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SOUTH DAKOTA V. WAYFAIR: AN ILL-CONCEIVED BLOW TO THE FREE FLOW OF INTERSTATE COMMERCE

ABSTRACT

For more than a century, brick-and-mortar retailers have been losing local customers—first with the rise of mail-order houses and then more acutely with the rapid growth of online retail. As a result, states have noticed a significant loss in sales tax revenue. While an equivalent amount of tax is typically still owed to the state in the form of a use tax, which is to be remitted to the state by the customer, because these taxes are not automatically collected at the time of the sale, customers have overwhelmingly elected not to pay them. In an effort to recover this lost tax revenue, a number of states have passed legislation obligating out-of-state retailers—particularly large mail-order houses and internet retailers—to collect and remit sales taxes in the same manner as in-state businesses. Twice in the twentieth century, the Supreme Court of the United States found such legislation to be unconstitutional on either Due Process or Commerce Clause grounds, or both. From these decisions, the "physical presence rule" was born; it required that a business have qualifying property or sales force within a state before the state could compel the business to collect and remit sales taxes. In an act of desperation, South Dakota challenged the physical presence rule in 2016, and in June 2018, the Supreme Court reversed its position, abrogating the rule it had previously established and upheld. This Note argues that the Supreme Court's decision was flawed in both its analysis and outcome and that state legislation, such as the legislation passed by South Dakota, places an unconstitutional burden on interstate commerce and may violate certain retailers' due process rights.

INTRODUCTION

On June 21, 2018, the Supreme Court of the United States handed down a five-to-four decision in *South Dakota v. Wayfair, Inc.*[1] that bore considerable sales tax implications for retailers engaging in interstate sales. Prior to this decision—since before the advent of internet retail and perhaps even fostering its growth[2]—companies engaging in interstate commerce were spared the task of collecting and remitting sales taxes in any state in which they lacked a "physical presence."[3] In other words, a seller had to have a physical presence, such as "retail outlets, solicitors, or property within a

1. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018).

2. *See id.* at 2097; *see also id.* at 2101, 2104 (Roberts, C.J., dissenting) (noting that "[e]-commerce has grown into a significant and vibrant part of our national economy against the backdrop of established rules, including the physical-presence rule" and that such rules "may well have been an unintended factor contributing to the growth of e-commerce").

3. *See id.* at 2091–92.

state," before the state could compel the seller to collect and remit taxes on the state's behalf.[4] The resulting bright-line rule, which has come to be known as "the physical presence rule,"[5] served to "firmly establish[] the boundaries of legitimate state authority to impose a duty *to collect* sales . . . taxes."[6]

Even though remote sellers have not always been required to collect sales taxes in states where they lack a physical presence, the buyer still owes the tax.[7] A "complementary sales tax and use tax regime" is employed in every state that imposes a sales tax, which is all but five states.[8] More specifically, when sales taxes are due but not collected by the seller for whatever reason, the buyer is responsible for paying a "use tax" to the state at a rate equal to the state's sales tax.[9] Even so, where such taxes have not been directly collected by the seller at the time of purchase, buyers in great numbers have historically forgone paying them altogether.[10] It is estimated that uncollected sales and use taxes collectively amount to tens of billions of dollars of lost tax revenue annually for the states.[11] In South Dakota alone, it is estimated that $48 to $58 million of revenue is lost each year.[12]

Although the Supreme Court had been unwilling to grant states the authority to compel out-of-state sellers to collect sales taxes in the past,[13] in

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4. *Id.* at 2091 (quoting Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 754–55 (1967)); *see also* Quill Corp. v. North Dakota, 504 U.S. 298, 315 (1992) ("Whether or not a [s]tate may compel a vendor to collect a sales or use tax may turn on the presence in the taxing [s]tate of a small sales force, plant, or office.").

5. *Wayfair, Inc.*, 138 S. Ct. at 2088 (2018).

6. *Quill Corp.*, at 315 (emphasis added). In general, a seller calculates and adds sales taxes to the cost of taxable goods and services and then remits such taxes to the state. Accordingly, sales taxes are *paid* by the buyer and are *collected* by the seller. *See infra* Part II.

7. *See* Marc Brandeis & Daniel W. Layton, *South Dakota v. Wayfair: From International Shoe to Interstate Sales Tax*, 60 ORANGE COUNTY LAW. 32, 32 (2018) (noting that "[t]here is a common misconception that tax is not due from a purchase made from an out-of-state seller who does not collect tax").

8. *See id.* ("[A]ll of the forty-five states, including California, that impose sales tax also impose a 'use tax'."); *see also* Emily Stewart, *One Chart Shows the Impact of the Supreme Court's Big Sales Tax Decision*, VOX (June 21, 2018, 11:40 AM), https://www.vox.com/policy-and-politics/2018/6/21/17488472/south-dakota-wayfair-amazon-stock (noting that "all but five states—Alaska, Delaware, Montana, New Hampshire, and Oregon—impose sales taxes").

9. *Wayfair, Inc.*, 138 S. Ct. at 2088.

10. *See id.* (noting the "impracticability" of collection and that "consumer compliance rates are notoriously low" when South Dakota must rely on its residents to pay the use tax owed on their purchases from out-of-state sellers that lack a physical presence); *see also* The Associated Press, *Supreme Court Hears Case on Online Sales Tax*, CBS NEWS (Apr. 16, 2018, 7:04 AM), https://www.cbsnews.com/news/supreme-court-hears-case-on-online-sales-tax/ ("States generally require consumers who [were not] charged sales tax on a purchase to pay it themselves . . . [b]ut . . . have found that only about 1 percent to 2 percent actually pay.").

11. *Wayfair, Inc.*, 138 S. Ct. at 2088 (citing tax reports estimating lost revenue to range anywhere from $8 to $33 billion).

12. *Id.* (citing lost revenue figures given by South Dakota's Department of Revenue).

13. *See id.* at 2102 (Roberts, C.J. dissenting) (noting that it "is neither the first, nor the second, but the third time [the Supreme] Court has been asked whether a [s]tate may obligate sellers with no physical presence within its borders to collect tax on sales to residents").

2016, the South Dakota legislature decided to test the waters once again and passed Senate Bill 106 (S.B. 106).[14] S.B. 106 was introduced as an emergency measure to boost tax revenue by addressing South Dakota's inability to recover use taxes from its residents on purchases made from remote sellers.[15] It requires that certain out-of-state sellers, even those without a physical presence in South Dakota, collect sales tax "*as if* the seller had a physical presence in the state."[16] Under S.B. 106, any remote seller that earns more than $100,000 in gross revenue from goods or services delivered in South Dakota or conducts 200 or more taxable transactions within the state, either in the current calendar year or in the previous year, is obligated to collect and remit sales taxes.[17] Spurred by South Dakota's plea for the Supreme Court to review its precedent in light of the current economic times, the Court agreed to "reconsider the scope and validity of the physical presence rule."[18]

Prior to *Wayfair*, which challenged the constitutionality of S.B. 106, the Supreme Court had twice before faced the question of "whether an out-of-state retailer that delivered goods by mail or common carrier to customers located within the taxing [s]tate could constitutionally be required to collect and pay state taxes on those transactions."[19] A quarter century earlier, this issue was addressed in *Quill Corp. v. North Dakota*[20] and a quarter century before that in *National Bellas Hess, Inc. v. Department of Revenue of Illinois*.[21] In both instances, the Supreme Court held that a seller that lacked

14. *See* S.D. Codified Laws § 10-64-2 (2016); *see* S.D. Codified Laws § 10-64-1(10) (2016) ("[T]he [South Dakota] Legislature recognizes that the enactment of this law places remote sellers in a complicated position, precisely because existing constitutional doctrine calls this law into question."); *see also* SOUTH DAKOTA LEGISLATIVE RESEARCH COUNCIL, https://sdlegislature.gov/Legislative_Session/Bills/Bill.aspx?Bill=106&Session=2016 (last visited Apr. 18, 2020).

15. *See* S.D. Codified Laws § 10-64-1 (2016) ("The Legislature finds that . . . [t]he inability to effectively collect the sales or use tax from remote sellers who deliver tangible personal property, products transferred electronically, or services directly into South Dakota is seriously eroding the sales tax base of this state . . . .").

16. S.D. Codified Laws § 10-64-2 (2016) (emphasis added).

17. *See id.* Oddly, the dollar threshold and the transaction threshold differ in that the one-hundred-thousandth dollar earned is *not* taxable whereas the two-hundredth transaction completed is taxable. While perhaps *de minimis*, deciphering the exact threshold from one tax jurisdiction's sales tax statutes to the next could present a further challenge for remote sellers and compliance software, and it could inadvertently lead to errors as well as litigation resulting from such errors. *Id.*

18. *Wayfair, Inc.*, 138 S. Ct. at 2088–89 ("South Dakota conceded that the Act cannot survive under *Bellas Hess* and *Quill* but asserted the importance, indeed the necessity, of asking [the Supreme] Court to review those earlier decisions in light of current economic realities.").

19. Brief for the United States as Amicus Curiae Supporting Petitioner at 4, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494). For the sake of clarity, this might have been written "collect and *remit* state taxes" rather than "collect and pay state taxes." *See infra* note 68 (discussing the circumstances under which a vendor may be obligated to pay sales taxes on behalf of a customer).

20. Quill Corp. v. North Dakota, 504 U.S. 298 (1992).

21. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753 (1967).

"a physical presence" in the state could not be so obligated.[22] In *Wayfair*, however, the Supreme Court changed course[23] and dealt a mighty blow to remote sellers—particularly internet retailers—as well as the free flow of interstate commerce as a whole.[24]

Part I of this Note explores the limitations that the Commerce Clause[25] and the Due Process Clause[26] place on a state's authority to require out-of-state sellers to collect and remit sales or use taxes. Part II makes note of the inapposite framework under which the Supreme Court decided *Wayfair* and suggests the proper framework under which the decision should have been made. Part III argues that the Supreme Court failed to properly assess the impact that state sales tax laws like South Dakota's S.B. 106 will have on interstate commerce in potential violation of the Commerce Clause and also the risk that such laws may violate certain out-of-state sellers' due process rights. Part IV proposes that Congress should extend the protections of Public Law 86-272 to the collection of sales taxes to preserve the effect of the physical presence rule and that, despite a state's authority to impose sales taxes on its residents, the extensive growth of internet retail has perhaps rendered the collection of sales taxes too complex and costly to justify their continued implementation and protection by the courts.

I. CONSTITUTIONAL LIMITS ON THE AUTHORITY OF STATES TO TAX OUT-OF-STATE SELLERS

Prior to the 1950s, states were generally precluded from taxing interstate commerce, including interstate sales.[27] Over the second half of the twentieth century, however, the Supreme Court began allowing states to tax certain interstate activities where businesses benefitted from government services.[28] Even so, twice during this time, first in *Bellas Hess* and then in *Quill*, the Supreme Court cited either Due Process or Commerce Clause grounds, or both, for striking down state laws that required out-of-state vendors to collect sales taxes on behalf of their in-state customers.[29] While, in effect, there is some overlap between the Due Process and Commerce Clauses, each clause reflects a different concern and should therefore be analyzed as if each were

22. *See Nat'l Bellas Hess, Inc.*, 386 U.S. at 758; *see also Quill Corp.*, 504 U.S. at 317–18.

23. *See Wayfair, Inc.*, 138 S. Ct. at 2099 (concluding "that the physical presence rule . . . is unsound and incorrect").

24. *But see id.* at 2090 (noting that the Supreme Court has, in general, been tasked by Congress with the *protection* of "the free flow of interstate commerce").

25. *See* U.S. CONST. art. 1, § 8, cl. 3.

26. *See* U.S. CONST. amend. XIV, § 1.

27. *See* Brief of Tax Foundation as Amicus Curiae in Support of Neither Party at 5–6, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494) (citing Freeman v. Hewitt, 329 U.S. 249, 252–53 (1946) and Leloup v. Port of Mobile, 127 U.S. 640, 648 (1888)).

28. Brief of Tax Foundation, *supra* note 27, at 6.

29. *See* Quill Corp. v. North Dakota, 504 U.S. 298, 305 (1992); *see also* Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 756 (1967).

separate and distinct from the other.[30] That said, the Supreme Court has often elided the distinction between the two clauses.[31]

In general, the Commerce Clause limits a state's ability to compel out-of-state businesses to pay and collect taxes, but it does not render states powerless to tax any form of interstate commerce.[32] Especially within their borders and in respect to their residents, states are accorded broad powers of taxation;[33] however, the U.S. Constitution specifically grants Congress the power "[t]o regulate [c]ommerce . . . among the several [s]tates."[34] Moreover, the Supreme Court has consistently held this grant of authority to Congress "to contain a further, negative command, known as the [D]ormant Commerce Clause, prohibiting certain state taxation even when Congress has failed to legislate on the subject."[35] In turn, modern Commerce Clause jurisprudence recognizes two restrictions on the states' authority to regulate interstate commerce: state regulations may neither "discriminate against interstate commerce" nor may states "impose undue burdens on interstate commerce."[36]

30. *Quill Corp.*, 504 U.S. at 305–06.

31. *See* Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 756 (1967) (finding that a claim of due process violation and creating an unconstitutional burden upon interstate commerce "are closely related"); *see also* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2091 (2018) (finding that "*Bellas Hess* linked due process and the Commerce Clause together"); E. Kendrick Smith, Michael Wynne & Douglas Wick, *Chaos Ahead for Remote Sellers*, LAW360 (July 20, 2018), https://www.law360.com/articles/1065361/chaos-ahead-for-remote-sellers (noting that "[t]he court [in *Wayfair*] has effectively collapsed the commerce clause nexus analysis into a due process analysis"); *see infra* Part III.

32. *See Quill Corp.*, 504 U.S. at 305 (noting that the Due Process Clause and Commerce Clause "pose distinct limits on the taxing powers of the [s]tates"); *see also* Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 288 (1977) ("[T]he Court has rejected the proposition that interstate commerce is immune from state taxation."); W. Live Stock v. Bureau of Revenue, 303 U.S. 250, 254 (1938) ("It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden . . . . and the bare fact that one is carrying on interstate commerce does not relieve him from many forms of state taxation which add to the cost of his business.").

33. *See Complete Auto Transit, Inc.*, 430 U.S. at 280 (noting that the Court has recognized that "a [s]tate could constitutionally tax local manufacture, impose license taxes on corporations doing business in the [s]tate, tax property within the [s]tate, and tax the privilege of residence in the [s]tate and measure the privilege by net income, including that derived from interstate commerce"); *see also Wayfair, Inc.*, 138 S. Ct. at 2091.

34. U.S. CONST. art. 1, § 8, cl. 3.

35. Comptroller of Treasury v. Wynne, 135 S. Ct. 1787, 1794 (2015) (quoting Oklahoma Tax Comm'n v. Jefferson Lines, Inc., 514 U.S. 175, 179 (1995)); *accord* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2089 (2018) ("Although the Commerce Clause is written as an affirmative grant of authority to Congress, this Court has long held that in some instances it imposes limitations on the [s]tates absent congressional action."); *Quill Corp.*, 504 U.S. at 309 ("[T]he Commerce Clause is more than an affirmative grant of power; it has a negative sweep as well . . . [and by its own power, it] prohibits certain state actions that interfere with interstate commerce.").

36. *Wayfair, Inc.*, 138 S. Ct. at 2091; *see Comptroller of the Treasury*, 135 S. Ct. at 1794 ("[A] [s]tate may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the [s]tate . . . . Nor may a [s]tate impose a tax which discriminates against interstate commerce either by providing a direct commercial advantage to local business, or by subjecting interstate commerce to the burden of multiple taxation.").

Independently, the Due Process Clause also places limitations on a state's authority to burden individual businesses engaging in interstate commerce. First, due process requires "that a 'minimum connection' exist 'between a state and the person, property[,] or transaction that it seeks to tax.'"[37] While a business's connection with a state can understandably be enhanced by being physically located within the state, a physical presence is not necessary to satisfy the demands of due process.[38] Second, due process requires that the income attributed to a state for tax purposes is "rationally related to values connected with the taxing [s]tate."[39] Unlike the Commerce Clause—which seeks to "prevent [s]tates from engaging in economic discrimination so they [do] not divide into isolated, separable units"[40]—due process "centrally concerns the fundamental fairness of government activity" and therefore whether "an individual's connections with a [s]tate are substantial enough to legitimate the [s]tate's exercise of power over [the individual]."[41] In sum, while both clauses share a fundamental concern for fair treatment, the Due Process Clause seeks to ensure that an individual business is not treated unfairly by the government, whereas the Commerce Clause aims to prevent states from adopting laws and regulatory practices that negatively affect interstate commerce, especially by means of treating out-of-state businesses unfairly.[42]

Implicating both clauses, the first challenge to state legislation that sought to obligate an out-of-state seller to collect sales taxes came in 1967.[43] That year, in *Bellas Hess*, the Supreme Court held that a Kansas mail-order house "'whose only connection with customers in [Illinois was] by common carrier or the United States mail' lacked the requisite minimum contacts with the [s]tate required by both the Due Process Clause and the Commerce

37. Brief for the United States as Amicus Curiae Supporting Petitioner at 13 n. 1, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494) (quoting *Quill Corp.*, 504 U.S. at 305–06); *see* Miller Brothers Co. v. Maryland, 347 U.S. 340, 344–45 (1954).

38. *See Wayfair, Inc.*, 138 S. Ct. at 2093; *see also* Burger King Corp. v. Rudzewicz, 471 U.S. 462, 476 (1985).

39. *Quill Corp.*, 504 U.S. at 306 (quoting Moorman Mfg. Co. v. Bair, 437 U.S. 267, 273 (1978)) (internal quotation marks omitted); *see* Norfolk & W. R. Co. v. Mo. State Tax Comm'n, 390 U.S. 317, 324 (1968) ("[A] [s]tate is not entitled to tax tangible or intangible property that is unconnected with the [s]tate.").

40. *Wayfair, Inc.*, 138 S. Ct. at 2093–94; *accord* Hughes v. Oklahoma, 441 U.S. 322, 325 (1979) (noting that the Commerce Clause reflected the Framers' desire "to avoid the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the [s]tates").

41. *Quill Corp.*, 504 U.S. at 312.

42. Notably, because due process concerns individual protections from both state and federal government, unlike its authority to regulate interstate commerce under the Commerce Clause, Congress does not have the power to authorize violations of the Due Process Clause. *See id.* at 305.

43. *See* Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 755 (1967) (noting that the relevant Illinois statute required a seller to collect sales taxes on orders "received or accepted within or without [the] [s]tate").

Clause" to impose the duty of sales tax collection upon it.[44] The mail-order house had been sending catalogues to its active or recent customers twice a year and did not otherwise advertise in Illinois.[45] At that time, the Court noted that "it is difficult to conceive of commercial transactions more exclusively interstate in character than the mail order transaction . . . involved."[46] The Illinois statute, which significantly pre-dated the internet, only conceived of retailers that were "engaging in soliciting orders . . . by means of catalogues or other advertising," so physical sales materials were often entering the state at the time.[47]

In 1992, the Supreme Court in *Quill* revisited its earlier decision in *Bellas Hess*.[48] Like *Bellas Hess*, *Quill* also involved a mail-order house that solicited business through catalogs and flyers.[49] This time, the mail-order house had been placing advertisements in national periodicals and engaging in telemarketing.[50] Following a 1987 revision to its definition of "retailer" to include one who engaged in "regular or systematic solicitation of a consumer market in th[e] state," North Dakota sought the payment of sales taxes from certain out-of-state businesses, including the mail-order house.[51] In response, the mail-order house challenged North Dakota's constitutional authority to compel it to collect and remit sales taxes since the business had "neither outlets nor sales representatives in the [s]tate."[52] While the Supreme Court in *Bellas Hess* had analyzed the Commerce and Due Process Clauses together, it reviewed them separately in *Quill* and overruled the due process but not the Commerce Clause holding.[53]

In *Quill*, the Supreme Court noted an evolution in due process jurisprudence since *Bellas Hess*, especially in "the area of judicial jurisdiction."[54] By the advent of *Quill*, it had been determined that a lawsuit could be maintained against a corporation that "purposefully avail[ed] itself of the benefits of an economic market in the forum [s]tate," even if the corporation had no physical presence in that state.[55] Accordingly, the Court in *Quill* concluded that because a lawsuit could be brought against certain

44. *Wayfair, Inc.*, 138 S. Ct. at 2091 (quoting *Nat'l Bellas Hess, Inc.*, 386 U.S. at 754–55).

45. *See Nat'l Bellas Hess, Inc.*, 386 U.S. at 754.

46. *Id.* at 759.

47. *Id.* at 755 (citation omitted).

48. *See generally* Quill Corp. v. North Dakota, 504 U.S. 298 (1992) (reviewing the *Bellas Hess* decision in light of both due process and Commerce Clause developments in the Court's jurisprudence over the previous 25 years).

49. *Cf. id.* at 300, 302, *with* Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 754 (1967).

50. *Quill Corp.*, 504 U.S. at 302–03 (citation omitted).

51. *Id.* at 302–03 (citation omitted).

52. *Id.* at 301.

53. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2091 (2018) (citing *Quill Corp.*, 504 U.S. at 307–08, 317–18).

54. *Quill Corp.*, 504 U.S. at 307; *see* discussion *infra* Section III.B.

55. *Quill Corp.*, 504 U.S. at 307.

out-of-state companies, "[c]omparable reasoning" justified allowing a state to impose a duty to collect sales taxes on certain companies as well.[56] More specifically, the Court concluded that the Due Process Clause did not prohibit a state from imposing a duty to collect sales taxes on an out-of-state mail-order house that "purposefully directed its activities at [the state's] residents" by engaging in the "continuous and widespread solicitation of business" there.[57] Despite finding state legislation that imposed a duty to collect sales taxes on certain out-of-state businesses permissible under the Due Process Clause, the Supreme Court found such legislation impermissible under the Commerce Clause.[58] The physical presence rule from *Bellas Hess* was reaffirmed in *Quill*.[59]

II. THE KEY ISSUE IN *WAYFAIR* WAS IMPROPERLY FRAMED

In a handful of cases leading up to its decision in *Wayfair*, the Supreme Court had been asked to resolve two disparate, yet seemingly similar, issues. At certain times, the Court was asked to determine whether a state had the constitutional authority to hold a business responsible for the *payment* of a state tax—specifically an out-of-state business that was operating, at least marginally, within the taxing state.[60] At other times, the Court was asked to determine whether a state had the constitutional authority "to deputize an out-of-state retailer as its collection agent,"[61] that is, to determine whether a state had the authority to hold an out-of-state business responsible for the *collection* of a state tax that the business itself had no obligation to pay. Although the nature of these inquiries is distinct, the Supreme Court has not always been successful in clearly distinguishing between them.

In *Quill*, for instance, the Supreme Court presented the issue as involving a state's attempt to impose a duty on out-of-state vendors to collect sales taxes from in-state customers, but at times, the Court also indicated that there was

56. *Id.* at 308.

57. *Id.*; *accord* Brief for the United States, *supra* note 37, at 4.

58. *See Quill Corp.*, 504 U.S. at 314–15 (finding that the "bright-line rule of *Bellas Hess* furthers the ends of the dormant Commerce Clause" and avoids placing an undue burden on interstate commerce); *see also Wayfair, Inc.*, 138 S. Ct. at 2092 ("[T]he *Quill* majority concluded that the physical presence rule was necessary to prevent undue burdens on interstate commerce.").

59. *See Quill Corp.*, 504 U.S. at 317–18 (1992); *accord Wayfair, Inc.*, 138 S. Ct. at 2091–92 ("[T]he Court in *Quill* . . . reaffirmed the physical presence rule.").

60. *See, e.g.*, Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 277 (1977) (assessing the constitutionality of a state tax imposed on a Michigan corporation that transported motor vehicles from train stops in Mississippi to car dealerships in Mississippi); *e.g.*, Polar Tankers, Inc. v. City of Valdez, 557 U.S. 1, 5 (2009) (assessing the constitutionality of an Alaskan city's ordinance that ultimately imposed a tax on large oil tankers that entered its port and were owned by a non-Alaskan company); *e.g.*, Mobil Oil Corp. v. Comm'r of Taxes, 445 U.S. 425, 427 (1980) (assessing the "constitutional limits on a nondomiciliary [s]tate's taxation of income received by a domestic corporation in the form of dividends from subsidiaries and affiliates doing business abroad").

61. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 757 (1967); *see, e.g.*, *Quill Corp.*, 504 U.S. at 302–03.

a question of whether the transactions were themselves taxable.[62] Specifically, the Court suggested that the physical-presence requirement from *Bellas Hess* served to avoid undue burdens on interstate commerce by demarcating "a discrete realm of commercial activity *that is free from interstate taxation*."[63] The Court further attributed the growth of the mail-order industry, in part, to "the bright-line *exemption from state taxation*" that the physical-presence requirement created.[64] These, however, are mischaracterizations of the issue. In both *Bellas Hess* and *Quill*, sales taxes are being imposed on residents of the taxing state, and the validity of these taxes is not in question.[65] Moreover, having never been obligated to pay sales taxes, the out-of-state seller is clearly not exempt from paying taxes under *Bellas Hess* but instead spared from collecting them.

Like *Quill* before it, the *Wayfair* opinion similarly suffers from mischaracterizations of the key issue. Again, the Court acknowledges that it must "determine when an out-of-state seller can be required to collect and remit [a state sales tax.]"[66] Later in the opinion, however, the Court asserts that "*Quill* has come to serve as a judicially created *tax shelter for businesses*,"[67] irrespective of the fact that no out-of-state business has an underlying duty *to pay* sales taxes.[68] This duty remains with the buyer in the form of a use tax.[69] Additionally, with a questionable use of square brackets,

62. *See* Brief for the United States, *supra* note 37, at 14; *see also Quill Corp.*, 504 U.S. at 301, 315 (describing the issue as involving "a [s]tate's attempt to require an out-of-state [seller] . . . to collect and pay a use tax" and noting the physical presence rule "firmly establishes the boundaries of legitimate state authority to impose a duty to collect sales and use taxes").

63. *Quill Corp.*, 504 U.S. at 314–15 (emphasis added); *accord* Brief for the United States, *supra* note 37, at 14.

64. *Quill Corp.*, 504 U.S. at 316 (emphasis added); *accord* Brief for the United States, *supra* note 37, at 14.

65. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2092 (2018) ("It has long been settled that the sale of goods or services has a sufficient nexus to the [s]tate in which the sale is consummated to be treated as a local transaction taxable by that [s]tate."); *see also* Oklahoma Tax Comm'n v. Jefferson Lines, Inc., 514 U. S. 175, 184 (1995).

66. *Wayfair, Inc.*, 138 S. Ct. at 2087, 2093 (noting that "the central dispute is whether South Dakota may require remote sellers to collect and remit the tax without some additional connection to the state").

67. *Id.* at 2094.

68. The duty to pay sales taxes belongs primarily to the consumer. Critically, before any seller could have a duty to pay the sales taxes itself, it must first have a duty to collect the tax. This threshold issue—whether a state law that imposes just such a *collection duty* on an out-of-state seller is constitutional—is precisely the issue that *Wayfair* seeks to resolve. *See Wayfair, Inc.*, 138 S. Ct. at 2087. Consequently, if a seller is determined to have a duty to collect a sales tax and fails to do so, it would then, and only then, be responsible for its payment. *See* Brief for Etsy, Inc. as Amicus Curiae Supporting Respondents at 24, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494) (noting that "[a] business that fails to collect the tax from earlier purchasers, and then later exceeds the threshold, presumably itself will be on the hook for remitting the amounts owed or be in violation of the law").

69. This is not to say that an out-of-state seller does not benefit at all from a consumer being more easily able to evade paying sales taxes, as consumers effectively pay a lower price for goods if they forgo their obligation to pay the use tax to the state. Even so, making tax evasion easier for

the Supreme Court in *Wayfair* modified its earlier finding in *Polar Tankers, Inc. v. City of Valdez*.[70] In *Polar Tankers*, the Supreme Court found that a "substantial nexus" is established "when the taxpayer 'avails itself of the substantial privilege of carrying on business' in that jurisdiction."[71] In *Wayfair*, using square brackets, the Court expanded this finding not only to cover the activities of *taxpayers* but also those of *tax collectors*.[72] In *Polar Tankers*, however, the obligation *to pay* the tax was challenged by the taxpayer, while the obligation *to collect* the tax did not factor into the opinion.[73]

As with the states' authority in *Bellas Hess* and *Quill*, South Dakota's authority to impose a sales tax on in-state buyers is neither challenged nor at issue in *Wayfair*.[74] In *Wayfair*, the Supreme Court correctly asserts "that South Dakota has the authority to tax . . . sales of tangible personal property, products transferred electronically, or services for delivery into South Dakota."[75] Regardless of whether the seller collects the sales tax, it is imposed on the consumer and is owed by the consumer at the time of the transaction.[76] As the tax itself is not challenged, the Supreme Court need not inquire whether South Dakota *may tax* particular events or transactions between its residents and out-of-state sellers but only whether the state can require out-of-state sellers *to collect and remit* such taxes.[77] At the heart of this confusion is the Supreme Court's treatment of *Complete Auto Transit, Inc. v. Brady*[78] starting in its opinion in *Quill*.

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consumers is not equivalent to the seller being spared from owing state tax, so it is inaccurate to state that the physical presence rule creates a tax shelter for businesses.

70. *See infra* note 72 (clarifying the Court's modification); *see also* Polar Tankers, Inc. v. City of Valdez, 557 U.S. 1, 11 (2009).

71. *Polar Tankers, Inc.*, 557 U.S. at 11.

72. *See Wayfair, Inc.*, 138 S. Ct. at 2099. *Compare id.* ("[S]uch a nexus is established when the taxpayer [or collector] 'avails itself of the substantial privilege of carrying on business' in that jurisdiction."), *with Polar Tankers, Inc.*, 557 U.S. at 11 ("[S]uch a nexus is established when the taxpayer 'avails itself of the substantial privilege of carrying on business' in that jurisdiction.").

73. *Polar Tankers, Inc.*, 557 U.S. at 5 (invalidating a city ordinance that imposed a property tax on certain boats, the application of which was limited in effect to large oil tankers that were owned by an out-of-state corporation).

74. *Wayfair, Inc.*, 138 S. Ct. at 2087, 2092 ("All concede that taxing the sales in question here is lawful" and "agree that South Dakota has the authority to tax these transactions.").

75. *Id.* at 2092 (emphasis and internal quotation marks omitted); *accord* Okla. Tax Comm'n v. Jefferson Lines, 514 U.S. 175, 184 (1995) ("It has long been settled that a sale of tangible goods has a sufficient nexus to the [s]tate in which the sale is consummated to be treated as a local transaction taxable by that [s]tate."); Brief for the United States, *supra* note 37, at 8 ("States indisputably may tax sales to state residents by out-of-state retailers.").

76. *See* Brief for the United States, *supra* note 37, at 17–18; *see also* Miller Bros. Co. v. Maryland, 347 U.S. 340, 352–53 (1954) ("The collection of the use tax from inhabitants is a difficult administrative problem, and if out-of-state vendors can be compelled to collect it and remit it to the taxing state, it simplifies administration. But this raises questions of great importance to particular taxpayers, to the course of commercial dealing among the states and as to appropriation by other states of tax resources properly belonging to the state where the event occurs.")

77. *See* Brief for the United States, *supra* note 37, at 13.

78. Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977).

In *Complete Auto*, the Supreme Court established a test for when a tax will be "*sustained* . . . against [a] Commerce Clause challenge."[79] A Michigan-based corporation had been in the business of transporting cars—which were manufactured outside of Mississippi—from a train station located in Jackson, Mississippi to dealerships throughout the rest of the state.[80] At that time, Mississippi imposed taxes on all "transportation companies" that received payment for the transportation of goods or people between "points within [the s]tate."[81] After being assessed sales taxes and interest for its services over a three-year period, the Michigan-based corporation contended that transporting the cars to the dealerships was only part of a greater interstate movement and that the taxes were "unconstitutional as applied to operations in interstate commerce."[82]

While *Complete Auto* presented a state tax issue, the issue was whether Mississippi could require an out-of-state car manufacturer *to pay* state taxes for transporting cars from the train station in Mississippi to dealerships throughout the rest of the state. In other words, the state challenged the notion that the purely in-state final leg of the cars' journey to a dealership was immune from taxation just because the cars had originated from an out-of-state manufacturing plant. The Supreme Court was interested only in the effect that a state tax would have on interstate commerce and rejected the "proposition that interstate commerce is immune from state taxation" when such taxes did not produce "a forbidden effect."[83] Next, putting forward a four-prong test, the Court determined that a state tax imposed on an out-of-state business will be sustained: "[1] when the tax is applied to an activity with a *substantial nexus* with the taxing [s]tate, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the [s]tate."[84]

In *Quill*, the Supreme Court reviewed contemporaneous Commerce Clause jurisprudence and contemplated the impact that its decision in *Complete Auto* might have on *Bellas Hess*.[85] The appropriate conclusion should have been none whatsoever. Nevertheless, the Court found that while its decision in *Complete Auto* did not "undercut the *Bellas Hess* rule,"[86] *Bellas Hess* ultimately concerned the first prong of the *Complete Auto* test and "[stood] for the proposition that a vendor whose only contacts with the taxing state are by mail or common carrier lacks the 'substantial nexus'

79. *Id.* at 279 (emphasis added).

80. *See id.* at 276.

81. *See id.* at 275.

82. *Id.* at 277.

83. *Id.* at 288; *accord* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2091 (2018).

84. *Complete Auto Transit, Inc.*, 430 U.S. at 279 (emphasis added). This set of requirements is what has come to be known as the "*Complete Auto* test." *See Wayfair, Inc.*, 138 S. Ct. at 2091, 2099.

85. Quill Corp. v. North Dakota, 504 U.S. 298, 310–11 (1992).

86. *Id.* at 312. In *Quill*, "the *Bellas Hess* rule" refers to the physical-presence requirement. *See id.* at 301, 317–18.

required by the Commerce Clause."[87] In other words, the Court determined that the physical presence rule was grounded in the first prong of the *Complete Auto* test—the substantial-nexus requirement.[88] This introduction of the substantial-nexus requirement and "attempt to harmonize *Bellas Hess* and *Complete Auto*" was not only unnecessary but also misconceived.[89]

Both *Bellas Hess* and *Quill* were only concerned with the seller's obligation to collect taxes that were paid by the in-state buyer, not the sellers. *Complete Auto*, in contrast, provides a framework for determining the validity of a state tax that is being imposed on an out-of-state seller and is facing Commerce Clause scrutiny. Under *Complete Auto*, an activity that lacked a substantial nexus to the taxing state, thus failing the first prong of the *Complete Auto* test, simply could not be taxed.[90] *Bellas Hess*, *Quill*, and *Wayfair* were fundamentally never about a state's taxing authority because the validity of the sales tax being imposed on in-state buyers was never at issue,[91] and no tax was being imposed on businesses at all. Instead, these cases sought to determine the constitutional limits of a state's power to impose an administrative duty—which happened to be tax collection—on businesses located entirely outside of the state. In the end, the introduction of the *Complete Auto* test in *Quill* unnecessarily injected the framework for analyzing the validity of a state taxes under the Commerce Clause into a line of cases where the underlying validity of the state taxes was never at issue.

After *Quill*, the Supreme Court repeated its folly in *Wayfair* and again looked to *Complete Auto* as well as to *Polar Tankers*.[92] Nevertheless, because *Wayfair*'s key issue is regulatory in nature—a state imposing a collection duty on an out-of-state seller where the underlying tax is clearly valid—it would be more appropriately analyzed under "[D]ormant Commerce Clause precedents that have addressed the [s]tates' imposition of regulatory burdens *other than* taxes."[93] Rather than looking to *Complete Auto* and *Polar Tankers*, the general balancing framework set forth in *Pike v. Bruce Church, Inc.*[94]

87. *Id.* at 311. The introduction of the *Complete Auto* test in *Quill* was unwarranted but its application was also flawed. In *Quill*, the first prong of the *Complete Auto* test is understood not to have been met in *Bellas Hess*, as a seller "whose only contact with the taxing [s]tate are by mail or common carrier lacks the 'substantial nexus' required by the Commerce Clause;" however, "the commercial activity clearly *does* have a 'substantial nexus' to the taxing [s]tate, even when the retailer's only contact with that [s]tate involve deliveries by mail or common carrier." *Id.* at 311; Brief for the United States, *supra* note 37, at 17.

88. *See Wayfair, Inc.*, 138 S. Ct. at 2092 (noting that the *Quill* court "grounded the physical presence rule in *Complete Auto*'s requirement that a tax have a 'substantial nexus' with the activity being taxed"); *see also Quill Corp.*, 504 U.S. at 311.

89. *See* Brief for the United States, *supra* note 37, at 8, 14–17.

90. *See id.* at 15.

91. *See Wayfair, Inc.*, 138 S. Ct. at 2092. The Supreme Court in *Wayfair* correctly noted that "[i]t ha[d] long been settled that the sale of goods or services has a sufficient nexus to the [s]tate in which the sale is consummated to be treated as a local transaction taxable by that [s]tate." *Id.*

92. *See id.* at 2099.

93. *See* Brief for the United States, *supra* note 37, at 17–18.

94. Pike v. Bruch Church, Inc., 397 U.S. 137 (1970).

would have been a more appropriate starting place for the Dormant Commerce Clause concerns that arose in *Wayfair*. In *Pike*, the Supreme Court determined that state laws that impose only "incidental" burdens on interstate commerce and "regulate[] even-handedly to effectuate a legitimate local public interest . . . will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits."[95]

III. THE CONSTITUTIONAL ANALYSIS IN *WAYFAIR* IS FLAWED

In *Bellas Hess*, *Quill*, and *Wayfair*, the difference between the protections that the Due Process Clause provides out-of-state sellers and the implications that the Dormant Commerce Clause has on a state's authority to regulate or impose duties on out-of-state sellers engaged in interstate commerce are not always clearly articulated. Starting in *Bellas Hess*, the Supreme Court "conflated due process and commerce clause concerns"[96] and simply determined that a seller without a physical presence in the state "lacked the requisite *minimum contacts* with the [s]tate required by both [clauses]."[97] In *Quill*, however, the Court spelled out the significance of the difference between the clauses and suggested that *Complete Auto*'s "'substantial nexus' requirement is not, like due process' 'minimum contacts' requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce."[98] Despite the Court's efforts in *Quill*, in *Wayfair*, it "effectively collapsed the commerce clause analysis into a due process analysis" once again.[99]

In *Wayfair*, without the physical presence rule in effect, the Court sought to resolve the issue at hand under the first prong of the *Complete Auto* test.[100] The first prong "simply asks whether the tax applies to an activity with a *substantial nexus* with the taxing state."[101] While this was a misguided application of the *Complete Auto* test,[102] the Court still found that—in addition to a taxpayer—a *tax collector* also establishes a substantial nexus with a state when it "avails itself of the substantial privilege of carrying on

95. *Id.* at 142; *Wayfair, Inc.*, 138 S. Ct. at 2091.

96. Smith, Wynne & Wick, *supra* note 31.

97. *Wayfair, Inc.*, 138 S. Ct. at 2091; *see* Int'l Shoe Co. v. Washington, 326 U.S. 310, 316 (1945) ("[D]ue process requires only that in order to subject a defendant to a judgment in personam, if he be not present within the territory of the forum, he have certain *minimum contacts* with it such that the maintenance of the suit does not offend traditional notions of fair play and substantial justice.") (emphasis added).

98. Quill Corp. v. North Dakota, 504 U.S. 298, 313 (1992).

99. Smith, Wynne & Wick, *supra* note 31.

100. *See Wayfair, Inc.*, 138 S. Ct. at 2099.

101. *Id.* (emphasis added).

102. *See supra* Part II (suggesting that the Court mistakenly introduced this framework for determining the validity of a state sales tax when only the validity of South Dakota's law requiring out-of-state retailers *to collect* such taxes from their South Dakota customers was at issue).

business" in that state.[103] While this "availment" language is quoted from *Polar Tankers*, its origin is the due process clause analysis from *Mobil Oil Corp. v. Commissioner of Taxes of Vermont*[104] rather than a Commerce Clause analysis.[105]

The Supreme Court next determined that a substantial nexus with South Dakota is clearly established by the large, national retailers in question based on "both the economic and virtual contacts [that they] have with the [s]tate."[106] The Court noted that South Dakota's S.B. 106 only applied "to sellers that deliver more than $100,000 of goods or services in South Dakota or engage in 200 or more separate transactions for the delivery of goods and services into the [s]tate on an annual basis."[107] According to the Court, at least in South Dakota, this quantity of business "could not have occurred unless the seller availed itself of the substantial privilege of doing business" there and that such sellers "undoubtedly maintain an extensive virtual presence" in the state.[108] As for future guidance, the Court did not define "substantial nexus" outside of "its observation that South Dakota's statutory threshold of 200 sales transactions or $100,000 in sales revenue seems to meet it."[109]

Additionally, the Supreme Court questioned "whether some other principle in the Court's Commerce Clause doctrine might invalidate [South Dakota's S.B. 106]" and addressed the concern for potential "discrimination against or undue burdens upon interstate commerce."[110] Indeed, the Court noted that "these two principles guide the courts in adjudicating cases challenging state laws under the Commerce Clause."[111] While the Court suggested that South Dakota's tax system includes certain measures to avoid discriminatory effects or undue burdens on interstate commerce, its analysis is found wanting. Conceivably, as a result of collapsing its Commerce Clause analysis into a due process analysis, the Court in *Wayfair* shifted the brunt of its focus onto the potential individual unfairness that an out-of-state company may face in being obligated to collect and remit sales taxes (a due process

103. Polar Tankers, Inc. v. City of Valdez, 557 U.S. 1, 11 (2009); *see Wayfair, Inc.*, 138 S. Ct. at 2099 (expanding its earlier finding in *Polar Tankers* to include tax "collector[s]" as well as "taxpayers"); *see* Smith, Wynne & Wick, *supra* note 31 (noting that "[t]his is virtually identical to the due process clause rule stating 'if a foreign corporation purposefully avails itself of the benefits of an economic market in the forum state' it can be required to collect tax absent commerce clause considerations").

104. *See* Mobil Oil Corp. v. Comm'r of Taxes, 445 U.S. 425, 436–37 (1980).

105. *See* Smith, Wynne & Wick, *supra* note 31.

106. *Wayfair, Inc.*, 138 S. Ct. at 2099.

107. *Id.*

108. *Id.*

109. *See* Smith, Wynne & Wick, *supra* note 31.

110. *Wayfair, Inc.*, 138 S. Ct. at 2099. The Court had noted that "[o]ther aspects of the Court's doctrine can better and more accurately address any potential burdens on interstate commerce, whether or not *Quill*'s physical presence rule is satisfied." *Id.* at 2093.

111. *Id.* at 2091.

concern) and away from the overall impact that permitting such an obligation may have on interstate commerce (a Commerce Clause concern).

A. THE COMMERCE CLAUSE

The physical presence rule has perhaps "been the target of criticism over many years from many quarters,"[112] but it has also served to prevent states from enacting sales tax legislation that imposed undue burdens on interstate commerce in violation of the Commerce Clause. In *Wayfair*, by overruling its earlier decision in *Quill*—finding that "the physical presence rule . . . is an incorrect interpretation of the Commerce Clause"[113] and "unsound and incorrect"[114]—the Supreme Court failed to properly measure the burden that would be imposed on interstate commerce in the rule's absence. The majority in *Quill* acknowledged that the physical presence rule was "artificial at its edges"[115] but concluded that it was "necessary to prevent undue burdens on interstate commerce."[116] In *Wayfair*, the Court dismantled this safeguard and left little guidance in its place.[117]

By abrogating the physical presence rule, not only has South Dakota's S.B. 106 been permitted to stand but other states have been invited "to pass more onerous legislation to test the limits of the [D]ormant Commerce Clause, which will in turn only spur more litigation about the exact contours of what the Clause allows."[118] Within a year of the *Wayfair* decision, almost every state that imposes a sales tax enacted legislation similar to S.B. 106; moreover, several of these states have modified S.B. 106's statutory thresholds, lack key similarities to South Dakota in their tax systems, and are seeking to use the *Wayfair* decision to impose additional taxes other than

112. *Id.* at 2092 (quoting Direct Mktg. Assn. v. Brohl, 814 F.3d 1129, 1148, 1150–51 (10th Cir. 2016) (Gorsuch, J., concurring)); *see id.* at 2101 (Roberts, C.J., dissenting) (noting the majority, in overruling the physical presence rule, is acting to "expiate a mistake it made over 50 years ago"); *see also* Brief for the United States, *supra* note 37, at 7 ("[*Quill's*] bright-line rule, which lacks support in the Court's broader dormant Commerce Clause jurisprudence, is misconceived."). While the Court only offers a single example of criticism, states have been critical of the physical presence rule because it provides in-state buyers with a greater opportunity to avoid paying sales taxes, as the tax is not automatically collected by the out-of-state seller. The buyer is therefore responsible for paying a use tax, which many buyers fail to do.

113. *Wayfair, Inc.*, 138 S. Ct. at 2092.

114. *Id.* at 2099.

115. Quill Corp. v. North Dakota, 504 U.S. 298, 315 (1992); *see also Wayfair, Inc.*, 138 S. Ct. at 2095.

116. *Wayfair, Inc.*, 138 S. Ct. at 2092.

117. *See* B. Derek Rose and John P. Barrie, *INSIGHT: 'Wayfair' One Year Later—Where We Are and What's Next*, BLOOMBERG TAX (Oct. 23, 2019), https://news.bloombergtax.com/daily-tax-report-state/insight-wayfair-one-year-later-where-we-are-and-whats-next (stating that "many unanswered questions remain as to the extent and limits of the *Wayfair* decision and the collection of sales taxes" and noting, among other examples, that the Court "did not address whether the $100,000/200 transaction thresholds were minimums or whether a lower threshold would be permissible").

118. Brief for Etsy, *supra* note 68, at 29.

sales and use taxes.[119] Without sufficient guidance from the Court, each state's effort to shift tax collection duties onto out-of-state companies runs the risk of violating the Commerce Clause's prohibition against placing undue burdens on interstate commerce.

Even at the time *Wayfair* was decided, the burden that a state tax law like S.B. 106 placed on interstate commerce was more substantial than the Court took into account. First, in the absence of the physical presence rule, remote sellers undoubtedly face high compliance and litigation costs. Second, like South Dakota's S.B. 106, laws that seek to obligate foreign retailers to collect sales taxes will ultimately create market distortions that favor these foreign companies. Third, fledgling businesses are inadequately spared from the burdens of tax collection by the "safe harbor" provisions adopted in S.B. 106. Fourth, the Supreme Court's attempt to level the playing field for in-state and out-of-state retailers is based on a misguided sense of equity and an inaccurate understanding of the role that internet retailers play in society. Lastly, allowing each taxing jurisdiction to shift the local administrative burden of tax collection onto out-of-state sellers places a greater compliance burden on these remote sellers than local brick-and-mortar stores, which may produce a discriminatory effect prohibited by the Commerce Clause.

1. The Cost of Compliance and Litigating Errors

Since *Quill* was decided in 1992, the upheld physical presence rule had "permitted start-ups and small businesses to use the [i]nternet as a means to grow their companies and access a national market, without exposing them to the daunting complexity and business-development obstacles of nationwide sales tax collection."[120] As the *Wayfair* dissent noted, the majority "breezily disregard[ed] the costs that its decision will impose on [internet and remote] retailers."[121] With over 10,000 jurisdictions levying sales taxes at different rates and with different exemptions, accurately collecting and remitting sales taxes at the proper rate is no small task;[122] moreover, the need to determine which goods are taxable in each jurisdiction as well as each jurisdiction's tax-free holidays significantly contributes to the complexity of properly assessing taxes.[123] In fact, as taxing jurisdictions do not necessarily

119. *See* Rose & Barrie, *supra* note 117 ("Nearly every state imposing a sales tax has now enacted *Wayfair* legislation . . . . [M]any states are looking at applying *Wayfair* with respect to income taxes," and unlike South Dakota, several of these states are not compliant with the Streamlined Sales and Use Tax Agreement (SSUTA), which the Supreme Court considered in *Wayfair* in regard to the reduction of compliance burdens.); *see also Wayfair, Inc.*, 138 S. Ct. at 2098–99 (discussing the importance of South Dakota's adoption of the SSUTA).

120. *Wayfair, Inc.*, 138 S. Ct. at 2098.

121. *Id.* at 2103 (Roberts, C.J., dissenting).

122. *See id.*; *see also* Brief for Etsy, *supra* note 68, at 13–14.

123. *See Wayfair, Inc.*, 138 S. Ct. at 2103–04 (Roberts, C.J., dissenting).

correspond to ZIP codes, it can be dauting to even determine which tax jurisdiction's taxes, if any, are applicable to any given transaction.[124]

Even though software to lessen the compliance costs for online retailers might seem plausible, it does not currently exist[125] nor will any software in the foreseeable future be able to "accurately account for how thousands of tax codes (with inconsistent rules, jurisdiction to jurisdiction, that frequently change) apply to tens of thousands of products."[126] The majority in *Wayfair* speculates that, "[e]ventually, software . . . at a reasonable cost may make it easier for small businesses to cope with these problems,"[127] but even if such software were a reality, it would likely come at no small expense at first, which alone would place a significant burden on businesses seeking to engage in interstate commerce that they would not face otherwise. Furthermore, assuming that such software were viable and sophisticated enough to avoid making potentially costly errors, "the most arduous part of the process is often placing an item in the correct tax categories for each jurisdiction in which the product may be taxed."[128]

To further complicate this matter, some goods are exempted from sales tax based on the status of the seller; others are exempted based on their use, characteristics, or ingredients; and still others are exempted from sales tax based on the status of the buyer.[129] In determining whether sales tax should be collected, knowledge that one is selling a flag, for example, is insufficient by itself. Some states allow exemptions for their own flags as well as American flags.[130] Some states allow exemptions only for flags sold by "nonprofit veteran groups" or "government agencies."[131] In some states, nonprofit organizations are exempted from paying sales taxes, as are buyers that intend to use a good to manufacture another good, as are goods that will be resold or will be used in certain types of construction.[132] For the purpose of assessing sales taxes, it can also be necessary to make note of the ingredients of certain items and whether such items require refrigeration, as

124. Brief for Etsy, *supra* note 68, at 19 (noting "one part of the ZIP code area may be in a taxing jurisdiction, while another may not" and that the ZIP code 57717, for example, covers six different counties in three different states, one of which has no sales tax).

125. *See id.* at 2, 13 ("Modern tax compliance software does not have enough functionality to obviate the administrative burden that was the deciding concern for this Court in *Bellas Hess* and *Quill*.").

126. *Id.* at 2, 13–14 (noting that "the burden is multi-faceted" and requires "the mapping of thousands of tax codes (with their respective exceptions, exemptions, and holidays), the mapping of millions of unique products to those thousands of tax codes, and the overlaying of matrices of exemptions tied to the status of sellers and buyers," making it doubtful that such software will ever exist).

127. *Wayfair, Inc.*, 138 S. Ct. at 2098.

128. Brief for Etsy, *supra* note 68, at 9.

129. *See id.* at 16–18; *see, e.g.*, N.Y. Tax Law § 1115(s) (McKinney 2019) (exempting "the sale of any good or service necessary for the . . . maintenance of a guide dog").

130. *See* Brief for Etsy, *supra* note 68, at 16.

131. *See id.* at 17.

132. *See id.* at 18.

these can determine the taxability of the items in certain jurisdictions.[133] In turn, "[c]lassifying a product . . . for tax compliance purposes will not capture these nuanced differences in exemption laws[,]" and "it will be nearly impossible to capture every classification, every exemption, and every judicial or administrative interpretation of every exemption in every taxing jurisdiction across the country."[134]

The burden of complying with each taxing jurisdiction's sales tax also includes determining "whether an out-of-state seller has a substantial presence in the jurisdiction" or rather finding out and adhering to the sales thresholds at which an out-of-state seller is required to collect taxes in each jurisdiction.[135] While an out-of-state seller with fewer than 200 transactions is exempt from collecting sales tax in South Dakota,[136] the threshold figure is bound to vary from jurisdiction to jurisdiction—conceivably "in proportion to their population or total economy relative to South Dakota's."[137] Additionally:

> Once exposed to a [s]tate's taxation requirements, a seller must not only report and remit taxes, it must also respond to information requests, remain vigilant about continued compliance with the ever-changing requirements of state and local law, and defend itself from regulatory and judicial scrutiny in the form of audits and enforcement actions.[138]

This remains true for every tax jurisdiction in which a seller has made a sale.

The combined burden of compliance and the "significant financial and regulatory obligations, bearing potential civil and criminal liability for non-compliance" may very well "drive small businesses away from the interstate market."[139] Without the physical presence rule, "remote sellers will be exposed to the growing risks in multiple jurisdictions of state False Claims Act lawsuits and consumer fraud lawsuits, which are costly to defend even when baseless."[140] In several states,[141] False Claims Act lawsuits are allowed

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133. *See id.* at 15–16 (noting that, despite its appearance, any food product that contains flour or requires refrigeration is not "candy" under Washington law and therefore is not exempt); *see also Wayfair, Inc.*, 138 S. Ct. at 2103–04 (Roberts, C.J., dissenting) (noting that plain deodorant in Texas is taxable but not if it contains antiperspirant).

134. *See* Brief for Etsy, *supra* note 68, at 14, 17 ("Classifying a product for just one jurisdiction . . . requires knowledge not only of the applicable statutes and regulation, but also interpretive guidance from courts and administrative agencies addressing similar fact patterns.").

135. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2103 (2018) (Roberts, C.J., dissenting).

136. S.D. Codified Laws § 10-64-2 (2016).

137. Brief of Tax Foundation, *supra* note 27, at 16.

138. Brief for Etsy, *supra* note 68, at 23.

139. *See id.* at 22.

140. Smith, Wynne & Wick, *supra* note 31.

141. *See State False Claims Act Reviews*, OFF. INSPECTOR GEN., https://oig.hhs.gov/fraud/state-false-claims-act-reviews/index.asp (last visited Apr. 18, 2020) (listing the requirements to qualify for the financial incentive under section 1909 of the Social Security Act as well as the states that the Office of the Inspector General has approved).

to be brought against a business that is believed to have under-collected sales taxes. Consumer fraud lawsuits, on the other hand, can be brought for the perceived over-collection of sales taxes.[142] In turn, while these statutes were enacted to prevent fraud against consumers and the government, "they are frequently used by profit-driven third-parties to challenge the tax compliance of businesses in the hopes of reaping a financial reward."[143]

For a seller that is obligated to collect and remit sales taxes to a state in which it is not located, the burden of compliance is compounded by the heightened burden of having to litigate any errors—that is, lawsuits resulting from the perceived over- or under-collection of sales taxes—in *that* state. Under the Tax Injunction Act,[144] enacted in 1937, sellers are denied access to the federal courts for the purpose of litigating state tax disputes, so "any remote seller unhappy with a sales tax audit assessment or administrative hearing will be forced to litigate its dispute in the courts of the assessing state."[145] Notably, at the time *Wayfair* was decided, South Dakota already had legislation in place allowing consumers to pursue a lawsuit in order to recover sales taxes paid in excess of what was owed.[146]

Additionally, "while South Dakota portrays itself in [*Wayfair*] as the champion of small businesses, it is the smallest businesses that [will] be hurt" by abandoning the physical presence rule.[147] Even though newer and smaller businesses have smaller tax bills, they are generally more affected by compliance costs than larger, more established businesses due to a higher proportion of overhead and the inability to take advantage of economies of scale.[148] Small businesses are likely to be more affected by "the costs of additional employee training and hiring, compliance software, tax return preparation[,] and audit defense."[149] That said, the burden of sales tax compliance does not end with start-ups and smaller businesses. Its effect is also felt outside of the businesses themselves. In light of the decision in

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142. *See* Smith, Wynne & Wick, *supra* note 31; *see also* Kathleen Saunders Gregor, Elizabeth Smith & Stefan Herlitz, *Threat of Sales Tax Overcollection Suits Grows Post-Wayfair*, LAW360 (June 20, 2019), https://www.law360.com/tax-authority/articles/1169121/threat-of-sales-tax-overcollection-suits-grows-post-wayfair (providing background on the avenues for pursuing compliance-related sales tax actions against businesses post-*Wayfair*).

143. Smith, Wynne & Wick, *supra* note 31 ("Many of these lawsuits are baseless, but lucrative nonetheless because a seller, even if innocent, is faced with the choice of a lengthy and expensive trial or a much cheaper settlement.").

144. *See* 28 U.S.C.A. § 1341 (2018) ("The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under [s]tate law where a plain, speedy and efficient remedy may be had in the courts of such [s]tate.").

145. Smith, Wynne & Wick, *supra* note 31.

146. *See* S.D. Codified Laws § 10-59-24.1 (2005).

147. Brief for Etsy, *supra* note 68, at 10.

148. *See* Brandeis & Layton, *supra* note 7, at 33.

149. Smith, Wynne & Wick, *supra* note 31.

Wayfair, ripple effects will likely be felt in the financial industry, including mergers and acquisitions, venture capital, and private equity deals.[150]

2. The Substantial Effect on Foreign Markets

South Dakota's S.B. 106 "clearly applies to all goods and services purchased over the internet . . . [, including] goods coming into the state from another country."[151] While the Court in *Wayfair* did not address the implication of subjecting foreign companies to the complex sales tax laws of forty-four states and over 10,000 local jurisdictions,[152] in *South-Central Timber Development, Inc. v. Wunnicke*,[153] the Court noted that "[i]t is a well-accepted rule that state restrictions burdening foreign commerce are subjected to a more rigorous and searching scrutiny."[154] Inadvertently shaping foreign policy, it may not be the case that foreign companies are in the same technological position to comply with sales tax obligations as domestic companies and, likewise, may be prohibited from legally conducting business in the United States as a consequence of the passage of state laws like S.B. 106. Critically, like in-state consumers obligated to pay use taxes, foreign companies effectively have a responsibility to collect and remit sales taxes *only so long* as this obligation is enforceable and enforced.

In *Wayfair*, contrary to the Supreme Court's intentions, the abandonment of the physical presence rule did not resolve the perceived "online sales tax loophole"[155] but has instead ensured that it is only available for foreign rather than domestic sellers. In a sense, the Court moved the limiting line of the physical presence rule from state lines to the U.S. border. In fact, with the Supreme Court's due process limits on states' long-arm statutes, "South Dakota cannot assert specific personal jurisdiction over most out-of-state websites, much less those operating from abroad, without going far beyond what t[he] Court has recognized as consistent with [d]ue [p]rocess."[156] As the states lack the power to enforce the collection of sales taxes by foreign sellers without the passage of a treaty, foreign sellers will be able to escape the tax collection obligation that their domestic competitors will not be able to

150. *See* Ed Zimmerman, *SCOTUS Changes to Sales Tax Will Ripple Through to PE, VC & M&A Deals Involving Retailers*, FORBES (Aug. 21, 2018), https://www.forbes.com/sites/edwardzimmerman/2018/08/21/scotus-changes-to-sales-tax-will-ripple-through-to-pe-vc-ma-deals-involving-retailers/#5b3c8efb5867.

151. Brief of Professor John S. Baker, Jr. as Amicus Curiae Supporting Neither Party at 6–7, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494).

152. Brief for Etsy, *supra* note 68, at 14; *see* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2103 (2018).

153. *See generally* S.-Central Timber Dev., Inc. v. Wunnicke, 467 U.S. 82 (1984).

154. *Id.* at 100.

155. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2092 (2018). The "online sales tax loophole" is not an actual loophole, as a use tax is owed to the state for online sales in which sales tax has not been collected; however, it takes on the form of a loophole as a result of in-state consumers' non-compliance in regard to paying the use tax.

156. Brief of Professor Baker, *supra* note 151, at 12–13.

avoid.[157] If the "artificial competitive advantage" of helping customers evade the payment of sales tax is as great as the Court suggests in *Wayfair*,[158] then the abandonment of the physical presence rule might significantly distort the market, not only disincentivizing sellers from having any physical presence in the United States but encouraging domestic businesses to move abroad.

3. The "Safe Harbor" Provisions' Shortcomings

South Dakota's "safe harbor" provisions[159] are misleading. The threat of a potential tax liability alone is sufficient to ensure compliance for certain businesses.[160] In particular, ventures that lack the ability to accurately estimate the amount of business they might conduct in any given tax jurisdiction may feel compelled to collect sales taxes in order to avoid having to cover such taxes themselves at the end of the year. For instance, a business that anticipates collecting more than $100,000 of gross receipts or engaging in 200 or more transactions in South Dakota within a year yet subsequently fails do so would likely still collect sales taxes without ultimately having had a legal obligation to do so by the end of the year. This is because South Dakota requires out-of-state sellers to collect sales taxes if they reach the threshold "in the previous calendar year *or the current calendar year*."[161] In short, "a business that expects to sell more than a *de minimis* number of goods in South Dakota would need to collect sales taxes prophylactically beginning with sale one because of the *possibility* that later sales might trigger the collection requirement."[162] Alternatively, the seller could either cease doing business in the taxing jurisdiction before crossing any thresholds triggering

157. *See id.* at 14 (stating that "enforcement against websites in other countries would be unachievable without a treaty"); *see also* Rose & Barrie, *supra* note 117 ("[S]o long as a foreign retailer does not have property in the U.S. that could be attached to pay sales taxes, a state would have no effective means of enforcing its position that its *Wayfair* statute applied to international commerce.").

158. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2094 (2018).

159. *Id.* at 2089, 2099 ("[S.B. 106] applies a safe harbor to those who transact only limited business in South Dakota"—that is, "[S.B. 106] applies only to sellers that, on an annual basis, deliver more than $100,000 of goods or services into the State or engage in 200 or more separate transactions for the delivery of goods or services into the State."); *see also* S.D. Codified Laws § 10-64-2 (2016).

160. *See* Brief for Etsy, *supra* note 68, at 23–24 ("South Dakota's insistence that its safe harbor provisions ensure that out-of-state businesses with only minor sales volume in the [s]tate will not be saddled with onerous sales tax collection obligations blinks reality.").

161. S.D. Codified Laws § 10-64-2 (2016) (emphasis added).

162. Brief for Etsy, *supra* note 68, at 24.

an obligation to collect sales taxes or simply pay the sales taxes out of pocket.[163]

For fledgling internet sellers, which are unlikely to be able to accurately forecast sales numbers and the tax jurisdictions of their customers, it might seem most prudent to opt for collecting and remitting sales taxes without having an obligation to do so. This holds especially true for more optimistic sellers that are unwilling to bet against themselves or those that launch online retail websites in an effort to take advantage of contemporary trends and fads. For such sellers, South Dakota's safe harbor provisions do nothing to insulate them from the burden of sales tax compliance.[164] The Court's determination that these measures "afford small merchants a reasonable degree of protection" is largely unsupported, and in the calculus of determining the burden that laws like S.B. 106 place on interstate commerce, the weight that these provisions are given should be diminished accordingly.[165]

It is also noteworthy that marketplace operators—such as Amazon, eBay, and Etsy—may be held responsible for the collection of sales taxes and are unlikely to be able to gauge the number of transactions that a seller on their platform might conduct in any given sales tax jurisdiction. Again, in this popular arrangement,[166] South Dakota's safe harbor provisions are essentially meaningless. While a seller may ultimately fall short of the sales numbers that would demand the collection of sales taxes, an online marketplace would have no method of predicting this and would be prone to collect sales taxes beginning with the first sale. Furthermore, marketplace operators are not in the position to monitor and enforce a state's safe harbor thresholds because their online retailers "often sell their goods on multiple platforms," with, for instance, an estimated 58% of Etsy's sellers promoting goods in other venues.[167]

163. Incidentally, because of the safe harbors, the burden of determining whether sales taxes are owed will also be shared, to a lesser extent, by consumers who want to comply with state laws. To accurately account for the use taxes they owe to the state, such consumers will need to remain diligent as to whether sales taxes have already been collected by each remote seller. Where a seller later determines that uncollected sales taxes are owed and pays these taxes on behalf of an out-of-state consumer, there exists the possibility that the tax might be paid twice—that is, not only as a sales tax by the seller but also as a use tax by the consumer.

164. Crossing a 200-transaction threshold would be even more likely in a larger state than South Dakota, and the Supreme Court has given no indication that such a threshold would be unconstitutional elsewhere.

165. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2098 (2018).

166. *See* Brief for Etsy, *supra* note 68, at 21–22 (noting that Etsy had 1.9 million sellers as of December 31, 2017); *see also Number of Sellers on Amazon Marketplace*, MARKETPLACE PULSE (Apr. 18, 2020), https://www.marketplacepulse.com/amazon/number-of-sellers. As of April, 2020, "Amazon marketplace ha[d] 8.3 million total sellers worldwide. There [were] 2.1 million active sellers, the rest no longer [had] products listed for sale." *Id.*

167. Brief for Etsy, *supra* note 68, at 21.

4. A Misguided Sense of Equity

Much of the Supreme Court's basis in abandoning the physical presence rule in *Wayfair* was grounded in a sense of local businesses suffering from unfair competition and a desire to level the playing field for all vendors.[168] This line of reasoning is also misguided. In-state and out-of-state sellers do not face the same challenges, which is especially true in the wake of *Wayfair*, nor do they provide the same services or benefit equally from the taxes that are collected. To this end, remote internet sellers and local brick-and-mortar stores are not "economically identical actors" despite the Court's insistence that they are.[169] In-state retailers can offer immediacy, the ability to see and touch a product, and simpler returns; furthermore, since sales taxes are imposed at the point of sale,[170] they also benefit from collecting and remitting sales taxes within a single taxing jurisdiction. At the same time, in-state retailers may face additional overhead costs. Out-of-state sellers, in contrast, can offer the customer the convenience of being able to shop from home, yet they often face fierce global competition as well as the costs of shipping and packaging, of goods damaged in transit, and of returns. As a result of *Wayfair*, out-of-state sellers also face the additional burden of sales tax compliance in at least forty states with varying sales tax schemes.[171]

Critically absent in the Court's opinion is the fact that remote internet retailers are not merely a one-to-one alternative to local brick-and-mortar retailers; internet retailers provide an entirely new and different forum for transacting—one that defies borders by design and that customers may prefer irrespective of price variances. For example, in New York City, despite an abundance of brick-and-mortar retailers, the number of daily deliveries to households increased threefold from 2009 to 2017 and reached 1.1 million daily deliveries.[172] In 2019, daily deliveries exceeded 1.5 million, and the *New York Times* reported that due to "businesses that sell over the internet, the very fabric of major urban areas around the world is being

168. *Wayfair, Inc.*, 138 S. Ct. at 2095–96 ("*Quill*'s physical presence rule . . . is unfair and unjust to those competitors . . . who must remit the tax; to the consumers who pay the tax; and to the [s]tates that seek fair enforcement of the sales tax," and the rule "has prevented market participants from competing on an even playing field.").

169. *Id.* at 2094.

170. *See id.* at 2092–93 (2018) (citing that "[g]enerally speaking, a sale is attributable to its destination"); *see, e.g.*, N.Y. STATE DEP'T OF TAXATION & FIN., SALES TAX RATE PUBLICATIONS 1 (Mar. 26, 2010), https://www.tax.ny.gov/pdf/tg_bulletins/sales/b15_820s.pdf ("Sales and use tax rates in New York State reflect a combined statewide rate of 4%, plus the local rate in effect in the jurisdiction (city, county, or school district) where the sale or other transaction or use occurs.").

171. Rose & Barrie, *supra* note 117 ("[I]n the year since Wayfair, more than 40 states have enacted economic nexus statutes similar, but not necessarily, identical to, the South Dakota statute.").

172. *See* Matthew Haag & Winnie Hu, *1.5 Million Packages a Day: The Internet Brings Chaos to N.Y. Streets*, N.Y. TIMES (Oct. 27, 2019), https://www.nytimes.com/2019/10/27/nyregion/nyc-amazon-delivery.html.

transformed."[173] While the Court in *Wayfair* suggested that the physical presence rule has caused certain markets to "lack storefronts, distribution points, and employment centers that otherwise would be efficient or desirable,"[174] internet retailers have also empowered customers in these markets; the internet has made it possible and convenient to obtain almost anything, anywhere in the United States. In this light, it seems unreasonable to cast the consumer as a victim of internet retailers.

In addition, while the Court in *Wayfair* was critical of the artificiality of the physical presence rule,[175] South Dakota's thresholds of gross revenue and numbers of transactions that trigger an obligation to collect sales taxes are equally, if not more, artificial. The Court noted that "[t]he law at issue requires a merchant to collect the tax only if it does a considerable amount of business in the [s]tate"[176] yet provided no justification for why these particular thresholds are meaningful nor why an out-of-state business should enjoy any preferential treatment.[177] Under S.B. 106, a business could manage to avoid collecting and remitting sales taxes because it earned only $99,999 in annual gross revenue in South Dakota.[178] It is inherently unfair that a seller making one dollar more would be obligated to collect sales taxes as would an in-state seller making, for instance, $90,000 less. Although the Court maintained that "there is nothing unfair about requiring companies that avail themselves of the [s]tates' benefits to bear an equal share of the burden of tax collection[,]" it was simultaneously tolerant of safe harbor provisions that allow an entire subset of merchants doing business in South Dakota to operate without collecting taxes at all, likely helping "customers evade a lawful tax" in the process.[179]

Arguably, out-of-state sellers share neither an equal share of the burden of tax collection—as more resources must be expended on multi-jurisdiction compliance[180]—nor avail themselves of state benefits in any real sense. Even assuming, *arguendo*, that in-state and out-of-state sellers faced the same challenges in collecting sales taxes, the burden of doing so is effectively

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173. *Id.*

174. *Wayfair, Inc.*, 138 S. Ct. at 2094. *But see* Austan Goolsbee, *Never Mind the Internet. Here's What's Killing Malls*, N.Y. TIMES (Feb. 13, 2020), https://www.nytimes.com/2020/02/13/business/not-internet-really-killing-malls.html (asserting that three major economic forces have had a greater impact on brick-and-mortar retail than the internet, that "internet shopping still represents only 11 percent of the entire retail sales total," and that "more than 70 percent of retail spending in the United States is in categories that have had slow encroachment from the internet").

175. *See Wayfair, Inc.*, 138 S. Ct. at 2095.

176. *Id.* at 2098.

177. The safe harbor provision could be grounded in *Pike*'s balancing framework; however, the Court does not make this point. *See* Pike v. Bruch Church, Inc., 397 U.S. 137, 142 (1970).

178. As noted above, it is unlikely that any business that faced the potential of crossing either the gross-revenue threshold or number-of-transaction threshold would risk not collecting sales tax and, consequently, become liable for the out-of-pocket payment of the tax in the event that either threshold were inadvertently crossed.

179. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2096 (2018).

180. *See infra* Section III.A.5.

greater on out-of-state sellers that do not meaningfully benefit from the tax revenue. Sellers with at least some ownership stake in the state, opposed to entirely out-of-state sellers, benefit from the expenditure of sales taxes after they are collected for the state. Thus, the burden that a South Dakota business faces in collecting South Dakota's sales taxes is at least partially mitigated. This is not true in the case of out-of-state retailers that have no physical presence in the state. By stripping away the physical presence rule, the Court should have weighed the additional burden that it was allowing to be placed on out-of-state sellers in regard to the benefits that these businesses actually receive from the state.[181]

5. The Discriminatory Effect

While the Commerce Clause has been understood to prohibit the states from placing an undue burden on interstate commerce, it also prohibits the states from discriminating against interstate commerce.[182] The Court in *Wayfair* took note that "[s]tate laws that discriminate against interstate commerce face 'a virtually *per se* rule of invalidity,'"[183] later commenting that "[c]omplex state tax systems could have the effect of discriminating against interstate commerce."[184] This assessment is logical. In order to combat the impracticability of collecting a use tax from the "multitude of individual purchasers,"[185] states like South Dakota have turned to retailers to collect such taxes on their behalf. Following *Wayfair*, states have been further empowered to shift this regulatory burden of tax collection onto remote retailers in addition to their own brick-and-mortar retailers. Although this treatment of retailers appears even-handed at first blush, the practical effect on the individual retailers varies greatly.

Local brick-and-mortar retailers need only collect and remit sales taxes at the appropriate rate in the taxing jurisdiction in which they are located.[186] They do not face the potential of having to litigate disputes in distant courtrooms, the need for purchasing multi-jurisdictional tax software or researching tax statutes themselves, nor do they need to collect personal information from their customers in order to properly assess sales taxes or make a sale. Remote internet sellers, in contrast, will have to endure a more difficult and costly process in order to comply with the laws of each taxing

181. *See* Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 759–60 (1967) (expressing concern that an out-of-state business will be "entangle[d] . . . in a virtual welter of complicated obligations to local jurisdictions with no legitimate claim to impose 'a fair share of the cost of the local government'").

182. *See Wayfair, Inc.*, 138 S. Ct. at 2091.

183. *Id.* (citing Granholm v. Heald, 544 U.S. 460, 476, 125 S. Ct. 1885 (2005)).

184. *Id.* at 2099.

185. *Id.* at 2088 (citing National Geographic Soc. v. Cal. Bd. of Equalization, 430 U.S. 551, 555 (1977)).

186. *See supra* note 170.

jurisdiction.[187] While the taxing jurisdiction is not imposing a direct tax on retailers in either case, the compliance costs that it is indirectly creating for remote internet retailers far exceeds those that it is placing on its own brick-and-mortar retailers.[188] In turn, without the physical presence rule's protection, local retailers are not actually on "an even playing field" but are instead themselves enjoying "an arbitrary advantage over their competitors" because they are spared from having to build the high costs of multi-jurisdictional sales tax compliance into the price of their goods and services.[189]

B. THE DUE PROCESS CLAUSE

In *Wayfair*, the Supreme Court largely skirted undertaking a due process analysis and instead relied on its earlier determinations in *Quill* and *Burger King Corp. v. Rudzewicz*.[190] Prior to the Court's opinion in *Quill*, the furthest extension of the "minimum connection" requirement of due process was in a case involving the collection of sales or use taxes was recognized in 1960 when the Court upheld "a use tax despite the fact that all of the seller's in-state solicitation was performed by independent contractors."[191] By 1986, in a case where Burger King sought to bring an action in Florida for breach of contract against two out-of-state defendants, the Court found that "[s]o long as a commercial actor's efforts are 'purposefully directed' toward residents of another [s]tate, [the Court has] consistently rejected the notion that an absence of physical contacts can defeat personal jurisdiction there."[192] Consequently, a physical presence is no longer prerequisite for bringing an action against an out-of-state defendant in state court.

A few years later, in *Quill*, the Court reiterated that "if a foreign corporation purposefully avails itself of the benefits of an economic market in the forum [s]tate, it may subject itself to the [s]tate's *in personam* jurisdiction even if it has no physical presence in the [s]tate."[193] Drawing from these decisions, the Court in *Wayfair* found that "[t]he reasons given in *Quill* for rejecting the physical presence rule for due process purposes apply as well to the question whether physical presence is a requisite for an out-of-state seller's liability to remit sales taxes."[194]

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187. *See supra* Part III.A.1.
188. *But see Wayfair, Inc.*, 138 S. Ct. at 2099 (concluding that "since in-state businesses pay the taxes as well, the risk of discrimination against out-of-state sellers is avoided").
189. *Id.* at 2096.
190. *See id.* at 2093; Burger King Corp. v. Rudzewicz, 471 U.S. 462 (1986).
191. Quill Corp. v. North Dakota, 504 U.S. 298, 306 (1992) (citing Scripto Inc. v. Carson, 362 U.S. 207, 212–13 (1960)).
192. *Rudzewicz*, 471 U.S. at 468–69, 476.
193. *Quill Corp.*, 504 U.S. at 307.
194. *Wayfair, Inc.*, 138 S. Ct. at 2093.

Unlike in *Wayfair*, however, both *Bellas Hess* and *Quill* were decided before the internet played much, if any, role in interstate commerce.[195] In both cases, there was no question that the mail-order houses were engaging in the "continuous and widespread solicitation of business" and "purposefully direct[ing]" their activities—including mass catalog mailings, telemarketing calls, and advertisements—at the residents of states in which these businesses were not physically located.[196] In *Quill*, for instance, the state court noted that North Dakota "disposed of 24 tons of catalogs and flyers mailed by [the mail-order house] into the [s]tate every year."[197] It was the "magnitude" of the mail-order house's contacts with North Dakota and "the benefits [that it] receive[d] from access to the [s]tate" that were deemed to be sufficient for due process purposes.[198]

First, considering the prevalence of internet sales today, the means by which such transactions are accomplished, and the technological capacity to buy and sell goods without "a deluge of catalogs,"[199] *Wayfair* offered an opportunity for the Court to reexamine the due process considerations. Whereas traditional mail-order catalogues often target an addressee and demand the attention of a recipient, internet sales do not always involve solicitation. Furthermore, individual online retailers are often sought out by shoppers to a greater extent than the reverse. Unlike the mail-order houses in *Bellas Hess* and *Quill*, a great number of online retailers are presumably not sending catalogs or targeting particular residents within a state.[200] In reality, "[o]ut-of-state and out-of-country websites do not target any particular state" but rather "hope to sell to a worldwide audience."[201]

Second, the Court's fidelity to *Burger King* in both *Quill* and *Wayfair* is questionable. The test for *in personam* jurisdiction and the due process

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195. *See* Brief of Professor Baker, *supra* note 151, at 4 (noting that "[t]he general public first gained access to the internet in 1991," so "[t]he sale of goods over the internet was virtually non-existent when [the] Court decided [*Quill*] in 1992").

196. *Quill Corp.*, 504 U.S. at 308 (citing Burger King Corp. v. Rudzewicz, 471 U.S. 462 (1985)); *see* Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 754–55 (1967).

197. *Quill Corp.*, 504 U.S. at 304; *cf.* Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 754 (1967) ("Twice a year catalogues are mailed to the company's active or recent customers throughout the Nation" and that flyers "are occasionally mailed to past and potential customers.").

198. *Quill Corp.*, 504 U.S. at 308.

199. *Id.*

200. *See* Rebecca R. Ruiz, *Catalogs, After Years of Decline, Are Revamped for Changing Times*, N.Y. TIMES (Jan. 25, 2015), https://www.nytimes.com/2015/01/26/business/media/catalogs-after-years-of-decline-are-revamped-for-changing-times.html ("After years of decline, the number of catalogs mailed in the United States increased in 2013, to 11.9 billion . . . about 60 percent of what it was at its peak in 2007."); *see also* Anna Molin, *H&M Stops the Presses, Shreds its Print Catalog After 39 Years*, BLOOMBERG (May 2, 2019), https://www.bloomberg.com/news/articles/2019-05-02/h-m-stops-the-presses-shreds-its-print-catalog-after-39-years ("Swedish fashion giant Hennes & Mauritz AB said it ceased publication of its print catalog after 39 years . . . follow[ing] dwindling interest from customers in flipping through glossy pages of inventory when they can find the latest deals with their mobile phones or computer screens.").

201. Brief of Professor Baker, *supra* note 151, at 13.

requirement for imposing a duty on an out-of-state seller to collect and remit taxes for an in-state buyer are not clearly identical. While Justice Scalia, in his concurrence in *Quill*, noted that the Court declined to "distinguish between jurisdiction to tax and jurisdiction to compel collection of taxes as agent for the [s]tate," he also acknowledged that the due process standards for "adjudicative jurisdiction" and those for "legislative (or prescriptive) jurisdiction" perhaps require different treatment.[202] In *Burger King*, the Court found that it was reasonable to require an individual to "submit to *the burdens of litigation*" in a state in which he had "'deliberately' . . . engaged in significant activities"[203] or in which he had "created 'continuing obligations' between himself and residents."[204] The Court reasoned that such an individual had "availed himself of the privilege of conducting business" in that state and that his activities were shielded by "the benefits and protections" of that state's laws.[205]

The underlying question then concerns the necessary degree of availment and whether a virtual internet presence or the completion of an internet sale can truly constitute a seller's activities being "purposefully directed" at another state and the "continuous and widespread solicitation of business."[206] After *Burger King*, while there is no doubt that the courts of a plaintiff's state could have jurisdiction over an out-of-state defendant with sufficient ties to the state for an action for breach of contract,[207] it is less apparent that a state has the authority to compel a business to collect the state's taxes just because it has a website that is accessible within the state or because it completed a sale within the state. While it may be the case that a business's virtual presence could be so pervasive as to satisfy due process, mere virtual presence is a poor proxy for physical presence and should not alone satisfy the minimum due process requirements.

1. The Pitfalls of Virtual Presence

While South Dakota sought only to require large, national retailers to collect and remit sales taxes,[208] the concept of using an internet website to place an online seller within the bounds of a state's regulatory jurisdiction is

202. *See Quill Corp.*, 504 U.S. at 319–20 (Scalia, J., concurring in part and concurring in the judgement). "Adjudicative jurisdiction" concerns the courts' authority to entertain suits, whereas "legislative jurisdiction" concerns the authority to make and apply laws. *See* Howard M. Wasserman, *Prescriptive Jurisdiction, Adjudicative Jurisdiction, and the Ministerial Exemption*, 160 U. PA. L. REV. PENNUMBRA 289, 298, 302 (2012).

203. Burger King Corp. v. Rudzewicz, 471 U.S. 462, 475–76 (1986) (quoting Keeton v. Hustler Magazine, Inc., 465 U.S. 770, 781 (1984)) (emphasis added).

204. *Id.* at 476 (quoting Travelers Health Ass'n v. Com. of Va. *ex rel.* State Corp. Comm'n, 339 U.S. 643, 648 (1950)).

205. *Id.* at 475–76.

206. *See Quill Corp.*, 504 U.S. at 308.

207. *See Rudzewicz*, 471 U.S. at 487.

208. *See* S.D. Codified Laws § 10-64-2 (2016) (exempting businesses that conducted fewer than 200 taxable transactions or collected less than $100,000 in gross revenue within the state).

fundamentally problematic and should not have been so readily adopted.[209] In *Wayfair*, the Court recognized "virtual presence" or "virtual connections to the [s]tate" as something akin to "physical presence" and adequate for the purpose of meeting *Complete Auto*'s substantial nexus requirement.[210] Nevertheless, it is not immediately clear why a seller is seen as virtually setting up shop in the buyer's state rather than the buyer using the internet to travel virtually to the out-of-state seller's shop to make an online purchase—this is especially the case if the buyer creates a profile on the seller's website and therefore has a virtual presence of its own.[211]

Massive internet retailers, such as Wayfair, Amazon, and Overstock, may purchase advertisements across the United States and are perhaps easier to see as having a "pervasive [i]nternet presence."[212] This strengthens the Court's finding that such sellers make themselves available in the buyer's state.[213] In such cases, *Quill*'s due process requirement that a seller engage in "continuous and widespread solicitation of business"[214] in the taxing state may very well be met. In contrast, a small-scale seller of an atypical good—one that a buyer in another state might spend hours scouring the internet to find—can hardly be said to have the same *pervasive* presence in the buyer's state. Here, it would seem equally logical to recognize the buyer as virtually traveling to the seller's state to make the purchase. Regardless of the dollar amount of the sale or the number of sales of this sort that occur, this type of seller cannot be described as engaging in "continuous and widespread solicitation of business."[215]

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209. *See* Brief of Professor Baker, *supra* note 151, at 14 ("Having any and every government in the world able to assert jurisdiction over virtually every website would be welcome to those countries seeking control over the internet.").

210. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2095 (2018) ("It is not clear why a single employee or a single warehouse should create a substantial nexus while 'physical' aspects of pervasive modern technology should not. For example, a company with a website accessible in South Dakota *may be said to have a physical presence* in the [s]tate via the customers' computers.") (emphasis added); *see id.* at 2094 (finding that it "makes no sense" to draw a distinction between collecting sales tax from a business with "a small warehouse" in South Dakota and collecting sales tax from a business with "a pervasive [i]nternet presence" in South Dakota); *see also id.* at 2099 (finding that "the nexus is clearly sufficient based on both the economic and *virtual contacts* respondents have with the [s]tate").

211. Despite the fact that a sale is generally attributable to its destination for tax purposes, it does not necessarily place the seller within the state's regulatory jurisdiction. *See Wayfair, Inc.*, 138 S. Ct. at 2092–93.

212. *Id.* at 2094. The Court also uses the phrases "pervasive virtual presence" and "extensive virtual presence." *See id.* at 2095, 2099.

213. *See id.* at 2099 (finding that large, national companies that maintain an "extensive virtual presence" and do sufficiently large quantity of business within South Dakota satisfy the substantial nexus test "based on both the economic and virtual contacts [such companies] have with the [s]tate").

214. Quill Corp. v. North Dakota, 504 U.S. 298, 308 (1992).

215. *Id.*

IV. MOVING FORWARD IN THE WAKE OF THE *WAYFAIR* DECISION

A. THE EFFECT OF THE PHYSICAL PRESENCE RULE SHOULD BE REVIVED

Despite the Supreme Court's decision in *Wayfair*, Congress should enact protections similar to the bright-line physical presence rule. The task of complying with the sales tax regime of every taxing jurisdiction across the United States places an undue burden on interstate commerce and may impact international commerce. The compliance burden is unfair to remote online retailers and their customers, and it allows states to enact legislation that will ultimately have a distortionary effect on the developing internet commerce market. At the time the Supreme Court decided *Bellas Hess* in 1967, long before the arrival of the internet, the Court expressed a concern that:

> if Illinois can impose such burdens, so can every other [s]tate, and so, indeed, can every municipality, every school district, and every other political subdivision throughout the Nation with power to impose sales and use taxes. The many variations in rates of tax, in allowable exemptions, and in administrative and record-keeping requirements could entangle [a company's] interstate business in a virtual welter of complicated obligations to local jurisdictions. . . .[216]

Following the Court's decision in *Wayfair*, an internet retailer's entire business is now subjected to just such a "welter of complicated obligations."[217]

By the time of *Quill*, in 1992, the Supreme Court pointed out that Congress had enacted Public Law 86-272, which prohibits states from imposing a net income tax on an individual if that individual's "only business activities within such [s]tate [involve] the solicitation of orders [approved] outside the [s]tate [and] filled . . . outside the [s]tate."[218] The enactment of this law was in response to the Supreme Court's decision in *Northwestern States Portland Cement Co. v. Minnesota*[219] that held that "so long as the taxpayer has an adequate nexus with the taxing [s]tate, 'net income from the interstate operations of a foreign corporation may be subjected to state taxation.'"[220] This course of action is again appropriate. Congress should consider extending the immunity conferred by Public Law 86-272 to cover the obligation of collecting sales taxes as well.[221]

216. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 759–60 (1967).
217. *See id.* at 760.
218. *Quill Corp.*, 504 U.S. at 298, 316 n. 9.
219. Nw. States Portland Cement Co. v. Minnesota, 358 U.S. 450 (1959).
220. *Quill Corp.*, 504 U.S. at 316 n. 9 (quoting Nw. States Portland Cement Co. v. Minnesota, 358 U.S. 450, 452 (1959)).
221. *See* Smith, Wynne & Wick, *supra* note 31.

While states like South Dakota would retain the authority to tax in-state consumers for purchasing goods and services from remote internet retailers, they would not be permitted to demand collection of these sales taxes directly by the seller. An expansion of Public Law 86-272 would effectively eliminate the liability that sales tax collection entails for remote sellers. It would also allow the state to continue to pursue sales taxes; however, it correctly places the burden where it belongs: "on the state seeking to collect the tax and on the in-state consumer" who benefits from the tax.[222] In the same way that the Court has proven sympathetic to South Dakota in regard to the impracticability of collecting a use tax from its numerous residence, Congress should be sympathetic to internet sellers in regard to the impracticability of complying with the complex, individual sales taxes schemes of possibly over 10,000 jurisdictions.[223] An expansion of Public Law 86-272 could accomplish this.

B. SALES TAX REGIMES SHOULD NOT BE PROTECTED BY THE COURTS

The functionality of sales taxes themselves should be evaluated. At its core, the *Wayfair* decision is a desperate measure to breathe life into a failing tax structure, and it showcases the Court's determination to resolve South Dakota's problem of collecting use taxes from its own residents by allowing the state to shift the logistical burden to remote sellers. While a state may have the authority to tax its residence in a number of ways, it is not the role of the Court to facilitate the collection of taxes that are administratively too difficult for the state to collect, nor should it lead the charge to empower states to impose this burden on sellers that have no interest in the state apart from the consumer of their goods or services. Simply because a tax is constitutional, it is not a guarantee that a tax is economical when considering collection and enforcement. States may very well have the authority to tax all sorts of activity, even though doing so would not be practicable.

Sympathetic to South Dakota's plea for help, the Court took special note that "because South Dakota has no state income tax, it must put substantial reliance on its sales and use taxes for the revenue necessary to fund essential services."[224] South Dakota, nevertheless, like all states, has the capacity to collect income tax. In fact, only seven states currently have no income tax.[225] If the challenge of collecting sales and use taxes proves too great for a state

222. *Id.*
223. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2103–04 (Roberts, C.J., dissenting) (noting both the vast number and complexity of existing taxing jurisdictions).
224. *Id.* at 2088.
225. Alaska, Florida, Nevada, South Dakota, Texas, Wyoming, and Washington are the only "states that have no personal income tax." *See States with the Highest and Lowest Taxes*, INTUIT TURBOTAX, https://turbotax.intuit.com/tax-tips/fun-facts/states-with-the-highest-and-lowest-taxes/L6HPAVqSF (last visited Apr. 18, 2020).

to accomplish on its own in the modern era of global internet commerce,[226] it may be necessary to find alternative tax schemes. To this point, there are already five states that do not collect sales or use taxes at all—an indication that states can, in reality, fund essential services without their collection.[227]

The burden that sales taxes place on remote internet retailers, stemming from having to navigate a complex body of law in each taxing jurisdiction in which it conducts business,[228] far outstrips the burden such taxes place on traditional brick-and-mortar stores. Consequently, this burden runs the risk of artificially manipulating—perhaps even stunting the growth of—the entire internet commerce market. As has been suggested, the harm that the physical presence rule inflicts on brick-and-mortar stores may, in effect, be considerable;[229] however, the playing field is not evened by locally imposing a requirement to collect sales taxes on remote internet sellers. Following *Wayfair*, the "arbitrary advantage"[230] that the Court was concerned about has only been taken away from remote online retailers and given to local brick-and-mortar retailers. Instead of remote online retailers benefiting from making it easy for customers to evade paying taxes and essentially allowing them to offer lower prices,[231] now brick-and-mortar stores gain a competitive advantage by avoiding the high costs of multi-jurisdictional sales tax compliance and can pass these savings on to their customers by offering lower prices than their online competitors. If the goal was truly an even playing field, then sales and use taxes might be eliminated altogether.

Additionally, there is something inherently protectionist in harming the bourgeoning internet commerce market—which, borderless, is perhaps the purest expression of interstate commerce—to advantage local brick-and-mortar retailers. Moreover, doing so also harms the customer that might prefer to shop online rather than in a store or who might be too old or otherwise incapable of doing so. Internet retail giants like Amazon already collect sales taxes in every state that imposes them and, therefore, have already shouldered the compliance burden. In the aftermath of *Wayfair*, the

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226. *But cf.* Smith, Wynne & Wick, *supra* note 31 (suggesting "there is nothing to prevent a state from simply requiring e-commerce sellers to send in-state purchasers to a 'landing page' run by the state, who would there and then collect the tax directly from the consumer after the sale is consummated").

227. *See* Stewart, *supra* note 8; *cf.* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2088 (2018) (noting that such "taxes account for over 60 percent of [South Dakota's] general fund" and are "necessary to fund essential services").

228. *See supra* Part III.A.1.

229. *See, e.g.*, Brief for International Council of Shopping Centers, Investment Program Association, Nareit, National Association of Realtors®, Real Estate Roundtable, National Multifamily Housing Council, NAIOP, American Farm Bureau Federation, and South Dakota Farm Bureau Federation in Support of Petitioner at 3–4, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494).

230. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2086 (2018).

231. *See* Brief of International Council of Shopping Centers, *supra* note 229, at 4 ("Local businesses struggle and increasingly fail to compete against online retailers that can offer customers identical goods for what is in effect up to a 10 percent discount.").

position of these giants has been solidified against competition from newer, smaller internet retailers that will, in contrast, face sales tax compliance burdens from the onset.[232] The Court in *Wayfair* insists that "it is certainly not the purpose of the Commerce Clause to permit the Judiciary to create market distortions."[233] Despite disregarding principles of *stare decisis*,[234] it has done exactly this by eliminating the Commerce Clause protections to interstate commerce that it put in place in *Bellas Hess* and reaffirmed in *Quill*.[235]

CONCLUSION

For half a century, the physical presence rule provided a necessary protection to companies that sought to do business across state lines, especially internet retailers of the modern era. By deciding *Wayfair* under an inapposite framework and failing to properly measure the burden that local sales tax laws place on remote sellers, the Supreme Court readily eviscerated this protection, harming interstate commerce in the process. Consequently, established internet retailers that already collect sales taxes, local brick-and-mortar businesses, and foreign companies have been given a competitive advantage over fledgling internet retailers that must now overcome the challenge of sales tax compliance in over forty states as well as the resultant litigation from any errors that might transpire. To address the problems stemming from the *Wayfair* decision, Congress should extend the protections of Public Law 86-272 to restore the effect of the physical presence rule. While states would still be able to pursue the collection of sales and use taxes, the states would lack the authority to obligate remote sellers to collect such taxes on their behalf. That said, in light of the upsurge of global internet commerce, courts and legislatures alike should brace for the fact that sales taxes may very well be impracticable moving forward.

Revel Shinn Atkinson[*]

232. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2103 (2018) (Roberts, C.J., dissenting) ("Some companies, including the online behemoth Amazon, now voluntarily collect and remit sales tax in every [s]tate that assesses one—even those in which they have no physical presence."); *see also id.* at 2104 (Roberts, C.J., dissenting) (quoting U.S. GOV'T ACCOUNTABILITY OFF., GAO-18-114, SALES TAXES 22 (2017)) ("[C]osts will likely increase the most for businesses that do not have established legal teams, software systems, or outside counsel to assist with compliance related questions.").

233. *Id.* at 2094.

234. *See id.* at 2102 (Roberts, C.J., dissenting) ("If *stare decisis* applied with special force in *Quill*, it should be an even greater impediment to overruling precedent [in *Wayfair*] . . . .").

235. *See supra* Part I.

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