



Supreme Court Overturns Physical Presence Rule for Sales Tax Collection

The U.S. Supreme Court held in *South Dakota v. Wayfair* that the Commerce Clause does not require a retailer to be physically present before a state can enforce tax collection obligations. Justice Kennedy wrote the majority opinion, joined by Justices Thomas, Ginsburg, Alito, and Gorsuch. The Court's decision overturns 50 years of precedent.

South Dakota, seeking to test that precedent, passed a law requiring all retailers making more than either 200 transactions or \$100,000 worth of sales to South Dakota customers to collect South Dakota sales tax. Three internet retailers—Wayfair, Overstock, and Newegg—sued, invoking the settled physical-presence requirement.

The Court concluded that a retailer's physical presence is unnecessary for the "substantial nexus" that the Commerce Clause requires. A retailer achieves substantial nexus simply by "availing itself of the substantial privilege of carrying on business in that jurisdiction." Moreover, even if the Court's precedent had been correct when decided, "modern e-commerce" made the physical presence requirement "artificial in its entirety." And although Congress's power to regulate interstate commerce meant that it could change the physical presence rule, the majority considered that an insufficient reason to retain flawed precedent by which the Court had imposed a "false" "constitutional default rule" on Congress. The majority also was unmoved by concerns about the burdens their decision will place on small- and medium-sized businesses.

As to the internet retailers facing the South Dakota tax, the Court ruled that "[h]ere, the nexus is clearly sufficient based on both the economic and virtual contacts respondents have with the State." Nexus was sufficient under the due process clause because of the quantity of business conducted and the "extensive virtual presence" they had in South Dakota.

The Court declined, however, to rule whether South Dakota's law as applied violated "some other principle" in the Commerce Clause, instead remanding for further proceedings on this point. The Court did praise several features of South Dakota's rule: the "200 transactions or \$100,000" safe harbor, the lack of retroactive liability, its participation in the Streamlined Sales and Use Tax Agreement, and free, state-provided software that immunizes remote sellers from audit liability. But the Court did not hold that such features are required and did repeatedly cite the United States' amicus brief, which argued that a single sale into a state, or the existence of a "cookie" on an in-state customer's phone or computer, is constitutionally sufficient.

Justices Thomas and Gorsuch each filed a concurring opinion, questioning the Court's dormant Commerce Clause jurisprudence. Chief Justice Roberts dissented, joined by Justices Breyer, Sotomayor, and Kagan, invoking *stare decisis*. He argued that Congress was best equipped to determine the tax collection obligations for remote sellers and faulted the majority for downplaying the administrative costs that multistate (and local) sales tax compliance places on small businesses.



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