regulatory requirements."[107]

The Guidelines' commentary elaborates in further detail on the application of each method, recognizing that each of the approaches may be appropriate for particular circumstances, and suggests that whatever approach is adopted should reflect "a sound balance between the interests of business (both suppliers and customers) and tax administrations."[108]

c. *Specific place-of-taxation rules (B2C and B2B)*

The Guidelines recognize that the general place-of-taxation rules for B2B and B2C transactions may not identify an appropriate place of taxation in all circumstances and that more targeted rules might be more likely to identify an appropriate place of taxation in some specifically defined circumstances. In response to this possibility, it is noteworthy what the Guidelines do *not* do. The Guidelines do not undertake to provide tax administrations with a list of specific place-

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place-of-taxation rules for supplies provided to groups of related companies based on separate business agreements applicable to each separate supply). It should also be noted that the Guidelines are drafted on the assumption that the "parties involved act in good faith and all transactions are legitimate and with economic substance." OECD, VAT/GST GUIDELINES, *supra* note 5, at 78.

106. *See* OECD, VAT/GST GUIDELINES, *supra* note 5, at 32 (providing that "when the customer has establishments in more than one jurisdiction, the taxing rights accrue to the jurisdiction(s) where the establishment(s) using the service or intangible is (are) located").

107. *Id.*

108. *See id.* at 32–34; *see also* Hellerstein, *Hitchhiker's Guide*, *supra* note 4, at 20–21 (elaborating on the Guidelines' commentary on each method to determine the establishment of a MLE that uses a service or intangible and to determine where that service or intangible is used).

of-taxation rules for application in particular circumstances where such rules might be regarded as superior to the "general" alternative. In part, this reticence reflects the recognition that the Guidelines represent "soft law," and there is a prudential limit to the number and precision of the "rules" the Guidelines can provide without becoming overly prescriptive.[109] Nevertheless, there is no such limit to the guidance that the Guidelines can and do provide as to when it may be appropriate to adopt a specific rule.

i. The evaluation framework for assessing the desirability of a specific place-of-taxation rule

For the reasons suggested in the preceding paragraph and with the notable exception of supplies related to tangible property,[110] the Guidelines provide a framework for evaluating the desirability of a specific place-of-taxation rule rather than recommending a set of specific place-of-taxation rules for circumstances in which the general rule may lead to an inappropriate result. Guideline 3.7 thus provides:

> The taxing rights over internationally traded services or intangibles supplied between businesses may be allocated by reference to a proxy other than the customer's location . . . when both the following conditions are met:
>
> a. The allocation of taxing rights by reference to the customer's location does not lead to an appropriate result when considered under the following criteria:
>
> - Neutrality
> - Efficiency of compliance and administration
> - Certainty and simplicity
> - Effectiveness
> - Fairness.
>
> b. A proxy other than the customer's location would lead to a significantly better result when considered under the same criteria.
>
> Similarly, the taxing rights over internationally traded business-to-consumer supplies of services or intangibles may be allocated by reference to a proxy other than [those provided in the general rules], when both the conditions are met as set out in a. and b. above.[111]

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109. OECD, VAT/GST GUIDELINES, *supra* note 5, at 57 ("It is neither feasible nor desirable to provide more prescriptive instructions on what should be the outcome of the evaluation for all supplies of services and intangibles.").

110. *See infra* Section III.A.3.c.ii (providing an overview of the Guidelines' slightly broader suggestions for taxation treatment of tangible property).

111. OECD, VAT/GST GUIDELINES, *supra* note 5, at 55. The evaluation framework for determining whether a specific place-of-taxation rule is appropriate involves a

Although Guideline 3.7 does "not aim to identify the types of supplies of services or intangibles, nor the particular circumstances or factors, for which a specific rule might be justified,"[112] the Guidelines' explanatory material proceeds to do just that, offering examples of "circumstances where a specific rule might be desirable" in both the B2B and B2C contexts.[113] In the B2B context, the Guidelines suggest that the general place-of-taxation rule for on-the-spot B2C supplies might be appropriate as a special place-of-taxation rule for on-the-spot B2B supplies.[114] Adoption of the same rule for on-the-spot supplies for both B2B and B2C supplies would relieve businesses supplying such services (for example, restaurant services or access to events) of the compliance burden of having to distinguish between final consumers and businesses when making their taxing decisions under the general rules.[115] Such a special rule might thereby lead to a "significantly better result" compared to the application of the general rule under the criteria of efficiency, certainty, simplicity, etc.[116]

In the B2C context, the Guidelines identify international transport as a candidate for a special rule because the general rule of physical performance for on-the-spot supplies[117] might lead to an inappropriate result when measured by the criteria of efficiency, certainty, and simplicity, given the fact that the service is performed in multiple jurisdictions.[118] Similarly, the Guidelines suggest that the general rule of the customer's usual residence, for other than on-the-

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two-step inquiry. First, one must evaluate the merits of the general rule as applied to the type of supply in question under the criteria set forth in the Guideline. If the general rule produces an appropriate result, that is the end of the inquiry. However, if the general rule does not produce an appropriate result, then one must undertake an additional two-step inquiry. First, one must evaluate the merits of the proposed specific rule under the criteria set forth in the Guideline. Second, one must then compare the results of evaluating the general and specific rules under the Guidelines' evaluation criteria. Only if the specific rule leads to a "significantly better result" should one adopt a specific rule.

112. *Id.* at 56.

113. *Id.* at 57–58.

114. *See supra* note 71 and accompanying text (discussing the Guidelines' suggestion to substitute a specific place-of-taxation rule for on-the-spot B2B supplies for the general B2B place-of-taxation rule).

115. OECD, VAT/GST GUIDELINES, *supra* note 5, at 48, 57–58.

116. *Id.* at 58.

117. *Id.* at 47 (explaining the taxation treatment of on-the-spot supplies, as discussed *supra* Section III.A.3.a.i).

118. *Id.* at 58.

spot supplies,[119] might lead to an inappropriate result for services and intangibles that are performed at a readily identifiable location and require the physical presence of the person consuming the supply, but not the physical presence of the person performing it; for example, "the provision of Internet access in an Internet café or a hotel lobby" or "the access to television channels for a fee in a hotel room."[120] In such cases, a special rule based on the actual location of the customer at the time of the supply might be a better proxy for predicting actual consumption and for administering the VAT than a rule based on the customer's usual residence.[121]

ii. Tangible property

While the Guidelines generally disavow any intent to identify, let alone prescribe, a specific place-of-taxation rule for particular circumstances where such a rule might lead to a better result than the applicable general rule,[122] when it comes to tangible property, the Guidelines are a little less diffident about endorsing specific place-of-taxation rules. This simply reflects and recognizes the reality that many VAT regimes have directly or indirectly embraced place-of-taxation rules for services and intangibles provided in connection with tangible property based on the location of the property.[123] Because the types of supplies at which the specific place-of-taxation rules are directed will typically fall outside the scope of what one

119. *See id.* at 48 (discussing the "usual residence" rule for B2C supplies, as quoted and discussed in *supra* Section III.A.3.a.ii).

120. *Id.* at 58.

121. *Id.*

122. *See supra* note 109 and text accompanying note 111 (describing the Guidelines' general disavowal of an intent to prescribe specific place-of-taxation rules).

123. OECD, VAT/GST GUIDELINES, *supra* note 5, at 58–59. The distinction between "directly" and "indirectly" differentiates those VAT regimes that have adopted specific place-of-taxation rules for particular types of supplies, including tangible property, from those VAT regimes (like New Zealand's) that often reach a similar conclusion based on an "iterative" approach to determining the appropriate place of taxation. *Compare, e.g.*, EU VAT Directive, *supra* note 55, art. 45 (place of supply for services "connected with immovable property" is "the place where the property is located"), *and id.* art. 52 (place of supply for nontaxable persons for work on "movable tangible property" is "where the services are physically carried out"), *with* COCKFIELD ET AL., TAXING GLOBAL DIGITAL COMMERCE, *supra* note 4, § 6.01[A] (elaborating on the distinction between the "categorization approach" and "iterative approach" to designing VAT place-of-taxation rules).

would characterize as a "remote sale,"[124] and hence outside the scope of this Article, we simply describe these rules briefly in the margin.[125]

B. Implications of the Global Perspective for the U.S. Subnational Retail Sales Tax

As we have already seen, the broad lessons that emerge from the global perspective on taxing remote sales provide meaningful guidance for, and are generally reflected in, the U.S. RST.[126] The

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124. *See supra* note 1 (defining "remote sale" for the purposes of this Article).

125. *See* OECD, VAT/GST GUIDELINES, *supra* note 5, at 59 ("For internationally traded supplies of services and intangibles directly connected with immovable property, the taxing rights may be allocated to the jurisdiction where the immovable property is located."). Unlike the Guidelines' other place-of-taxation rules that assign taxing rights to a particular jurisdiction, the Guideline for immovable property is merely permissive ("taxing rights *may be* allocated"), and therefore, consistent with the language of Guideline 3.7. *Id.* (emphasis added). Furthermore, the Guidelines' explanatory guidance directed to Guideline 3.8 makes it clear that the application of Guideline 3.8 should be informed by the evaluation criteria reflected in Guideline 3.7. *Id.* The Guidelines identify two categories of services or intangibles directly connected with immovable property regarding which "it is reasonable to assume" that the specific rule would lead to a significantly better result than the relevant general rule under the evaluation criteria of Guideline 3.7: (1) "the transfer, sale, lease or the right to use, occupy, enjoy or exploit immovable property," and (2) "supplies of services that are physically provided to the immovable property itself, such as constructing, altering and maintaining the immovable property." *Id.* For other supplies of services and intangibles directly connected with immovable property, the Guidelines suggest that further evaluation under Guideline 3.7 would be required before the propriety of adopting the specific rule could be determined. *See id.* at 59–60 (defining "directly connected" as "a very close, clear and obvious link or association between the supply and the immovable property"). These other services and intangibles include services that are not physically performed on immovable property, but that relate to clearly identifiable, specific immovable property, such as architectural services. *Id.* at 60.

As for movable tangible property, the Guidelines do not propose even a permissive specific place-of-taxation rule for such property. This may be explained in part by the fact that, with respect to B2B supplies of services and intangibles connected with movable property, the Guidelines view the application of the general rule based on customer location as generally leading to an appropriate result. *Id.* at 61. As for B2C supplies of services and intangibles connected to movable property—such as repairing, altering, or maintaining the property, and the rental of specific movable property where this is considered a service—the Guidelines encourage jurisdictions to consider adopting a place-of-taxation rule based on the location of movable tangible property. *Id.* Such an approach would, according to the Guidelines, "provide a reasonably accurate reflection of the place where the consumption of the services or intangibles is likely to take place and is relatively straightforward for suppliers to apply in practice." *Id.*

126. *See supra* Part I (concluding that remote sales should be taxed); *supra* Part II (concluding that remote sales should be taxed at destination).

implications of the more specific implementing rules for consumption taxation at the global level, however, tend to be more varied in their application to the U.S. RST, a point this Article has already anticipated.[127] The explanation for this difference lies in the inescapable fact that, although the challenges associated with the taxation of remote sales in the digital age are global, the regimes that tax such sales are not.[128]

Nevertheless, despite the significant differences between global consumption tax regimes implemented through a staged-collection process and a single-stage consumption tax like the U.S. RST, and despite the failure of the U.S. RST generally to tax services and intangibles, which are the focus of the detailed implementing place-of-taxation rules in the global context, the implementation of the destination principle in the global context offers some guidance that may be useful for the U.S. RST with regard to taxation of remote sales.

Perhaps the most important guidance that the global perspective on implementing the destination principle contains for the U.S. RST with regard to remote sales (or what the OECD's Base Erosion and Profit Shifting ("BEPS") Project refers to as "remote digital supplies"[129]) bears on the appropriate place of taxation. Despite the general limitation of the U.S. RST to sales of tangible personal property,[130] the U.S. RST has always taxed some services (telecommunications services, for example), and, in recent years, it has increasingly taxed sales of specified digital products, particularly those that are economic substitutes for what were once tangible products (such as software, videos, books, and music).[131] Indeed, there has been enormous interest in and controversy over the question of taxation of cloud computing under the U.S. RST and, among other things, as to where sales of cloud computing should be taxed.[132]

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127. *See supra* notes 36–37 and accompanying text (describing the implications of the destination principle under VATs for RSTs).

128. *See supra* note 2 and accompanying text (observing that it is appropriate to view the U.S. RST from a global perspective).

129. *See supra* note 1 (noting the OECD Base Erosion and Profit Shifting ("BEPS") project's concern with "remote digital supplies").

130. *See supra* note 18 and accompanying text (indicating that the U.S. RST generally fails to include many services in the tax base).

131. *See* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 13.06 (discussing sales taxation of computer software).

132. *See* Walter Hellerstein & John Sedon, *State Taxation of Cloud Computing: A Framework for Analysis*, 117 J. TAX'N 11, 23–24 (2012) (noting uncertainty over the question of whether sales of cloud computing transactions should be sourced to the location of the server or the location of the user); *see also* 2 HELLERSTEIN,

In light of the difficulties of identifying the appropriate "state of destination" for taxing remote sales of digital products, those in a position to influence the design of the U.S. RST might well take a page or two from the OECD VAT/GST Guidelines' playbook and embrace both the Guidelines' "residual" rule[133] for B2C supplies where "the jurisdiction in which the customer has its usual residence has the taxing rights over [B2C] supplies of services and intangibles"[134] and the general rule of customer location for B2B supplies.[135] For the reasons described above,[136] the usual residence rule for B2C supplies constitutes an ideal "proxy" for services that can be provided and consumed remotely,[137] including "online supplies of software and software maintenance; online supplies of digital content (movies, TV shows, music, etc.); digital data storage; and online gaming."[138] For analogous reasons, the customer location rule constitutes "the appropriate proxy for the jurisdiction of business use."[139] Moreover, there is powerful precedent for a residence-based rule for taxing remote B2C sales and B2B sales, albeit a precedent that required congressional intervention,[140] namely, federal legislation authorizing the states to tax charges for wireless telecommunications at the customer's "place of primary use," defined as "the residential street address or the primary business street address of the customer . . . within the licensed service area of the . . . service provider."[141]

HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 13.06A (observing that some of the problems presented by cloud computing can be resolved by "the application of familiar principles to unfamiliar transactions").

133. *See supra* Section III.A.3.a.ii (discussing OECD, VAT/GST GUIDELINES, *supra* note 5, at 47 and distinguishing the "usual residence" rule for B2C supplies from the rule for "on-the-spot" B2C supplies).

134. OECD, VAT/GST GUIDELINES, *supra* note 5, at 48; *see also supra* note 73 (discussing "usual residence" rule for B2C supplies).

135. *See supra* Section III.A.3.b.ii (discussing Guideline 3.2 in OECD, VAT/GST GUIDELINES, *supra* note 5, at 29).

136. *See supra* Section III.A.3.a.ii (describing the "usual residence" rule for B2C supplies of services and intangibles).

137. OECD, VAT/GST GUIDELINES, *supra* note 5, at 48.

138. *Id.*

139. *Id.* at 29.

140. In this respect, what follows anticipates the concluding Parts of this Article. *See infra* Part IV and Conclusion.

141. 4 U.S.C. § 124(8) (2012).

IV. HOW CAN REMOTE SALES BE TAXED EFFECTIVELY UNDER A CONSUMPTION TAX IN THE DIGITAL AGE?

Once it has been determined that remote sales should be taxed at destination under a consumption tax, the remaining question is "how?," or, more precisely, "how can remote sales be taxed *effectively* at destination *in the digital age*?"

A. The Global Perspective

1. Business-to-consumer transactions

From a global perspective, the practical tax challenges associated with the enforcement of the "usual residence" rule in connection with "remote digital supplies to consumers" are daunting.[142] The challenges are attributable to the fact that even if the jurisdiction of the customer's usual residence imposes a legal obligation on the remote supplier to register in the customer's jurisdiction and to collect the tax on the supply, "it can often be complex and burdensome for non-resident suppliers to comply with such obligations in jurisdictions where they have no business presence, and equally difficult for tax administrations to enforce and administer them."[143] The lack of effective "enforcement jurisdiction"[144] with respect to such supplies is attributable not only to the questionable power to enforce a collection obligation against remote suppliers, but also because any payment obligations that jurisdictions impose directly on the private customer, notwithstanding their unquestionable legal power to impose such obligations on their residents, is unlikely to generate much revenue in the absence of meaningful sanctions for failing to comply with such obligations.[145] Despite these problems, the Guidelines conclude

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142. OECD, FINAL REPORT, *supra* note 1, at 121–22. As noted at the outset, this Article considers such sales to embrace those with respect to which the supplier has no physical presence in the jurisdiction of the customer's usual residence. *See id.* at 121.

143. OECD, VAT/GST GUIDELINES, *supra* note 5, at 49; *see also* OECD, FINAL REPORT, *supra* note 1, at 121 (observing that jurisdictions often collect an "inappropriately low" amount of VAT on digital supplies and that this creates a burden on competing domestic suppliers who are paying the full VAT owed).

144. *See generally* Hellerstein, *Jurisdiction to Tax Income and Consumption in the New Economy*, *supra* note 48 (elaborating on concepts of "substantive jurisdiction" and "enforcement jurisdiction").

145. *See* OECD, VAT/GST GUIDELINES, *supra* note 5, at 50 (noting that the reverse charge mechanism does not offer an appropriate solution for collecting VAT on B2C supplies because of the absence of meaningful sanctions for non-compliance); Hellerstein, *Permanent and Other Establishments*, *supra* note 4, at 349–50 (discussing the

that "at the present time, the most effective and efficient approach to ensure the appropriate collection of VAT on cross-border [B2C] supplies is to require the non-resident supplier to register and account for the VAT in the jurisdiction of taxation."[146]

The Guidelines have no "silver bullet" to solve all the problems associated with the recommendation that non-resident suppliers be required to register and account for VAT in the customer's jurisdiction on cross-border B2C supplies of services and intangibles. After all, they are guidelines, not fairy tales. What the Guidelines do recommend, however, in keeping with their generally practical approach to the problems raised by VAT on cross-border trade in services and intangibles, are measures that jurisdictions can take to encourage and facilitate compliance by non-resident suppliers with the tax collection regime in the customer's jurisdiction. Specifically, they recommend that jurisdictions consider establishing a simplified registration and compliance regime for non-resident suppliers in connection with cross-border B2C supplies of services and intangibles.[147] The simplified regime would operate separately from the traditional registration and compliance regime and would not offer the same rights, such as input tax recovery, nor impose the same obligations, such as full reporting, as in a traditional regime.[148] To assist taxing jurisdictions in developing their framework for collecting VAT on B2C supplies of services and intangibles from non-resident suppliers and to increase consistency among compliance processes across jurisdictions—an important concern to businesses faced with multijurisdictional VAT obligations—the Guidelines outline the principal features of a simplified registration and compliance regime for such suppliers, balancing the need for simplification and the need of tax administrations to safeguard the revenue.[149]

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problems in aligning substantive jurisdiction and enforcement jurisdiction in the B2C context). By contrast, in the B2B context, the tax compliance obligation can be effectively shifted to the business purchaser, who is ordinarily registered for VAT purposes. *See supra* note 50 and accompanying text; *infra* Section IV.A.2.

146. OECD, VAT/GST GUIDELINES, *supra* note 5, at 50.

147. *Id.*

148. *Id.* In most cases, a non-resident supplier with no location in a jurisdiction would not incur any input tax for which it would be entitled to recovery, so the denial of input tax recovery would not subject it to irrecoverable input tax. If a non-resident supplier were in a position where it would incur irrecoverable input tax, however, it could always choose to register under the traditional regime. *Id.*

149. *Id.* at 50–51.

The Guidelines identify (and briefly elaborate upon) the following main features of a simplified registration-based collection regime for B2C supplies of services and intangibles by non-resident suppliers:

- Simplified registration procedure, with required information kept to a minimum and the availability of on-line registration at the tax administration's Website;
- No input tax recovery, but non-resident suppliers could register under a normal compliance regime and recover input tax according to normal rules;
- Simplified returns, with option to file electronically;
- Electronic payment methods;
- Simplified and electronic record keeping requirements;
- Elimination of invoicing requirements, or issuing invoices in accord with rules of supplier's jurisdiction;
- Online availability of all information necessary to register and comply with a simplified regime;
- Use of third-party service providers to assist in tax compliance;
- Possible use of a simplified regime in the B2B context if the business customer is entitled to full input tax credit and the jurisdiction does not differentiate between B2B and B2C supplies; and
- Compliance burdens proportional to revenues involved and objectives of maintaining neutrality between domestic and foreign suppliers.[150]

It is worth noting that a number of jurisdictions have already adopted a simplified registration and compliance regime for non-resident suppliers in connection with cross-border B2C supplies of services and intangibles. Most significantly, in 2002, the EU, which currently comprises twenty-eight Member States, adopted such a regime for certain electronically supplied B2C services from non-EU suppliers to EU customers in conjunction with the so-called E-Commerce Directive, a regime that was effectively extended to equivalent intra-EU cross-border B2C services effective 2015.[151] The

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150. *Id.* at 51–54. The Guidelines note the important role that technology plays (and will continue to play) in the tax compliance process, but deliberately focus on simplification of administrative and compliance procedures, in recognition of the fact that technology will be effective only if the core elements of the compliance process are sufficiently clear and simple, and, in any event, that the relevant technologies will continue to evolve over time. *Id.* at 51.

151. *See* Directive 2002/38 of the Council of May 7, 2002 on the Value Added Tax Arrangements Applicable to Radio and Television Broadcasting Services and Certain

E-Commerce Directive required a non-EU supplier making online supplies of digital deliveries to final consumers to register, collect, and remit VAT to the relevant EU country under simplified administrative procedures.[152] Among the key administrative simplifications were the ability of a non-EU supplier to register in a single "Member State of identification," charge and collect VAT according to the rate of the Member State where its customers reside, and pay the amounts due to the tax administration it had elected, with the tax administration reallocating the VAT revenue to the customer's Member State.[153] In 2016, New Zealand enacted legislation (effective October 1, 2016) that applies its goods and services tax (GST) to offshore suppliers making cross-border supplies of "remote" services and intangibles to New Zealand consumers.[154] The new rules require non-resident suppliers of "remote" services (including e-books, music, videos, and software purchased from offshore websites) to New Zealand consumers to register and return GST on these supplies if they exceed or are expected to exceed NZ$60,000 in a twelve-month period.[155] The Special Report from New Zealand Inland Revenue describing the legislative changes note that they "broadly follow [OECD] guidelines, as well as similar rules that apply in other jurisdictions, such as Member States of the European Union, Norway, South Korea, Japan,

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Electronically Supplied Services, 2002 O.J. (L 128) 1 (EC); Council Regulation 792/2002 of May 7, 2002 on Administrative Cooperation in the Field of Indirect Taxation (VAT) as Regards Additional Measures Regarding Electronic Commerce, art. 1, 2002 O.J. (L 128) 1, 2 (EC) [hereinafter E-Commerce Directive] (outlining the "special scheme" for electronically supplied services). These rules are now embodied in the current EU VAT Directive. EU VAT Directive, *supra* note 55, art. 58, 358–69; *see* TAXATION & CUSTOMS UNION, EUROPEAN COMM'N, GUIDE TO THE VAT MINI ONE STOP SHOP 2 (2013), http://eeas.europa.eu/delegations/china/documents/news/0307_2_en.pdf (providing guidance on how to account for the VAT due on supplies when taxable persons supply electronic services to non-taxable persons); *see also* Hellerstein & Gillis, *supra* note 4, at 468–71 (discussing the EU's rules governing application of VAT to cross-border trade in the B2B and B2C contexts).

152. EU VAT Directive, *supra* note 55, art. 360–62, 367.

153. *Id.*

154. POL'Y & STRATEGY, INLAND REVENUE, GST ON CROSS-BORDER SUPPLIES OF REMOTE SERVICES 1 (2016) [hereinafter GST ON CROSS-BORDER SUPPLIES], http://taxpolicy.ird.govt.nz/sites/default/files/2016-sr-gst-cross-border-supplies.pdf (alternatively referred to as the "Special Report").

155. *Id.*

Switzerland[,] and South Africa."[156] The Report further notes that Australia enacted similar rules that will apply beginning July 1, 2017.[157]

2. Business-to-business transactions

In contrast to the difficult enforcement challenges that global consumption tax regimes encounter with respect to remote B2C supplies of services and intangibles,[158] there is a solution to the enforcement problem with respect to remote B2B supplies of services and intangibles, namely, the "reverse charge" (or self-assessment) mechanism, to which this Article briefly alludes above.[159] Under the reverse charge mechanism, the business customer accounts for any tax due in its jurisdiction. In the cross-border context, such an approach ordinarily has the distinct advantage of relieving the supplier of any obligation to be identified for VAT purposes or to account for tax in the customer's jurisdiction. The OECD's VAT/GST Guidelines, in accord with an earlier suggestion found in the Ottawa Taxation Framework Conditions,[160] recommend that the VAT be implemented in the B2B context through the use of the reverse charge mechanism when this is consistent with the design of the national consumption tax system.[161]

As the Guidelines elaborate:

> The reverse charge mechanism has a number of advantages. First, the tax authority in the jurisdiction of business use can verify and ensure compliance since that authority has personal jurisdiction over the customer. Second, the compliance burden is largely shifted from the supplier to the customer and is minimised [sic] since the customer has full access to the details of the supply. Third, the administrative costs for the tax authority are also lower because the supplier is not required to comply with tax obligations in the customer's jurisdiction (e.g. VAT identification, audits, which would otherwise have to be administered, and translation and

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156. *Id.* at 6.
157. *Id.*
158. Services that obviously include (and, indeed, may largely comprise) remote digital supplies.
159. *See supra* note 50 and accompanying text.
160. The Ottawa Taxation Framework Conditions provided: "Where business and other organisations [sic] within a country acquire services and intangible property from suppliers outside the country, countries should examine the use of reverse charge, self-assessment or other equivalent mechanisms where this would give immediate protection of their revenue base and of the competitiveness of domestic suppliers." OECD, TAXATION AND ELECTRONIC COMMERCE, *supra* note 7, at 231.
161. OECD, VAT/GST GUIDELINES, *supra* note 5, at 35.

> language barriers). Finally, it reduces the revenue risks associated with the collection of tax by non-resident suppliers, whether or not that supplier's customers are entitled to deduct the input tax.[162]

B. *Implications of the Global Perspective for the U.S. Subnational Retail Sales Tax*

In considering the relevance of the global perspective on the effective enforcement of taxes on remote sales in the digital age to such enforcement under the U.S. RST, we should recognize at the outset that whatever commonalities exist between international and subnational RST cross-border consumption tax issues, there is a fundamental difference in the power to address these issues in the two contexts and, in particular, that this difference may inform the answer to the question, "How can remote sales be taxed effectively under a consumption tax in the digital age?" in the respective contexts. As this Article already observed,[163] there is no effective "enforcement jurisdiction"[164] in the international B2C context, and this has shaped the response of the global tax community, both through the OECD Guidelines and in national laws, to the taxation of cross-border B2C supplies of services and intangibles. By contrast, in the U.S. subnational context, there is ample power to create enforcement jurisdiction over all aspects of intra-U.S. cross-border commercial activity,[165] and the existence of such power may affect the determination of the most appropriate response to intra-U.S. remote sales and the relevance of the global perspective on taxing remote sales.

Despite the unquestioned existence of such power, no discussion of the U.S. RST can ignore the U.S. Supreme Court's decision in

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162. *Id.* at 38.

163. *See supra* Section IV.A.1.

164. *See generally* Hellerstein, *Jurisdiction to Tax Income and Consumption in the New Economy*, *supra* note 48 (elaborating on concepts of "substantive jurisdiction" and "enforcement jurisdiction").

165. *See generally* Walter Hellerstein, *Federal Constitutional Limitations on Congressional Power to Legislate Regarding State Taxation of Electronic Commerce*, 53 NAT'L TAX J. 1307 (2000) (observing that the U.S. Supreme Court consistently has affirmed Congress's broad power to regulate state taxation of electronic commerce and, specifically, to require out-of-state vendors to collect taxes on sales to in-state customers). The U.S. subnational states stand in no better position vis-à-vis international commercial activity (and, specifically, remote supplies into the United States from foreign suppliers) than does the United States itself. Accordingly, with respect to international cross-border activity, global perspectives on taxation of remote sales that are influenced by concerns over enforcement jurisdiction would appear to be equally applicable to the U.S. subnational states.

Quill Corp. v. North Dakota,[166] which held that the Commerce Clause prohibits a state from requiring a seller, with no physical presence in the state, from collecting a use tax imposed on goods sold to customers in the state.[167] *Quill*'s holding has been the focus of considerable controversy ever since it was decided, and that controversy has only become more intense with the increasing importance of remote sales.[168] Indeed, any meaningful solution to the problem of taxing remote sales under the U.S. RST will require congressional legislation that overrides the rule of *Quill*.

1. Business-to-consumer transactions

The principal guidance from a global perspective (as reflected in the OECD's VAT/GST Guidelines) on taxing remote B2C supplies of services and intangibles is that jurisdictions should consider establishing simplified registration and compliance regimes for non-resident suppliers.[169] The Guidelines elaborate upon this guidance in some detail,[170] and a number of regimes have already taken it to heart.[171]

The global guidance for taxing remote B2C supplies would appear to apply generally to the taxation of remote B2C sales under the U.S. RST. Indeed, insofar as there is no enforcement jurisdiction under existing U.S. constitutional restraints on states' ability to require remote vendors to collect taxes on remote sales,[172] states' adoption of simplified registration and compliance regimes to encourage and facilitate collection of taxes on remote sales would seem to be advisable for essentially the same reasons that it is advisable in the global context. In fact, effective October 2015, Alabama adopted just such a regime, the Simplified Seller Use Tax Remittance Act.[173] The legislation allows out-of-state sellers to register voluntarily to collect

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166. 504 U.S. 298 (1992).

167. *Id.* at 301–02, 317–18.

168. *Quill* and the issues it raises are considered in detail in 1 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 6.03, and 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 19.02[3], as well as in other articles in this Issue.

169. OECD, VAT/GST GUIDELINES, *supra* note 5, at 50.

170. *Id.* at 51–54; *see also supra* Section IV.A.1 (listing the Guidelines' recommendations for a simplified registration-based collection regime).

171. *See* GST ON CROSS-BOARDER SUPPLIES, *supra* note 154, at 5–6 (listing five countries and the EU as having implemented a simplified registration and compliance regime in some form).

172. Quill Corp. v. North Dakota, 504 U.S. 298 (1992), discussed *supra* notes 176–77 and accompanying text.

173. ALA. CODE §§ 40-23-191 to -199 (2016).

Alabama tax on sales into the state, report electronically, and avoid the complexity of calculating combined state and local tax rates.[174]

To suggest, however, that states should embrace the global guidance regarding remote sales, as Alabama has, tells only half the story for reasons suggested in the introductory paragraph to this subsection.[175] Because there is ample congressional power to authorize the states to require remote sellers to collect taxes on sales into a state, it would be a sin of omission to leave the impression that the global perspective, without more, provides the appropriate guidance for states to follow regarding remote sales. Rather the appropriate guidance for a federal country like the United States with central authority over subnational cross-border tax administration, or even "a group of countries that is bound by a common legal framework for their consumption tax systems,"[176] to wit, the EU, is that simplification (including harmonization) of consumption tax regimes *along with mandatory vendor collection obligations under the simplified system* is the appropriate guidance for such systems. Indeed, for many years, the EU VAT Directive has facilitated implementation of the destination principle in the B2C context with respect to goods by requiring EU suppliers whose B2C sales into a Member State exceed a specified threshold to register for VAT in the destination state and to charge the destination state's VAT on such sales.[177] This approach is also reflected in proposed legislation in the United States for simplification and harmonization of the U.S. RST, along with mandatory vendor collection subject to various thresholds.[178]

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174. *Id.* § 40-23-192(a)–(b).

175. *See supra* Section IV.B.

176. OECD, TAXATION AND ELECTRONIC COMMERCE, *supra* note 7, at 45 n.6 (the OECD commonly uses this vernacular to describe the EU). This precise language is repeated in the Guidelines, OECD, VAT/GST GUIDELINES, *supra* note 5, at 20. These statements are designed to make it clear that the EU may adopt *intra-EU* cross-border VAT rules that may not be consistent with the OECD's guidance for *international* cross-border consumption tax issues. *Id.*

177. EU VAT Directive, *supra* note 55, art. 33, 34; Hellerstein & Gillis, *supra* note 4, at 466–67.

178. *See* Marketplace Fairness Act of 2015, S. 698, 114th Cong. § 2 (2015); Remote Transactions Parity Act of 2015, H.R. 2775, 114th Cong. § 2 (2015). For an analysis of the merits of earlier versions of similar proposed legislation, see Walter Hellerstein, *Federal-State Tax Coordination: What Congress Should or Should Not Do*, 64 ST. TAX NOTES 453 (2012) (reprinting the Author's April 25, 2012 testimony before a U.S. Senate Finance Committee hearing addressed to what federal tax reform means for state and local tax and fiscal policy), and McLure & Hellerstein, *supra* note 19 (discussing legislation proposed in 2004 that would have allowed states to require

2. Business-to-business transactions

In the B2B context, the guidance from a global perspective (as reflected in the OECD's VAT/GST Guidelines) for enforcement of the destination principle with respect to cross-border supplies of services and intangibles was to use the reverse charge.[179] For most of the reasons advanced in the global context, the guidance would appear generally to apply to the taxation of remote B2B sales under the U.S. RST as well. First, the tax authority in the business purchaser's jurisdiction can ensure compliance because it will have personal jurisdiction over the business customer. Second, the compliance burden is shifted from the vendor to the customer, which tends to minimize the collection burden because the customer has knowledge of the relevant details of the sale. Third, the tax authority's administrative costs are lower because the out-of-state vendor need not comply with the jurisdiction's tax obligations. Fourth, it minimizes the revenue risks associated with the collection of taxes from non-resident vendors.[180]

In fact, the reverse charge is no stranger to the U.S. RST. The reverse charge mechanism is analogous to the use of a "direct pay" permit under which some business taxpayers, especially larger purchasers, may register with states and agree to "self-assess" a use tax on all taxable goods and services they purchase.[181] The Federation of Tax Administrators describes the direct payment process as follows:

> Direct pay is an authority granted by a tax jurisdiction that generally allows the holder of a direct payment permit to purchase otherwise taxable goods and services without payment of tax to the supplier at the time of purchase. (Also in the case of exempt transactions, it allows a holder to purchase without issuing exemption certificates.) Suppliers are to be furnished a written notification of the purchaser's direct pay authority (often a numeric designation). The holder of the direct payment permit is to timely review its purchases and make a determination of taxability and then report and pay the applicable tax due directly to

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out-of-state sellers to collect taxes on remote sales if the state simplified its tax system in accordance with the Streamlined Sales Tax Project).

179. *See supra* Section IV.A.2. As noted there, such services obviously include (and, indeed, may largely comprise) remote digital supplies.

180. OECD, VAT/GST GUIDELINES, *supra* note 5, at 38.

181. *See* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 16.01[2] (describing the "direct pay" mechanism).

the tax jurisdiction. The permit holder's tax determinations and adequacy of payment are subject to audit by the tax jurisdiction.[182]

In light of the existence of "direct pay" authority under U.S. RSTs and its advantages from a tax enforcement standpoint, particularly with regard to remote sales, one may wonder why states have not generally adopted the "direct pay" mechanism as a mandatory requirement for all remote B2B sales, thereby addressing, if not substantially resolving, the enforcement issues with regard to such sales, rather than relegating it to a voluntary system that tends to be confined to larger purchasers. The answer probably lies in the fact that, in contrast to VAT regimes under which most businesses are already registered as part of the staged-collection process, many businesses are not registered under the single-stage U.S. RST. Accordingly, imposition of a universal "direct pay" requirement for business purchasers under the U.S. RST would impose a substantial new tax compliance obligation on previously unregistered vendors. That said, in light of the increasing enforcement challenges of remote sales in the B2B context under the U.S. RST, states might well consider expanding the scope of "direct pay" authority and, perhaps with appropriate thresholds for small purchasers, making direct payment mandatory rather than voluntary.

CONCLUSION

This Article ends where it began, with three fundamental questions relating to the global perspective on taxing remote sales in the digital age, but now with proposed answers. First, should remote sales be taxed under a consumption tax? The answer is "Yes."[183] Second, where should such sales be taxed? The answer is "At destination."[184] Third, how can remote sales be taxed effectively in the digital age? The answer is "By adopting simplified registration and compliance regimes for non-resident suppliers in the B2C context and by adopting the reverse charge mechanism in the B2B context."[185] As for the implications of the global perspective for the U.S. RST, the

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182. FED'N OF TAX ADM'RS., MODEL DIRECT PAYMENT PERMIT REGULATION 1 (2000), www.taxadmin.org/assets/docs/Publications/dpay.pdf; *see* MULTISTATE TAX COMM'N, MODEL DIRECT PAYMENT PERMIT REGULATION 122 (2000), http://www.mtc.gov/uploadedFiles/Multistate_Tax_Commission/Uniformity/Uniformity_Projects/A_-_Z/ModelDirectPaymentPermitReg.pdf (defining "direct payment permit" and explaining the process of and prerequisites for applying for such a permit).

183. *See supra* Part I.

184. *See supra* Part IV.

185. *See supra* Part III.

answer to the first two questions should be the same in both contexts, and it generally is, with the glaring exception of the U.S. RST's failure to tax the sale of services, remote or otherwise. With regard to the third question, the U.S. RST is actually better positioned to provide for robust enforcement of a tax on remote sales, whether in the B2C or B2B contexts, because of its national authority to require remote vendors to collect tax on intra-U.S. cross-border sales. Our failure to provide such authority and to jettison the archaic rule of *Quill Corp. v. North Dakota*[186]—a "case questionable even when decided" that "now harms [s]tates to a degree far greater than could have been anticipated earlier"[187]—is a self-inflicted wound that can be easily repaired with congressional surgery.

APPENDIX A: EQUIVALENCE BETWEEN THEORETICALLY IDEAL VAT AND RST

The central design feature of a VAT—the staged-collection process whereby each business in the supply chain remits a tax on the difference between the VAT imposed on its inputs and the VAT imposed on its outputs (i.e., its "value added")—coupled with the fundamental principle that the burden of the tax should not rest on businesses, requires a mechanism for relieving businesses of the burden of the VAT they remit. The method employed by most VAT regimes is the invoice-credit method, under which the business receives a credit for the tax it pays on its purchases (input tax) against the tax that it collects on its sales (output tax).[188]

The invoice-credit method can be illustrated by the following example.[189] Let us assume that a ten percent VAT is applied to the production and sale of notepads. We further assume that a tree

186. 504 U.S. 298, 311 (1992) (holding that vendors with no physical presence in a state lack the substantial nexus with the state that is a prerequisite to the state's authority to impose tax-collection duties on the vendors under the Commerce Clause).

187. Direct Mktg. Ass'n v. Brohl, 135 S. Ct. 1124, 1135 (2015) (Kennedy, J., concurring).

188. If the output tax is less than the input tax paid, e.g., for a start-up business or a business that exports its product (and therefore collects no tax on its sales), the business taxpayer can recover the difference from the taxing authority in the form of a refund. OECD, VAT/GST GUIDELINES, *supra* note 5, at 11. Although the VAT is a tax on transactions, it is worth noting that VAT returns (like U.S. RST returns) are normally filed on a periodic basis (monthly, bi-monthly, or quarterly), reflecting all relevant transactions occurring within the taxable period.

189. This example is taken from Hellerstein & Duncan, *supra* note 4, at 990.

farmer, who makes no purchases,[190] harvests trees and sells them to a paper mill for $100, plus a $10 VAT; the paper mill, in turn, produces paper that it sells to a printer for $150, plus a $15 VAT against which it credits the $10 VAT it paid, remitting the $5 balance to the government; the printer, in turn, binds and colors the paper, selling it to the retailer for $300 plus a $30 VAT against which it credits the $15 VAT it paid, remitting the $15 balance to the government; and the retailer sells the notepads to consumers for $500 plus a $50 VAT against which it credits the $30 VAT it paid, remitting the $20 balance to the government. These transactions are illustrated in the following table.[191]

Table 1: Invoice-Credit Method Under Ten Percent VAT

	Purchases	*Sales*	*Output Tax*	*Input Tax Credit*	*Net VAT Liability*
Tree Farmer	$0	$100	$10	$0	$10
Paper Mill	$100	$150	$15	$10	$5
Printer	$150	$300	$30	$15	$15
Retailer	$300	$500	$50	$30	$20
Total					$50

The ultimate result would be no different under an ideal RST with the same assumed facts. Assume that a ten percent RST is applied to the production and sale of notepads under the same economic assumptions that governed the VAT transactions described above. The tree farmer harvests trees and sells them to a paper mill for $100, charging no tax because he receives a "resale certificate" from the

190. This unrealistic (but harmless) assumption simply allows us to start the VAT chain with the tree farmer's sale rather than further "upstream" in the economic process (i.e., suppliers who sell to the tree farmer). We also assume unrealistically (but harmlessly) that the transactions described are the only transactions in which the various economic actors engage, thereby limiting the output tax and input tax credits to those generated by those transactions.

191. It is worth noting that the "purchase" and "sales" columns reflect a VAT-exclusive "price" to which the VAT is applied. Under most VATs, the actual sales price is VAT-inclusive, so that the tree farmer's price to the paper mill would be $110, the paper mill's price to the printer would be $165, etc. A more accurate—but for an American reader probably more confusing—table would have used the term "value" or "taxable value" for the column labeled "sales." It also would have complicated the comparison between a VAT and a RST.

paper mill.[192] The paper mill, in turn, produces paper that it sells to a printer for $150, again charging no tax because it receives a resale certificate from the printer. The printer, in turn, binds and colors the paper, selling it to the retailer for $300, again charging no tax because it receives a resale certificate from the retailer. Finally, the retailer sells the notepads to consumers for $500 plus a $50 RST, which it remits to the government. These transactions are illustrated in the following table.

Table 2: Application of Ten Percent RST to Facts of VAT Example

	Purchases	*Sales*	*Output (Sales) Tax*	*Input Tax Credit*	*Sales Tax Liability*
Tree Farmer	$0	$100	$0 (exempt sale for resale)	Not Applicable	$0
Paper Mill	$100	$150	$0 (exempt sale for resale)	Not Applicable	$0
Printer	$150	$300	$0 (exempt sale for resale)	Not Applicable	$0
Retailer	$300	$500	$50	Not Applicable	$50
Total					$50

The demonstration of the equivalence between these two sets of transactions under an ideal VAT and RST is hardly original.[193]

192. A seller, who generally must charge RST on taxable items, is relieved of this obligation if it receives a resale certificate from the purchaser, which indicates that the item is purchased for resale. Under these circumstances, the sale is exempt from tax. *See generally* 2 HELLERSTEIN, HELLERSTEIN & SWAIN, STATE TAXATION TREATISE, *supra* note 4, ¶ 14.02 (explaining when a sale for resale may be excluded from tax).

193. *See, e.g.*, Sijbren Cnossen, *A VAT Primer for Lawyers, Economists, and Accountants*, 55 TAX NOTES INT'L 319, 321 (2009) (demonstrating in Table 1 the equivalence of taxation between various forms of consumption tax, including VAT and RST).