

ALERT - New Sales Tax Rules - South Dakota v. Wayfair, Inc.

In a five (5) to four (4) decision, issued June 21, 2018, the Supreme Court ruled that states have the power to make businesses collect sales taxes, even in circumstances where the business does not have a physical presence. Prior to this ruling and commonly observed in the online retailing space, businesses were not required to collect sales tax on transactions if the business did not have a physical presence in the state of the customer.

This physical presence standard originated from the *Quill Corp. v. North Dakota* decision, which ruled that businesses need to have at least some physical connection with a state for that state to require that company to pay taxes. In our current economy, this created what many believed to be a significant loophole and also a means for out of state retailers to undercut local retailers and wholesalers.

States have attempted to combat the *Quill Corp. v. North Dakota* decision, by requiring tax filers to disclose their annual transactions that were not previously subject to sales tax. Ultimately, these efforts did little to mitigate the situation, with government estimates that between \$9 billion to \$13 billion in potential tax revenue was left on the table.¹

This prompted South Dakota, which has no state income tax and relies heavily on its sales and use taxes, to pass a new law in 2016. The statute imposes an “economic presence test” on out-of-state retailers to subject them to sales tax liability. The

measure applies to any retailer with at least \$100,000 in sales or at least 200 individual transactions in the state. South Dakota sued several out-of-state internet retailers, seeking to require them to begin collecting taxes. Three (3) decided to fight — Wayfair, a retailer of home goods; Overstock.com, a general retailer; and Newegg.com, which specializes in tech products.²

In Justice Kennedy’s opinion, he cited marketing materials from Wayfair, “Its advertising seeks to create an image of beautiful, peaceful homes, but it also says that ‘one of the best things about buying through Wayfair is that we do not have to charge sales tax.’ What Wayfair ignores in its subtle offer to assist in tax evasion is that creating a dream home assumes solvent state and local governments.”³

In the dissent, authored by Justice John Roberts, he touched on the common issue of who should make this decision, “any alteration to those rules with the potential to disrupt the development of such a critical segment of the economy should be undertaken by Congress.”⁴ Arguably, as many would agree with that position, Justice Kennedy noted that “in effect, *Quill* has come to serve as 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,”

² Mark Walsh. “Opinion Analysis: Court Expands States’ Ability to Require Internet Retailers to Collect Sales Tax.” *SCOTUSblog*, SCOTUSblog, 21 June 2018, www.scotusblog.com/2018/06/opinion-analysis-court-expands-states-ability-to-require-internet-retailers-to-collect-sales-tax/#more-271755.

³ *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 735.

⁴ *Id.*

¹ Shieber, Jonathan. “States Will Be Able to Charge Sales Tax on Online Purchases Thanks to the Supreme Court.” *TechCrunch*, TechCrunch, 21 June 2018, techcrunch.com/2018/06/21/states-will-be-able-to-charge-sales-tax-on-online-purchases-thanks-to-the-supreme-court/.

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thus it is reasonable for the policy to be reversed by the judiciary.⁵

This decision may impact your business if you operate as a retailer or wholesaler engaged in interstate commerce. Specifically, if your business is selling goods and/or services across state lines, going forward your business may be required to account for sales tax on these transactions. This is especially prevalent in the e-commerce industry, where products are offered for sale across the country and not solely in the physical location of the retailer or wholesaler. If you believe this decision may impact your business, you should track carefully further developments, as states are now permitted to impose sales taxes on these transactions.

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⁵ *Id.*

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