

DISTRICT COURT, COUNTY OF JEFFERSON, COLORADO 100 Jefferson County Parkway Golden, CO 80401	DATE FILED: June 22, 2022 4:45 PM FILING ID: 4599CC7711295 CASE NUMBER: 2022CV30710
WAYFAIR LLC, Plaintiff v. CITY OF LAKEWOOD, COLORADO and MARK FERRANDINO in his capacity as EXECUTIVE DIRECTOR OF THE COLORADO DEPARTMENT OF REVENUE, Defendants	<p style="text-align: center;">▲ COURT USE ONLY ▲</p>
GEORGE S. ISAACSON (<i>pro hac vice</i> pending) MARTIN I. EISENSTEIN (<i>pro hac vice</i> pending) DAVID SWETNAM-BURLAND (<i>pro hac vice</i> pending) JAMIE E.T. SZAL (<i>pro hac vice</i> pending) Brann & Isaacson P.O. Box 3070 Lewiston, ME 04243-3070 Phone Number: 207-786-3566 FAX Number: 207-783-9325 gisaacson@brannlaw.com meisenstein@brannlaw.com dsb@brannlaw.com jszal@brannlaw.com ADAM W. CHASE, Atty. Reg. No. 20750 Hutchinson Black & Cook, LLC 921 Walnut St., Suite 200 Boulder, CO 80302 Phone Number: 303-441-7456 FAX Number: 303-442-6593 chase@hbcboulder.com Attorneys for Plaintiff	Case No.: Division:
COMPLAINT	

Pursuant to C.R.S. §§ 29-2-106.19(8)(a) and 39-21-105(3), Plaintiff Wayfair LLC (“Wayfair” or “Company”) gives written notice that it is appealing to this Court a final sales tax determination of Defendant City of Lakewood (“City” or “Lakewood”). To that end, Wayfair brings this complaint against the City and Defendant Mark Ferrandino (“Director”) in his capacity as the Executive Director of the Colorado Department of Revenue (“Department”), and states as follows:

INTRODUCTION

1. Wayfair, a leading e-commerce retailer based in Massachusetts, here challenges the authority of the City of Lakewood to issue a Notice of Deficiency (“Notice”) for hundreds of thousands of dollars in sales tax, interest, and penalties for the time period, May 2018 to May 2021 (“Tax Period”). The Commerce Clause of the U.S. Constitution prohibits a municipality from imposing tax obligations on out-of-state businesses, such as Wayfair, that unduly burden or discriminate against interstate commerce. Because the City’s sales tax ordinance in effect during the Tax Period *did* impose an undue burden *and* discriminated against interstate commerce during the Tax Period, among other reasons, Wayfair asks this Court to cancel the Notice and abate the assessment of tax, interest, or penalties against Wayfair.

2. Wayfair asserts an affirmative claim against the Director because the Department imposed an undue burden on interstate commerce during the Tax Period by failing to provide the safeguards and support required for out-of-state taxpayers as set out in greater detail below.

THE PARTIES

3. Wayfair is a Delaware limited liability company based in Boston, Massachusetts. It is one of the world's largest online destinations for the home, selling home goods at retail over the internet.

4. Lakewood is a home rule city in the State of Colorado ("State").

5. The Director is the head of the Department, a State agency. Pursuant to C.R.S. §§ 29-6-106.1(8)(d) and 39-21-105(6), the Director is a party to this proceeding.

JURISDICTION AND VENUE

6. The Court has jurisdiction over and venue is proper in this action pursuant to C.R.S. § 29-2-106.1(8)(b)(II).

FACTUAL BACKGROUND

The Notice of Deficiency

7. On October 20, 2021, the City issued the Notice, attached as Exhibit A, to Wayfair, asserting that Wayfair owes Lakewood \$460,518.69 in tax, \$46,051.87 in penalty, and \$97,751.61 in interest, totaling \$604,322.17 (plus any interest accruing after the date of the Notice).

8. Wayfair disputes that it owes any such amount of sales tax, interest, or penalty.

9. On October 21, 2021, Wayfair and the City executed an agreement authorizing Wayfair to proceed with its challenge to the Notice directly before the Executive Director of the Colorado Department of Revenue. A copy of that agreement is attached as Exhibit B.

10. After further discussions, on May 23, 2022, Wayfair and the City executed an agreement authorizing Wayfair to proceed with its challenge to the Notice directly in this Court. A copy of that agreement is attached as Exhibit C.

Wayfair's Business

11. Wayfair sells home furnishings and other goods on the Internet from its headquarters in Massachusetts. Wayfair has no offices, employees, or representatives in Colorado or Lakewood, except that in September 2017, Wayfair opened a distribution facility in Aurora, Colorado and employed personnel in that facility. Wayfair began collecting the State and State-administered local taxes and remitting them to the Department.

12. Wayfair did not employ drivers for deliveries at the facility until July 16, 2018. On or about July 16, 2018, Wayfair began to use drivers it employed to make deliveries in Lakewood and other locations for shipments.

13. The vast majority of items sold by Wayfair to Lakewood are delivered from out-of-state locations by common carrier and a small number are delivered by Wayfair truck drivers from its Aurora facility.

The City Sales Tax

14. During the Tax Period, Lakewood imposed a 3% sales tax on the retail sale of tangible personal property to persons located within its borders (subject to the exception discussed below).

15. The sales tax applied to sales from sellers outside Lakewood that made sales into Lakewood.

16. The relevant Lakewood Municipal Code definition of “engaged in business in the City” in effect as of July 16, 2018 was:

- A. *Engaged in Business in the City* means performing or providing services or selling, leasing, renting, delivering or installing Tangible Personal Property for Storage,

Use or consumption, within the city. Engaged in Business in the city includes, but is not limited to, any one of the following activities by a Person:

- B. Directly, indirectly or by a subsidiary maintains a building, store, office, salesroom, warehouse or other place of Business within the city;
- C. Sends one or more employees, agents or commissioned salespersons into the city to solicit Business or to install, assemble, repair, service or assist in the use of its products or for demonstration or other reasons;
- D. Maintains one or more employees, agents or commissioned salespersons on duty at a location within the city;
- E. Owns, leases, rents or otherwise exercises control over real or personal property within the city; or
- F. If the Person is a Retailer in the State of Colorado, the Person makes more than one delivery into the city within a 12-month period;

17. The municipal ordinance enacted by Lakewood that became effective on January 16, 2021 (replacing the definition of “Engaged in Business in the City” in the foregoing paragraph) provides:

Economic Nexus

G. Means the connection between the city and a Person not having a physical nexus in the State of Colorado, which connection is established when the Person makes retail sales into the city, and:

- 1. In the previous calendar year, the Person has made retail sales into the State exceeding the amount specified in C.R.S. § 36-102(3)(c), as amended; or

2. In the current calendar year, ninety (90) days has passed following the month in which the Person has made retail sales into the State exceeding the amount specified in C.R.S. § 36-102(3)(c), as amended.

3. This definition does not apply to any Person who is doing business in this state but otherwise applies to any other Person.

4. For the purpose of clarity, the definition of "Person" includes any Marketplace Facilitator.

Engaged in Business in the City means performing or providing services or selling, leasing, renting, delivering or installing Tangible Personal Property for Storage, Use or consumption, within the city. Engaged in Business in the city includes, but is not limited to, any one of the following activities by a Person:

- A. Directly, indirectly or by a subsidiary maintains a building, store, office, salesroom, warehouse or other place of Business within the city;
- B. Sends one or more employees, agents or commissioned salespersons into the city to solicit Business or to install, assemble, repair, service or assist in the use of its products or for demonstration or other reasons;
- C. Maintains one or more employees, agents or commissioned salespersons on duty at a location within the city;
- D. Owns, leases, rents or otherwise exercises control over real or personal property within the city;
- E. If the Person is a Retailer in the State of Colorado, the Person makes more than one delivery into the city within a 12-month period; or

F. Makes retail sales sufficient to meet the definitional requirements of "Economic Nexus" as set forth in this section.

16. Lakewood amended its ordinances concerning the administration/collection of sales/use tax effective on January 16, 2021 to join the Colorado State Department of Revenue's Sales & Use Tax System (SUTS) as described in the following stipulation. This was the first time that a retailer could use the state-wide system providing for geo codes.

17. Taxpayers who use the SUTS to determine applicable use tax rates are held harmless for any incorrect data reported by that system as of April 1, 2021; before joining the SUTS, Lakewood did not provide a similar protection to taxpayers reporting use tax directly to the City.

18. The city limits of Lakewood include addresses in multiple zip codes, including: 80123, 80226, 80227, 80228, 80232, 80214, 80215, 80401, 80235, 80123, 80127, and 80465. Many of these zip codes, *i.e.*, 80123, 80214, 80215, 80227, 80228, 80235, 80401, and 80465 cover geographic areas that include addresses within the Lakewood city limits and addresses outside the city limits. For those zip codes, a retailer cannot rely on the zip code associated with an address alone to ascertain whether that address is inside or outside of the City of Lakewood.

The Belmar Public Improvement Fee

19. The Belmar district (Belmar or district) is a geographical area within Lakewood defined by ordinance.

20. Pursuant to a plan to redevelop the Belmar district, a covenant was placed on the Belmar district by its developer.

21. The covenant created a Public Improvement Fee (PIF) of 2.5% on in-person sales in Belmar.

22. The covenant provided that, in accordance with a public financing amendment, the public improvements costs connected with the Belmar district would be paid, in part, through a waiver by the City of one-half of its then-2% sales tax (*i.e.*, 1%) coupled with the imposition, through the recording of a PIF covenant, of a PIF in the amount of 2.5% on all retail sales within the district.

23. The PIF was in effect during all time periods at issue in this proceeding.

24. The PIF is a fee not a tax, which is applied to in-person sales of goods made in Belmar.

25. For purposes of calculating applicable sales tax, the amount of the taxable sales price of a good sold at retail in Belmar includes the PIF.

26. The PIF does not become, and cannot be used as, revenue of the City of Lakewood.

27. Rather, the PIF is used to finance the costs of new public improvements in the Belmar district, such as public parking, streets, utilities, parks, public spaces, and public art.

28. Funds from the PIF are used exclusively for such public improvements to the district.

29. The PIF was not adopted by referendum, and Lakewood is not a party to the covenant establishing the PIF.

30. The PIF is imposed on retailers operating businesses on land in the Belmar district, and the obligation to pay it runs with the land until the bonds for capital improvements to the district are paid and the PIF expires, an event which has not yet occurred.

31. After the covenant was entered, Lakewood signed an agreement with the developer of Belmar to reduce the Lakewood sales tax in the district to 1% (the abatement) and adopted an ordinance that did so.

32. Pursuant to that ordinance, O-2002-7, the City of Lakewood temporarily waived one half of its two percent (2%) sales tax (resulting in a one percent (1%) sales tax) imposed pursuant to the City's sales and use tax ordinance for any sale occurring within the Belmar district.

33. The abatement was in effect during all time periods at issue in this proceeding.

34. After the City raised its sales tax rate to 3%, the abatement to 1% for sales consummated in the Belmar district remained in effect, *i.e.*, sales in the district were subject to a 1%, not 3%, sales tax.

35. The abatement applies to all sales consummated in the district, for goods not sent outside the district for delivery.

36. Specifically, a sale made by a retailer within the district, whether transferred to the buyer at a store, *e.g.*, the Best Buy Belmar store, located at 384 S. Wadsworth Blvd., Lakewood CO 80226, or delivered to a residential address within the district is at only a 1% sales tax rate, not the 3% rate charged elsewhere inside Lakewood but outside the district.

37. A purchase from a merchant physically located in the Belmar district would also require the payment of a PIF at the rate of 2.5% of the purchase price, in addition to the sales tax of 1% whereas a purchase from a merchant located outside of the Belmar district but delivered into the Belmar district requires a payment of a sales tax of 3% but no PIF payment.

38. A sale made by a retailer outside the district and delivered to a residential address within the district is not eligible for the abatement, but is subject to the general Lakewood sales tax rate of 3%.

39. In other words, a sale made on the Internet by a retailer located outside Belmar, whether located in Lakewood or another state, is subject to a 3% sales tax rate.

The Dormant Commerce Clause

40. The Commerce Clause, U.S. Const. art. I, § 8, cl. 3, places certain material limitations on the authority of a state or local government to impose obligations to collect and remit sales tax on an out-of-state business. Those limitations have been defined by the Supreme Court in a series of opinions.

41. “Two primary principles...mark the boundaries of a State’s authority to regulate interstate commerce. First, state regulations may not discriminate against interstate commerce; and second, States may not impose undue burdens on interstate commerce.” *South Dakota v. Wayfair, Inc.*, 138 S.Ct. 2080, 2090-91 (June 21, 2018).

42. “These principles also animate the Court’s Commerce Clause precedents addressing the validity of state taxes.” *Wayfair*, 138 S.Ct. at 2091. They govern municipal ordinances as well. *See, e.g., Dean Milk Co. v. City of Madison, Wis.*, 340 U.S. 349 (1951) (invalidating municipal ordinance on Commerce Clause grounds).

43. The Supreme Court has set out a four-part test for whether a state or municipal tax comports with the Commerce Clause, U.S. Const., art. I, § 8, cl. 3, in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). The test

consider[s] not the formal language of the tax statute but rather its practical effect, and [] sustain[s] a tax against Commerce Clause challenge when the tax [1] is

applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State.

Id. at 279 (brackets added).

44. With respect to the “nexus” prong of the test, until June 21, 2018, the applicable test required a sufficient *physical* presence in the taxing jurisdiction. *See National Bellas Hess, Inc. v. Ill. Dep’t of Revenue*, 386 U.S. 753, 759-60 (1967); *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

45. As of June 21, 2018, when the Supreme Court issued its opinion in *Wayfair*, sufficient nexus can be established through economic and virtual contacts with the taxing jurisdiction, provided the taxing jurisdiction provides adequate safeguards against discrimination and an undue burden are provided. *Wayfair*, 138 S.Ct. at 2099-2100.

COUNT I
Undue Burden on Interstate Commerce in Violation
of the Commerce Clause of the United States Constitution, Art. I, Sec. 8, Cl. 3
(The City and the Director)

46. *Wayfair* repeats and incorporates the foregoing paragraphs as if set forth here.

47. By issuing the Notice, the City asserted the authority to impose sales tax collection and remittance obligations on *Wayfair* for the Tax Period.

48. The application of the Lakewood sales tax to *Wayfair* in the Notice imposes an undue burden on interstate commerce.

49. Specifically, the City has asserted the authority to require *Wayfair* to collect and remit Lakewood sales tax during a Tax Period during which neither the City nor the Director provided, for example, a single, state-wide system of tax administration for all state and local taxes; nor did the City or Director provide access to tax administration software paid for by the City

and/or State that, if used, would immunize Wayfair from audit liability. Neither the City nor the Director took reasonable measures to mitigate the burdens on an out-of-state business, such as Wayfair, of attempting to comply with the complex, overlapping, and competing sales tax ordinances of the State, 71 home rule jurisdictions, regional transportation districts, special districts, and statutory municipalities in Colorado.

50. The City is one of 71 home rule jurisdictions in Colorado, each with its own tax regime. Home rule cities, including Lakewood, charge a separate registration fee to a retailer such as Wayfair. Moreover, each of these jurisdictions claim the right to audit out-of-state retailers like Wayfair, potentially exposing a company like Wayfair to 70-plus individual audits for the same tax period.

51. In addition to separate sales taxes for each home rule city, the State of Colorado imposes a sales tax, as do numerous, often overlapping regional transportation districts, special districts, and statutory municipalities—not to mention the other 45 states (including the District of Columbia) that impose sales taxes, and numerous local jurisdictions within those states.

52. Attempting to comply with the requirements of all of these taxing jurisdictions is complicated and expensive. For example, to file the Colorado state return plus returns for the 71 home rule jurisdictions requires a company like Wayfair to compile a 150-page spreadsheet for each return filed.

53. Moreover, neither the City nor the Director provides a common database or other repository of the definitions each of these jurisdictions applies to identify taxable and non-taxable goods and services.

54. Further, during the Tax Period, neither the City nor the Director provided a database or software that a retailer could use secure in the knowledge that, if it did, it would be immunized from audit liability for any errors.

55. On top of that, although the State provides some compensation for the expenses related to tax collection, the City does not provide any such compensation.

56. The overwhelming burden of these obligations exposes Wayfair's business to a number of harms, including, to name but a few: claims of over-collection by customers; the tarnishing of Wayfair's good will; and the out-of-pocket cost to Wayfair of collecting and remitting home rule sales taxes without compensation from cities like Lakewood.

57. Attempting to navigate these complex, overlapping, and competing obligations is an administrative nightmare, and an undue burden on interstate commerce.

58. Moreover, by failing to provide adequate safeguards and support for out-of-state retailers, the City and the Director placed a further undue burden on interstate commerce.

59. Based on the foregoing, the Court should cancel the Notice and abate any assessment of tax, interest, or penalties against Wayfair.

COUNT II
Discrimination against Interstate Commerce in Violation
of the Commerce Clause of the United States Constitution, Art. I, Sec. 8, Cl. 3
(Lakewood)

60. Wayfair repeats and incorporates the foregoing paragraphs as if set forth here.

61. By issuing the Notice, the City has asserted the authority to impose sales tax collection and remittance obligations on Wayfair.

62. The application of the Lakewood sales tax to Wayfair in the Notice discriminates against interstate commerce in at least the following ways.

63. *First*, the City discriminated against out-of-state retailers by treating them differently from retailers physically located in the Belmar district who were authorized to charge a lower rate of tax.

64. *Second*, the City discriminated against out-of-state retailers, such as Wayfair, by applying a different sourcing rule to their sales than applied to sales by businesses located in the City. While a business located in the City could treat a sale it made as sourced to its physical location, a business like Wayfair, that made online sales from outside the State was required to source those sales to the City, not the location from which they were made.

65. *Third*, for periods after January 16, 2021, the City discriminated against out-of-state retailers, such as Wayfair, by applying a definition of “Engaged in Business” that treats out-of-state retailers differently from similarly situated in-state retailers, *i.e.*, retailers based in Colorado, but not physically present in Lakewood.

66. As a result, the City imposes on out-of-state retailers obligations it does not impose on in-state retailers in violation of the Commerce Clause.

67. Based on the foregoing, the Court should cancel the Notice and abate any assessment of tax, interest, or penalties against Wayfair.

COUNT III
Wayfair Did Not “Engage in Business” in Lakewood
(City)

68. Wayfair repeats and incorporates the foregoing paragraphs as if set forth here.

69. Wayfair was not “engaged in business” in Lakewood during the Tax Period under the holding of *Associated Dry Goods Corp. v. City of Arvada*, 197 Colo. 491 (1979), which provides that, as a matter of Colorado law, “the taxpayer must be engaged in a business having a

fixed or transitory situs in the taxing jurisdiction,” *id.* at 495, and that “[d]elivery alone is an insufficient nexus.” *Id.* Wayfair did not have the required fixed or transitory situs with Lakewood during the Tax Period because its only presence was via delivery service provided by Wayfair in only a small percentage of Wayfair’s deliveries—the vast majority of Wayfair deliveries were from out of state by common carrier.

70. Under the ordinance in effect until January 16, 2021, the City could only impose an obligation to collect and remit sales tax on an out-of-state business if that company is “engaged in business” in Lakewood.

71. For time periods before January 16, 2021, Wayfair was not engaged in business in Lakewood as defined in the applicable ordinance.

72. Accordingly, it was improper for the City to assess sales tax, interest, and penalties against Wayfair, and the Court should cancel the Notice and abate any assessment of tax, interest, or penalties against Wayfair during that time period.

COUNT IV
Wayfair Lacked Substantial Nexus with Lakewood
under the Commerce Clause of the United States Constitution, Art. I, Sec. 8, Cl. 3

73. Wayfair repeats and incorporates the foregoing paragraphs as if set forth here.

74. Before June 21, 2018, the governing legal standard for determining whether a state or municipality could impose sales tax collection and remittance obligations on an out-of-state business was set out in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), *National Bellas Hess, Inc. v. Ill. Dep’t of Revenue*, 386 U.S. 753, 759-60 (1967), and *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992)

75. For the time period, May 1, 2018, to June 21, 2018, Wayfair did not have a sufficient physical presence nexus with the City to satisfy the nexus prong of the *Complete Auto* test.

76. Accordingly, it was improper for the City to assess sales tax, interest, and penalties against Wayfair for that time period, and the Court should cancel the Notice and abate any assessment of tax, interest, or penalties against Wayfair for that time period.

PRAYER FOR RELIEF

WHEREFORE, Wayfair requests that the Court:

- A. Cancel the Notice and abate any amount assessed against Wayfair;
- B. Award Wayfair its costs; and
- C. Award such further relief as the Court deems just and proper.

Respectfully submitted,

Dated: June 22, 2022

HUTCHINSON BLACK and COOK, LLC

By: /s/ Adam W. Chase
Adam W. Chase

Motions for pro hac vice admission pending:

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