NCSL Executive Committee Task Force on State and Local Taxation

Taxation in the On-Demand Economy

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Agenda

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- Delivery Services Overview
- Models
  - Traditional
  - Outsourcing
  - Customer-Arranged
  - Resale
- Taxation
- Predatory Lawsuits

Delivery Services Overview

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- In today's on-demand economy, delivery of just about anything you can imagine is available at the touch of a button.
- The same can be said for food—hence the recent development of the food delivery service industry (which largely did not exist 5 years ago).
- While still in it's early stages, this industry is one of the most heavily invested in startup sects in the past 3 years with companies like Blue Apron, Plated, Seamless and GrubHub leading the way.
  - There are literally hundreds of smaller and/or niche food delivery services that also occupy large portions of the market in many states and localities.
- Even more established companies like Uber and Starbucks (just to name a few) are beginning to exploit this ever-growing market.

Food Delivery Service Models

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- Wide variety in how companies structure food delivery.

1. **Traditional Model** – the customers contact the restaurant directly and the food is delivered by restaurant employees.
2. **Outsourcing Model** – the restaurant offers delivery by hiring a third party to deliver their food.
3. **Customer-Arranged Model** – the restaurant sells the food to the customer, who hires a third party to deliver it.
4. **Resale Model** – the customer purchases the food from a third party, who purchases it from a restaurant and then resells and delivers it to the customer.

Taxation of Food Delivery Services

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- While all four models many appear the same to the customer, the contractual structure chosen by the restaurant and third party (if any) frequently leads to different sales tax consequences based on state laws that did not envision the food delivery services that exist today.
- Common factors relevant in determining taxability include:
  - Who arranges for the delivery.
  - Whether the delivery charge is separately stated on the customer’s bill.
  - Whether the meal can be picked up (or not).
  - Where does the sale occur (*i.e.*, where is it sourced).

Taxation of Food Delivery Services (cont.)

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- As delivery services continue to exponentially grow in popularity and revenue, state policy makers must understand the various service models available in their state and how they are being taxed (or not). Policy questions include:
  - Is it fair to exempt delivery charges from common carriers, but not food delivery companies?
  - Should different results occur when delivery is via a third party?
  - Is the third party, the restaurant or both responsible for collecting?
  - Must the charge for delivery be separately stated on an invoice?
  - Does the current regime create a compliance burden for delivery services companies (consisting primarily of small start-up businesses)?
  - What result when the delivery crosses state/local lines?
- State policy makers are tasked with answering these questions and creating a logical set of rules that are easy to understand and comply with.

Predatory Lawsuits

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- There has been a significant increase in False Claims Act (under collection) and class action (over collection) lawsuits relating to the application of sales and use tax to delivery charges.
- <u>Examples</u>:
  - *Papa John's* and *Pizza Hut* class actions in Florida.
  - *Kean v. Wal-Mart* case in Illinois.
  - Hundreds of Illinois shipping and handling *qui tam* lawsuits.
- Companies entering this emerging market are pressured by the ever-increasing threat of a predatory lawsuit due to uncertainty in the law and complex compliance requirements.
  - A simple set of rules that delivery service businesses can easily implement will curb any uncertainty and eliminate the unwanted risk that currently surrounds them.

Questions?

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