

## Resources

### What The Supreme Court's *Wayfair* Ruling Means for Businesses

June 22, 2018

On June 21, 2018, the U.S. Supreme Court released its much-anticipated opinion in *South Dakota v. Wayfair, Inc.*, in which it held that physical presence within a State is no longer a prerequisite to the imposition of liability on out-of-state sellers to collect and remit sales taxes. In doing so, the Court overruled two of its own earlier cases—*National Bellas Hess, Inc. v. Department of Revenue of Illinois* and *Quill Corp. v. North Dakota*.

In *Wayfair*, the Court upheld a 2016 South Dakota sales tax law that required out-of-state sellers with no physical presence in the State to collect and remit sales tax if they annually delivered more than \$100,000 of goods or services into the State or engaged in 200 or more separate transactions for delivery of goods or services into the State. The law was not retroactive and had provisions for expeditious judicial review. South Dakota's courts had stricken the law as being contrary to the U.S. Supreme Court's previous holdings in *Bellas Hess* and *Quill*.

The Supreme Court, in a vigorous opinion authored by Justice Kennedy (and joined by Justices Thomas, Ginsburg, Alito, and Gorsuch), condemned the physical presence rule as being an "artificial, anachronistic rule that deprives States of vast revenues from major businesses" and is "removed from economic reality." Calling the rule a "judicially created tax shelter for businesses that decide to limit their physical presence and still sell their goods and services to a State's consumers," the Court found that it "intrudes on States' reasonable choices in enacting their tax systems" and in allowing "remote sellers to escape an obligation to remit a lawful state tax is unfair and unjust."

Concluding that the physical presence rule as stated in *Bellas Hess* and *Quill* was wrong when it was first developed, the Supreme Court noted that it is even more egregious in today's world, given the Internet's prevalence and power in the national economy. The Court was not moved by arguments that the physical presence rule has permitted start-ups and small businesses to use the Internet as a means of growing their companies and accessing a national market without the burden of nationwide sales tax collection.

In what is likely to become a three-part test used by lower courts in future cases determining the legality of state sales taxes as applied to out-of-state sellers, the Supreme Court noted that South Dakota's law: (1) has a safe harbor for merchants transacting only limited business in the State; (2) is not retroactive; and (3) was developed in the context of the State being a party to the Streamlined Sales and Use Tax Agreement. The Court allowed that some small businesses with only minimal contacts with a State may seek relief from burdensome tax collection systems under various other legal theories.

What does this mean for businesses? A majority of States already tax certain Internet sellers without a physical presence, most commonly through a "click-through" nexus, although other variations exist. Several States have adopted laws similar to that at issue in *Wayfair*. Now that the Supreme Court has validated South Dakota's law, it is fair to expect other States to follow suit in the hopes of increasing their tax revenues. Businesses that conduct electronic commerce, therefore, should be aware that changes may be forthcoming and be prepared to act.

The Supreme Court's decision in *Wayfair* leaves much uncertainty about the full extent of a State's powers of taxation and the permutations of remote seller tax laws that they might adopt. Added to the mix is the possibility that Congress could, under its power to regulate interstate commerce, enact legislation establishing limits on the ability of States to require out-of-state sellers to collect and remit sales tax.

Dykema is continuing to monitor developments in this area and is prepared to advise businesses of all sizes on their tax obligations in *Wayfair's* wake. For more information, please reach out to any of the attorneys listed as contacts on the left, or your Dykema relationship attorney.

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