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Overturning Quill: Why Wayfair Was Correctly Decided and What Lies Ahead

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OVERTURNING *QUILL*: WHY *WAYFAIR* WAS CORRECTLY DECIDED AND WHAT LIES AHEAD

"In the name of federalism and free markets, Quill does harm to both. The physical presence rule it defines has limited States' ability to seek long-term prosperity and has prevented market participants from competing on an even playing field."[1]

ABSTRACT

There is no easier way to shop than online. A consumer can purchase virtually anything with the simple click of a mouse. In the past, it was oftentimes cheaper for consumers to shop online not because many websites offered free shipping with a subscription or a minimum purchase, but because many websites were not required to charge sales tax. Avoiding the added expense of sales tax could save hundreds of dollars for a consumer over the course of a year. This protection was furnished by the "physical presence" rule established in *National Bellas Hess, Inc. v. Department of Revenue of Illinois* and *Quill Corp. v. North Dakota*. The physical presence rule barred states from requiring out-of-state retailers to collect and remit sales tax if that retailer did not maintain a physical presence in the taxing state. But consumers will no longer be awarded the benefits of this bargain. Recently, in *South Dakota v. Wayfair, Inc.*, the Court overturned the long-standing precedent established in *Bellas Hess* and *Quill*. States are now permitted to require out-of-state retailers to collect sales tax even if that retailer does not maintain a physical presence in the taxing state. In light of the Court's recent decision, state and local governments will no doubt begin to impose sales tax for online retail purchases. This Note will first walk through how we got to where we are today. It will then discuss why the Court's recent decision was correct and what the next steps are in addressing potential issues arising in the aftermath of *South Dakota v. Wayfair*.

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

I. INTRODUCTION

Since the birth of the Internet, e-commerce has grown to a size that some may have never thought possible and is still on the rise. You will be hard pressed to find someone under the age of say, maybe 60, who has not made a purchase online. This growth has led to a boom in the economy and in the retail industry. But it has led to a bust in state budgets. For over two decades, states have been unable to effectively charge sales tax—a majority of states' main source of income—on online purchases made from out-of-state retailers. This is because of the Supreme Court's 1967 decision of *National Bellas Hess, Inc. v. Department of Revenue of Illinois*[2] and its 1992 decision of *Quill Corp. v. North Dakota*.[3] These cases established the precedent that in order

2. 386 U.S. 753 (1967).
3. 504 U.S. 298 (1992).

for states to force out-of-state retailers to collect sales tax on retail purchases, the out-of-state retailer must have a physical presence in the state where the purchase is made.

In the decades since *Quill*, states have enacted an array of different laws in an attempt to compensate for the sales tax revenue lost to retail purchases made online. However, these laws do little to combat the problem and have only made up for a miniscule amount of the revenue lost. In 2015, states were offered a glimpse of hope when the Court issued its decision in *Direct Marketing Association v. Brohl*.[4] In that decision, Justice Kennedy (who joined in the majority opinion in *Quill*), in his concurring opinion, explicitly stated that the time had come for the Court to reexamine *Quill* and urged a state to challenge *Quill's* long-standing precedent. In 2016, South Dakota answered the call and passed legislation that went against *Quill* for the sole purpose of bringing a challenge to the Court.

Finally, in its June 2018 decision of *South Dakota v. Wayfair, Inc.*,[5] the Court overturned the physical presence requirement. States are now liberated from *Quill's* grasp and the playing field is leveled. But overturning *Quill* was only the beginning. State governments and Congress must now focus on providing a workable tax framework so that state and local governments, businesses, and consumers can thrive in light of the Court's most recent decision.

II. THE SUPREME COURT'S JURISPRUDENCE ON SALES AND USE TAXES IMPOSED ON OUT-OF-STATE RETAILERS

Prior to *Wayfair*, the Supreme Court had never directly been presented with the question of whether a state may impose a sales or use tax on online purchases made from an out-of-state retailer. However, the Court had held that states may not impose sales or use taxes on mail-order purchases from out-of-state retailers unless the retailer had a "substantial nexus" with the taxing state as required by the Commerce Clause of the Constitution.[6] The Court, in *Quill*, determined that in order to pass the "substantial nexus" test, the retailer must have a physical presence within the state where the purchase is made.[7] Even though the constitutionality of taxing online sales had never been decided by the Court, it was easy to see how its jurisprudence surrounding the taxation of mail-order purchases from out-of-state retailers did not allow for online sales to be taxed unless the retailer maintained a physical

4. 135 S. Ct. 1124 (2015).
5. 138 S. Ct. 2080 (2018).
6. *See Quill*, 504 U.S. at 311.
7. *See id.* at 317.

presence within the state where the purchase is made.[8] Over time, online purchases skyrocketed.[9] Along with this this economic shift came a shift in the Court's attitude towards the taxation of online purchases.[10] The soar in online purchases and the Court's shifting attitude finally gave way to allowing states to tax online purchases from out-of-state retailers.

A. ESTABLISHING THE PHYSICAL PRESENCE RULE: *NATIONAL BELLAS HESS, INC. V. DEPARTMENT OF REVENUE OF ILLINOIS*

In 1967, the Supreme Court decided *National Bellas Hess, Inc. v. Department of Revenue of Illinois*. *Bellas Hess* established the physical presence test relied on by the Court in *Quill*.[11] *Bellas Hess* came by way of an appeal of a judgment from the Illinois Supreme Court requiring that Bellas Hess collect and remit to the state use taxes imposed by Illinois statute.[12]

National Bellas Hess was a mail-order house incorporated in Delaware with its principal place of business located in North Kansas City, Missouri.[13] Twice a year, Bellas Hess mailed catalogues throughout the nation to its active or recent customers.[14] It also occasionally mailed advertising flyers to its past and potential customers.[15] To purchase merchandise, Bellas Hess' customers mailed their orders to Bellas Hess at its Kansas City location.[16] Bellas Hess then sent the ordered goods to the customers by either mail or common carrier.[17] Bellas Hess did not maintain any physical places of business in Illinois, did not employ any salesmen or representatives in Illinois, did not own property in Illinois, did not have a telephone listing in Illinois, and did not advertise in Illinois in any other way besides the catalogues and flyers.[18]

Under Illinois statute, "retailers maintaining a place of business in [Illinois]"[19] were required to collect from the purchaser and pay to the Depart-

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8. Ricky Hutchens, Note, *Desperate Times Call for Desperate Measures: States Lead Misguided Offensive to Enforce Sales Tax Against Online Retailers*, 68 VAND. L. REV. 575, 584 (2015).
9. *See* discussion *infra* Part VI.A.
10. *See* Direct Mktg. Ass'n v. Brohl, 135 S. Ct. 1124, 1134 (2015) (Kennedy, J., concurring).
11. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S 753, 758 (1967).
12. *Id.* at 754.
13. *Id.*
14. *Id.*
15. *Id.*
16. *Id.* at 754-55.
17. *Bellas Hess*, 386 U.S. at 755.
18. *Id.* at 754.
19. Under Illinois statute at the time, a "retailer maintaining a place of business in [Illinois]" included any retailer "[e]ngaging in soliciting orders within the State from users by means of catalogues or other advertising, whether such orders are received or accepted within or without this State." *Id.* at 755.

ment of Revenue a tax for tangible personal property purchased by consumers for use in Illinois.[20] The retailer was also required to provide a receipt to the purchaser if demanded and to "keep such records, receipts, invoices, and other pertinent books, documents, memoranda, and papers as the [Department] shall require, in such form as the [Department] shall require, and must submit to such investigations, hearings, and examinations as are needed by the [Department] to administer and enforce the use tax law."[21] Failure to comply with these requirements was punishable by a fine of up to $5000 and imprisonment of up to six months.[22]

Bellas Hess argued that the Illinois statute violated the Due Process Clause of the Fourteenth Amendment and created an unconstitutional burden upon interstate commerce.[23] The Court recognized that the tests for analyzing a Commerce Clause claim and an economic Due Process Clause claim were similar.[24] At the time, a state tax was permissible under the Due Process Clause when a state had offered something for which it could ask for a return.[25] For a state tax to survive the confines of the Commerce Clause, the tax "[could] only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys."[26]

Prior to *Bellas Hess*, the Court had upheld state use taxes in circumstances where the out-of-state seller maintained local retail stores and had agents soliciting and arranging sales out of state for the seller. However, the Court had not upheld state use taxes when the seller sent catalogs through the mail to customers or advertised through radio and newspapers.[27] The Court recognized the distinction between the cases where a state use tax was upheld and the cases where a tax was struck down.[28] That is, use taxes imposed on out-of-state sellers with retail outlets, solicitors, or property within a state were permissible; use taxes imposed on out-of-state sellers who did no more than communicate with customers by mail or common carrier, on the other hand, were not permissible.[29]

The Court held that use taxes imposed on out-of-state sellers with no physical presence in the state or locality violated the Due Process and Com-

20. *Id.*; *see also* Dep't of Revenue v. Nat'l Bellas Hess, Inc., 214 N.E.2d 755, 757 (Ill. 1966).
21. *Bellas Hess*, 386 U.S. at 755.
22. *Id.*
23. *Id.* at 756.
24. *Id.*
25. *Id.*
26. *Id.*
27. *Bellas Hess*, 386 U.S. at 757-58.
28. *Id.* at 758.
29. *Id.*

merce Clauses because "local jurisdictions [had] no legitimate claim to impose a 'fair share of the cost of the local government'" and because "[t]he very purpose of the Commerce Clause was to ensure a national economy free from such unjustifiable local entanglements."[30] Central to the Court's decision was the fact that if states could impose a use tax on out-of-state sellers, then any municipality or political subdivision would also be able to impose such a tax.[31] Subjecting out-of-state retailers to the many variations in tax rates, exemptions, and record-keeping requirements may have created an administrative nightmare for businesses, resulting in a burden on interstate commerce.[32] The Court's holding essentially established the physical presence test that was relied on in *Quill*.[33]

The Court concluded by pointing out that "[u]nder the Constitution, this is a domain where Congress alone has the power of regulation and control."[34] Congress's ability to regulate a state's imposition of a sales or use tax on an out-of-state retailer was also recognized by the Court in *Quill*.[35] Additionally, Chief Justice Roberts' dissent in *Wayfair* was based upon the premise that it was up to Congress, not the Court, to decide whether a state could impose a sales or use tax on out-of-state retailers.[36]

B. ESTABLISHING PHYSICAL PRESENCE AS A SUBSTANTIAL NEXUS: *QUILL CORP. V. NORTH DAKOTA*

Nearly three decades later, in *Quill Corp. v. North Dakota*, the Supreme Court dealt with the same issue that it did in *Bellas Hess*—whether sales and use taxes imposed on out-of-state retailers accord with the Due Process Clause and the Commerce Clause of the Constitution.[37] The *Quill* Court reaffirmed *Bellas Hess*, establishing a long-standing precedent that eventually led to online retailers having an unfair advantage over traditional brick and mortar sellers.[38] Until the Court's decision in *Wayfair*, *Quill* had effectively barred states from imposing sales or use taxes on online purchases made from out-of-state retailers.[39] This occurred in an era when e-commerce and online

30. *Id.* at 760.
31. *Id.* at 759.
32. *Id.* at 759-60.
33. *Bellas Hess*, 386 U.S. at 758.
34. *Id.*
35. *See* Quill Corp. v. North Dakota, 504 U.S. 298, 318 (1992).
36. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2104-05 (2018) (Roberts, C.J., dissenting).
37. *See Quill*, 504 U.S. at 305.
38. *Id.* at 317.
39. *Id.*

shopping was growing at an astounding rate and was shaping the way that consumers shop today.[40]

In *Quill*, the Court distinguished a state's taxing ability under the Fourteenth Amendment's Due Process Clause from a state's taxing ability under the Commerce Clause of Article I, § 8, clause 3 of the Constitution.[41] The Court ultimately held that an out-of-state seller may have the "minimum contacts" with a state required by the Due Process Clause, yet lack the "substantial nexus" required by the Commerce Clause.[42] Therefore, even though a state tax may be permissible under the Due Process Clause, it may not be permissible under the Commerce Clause.[43]

Quill was a Delaware corporation that sold office equipment and supplies throughout the United States.[44] Quill solicited its business through catalogs and flyers, advertisements, national periodicals, and telephone calls.[45] At the time, Quill's sales in North Dakota were almost $1 million to about 3000 customers, making it the sixth largest vendor of office supplies in the state.[46] Under North Dakota statute, Quill was required to collect a use tax from purchasers for property purchased for storage, use, or consumption within the state and remit it to the state.[47] After Quill refused to collect the use tax and remit it to the state, the state filed suit against Quill seeking a judgment finding that Quill was required to pay the taxes.[48]

Quill argued that the state did not have the power to compel it to collect a use tax from its North Dakota customers because of *Bellas Hess'* holding that such a requirement by a state violated the Due Process Clause and the Commerce Clause.[49] The trial court ruled in Quill's favor, finding the case indistinguishable from *Bellas Hess*.[50] On appeal, the North Dakota Supreme Court held that *Bellas Hess* should not have been applied because of changes in the economy and the law.[51] The state supreme court additionally pointed out that advances in computer technology "greatly eased the burden of compliance with a 'welter of complicated obligations' imposed by state and local taxing authorities," which was the *Hess* Court's central reasoning as to why

40. *See* discussion *infra* Part VI.A.
41. *Quill*, 504 U.S. at 312.
42. *Id.* at 313.
43. *Id.*
44. *Id.* at 302.
45. *Id.*
46. *Id.*
47. *Quill*, 504 U.S. at 302-03.
48. *Id.* at 303.
49. *Id.*
50. *Id.*
51. *Id.*

state and local use taxes burdened interstate commerce.[52] However, the United States Supreme Court disagreed and reversed the decision of the North Dakota Supreme Court.[53]

The Supreme Court first discussed what was required for state statutes imposing a tax on out-of-state sellers to be constitutional under the Due Process Clause and the Commerce Clause. A state law requiring an out-of-state seller to collect and remit use taxes may comply with the Due Process Clause if the seller maintains the required "minimum contacts" with the taxing state.[54] Under a four-part test established in *Complete Auto Transit, Inc. v. Brady*,[55] a state tax would survive a Commerce Clause challenge "so long as the 'tax [1] is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State.'"[56] The Court notably distinguished the Due Process Clause's "minimum contacts" requirement from the Commerce Clause's "substantial nexus" requirement, stating, "Although the 'two claims are closely related,' the Clauses pose distinct limits on the taxing powers of the States. Accordingly, while a State may, consistent with the Due Process Clause, have the authority to tax a particular taxpayer, imposition of the tax may nonetheless violate the Commerce Clause."[57]

The Court arrived at this conclusion because the Due Process Clause and the Commerce Clause reflect different constitutional concerns.[58] Specifically, due process concerns the fundamental fairness of governmental activity, while the Commerce Clause concerns the effects of state regulation on the national economy.[59] To illustrate, Congress has the power to authorize state actions that burden interstate commerce, but it does not have the power to authorize violations of the Due Process Clause.[60] From the states' perspective, even though a state tax may be valid under the Due Process Clause, it may not be valid under the Commerce Clause.[61]

Next, the Court analyzed the constitutionality of use taxes imposed on out-of-state sellers against a Due Process Clause challenge. In doing so, the Court relied on the evolution of the law in the area of judicial jurisdiction.

52. *Id.*
53. *Quill*, 504 U.S. at 303.
54. *Id.* at 305.
55. 430 U.S. 274 (1977).
56. *Quill*, 504 U.S. at 311 (citing *Complete Auto*, 430 U.S. at 279).
57. *Quill*, 504 U.S. at 305 (citation omitted).
58. *Id.* at 312.
59. *Id.*
60. *Id.* at 305.
61. *Id.* at 313.

Beginning with the infamous case of *International Shoe Co. v. Washington*,[62] the Court "framed the relevant inquiry as whether a defendant had minimum contacts with the jurisdiction 'such that the maintenance of the suit does not offend traditional notions of fair play and substantial justice.'"[63] For purposes of determining judicial jurisdiction, the Court had, over the years, abandoned the rigid physical presence requirement.[64] Applying a more flexible framework, a foreign corporation is now subject to jurisdiction where the corporation "purposefully avails itself of the benefits of an economic market in the forum State . . . even if it has no physical presence in the State."[65]

The *Quill* Court found that the same reasoning justified the collection and duty of a tax when a corporation is engaged in the "widespread solicitation of business within a State."[66] That is, if a corporation does business in a particular state, it "has 'fair warning that [its] activity may subject [it] to the jurisdiction of a foreign sovereign.'"[67] Ultimately, relying on the developments in the law of due process relating to judicial jurisdiction, the Court overruled *Bellas Hess'* requirement that, under the Due Process Clause, a state may only impose sales taxes on retailers maintaining a physical presence in the taxing state.[68]

After determining that state-imposed use taxes on out-of-state retailers were permissible under the Due Process Clause, the Court analyzed whether such a tax was permissible under the Commerce Clause.[69] Because state action rather than congressional action was the central issue, the Court, as it did in *Bellas Hess*, founded its analysis in the interpretation of the "negative" or "dormant" Commerce Clause.[70]

As previously mentioned, the four-part test established in *Complete Auto* governed the validity of state taxes under the Commerce Clause. The North Dakota Supreme Court held that the *Complete Auto* test, which was established subsequent to *Bellas Hess*, rendered *Bellas Hess* "obsolete."[71] The Supreme Court disagreed and determined that *Bellas Hess* continued to apply

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62. 326 U.S. 310 (1945).

63. *Quill*, 504 U.S. at 307 (quoting *Int'l Shoe*, 326 U.S. at 316).

64. *Id.* at 307.

65. *Id.*

66. *Id.* at 308.

67. *Id.* (quoting Shaffer v. Heitner, 433 U.S. 186, 218 (1977) (Stevens, J., concurring in judgment)).

68. *Id.*

69. *Quill*, 504 U.S. at 309.

70. *Id.* The dormant commerce clause prohibits certain state actions that interfere with interstate commerce. *Id.*

71. *Id.*

when deciding whether *Complete Auto's* "substantial nexus" requirement was satisfied.[72]

Coupling *Bellas Hess'* physical presence requirement with *Complete Auto's* substantial nexus requirement, the Court determined that in order to meet the substantial nexus requirement, a retailer must have a physical presence in the taxing state.[73] The Court found value in establishing such a bright-line rule in the area of sales and use taxes.[74] The Court reasoned:

> Such a rule firmly establishes the boundaries of legitimate state authority to impose a duty to collect sales and use taxes and reduces litigation concerning those taxes. . . . Moreover, a bright-line rule in the area of sales and use taxes also encourages settled expectations and, in doing so, fosters investment by businesses and individuals.[75]

The *Quill* majority ended its opinion by pointing out that the issue is one that Congress had the ultimate power to resolve.[76] The majority recognized the possibility that the Court's decision in *Bellas Hess*, holding that the Due Process Clause prohibited states from imposing use taxes, may have contributed to Congress's inaction.[77] Ultimately, the Court pointed out that any due process questions had been put to bed by its decision in *Quill* and urged Congress to take action.[78]

Quill reinforced the physical presence test established in *Bellas Hess* to determine whether a state tax imposed on an out-of-state retailer is permissible under the Commerce Clause.[79] This standard stood for over twenty-five years until, most recently, the Court decided *South Dakota v. Wayfair*. During this quarter century, e-commerce and Internet retail sales grew at an astounding rate, one which was likely unimaginable when *Quill* was decided.[80] In an attempt to combat the revenue losses they were experiencing because of untaxable Internet sales, states began to enact laws known as "Amazon statutes."

72. *Id.* at 311.
73. *Id.* at 314-15.
74. *Quill*, 504 U.S. at 317.
75. *Id.* at 315-16 (citations omitted).
76. *Id.* at 318.
77. *Id.*
78. *Id.* at 318. The Court urged Congress to take action by saying, "Congress is now free to decide whether, when, and to what extent the States may burden interstate mail-order concerns with a duty to collect use taxes." *Id.*
79. *Quill*, 504 U.S. at 314-18.
80. *See* discussion *infra* Part VI.A.

III. AMAZON STATUTES: A MEDIOCRE ATTEMPT BY STATES TO DEFEAT *QUILL*

The physical presence requirement established in *Bellas Hess* and reaffirmed in *Quill* seemingly rendered the states powerless in collecting sales taxes on purchases made from out-of-state retailers.[81] Because of the rise in online retailing since *Quill*, many states attempted to minimize their tax losses by enacting laws known as "Amazon statutes."[82] These laws were seen as the best-available option for states to recover a portion of the tax revenue that they would have otherwise not received.[83]

A. THE "CLICK-THROUGH NEXUS" APPROACH

New York, in 2008, was the first state to enact a statute that attempted to collect lost sales-tax revenue from online purchases.[84] The New York law adopted the "click-through nexus" approach.[85] This term is derived from the "click throughs" that occur when an individual or business (referred to as an affiliate or associate) places a link on its website directing consumers to an online retailer's website.[86] This approach sought to collect sales taxes from out-of-state retailers on sales made through affiliate or associate retailers located in the state.[87]

The New York law, specifically, required "vendors" to collect sales and use taxes.[88] Under the law, a "vendor" is defined as any entity which "solicits business" through "employees, independent contractors, agents or other representatives."[89] The statute presumed that sellers of taxable property and services met the requirement "if the seller enter[ed] into an agreement with a resident of this state under which the resident, for a commission or other consideration, directly or indirectly refer[red] potential customers, whether by a link on an Internet website or otherwise, to the seller."[90] Given the statutory language, in order to meet the requirement, an affiliate had to do more than

81. Hutchens, *supra* note 8, at 587.

82. ERIKA K. LUNDER & CAROL A. PETTIT, CONG. RESEARCH SERV., R42629, "AMAZON LAWS" AND TAXATION OF INTERNET SALES: CONSTITUTIONAL ANALYSIS 1 (2015).

83. *See* Hutchens, *supra* note 8, at 589-90.

84. Geoffrey E. Weyl, Comment, *Quibbling With Quill: Are States Powerless In Enforcing Sales and Use Tax-Related Obligations On Out-Of-State Retailers?*, 117 PENN ST. L. REV. 253, 265 (2012).

85. LUNDER & PETTIT, *supra* note 82, at 5.

86. *Id.*

87. *Id.*

88. N.Y. TAX LAW § 1101(b)(8) (McKinney 2013).

89. N.Y. TAX LAW § 1101(b)(8)(i)(C)(I) (McKinney 2013).

90. N.Y. TAX LAW § 1101(b)(8)(vi) (McKinney 2013).

simply place a link to the retailer's website on its own website.[91] The affiliate needed to refer potential consumers to the out-of-state retailer for some type of consideration, and gross sales from the affiliate must have amounted to more than $10,000 annually.[92] Additionally, the statutory presumption could be rebutted by the retailer if the retailer offered proof that "the residents' only activity in New York on behalf of the seller was to provide a link to the seller's website and that the residents did not engage in any in-state solicitation directed toward potential New York customers."[93]

Overstock.com and Amazon challenged the New York law on Due Process Clause and Commerce Clause grounds.[94] In *Overstock.com, Inc. v. New York State Department of Taxation and Finance*,[95] the New York Court of Appeals affirmed the constitutionality of the law.[96] The court held that the statutory presumption did not violate the Due Process Clause and that a substantial nexus existed when an out-of-state company employed affiliate retailers for compensation.[97]

Analyzing the Commerce Clause challenge first, the New York court cited the Supreme Court's decision in *National Geographic Society v. California Board of Equalization*.[98] That case explained the level of physical presence required for a state tax law to not violate the Commerce Clause.[99] The Court explained that "although an in-state physical presence is necessary, it 'need not be substantial. Rather, it must be demonstrably more than a "slightest presence."'"[100] Applying this standard, the court stated "[t]he presence requirement will be satisfied if economic activities are performed in New York by the seller's employees or on its behalf."[101]

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91. *See* Hutchens, *supra* note 8, at 590.

92. *Id.*

93. Overstock.com, Inc. v. New York State Dep't. of Taxation & Fin., 987 N.E.2d 621, 623 (N.Y. 2013). The New York court also referenced a memorandum issued by the Department of Taxation and Finance, which stated "[t]he presumption would be deemed successfully rebutted if the seller satisfies two conditions: (1) if the parties' contract prohibited the resident representative from engaging in any solicitation activities in New York State on behalf of the seller, and (2) if each resident representative submitted an annual, signed certification stating that the resident had not engaged in any of the proscribed solicitation." *Id.* at 624.

94. *Id.* at 622.

95. 987 N.E.2d 621 (N.Y. 2013).

96. *Overstock.com*, 987 N.E.2d at 622.

97. *Id.* at 621.

98. 430 U.S. 551 (1977).

99. *Overstock.com*, 987 N.E.2d at 625; *see also* Orvis Co., Inc. v. Tax Appeals Tribunal of New York, 654 N.E.2d 954 (N.Y. 1995).

100. *Overstock.com*, 987 N.E.2d at 625 (quoting *Orvis*, 654 N.E.2d at 961).

101. *Id.*

Based on the above-stated rule of law, the court determined that "the statute plainly satisfies the substantial nexus requirement."[102] The court found that active solicitation by New York individuals and corporations on behalf of out-of-state online retailers met the "demonstrably more than a 'slight presence' standard."[103] Moreover, the court pointed out that the law did not impose a tax on retailers – it was merely a means of collecting taxes that were "unquestionably due" from the individual purchasers themselves.[104]

The fact that New York residents were compensated for their solicitation played a key role in the court's decision.[105] Had New York residents not received compensation, the court would have found that a substantial nexus did not exist between the state and the online retailer.[106] The court rested its case on the conclusion that "if a vendor is paying New York residents to actively solicit business in this state, there is no reason why that vendor should not shoulder the appropriate tax burden."[107] The court held that the New York law did not violate the Commerce Clause of the Constitution.[108]

The court then analyzed the Due Process Clause challenge.[109] Amazon and Overstock argued that the law violated due process "because the statutory presumption is irrational and essentially irrebuttable."[110] Plaintiffs chose to challenge the law on its face; and the court held that Plaintiffs "failed to demonstrate that the statute is facially unconstitutional under . . . the Due Process Clause."[111] The court rejected Plaintiffs' argument that the law was irrational.[112] The court found that because affiliates were compensated based on the number of referrals they made, it was rational to presume that affiliates would "seek to increase their referrals by soliciting customers."[113] The court also rejected Petitioners' argument that the presumption was irrebuttable.[114]

102. *Id.* at 626.
103. *Id.*
104. *Id.*
105. *Id.*
106. *Overstock.com*, 987 N.E.2d at 626.
107. *Id.*
108. *Id.*
109. *Id.* at 626-27.
110. *Id.* at 626.
111. *Id.* at 627.
112. *Overstock.com*, 987 N.E.2d at 627.
113. *Id.* The court additionally stated that "it is not unreasonable to presume that affiliated website owners residing in New York State will reach out to their New York friends, relatives and other local individuals in order to accomplish this purpose." Additionally, the court found that the presumption would be less rational if it were applied to those who receive some types of "other consideration" as provided in the statute. This is because "it is difficult to distinguish that arrangement from traditional advertising." *Id.*
114. *Id.*

The court determined that the methods provided to rebut the statutory presumption were adequate even though they potentially placed an inconvenience on the online retailer.[115]

The challenge to New York's law survived constitutional muster.[116] Following the New York court's decision, a number of other states enacted similar legislation that sought to collect sales taxes from retailers participating in affiliate programs.[117] As a result, Amazon, who New York's law was aimed towards, largely abandoned its affiliate program in most states.[118] Having been defeated yet again, states then began to enact laws implementing notice and reporting requirements.

B. THE REQUIRED NOTIFICATION APPROACH

As an alternative to New York's Amazon law, a number of states enacted legislation taking an alternative approach to collecting sales tax from online retailers.[119] Led by Colorado, states began enacting statutes that required retailers who did not collect sales tax to report first to the consumer their obligation to pay a use tax and second to the state taxing agency the number of purchases made within the state.[120] In 2010, Colorado enacted a statute requiring retailers that did not collect Colorado sales tax to: (1) "notify Colorado purchasers that sales or use tax [was] due on certain purchases made from the retailer and that the state of Colorado require[d] the purchaser to file a sales or use tax return"; (2) provide a year-end notification to each Colorado purchaser of the dates of purchases, the amounts of each purchase, and the category of the purchase, as well as a reminder that the purchaser was obligated to file a sales or use tax return with the state of Colorado; and (3) file an annual statement with the department of revenue for each purchaser showing the total amount paid by the purchaser for the preceding calendar year.[121] If a retailer failed to conform to these reporting requirements, a penalty was imposed for each violation.[122]

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115. *Id.* The court explained that the methods provided for a retailer to rebut the presumption may be inconvenient for the retailer because "the presumption sensibly places the burden on the retailers to provide information about the activities of their own affiliates—information that Department of Taxation and Finance would have significant difficulty uncovering on its own." *Id.*

116. *Overstock.com*, 987 N.E.2d at 627.

117. Weyl, *supra* note 84, at 266.

118. *Id.*

119. LUNDER & PETTIT, *supra* note 82, at 6.

120. *Id.*

121. COLO. REV. STAT. ANN. § 39-21-112(3.5) (West 2010).

122. *Id.* A five-dollar penalty for each such failure was imposed on a retailer that failed to inform a purchaser that their purchase may have been subject to sales or use tax. COLO. REV. STAT. ANN. § 39-21-112(3.5)(c)(II) (West 2010). A ten-dollar penalty for each such failure was imposed on a retailer for failing to send the year-end report to the purchaser. COLO. REV. STAT. ANN. § 39-

The constitutional issues raised by Colorado's reporting law are obvious.[123] First, because the reporting requirements applied to retailers that did not have a physical presence in Colorado, it appears as though the statute violated the dormant commerce clause because it potentially burdened interstate commerce.[124] Second, the reporting requirements only applied to out-of-state retailers.[125] The reporting duties were not similarly imposed on Colorado businesses.[126] Thus, it appears as though the law was discriminatory on its face and could only be upheld if it survived strict scrutiny.[127]

The constitutional problems with the statute led to the Court's decision in *Direct Marketing Association v. Brohl*. In 2012, a federal district court struck down the Colorado law, finding *Quill* applied and that the law was discriminatory on its face and did not meet strict scrutiny.[128] On appeal, the Tenth Circuit dismissed the case, finding that the Tax Injunction Act (TIA) prohibited federal courts from hearing the case.[129] In a unanimous decision, the Supreme Court reversed and held that the TIA did not apply.[130] More importantly, however, was Justice Kennedy's concurring opinion, which called into question the justification for *Quill* and invited a challenge to its rationale.[131]

IV. *DIRECT MARKETING ASSOCIATION V. BROHL*: A CALL TO ACTION

In 2015, the Court decided *Direct Marketing Association v. Brohl*. *Direct Marketing* did not present an opportunity for the Court to directly overturn or reanalyze *Quill*. But Justice Kennedy, in his concurring opinion, invited the opportunity for the Court to hear a case that would allow it to reexamine *Quill* and *Bellas Hess*.[132] When *Direct Marketing* was decided,

21-112(3.5)(d)(III)(A) (West 2010). A ten-dollar penalty for each such failure was also imposed on a retailer for failing to provide the year end-report to the department of revenue. COLO. REV. STAT. ANN. § 39-21-112(3.5)(d)(III)(B) (West 2010). Each of these penalties could be rebutted by a showing of reasonable cause for such failure.

123. LUNDER & PETTIT, *supra* note 82, at 8.

124. *Id.*

125. *Id.*

126. *Id.*

127. *Id.* The standard set forth by the Court states that in order to survive strict scrutiny such a law would have to "advance a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives." New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 278 (1988).

128. Direct Mktg. Ass'n v. Huber, Civil No. 10-cv-01546-REB-CBS, 2012 WL 1079175, at *10 (D. Colo. Mar. 30, 2012).

129. Direct Mktg. Ass'n v. Brohl, 735 F.3d 904, 920 (10th Cir. 2013).

130. *See* discussion *infra* Part IV.

131. Direct Mktg. Ass'n v. Brohl, 135 S. Ct. 1124, 1135 (2015) (Kennedy, J., concurring).

132. *Id.*

Colorado required residents who purchased property from sellers that did not collect sales or use taxes to file a return and remit those taxes directly to the State Department of Revenue.[133] In an attempt to improve compliance with this requirement and in an attempt to increase tax revenue from online purchases, Colorado passed a law requiring retailers that did not collect sales or use taxes to notify Colorado customers of their tax liability and to report tax-related information to those customers and the Colorado Department of Revenue.[134]

A trade association of retailers claimed that the law violated the United States and Colorado Constitutions.[135] A federal district court granted partial summary judgment and permanently enjoined enforcement of the notice and reporting requirements.[136] On appeal, the question presented to the Supreme Court was whether the Tax Injunction Act (TIA),[137] which provides that federal district courts "shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State," deprived the district court of jurisdiction over the suit.[138] *Direct Marketing* did not call into question a state statue attempting to collect taxes from purchases made online by requiring out-of-state retailers to collect and pay a sales tax. Therefore, the Court did not analyze the constitutionality of such a statute. However, Justice Kennedy recognized the "injustice faced by Colorado and many other States."[139]

Justice Kennedy asserted that the *Quill* majority acknowledged that its conclusion was wrong when the case was decided.[140] Yet, based on the principle of *stare decisis*,[141] it still held that retailers must have a physical presence in the state in order for tax-collection duties to be imposed upon them under the Commerce Clause.[142] In fact, Kennedy confronted the fact that he himself (along with Justice Scalia and Justice Thomas) based his concurrence

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133. *Id.* at 1127 (majority opinion).

134. *Id.*

135. *Id.* at 1128.

136. *Id.* at 1129.

137. 28 U.S.C. § 1341 (2012).

138. *Direct Mktg.*, 135 S. Ct. at 1127.

139. *Id.* at 1134 (Kennedy, J., concurring).

140. *Id.* Kennedy stated, "the Court relied on *stare decisis* to reaffirm the physical presence requirement. . . . despite the fact that under the more recent and refined test elaborated in *Complete Auto Transit, Inc. v. Brady*, 'contemporary Commerce Clause jurisprudence might not dictate the same result' as the Court had reached in *Bellas Hess*." *Id.* (quoting Quill Corp. v. North Dakota, 504 U.S. 298, 311 (1992)).

141. Stare decisis is "[t]he doctrine of precedent, under which a court must follow earlier judicial decisions when the same points arise again in litigation." *Stare Decisis*, BLACK'S LAW DICTIONARY (9th ed. 2009).

142. *Direct Mktg.*, 135 S. Ct. at 1134 (Kennedy, J., concurring).

in the judgment of *Quill* on *stare decisis* alone.[143] He stated that upholding the rule established in *Bellas Hess* based on *stare decisis* "further underscores the tenuous nature of that holding."[144] Kennedy opined that the *Quill* Court's decision was "now inflicting extreme harm and unfairness on the States."[145] Kennedy contended that the *Quill* Court should have taken the opportunity to reevaluate *Bellas Hess* in light of *Complete Auto* and the technological and social changes taking place at the time.[146]

Kennedy went on to offer an array of statistics illustrating the growth of the Internet and Internet sales since *Quill* and the inability of states to effectively tax such sales.[147] At the heart of his concurrence, Kennedy stated:

> Given these changes in technology and consumer sophistication, it is unwise to delay any longer a reconsideration of the Court's holding in *Quill*. A case questionable even when decided, *Quill* now harms States to a degree far greater than could have been anticipated earlier. It should be left in place only if a powerful showing can be made that its rationale is still correct. . . . The legal system should find an appropriate case for this Court to reexamine *Quill* and *Bellas Hess*.[148]

Given the invitation offered by Kennedy enticing a state to challenge *Quill*, a number of states enacted statutes requiring out-of-state sellers to collect sales taxes for purchases made online or through other means.[149] Most notable of these statutes was South Dakota's, which directly challenged *Quill's* physical presence requirement by imposing a sales and use tax on any retailer conducting a certain amount of business within the state.[150] This statute and the reversal of *Quill* will be analyzed in the following section.

V. *SOUTH DAKOTA V. WAYFAIR, INC.*: ANSWERING THE CALL

After Justice Kennedy issued his concurring opinion in *Direct Marketing*, a number of states enacted statutes that attempted to collect sales and use taxes from remote sellers, even if the seller did not have a physical presence

143. *Id.*
144. *Id.*
145. *Id.*
146. *Id.* at 1134-35.
147. *Id.* at 1135.
148. *Direct Mktg.*, 135 S. Ct. at 1135 (Kennedy, J., concurring) (citation omitted).
149. *See* discussion *infra* Part V.
150. *See* discussion *infra* Part V.

in the state.[151] In 2017, Alabama, Indiana, North Dakota, Virginia, Tennessee, and Wyoming all passed legislation that addressed the sales tax issue.[152] When *Wayfair* was decided, new sales tax legislation had been passed or was pending in thirty-two out of the forty-five states that impose a sales tax. This legislation asserted either a nexus based on the sales activity in a state without regard to the seller's physical presence in the state or imposed requirements similar to Colorado's notice and reporting requirements previously discussed.[153] Additionally, forty-one out of the forty-five states that impose a sales tax had instituted some form of legislation that expanded physical nexus, such as New York did in its Amazon statute, by using affiliate programs as a way of establishing a physical presence.[154]

The most notable legislation was passed by South Dakota. In 2016, South Dakota passed Senate Bill 106.[155] Senate Bill 106 intentionally obligated sellers with no physical presence in the state to collect and remit sales tax if the seller's gross revenue exceeded $100,000 annually in the state or if the seller conducted 200 or more separate transactions annually in the state.[156] The bill itself expressly stated that the purpose of the legislation was to bring about a challenge to the Supreme Court's Commerce Clause jurisprudence on the sales tax issue.[157]

In light of this newly passed legislation, South Dakota commenced a civil action against Wayfair, Inc., Overstock.com, Inc., and Newegg, Inc., attempting to collect unpaid sales taxes on purchases made online through these companies.[158] Bound by the Supreme Court's precedent, the South Dakota Supreme Court ruled in favor of Wayfair, Overstock, and Newegg and affirmed the lower court's decision to enjoin South Dakota from enforcing the 2016 legislation.[159] The court recognized the invitation in Justice Kennedy's concurrence in *Direct Marketing* to challenge *Quill* and the persuasiveness of South Dakota's arguments.[160] However, the South Dakota court

151. Petition for Writ of Certiorari at 8, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494).

152. Elaine S. Povich, *Supreme Court to Decide Online Sales Tax Case*, PEW (Jan. 12, 2018), http://www.pewtrusts.org/en/research-and-analysis/blogs/stateline/2018/01/12/supreme-court-to-decide-online-sales-tax-case.

153. Petition for Writ of Certiorari, *supra* note 151, at 10.

154. *Id.* at 11. This type of legislation may "attribute a nexus to a seller based on the physical presence of an affiliate in the state . . . the activities of another party in the state . . . or the use of software or other electronic presence in the state. . . ." *Id.*

155. S.B. 106, 2016 Legis. Assemb., 91st Sess. (S.D. 2016).

156. *Id.*

157. *Id.*; State v. Wayfair, Inc., 2017 S.D. 56, ¶¶ 1, 11, 901 N.W.2d 754.

158. *Wayfair*, 2017 S.D. 56, ¶ 9, 901 N.W.2d 754.

159. *Id.* at ¶ 18.

160. *Id.* at ¶¶ 17-18.

did not take it upon itself to overturn the Supreme Court's physical presence requirement, but instead left the responsibility to the Court to overrule its previous decisions.[161]

As was the state's initial intention, the decision of the South Dakota Supreme Court was appealed by the state to the United States Supreme Court by petition for writ of certiorari.[162] On January 12, 2018, the Supreme Court granted certiorari.[163] Forty-one other states, two United States territories, and the District of Columbia joined South Dakota in its fight to overturn the physical presence requirement established in *Bellas Hess* and *Quill*.[164] Additionally, sixty-one amicus curiae briefs were filed with the Court weighing in on the issue.[165]

On appeal, South Dakota argued that *Quill* should be overruled because local governments were "severely and increasingly harmed by *Quill*, *Quill* unfairly harms local, brick-and-mortar businesses, and because *Quill* itself harms interstate commerce."[166] South Dakota based its argument on the fact that Internet commerce had grown astronomically in the decades since *Quill*.[167] Without a way for states to effectively collect sales or use taxes from online purchases, states' revenues continually declined as the popularity of online shopping increased.[168] This led to budget shortfalls in a number of states.[169] South Dakota and other states feared that these shortfalls would continually worsen if states remained unable to collect sales taxes from online purchases.[170]

South Dakota also raised the argument that *Quill* harmed local businesses because, in order to be price competitive with online sellers that did not have to collect sales tax, local business had to discount their prices, which erased their profit margin.[171] Finally, South Dakota creatively made the argument that *Quill* itself burdened interstate commerce.[172] This was based on the premise that *Quill*, rather than encouraging businesses to invest in jobs

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161. *Id.* at ¶ 18.

162. *Id.* at ¶ 11; Petition for Writ of Certiorari, *supra* note 151, at 5.

163. Order Granting Petition for Writ of Certiorari, South Dakota v. Wayfair, Inc., 138 S. Ct. 735 (2018) (No. 17-494).

164. *See* Brief for Colorado & 40 Other States et al. as Amici Curiae Supporting Petitioner, *Wayfair*, 138 S. Ct. 2080 (No. 17-494); Brief for Colorado & 34 Other States and the District of Columbia as Amici Curiae Supporting Petitioner, *Wayfair*, 138 S. Ct. 2080 (No. 17-494).

165. *See* Docket, *Wayfair*, 138 S. Ct. 2080 (No. 17-494).

166. Petition for Writ of Certiorari, *supra* note 151, at iii.

167. *Id.* at 12-15.

168. *Id.*

169. *Id.*

170. *Id.*

171. *Id.* at 15-17.

172. Petition for Writ of Certiorari, *supra* note 151, at 17-20.

and infrastructure in other states—or, more simply put, to engage in interstate commerce—provided an incentive for businesses to locate in one state and ship its product to all other states.[173] To quote South Dakota's Petition, "*Quill's* rule is at war with its own ends; it undermines rather than advances the economic union the dormant commerce clause is meant to promote."[174]

Rebutting these presumptions, Respondents (Wayfair, Newegg, and Overstock.com) argued that *Quill's* physical presence requirement should be upheld because the rule was not unworkable and because "changed circumstances do not warrant overturning *Quill*."[175] The crux of Respondents' argument was that overturning *Quill* would be detrimental to small businesses and startup companies.[176] Businesses would have to comply with the thousands of state and local tax jurisdictions throughout the United States.[177] Companies would also be subject to audits throughout the nation.[178] Respondents rebutted the presumption that advancements in computer software had made it easier for businesses to comply with state and local taxing regulations.[179] Costs of implementation, employee training, maintenance, and operation of the software were all factors that Respondents argued would burden business if they were forced to comply with thousands of tax regulations.[180]

Respondents also downplayed the impact that online sales had on state and local tax revenues since *Quill*.[181] They contended that the amount of revenue states would receive from taxing online sales was "grossly inflated."[182] However, conveniently, Respondents never refuted the amount of tax revenue that states contended they were losing by offering their own estimates.[183] Instead, Respondents simply attacked the credibility of the sources South Dakota used for its estimates.

Finally, Respondents offered alternative evidence that downplayed the expansion and popularity of online shopping and purported that the number of *taxable* online sales would not dramatically increase if *Quill* were to be overturned.[184] This was because many of the nation's largest retailers, such

173. *Id.*
174. *Id.* at 18.
175. Respondents' Brief in Opposition to Petition for Writ of Certiorari at iv, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494).
176. *Id.* at 20-28.
177. *Id.* at 25.
178. *Id.*
179. *Id.*
180. *Id.*
181. Respondents' Brief in Opposition to Petition for Writ of Certiorari, *supra* note 175, at 28-34.
182. *Id.*
183. *Id.*
184. *Id.*

as Amazon, already collected sales taxes in states that imposed such a tax.[185] However, Wayfair's arguments and its attack on the studies and statistics presented by South Dakota held little merit.[186]

Ultimately, the Supreme Court sided with South Dakota and the states.[187] On June 21, 2018, the Court issued its opinion in *South Dakota v. Wayfair, Inc.* overruling *Quill* and *Bellas Hess*.[188] Perhaps appropriately, Justice Kennedy wrote for the majority.[189]

After providing a synopsis of the issues presented to the Court and the historical context of the Court's Commerce Clause jurisprudence, the majority dove head first into its re-examination of *Quill* and *Bellas Hess*.[190] Wasting no time, Kennedy openly criticized the physical presence rule in the opening paragraph of his Commerce Clause analysis:

> Each year, the physical presence rule becomes further removed from economic reality and results in significant revenue losses to the States. These critiques underscore that the physical presence rule, both as first formulated and as applied today, is an incorrect interpretation of the Commerce Clause. . . . *Quill* is flawed on its own terms. First, the physical presence rule is not a necessary interpretation of the requirement that a state tax must be "applied to an activity with a substantial nexus with the taxing State." Second, *Quill* creates rather than resolves market distortions. And third, *Quill* imposes the sort of arbitrary, formalistic distinction that the Court's modern Commerce Clause precedents disavow.[191]

The majority seemed to draw back somewhat on *Quill's* staunch distinction between the Due Process Clause's "minimum contacts" requirement and the Commerce Clause's "substantial nexus" requirement.[192] The Court did not expressly say that the requirements are one in the same, but it drew them closer by stating: "The 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. Physical presence is not necessary to create a substantial nexus."[193] The Court denied the argument that subjecting small retailers to

185. Chris Isidore, *Amazon to Start Collecting State Sales Taxes Everywhere*, CNNTECH (Mar. 29, 2017, 2:59 PM), https://money.cnn.com/2017/03/29/technology/amazon-sales-tax/index.html.

186. Reply Brief at 9, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494).

187. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2099 (2018).

188. *Id.*

189. *Id.* at 2087.

190. *Id.* at 2087-92 (quoting Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977)).

191. *Id.* at 2092.

192. *Id.* at 2093.

193. *Wayfair*, 138 S. Ct. at 2093.

collecting sales and use taxes in a multitude of jurisdictions burdened commerce.[194] Reasoning that compliance costs were "largely unrelated to whether a company happens to have a physical presence in a State," the Court found that "[t]he physical presence rule is a poor proxy for the compliance costs faced by companies that do business in multiple States."[195] To illustrate, the Court provided the example that a small business with one salesperson in each state was forced to collect taxes in states where its goods were delivered, but a large corporation with salespersons in one central location and a website accessible in every state was not required to collect sales taxes "on otherwise identical nationwide sales."[196] Under such an example, small businesses might be burdened equally or more by compliance costs than large remote sellers. The Court was not persuaded by the *Quill* Court's reasoning and Wayfair's argument that compliance costs would unduly burden interstate commerce.[197]

The Court also found *Quill's* holding contrary to the Commerce Clause's intended purpose.[198] The Commerce Clause "was designed to prevent States from engaging in economic discrimination so they would not divide into isolated, separable units."[199] However, *Quill's* physical presence rule created a competitive advantage for remote sellers by sheltering them from state and local tax burdens.[200] The Court determined that the physical presence rule itself burdened rather than promoted interstate commerce because it discriminated against traditional brick and mortar retailers and "produce[d] an incentive to avoid physical presence in multiple States. . . . [T]he desire of businesses to avoid tax collection mean[s] that the market may currently lack storefronts, distribution points, and employment centers that otherwise would be efficient or desirable."[201] Stated bluntly, "Rejecting the physical presence rule is necessary to ensure that artificial competitive advantages are not created by this Court's precedents."[202]

Moreover, by treating identical actors differently,[203] the Court determined that the formalistic physical presence rule created by *Quill* was contrary to the case-by-case analysis employed by modern Commerce Clause

194. *Id.*
195. *Id.*
196. *Id.*
197. *Id.*
198. *Id.* at 2093-94.
199. *Wayfair*, 138 S. Ct. at 2093-94.
200. *Id.* at 2094.
201. *Id.*
202. *Id.*
203. The Court provided the following example: "Consider, for example, two businesses that sell furniture online. The first stocks a few items of inventory in a small warehouse in North Sioux

jurisprudence.[204] So long as a state law "avoids 'any effect forbidden by the Commerce Clause,' courts should not rely on anachronistic formalisms to invalidate it."[205] The Court advised states to consider "functional, marketplace dynamics" when "enacting and enforcing their tax laws."[206]

The majority also founded its opinion on the "'dramatic technological and social changes' of our 'increasingly interconnected economy.'"[207] Since *Quill*, "physical presence" has undertaken a different meaning than twenty-five years ago.[208] With widespread access to the Internet, marketing and distribution techniques have reformed to corroborate with today's modern economy. A company may have a physical presence in the state through the cookies it saves to a consumer's computer by way of the company's website, through the company's app that a consumer downloads, or by the data storage leased by the company in a state.[209] "Between targeted advertising and instant access to most consumers via any Internet-enabled device, 'a business may be present in a State in a meaningful way without' that presence 'being physical in the traditional sense of the term.'"[210] The Court decided that the physical presence rule was no longer the "bright-line test" that *Quill* intended it to be. Because of a company's ability to maintain "substantial virtual connections to [a] [s]tate," the Court held that the physical presence rule should not be maintained.[211]

As a matter of policy, the Court saw the physical presence rule as an impediment to states' and localities' ability to "perform critical public functions" and even implied that it allowed companies to assist in tax evasion.[212] For example, Wayfair provided its customers with home furnishings. In being able to purchase such items, consumers directly relied on state and local governments. To illustrate:

City, South Dakota. The second uses a major warehouse just across the border in South Sioux City, Nebraska, and maintains a sophisticated website with a virtual showroom accessible in every State, including South Dakota. By reason of its physical presence, the first business must collect and remit a tax on all of its sales to customers from South Dakota, even those sales that have nothing to do with the warehouse. But, under *Quill*, the second, hypothetical seller cannot be subject to the same tax for the sales of the same items made through a pervasive Internet presence." *Id.* (citations omitted).

204. *Id.* at 2095.

205. *Wayfair*, 138 S. Ct. at 2094-95 (quoting Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 285 (1977)).

206. *Id.* at 2095.

207. *Id.* (quoting Direct Mktg. Ass'n v. Brohl, 135 S. Ct. 1124, 1135 (2014) (Kennedy, J., concurring)).

208. *Id.*

209. *Id.*

210. *Id.* (quoting *Direct Mktg.*, 135 S. Ct. at 1135 (Kennedy, J., concurring)).

211. *Wayfair*, 138 S. Ct. at 2095.

212. *Id.* at 2096.

> State taxes fund the police and fire departments that protect the homes containing [Wayfair's] customers' furniture and ensure goods are safely delivered; maintain the public roads and municipal services that allow communication with and access to customers; support the "sound local banking institutions to support credit transactions [and] courts to ensure collection of the purchase price"; . . . and help create the "climate of consumer confidence" that facilitates sales.[213]

The Court saw it fit that when remote companies avail themselves of the benefits provided by state and local governments, they should not be exempted from compensating these governments for the services that the companies and their customers receive.[214] Arbitrarily taxing some, but not all, of the companies doing business in the state created marketplace inequality and threatened Commerce Clause objectives:

> In the name of federalism and free markets, *Quill* does harm to both. The physical presence rule it defines has limited States' ability to seek long-term prosperity and has prevented market participants from competing on an even playing field.[215]

The Court also addressed *stare decisis*, the doctrine on which *Quill* was largely decided, and which the dissent in *Wayfair* grounded its argument.[216] The majority concluded that *stare decisis* "can no longer support the Court's prohibition of a valid exercise of the State's sovereign power."[217] In the eyes of the Court, it was apparent that previous Commerce Clause decisions were prohibiting the States from exercising their sovereign power, and that it was time for the Court to correct its error.[218]

Finally, the majority addressed the dissent's second argument. That is, Congress, not the Court, should be the body to undertake reversal of the physical presence rule.[219] And again, the majority rejected this proposition. It found that "[i]t is inconsistent with the Court's proper role to ask Congress to address a false constitutional premise of this Court's own creation. . . . It is currently the Court, and not Congress, that is limiting the lawful prerogatives of the States."[220]

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213. *Id.* (citation omitted) (quoting Quill Corp. v. North Dakota, 504 U.S. 298, 328 (1992)).
214. *Id.*
215. *Id.*
216. *Id.*
217. *Wayfair*, 138 S. Ct. at 2096.
218. *Id.*
219. *Id.* at 2096-97.
220. *Id.*

After a half-century, the *Wayfair* Court finally overturned *Bellas Hess'* and *Quill's* ill-founded precedent.[221] The next section of this Note will first analyze why *Wayfair* was correctly decided. It will then discuss what is likely to come from *Wayfair* and what Congress must do to correct any deficiencies.

VI. WHY *WAYFAIR* WAS CORRECTLY DECIDED AND WHAT LIES AHEAD

A. WHY THE *WAYFAIR* COURT GOT IT RIGHT

Statistics show that, prior to *Wayfair*, states had lost an overwhelming amount of revenue because of their inability to tax online purchases.[222] Given the growth in Internet commerce since *Quill*, the Supreme Court was right to overturn the physical presence rule established in *Bellas Hess* and *Quill* and allow states to tax purchases made from remote sellers. When Quill was decided, mail-order and Internet sales totaled $180 billion.[223] In 2017, e-commerce sales totaled over $450 billion.[224] The inability of states to tax purchases made as part of this staggering growth has led to massive state budget shortfalls.[225]

It is estimated that in 2012 alone, states lost a total of approximately $23.2 billion in sales tax revenue.[226] Estimates of state revenue losses because of an inability to tax consistently ranged from $8 billion to $33 billion.[227] This is considerably more significant compared to the between $694 million and $3 billion that states were losing in 1992 when *Quill* was decided.[228] Had *Quill* not been overturned, the amount of revenue lost by states would have continued to increase in the wake of growing e-commerce and

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221. *Id.* at 2099.

222. Some argue that states are able to tax online purchases through a use tax. However, use tax compliance is estimated to be about 1.6% throughout the nation. Chana Joffe-Walt, *Most People Are Supposed To Pay This Tax. Almost Nobody Actually Pays It.*, NPR (Apr. 16, 2013, 3:55 AM), https://www npr.org/sections/money/2013/04/16/177384487/most-people-are-supposed-to-pay-this-tax.

223. Direct Mktg. Ass'n v. Brohl, 135 S. Ct. 1124, 1135 (2015) (Kennedy, J., concurring).

224. U.S. CENSUS BUREAU NEWS, U.S. DEP'T. OF COMMERCE, CB18-125, QUARTERLY RETAIL E-COMMERCE SALES: 2ND QUARTER 2018 (Aug. 17, 2018). This does not include mail-order or phone sales.

225. Sales taxes make up approximately 25% of total state revenue in the forty-five states that assess a sales tax. Olivia LaVecchia, *Internet Sales Tax Fairness*, INST. FOR LOCAL SELF-RELIANCE (July 7, 2016), https://ilsr.org/rule/internet-sales-tax-fairness/.

226. *Collecting E-Commerce Taxes | E-Fairness Legislation*, NAT'L CONFERENCE OF STATE LEGISLATURES, (Nov. 14, 2014), http://www ncsl.org/research/fiscal-policy/collecting-ecommerce-taxes-an-interactive-map.aspx#2.

227. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2088 (2018).

228. *Id.* at 2097.

Internet sales.[229] States were projected to lose more than $211 billion in remote sales revenue from 2018-2022.[230] The Court needed to provide some relief for states when it had become exponentially more difficult to raise revenue and provide for essential public services. This was a result of the Court's own doing, and it was right to correct its mishap.

Moreover, as a result of *Quill's* physical presence standard, businesses were being burdened by states' attempts to thwart *Quill* through Amazon statutes and similar laws. If *Quill's* standard had been reaffirmed by the *Wayfair* Court, more states would have undoubtedly established notice and reporting requirements such as those implemented in Colorado. These requirements had the potential to become more burdensome than collecting and remitting sales taxes. Notification had to be sent to each customer multiple times throughout the year, companies had to compile reports and submit them to the state, and penalties could be imposed if the notice and reporting requirements were not complied with. Again, as the Court recognized, *Quill* itself was proving unworkable as "physical presence" was becoming more difficult to define in an era of nonstop technological innovations leading to increased efforts by states to recover lost revenues.[231]

Due to the massive growth of the Internet, states suffered significant budget shortfalls because of *Quill's* physical presence rule. Finally, in *Wayfair*, the Court recognized its error and overturned *Quill's* wrongly decided precedent. However, the fight is not over, as states and Congress will have to establish workable boundaries in light of *Wayfair*.

B. POST-*WAYFAIR*: NEXT STEPS

Even though ultimately rejected by the Court, the argument that reversing *Quill* would subject small retailers to thousands of state and local tax jurisdictions was compelling and had merit.[232] But the fact that advancements in computer software make it easier for businesses to comply with state and local tax laws across many jurisdictions offers the impression that the burden

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229. Today, e-commerce accounts for approximately 13% of retail sales; by 2022, e-commerce is projected to account for approximately 17% of retail sales. Matt Linder, *E-commerce Is Expected to Grow to 17% of US Retail Sales by 2022*, DIG. COMMERCE 360 (Aug. 9, 2017), https://www.digitalcommerce360.com/2017/08/09/e-commerce-grow-17-us-retail-sales-2022/.

230. *Case for Fairness*, 21ST CENTURY RETAIL, http://www.efairness.org/case-for-fairness/index html (last visited Aug. 17, 2018).

231. *Wayfair*, 138 S. Ct. at 2097-98.

232. It is estimated that there are between 10,000 and 16,000 total taxing jurisdictions in the United States. Respondents' Brief in Opposition to Petition for Writ of Certiorari, *supra* note 175, at 26. South Dakota contends that the number of tax jurisdictions in the United States are "overstated," and that this estimate takes into account every separate jurisdiction wherever rate variations are theoretically possible. *See* Reply Brief, *supra* note 186, at 9.

on small business is vastly overstated.[233] In fact, "in the age of cloud computing, the marginal cost of adding additional tax jurisdictions beyond 6,000 (or even, say, 50) is functionally zero."[234] It must also be noted that many states will provide retailers with free software "if it allows them to obtain collection compliance."[235] Even though compliance with tax regulations from over 10,000 tax jurisdictions, in theory, sounds devastating, the fact of the matter is that any additional costs are nominal and the burden that would be imposed is over-exaggerated.[236]

In addition, seventeen of the top eighteen retailers had already begun collecting sales taxes prior to *Wayfair*.[237] Amazon collected sales taxes in every state that imposed a sales tax.[238] Provided with the fact that most retailers had already collected sales tax on online purchases, the Court's determination that subjecting retailers to multiple tax jurisdictions would have a minimal effect on interstate commerce is sound.

Granted, compliance with the requirements of several tax jurisdictions may be more detrimental to businesses conducting only a small portion of business in a taxing state. However, new state laws imposing sales tax on remote sellers will likely provide adequate minimums before sales taxes may be imposed on the seller. The requirements of South Dakota's law are that any retailer with over $100,000 in revenue or over 200 separate transactions annually in the State must collect and remit sales tax on retail purchases.[239] Some may consider this a relatively low bar in the grand scheme of online

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233. Reply Brief, *supra* note 186, at 9.

234. *Id.*

235. *Id.*

236. In its original complaint, South Dakota also brought suit against Systemax for failing to remit sales taxes to the State pursuant to the 2016 legislation. Preferring not to assert *Quill* as a defense to the lawsuit, Systemax reached a compromise with South Dakota, agreeing to voluntarily collect and remit sales taxes in compliance with the law if South Dakota were to dismiss its complaint against Systemax. Systemax began collecting and remitting sales taxes *the next day*. Petition for Writ of Certiorari, *supra* note 151, at 7.

237. Richard Wolf, *Supreme Court Will Decide If Online Retailers Must Collect Sales Tax*, USA TODAY (Jan. 12, 2018, 6:25 PM), https://www.usatoday.com/story/news/politics/2018/01/12/supreme-court-decide-if-online-retailers-must-collect-sales-tax/1021423001/.

238. Isidore, *supra* note 185. After states began to enact alternative nexus laws (such as click-through nexus laws, affiliated/related party nexus laws, and reporting/notification requirements previously discussed) Amazon began to reach agreements with states that it would collect and remit sales tax, and locate some type of facility in the state, if the state did not enforce collection of sales taxes for an agreed upon number of years. *See* Kendrack D. Lewis, *Is e-Fairness Legislation the New Cost of Doing Business Online? The Marketplace Fairness Act of 2013 and Its Impact on Amazon and E-Commerce, State Governments, and Traditional Retailers*, 40 T. MARSHALL L. REV. ONLINE 2, 8-14 (2014).

239. S.B. 106, 2016 Legis. Assemb., 91st Sess. (S.D. 2016).

retailing.[240] However, these minimums are suitable. For if a remote seller conducts $100,000 or 200 separate transactions worth of business annually in South Dakota, it likely conducts a significant amount of business in other states as well.

Hopefully, states do not take advantage of *Wayfair's* ruling by setting minimums significantly below those specified by South Dakota. However, if a state were to set minimums that were unduly burdensome towards small retailers and interstate commerce, say $10,000 in revenue or twenty transactions annually, the Court could find those statutes to be in violation of other Commerce Clause theories if challenged.[241] A considerable amount of litigation could arise from such a situation. This potential litigation may force states to narrowly focus their aim on retailers that they know will not be burdened by legislation requiring them to collect sales tax on online purchases. More likely is that Congress will finally be forced to do what it has been encouraged to do for the past half-century—enact legislation governing sales taxes imposed on out-of-state retailers.

First, states may be forced to simplify their tax codes so that the number of taxing jurisdictions within a state is limited. A number of states have already joined in a voluntary agreement among states known as the Streamlined Sales and Use Tax Agreement (SSUTA).[242] The purpose of the SSUTA is "to simplify and modernize sales and use tax administration in the member states in order to substantially reduce the burden of tax compliance."[243] An agreement among states such as the SSUTA makes compliance across multiple tax jurisdictions cheaper and easier for retailers, reducing the burden of compliance with state sales tax laws.[244] However, now that states have the power to freely impose sales taxes on out-of-state retailers, cooperation among states may not continue to the same degree as it did while *Quill* was the law of the land.[245] If a discord between states ensues, eventually becoming competitive and ultimately burdening interstate commerce, Congress will

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240. The United States Small Business Association considers retailers that do a minimum of $7.5 million in average annual receipts a "small business." However, there are some exceptions to these standards for some industries. *See* 13 C.F.R. § 121.201 (2018).

241. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2098-99 (2018).

242. A total of twenty-four states, including North and South Dakota, have enacted laws that are in full compliance with the SSUTA. The SSUTA is not binding law among states. States must pass laws that are in compliance with the SSUTA in order to be considered a full member state. Streamlined Sales and Use Tax Agreement (as amended May 3, 2018), Art. I §§ 103-04, *available at* http://www.streamlinedsalestax.org/ (last visited Sept. 12, 2018).

243. *Id.* § 102.

244. *How Does the Agreement Simplify Sales Tax Administration?*, STREAMLINED SALES TAX GOVERNING BD., INC., http://www.streamlinedsalestax.org/index.php?page=gen4 (last visited Aug. 19, 2018).

245. Brief of Amici Curiae United States Senators Ted Cruz et al. Supporting Respondents at 1, *Wayfair*, 138 S. Ct. 2080 (No. 17-494).

finally be forced to act. Rather than taking a "wait and see" approach, Congress should be proactive in enacting legislation.

Since 2001, Congress has introduced several bills addressing the physical presence rule.[246] But because there has never been a legitimate need for Congress to address the issue, legislation has never been passed. In 2017, three bills were introduced, each of which is currently pending.[247]

In the eleventh hour before *Wayfair* was decided, Senators Ted Cruz, Steve Daines, and Mike Lee filed an amicus brief urging the Court to uphold *Quill* so as to allow Congress the opportunity to finally reach a compromise and enact legislation altering *Bellas Hess'* and *Quill's* precedent.[248] But in the fifty years since *Bellas Hess* was decided, Congress never felt the need to act, despite being encouraged a trio of times by the Court. So why would the Court then have been persuaded by a threesome of senators that Congress was finally prepared to come up with a solution to the problem? Perhaps now, with an actual looming threat of burdened interstate commerce as a result of *Wayfair*, Congress will enact legislation providing states with an opportunity to collect sales taxes while still providing protections for small businesses. This Note will discuss the three pending bills before Congress and argue the effectiveness of each.

The first of these bills is the Marketplace Fairness Act of 2017 (Act).[249] The Marketplace Fairness Act allows each member state of the SSUTA to require remote sellers to collect and remit sales and use taxes for remote sales.[250] States that are not members of the SSUTA may require remote sellers to collect and remit sales and use taxes so long as they adopt and implement "minimum simplification requirements.[251] The Act specifies minimum simplification requirements relating to the administration of the tax, audits, and streamlined filing.[252] The Act also includes a small-seller exception.[253] This exception exempts sellers with less than $1 million annually in remote sales from having to collect and remit sales and use taxes on remote sales.[254]

246. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2102-03 (2018) (Roberts, C.J., dissenting).

247. *Id.* at 2102.

248. Brief of Amici Curiae United States Senators Ted Cruz et al. Supporting Respondents, *supra* note 245, at 4-5.

249. Marketplace Fairness Act of 2017, S. 976, 115th Cong. (2017).

250. *Id.* § 2(a).

251. *Id.* § 2(b).

252. *Id.* § 2(b)(2).

253. *Id.* § 2(c).

254. *Id.*

The House version of the Marketplace Fairness Act is the Remote Transactions Parity Act of 2017 (Remote Parity Act).[255] The Remote Parity Act, like the Marketplace Fairness Act, allows states participating in the SSUTA to require remote sellers to collect and remit sales and use taxes, as well as states not participating in the SSUTA so long as they adopt and implement minimum simplification requirements similar to those of the Marketplace Fairness Act.[256] The Remote Parity Act also carves out a remote-seller exception.[257] However, under the Remote Parity Act this exception is applied in phases.[258] States could only require the collection of sales and use taxes by a remote seller if the seller: (1) has gross annual receipts in excess of $10 million for the first year following the effective date, $5 million for the second year, and $1 million for the third year; or (2) utilizes an electronic marketplace for the purpose of making products or services available for sale to the public.[259]

The third bill currently before Congress is the No Regulation Without Representation Act.[260] This bill essentially codifies the physical presence rule.[261] It limits a state's ability to "tax or regulate a person's activity in interstate commerce only when such a person is physically present in the State. . . ."[262] The bill defines "physical presence" essentially the same as *Bellas Hess* and *Quill* did[263] and excludes certain activities that indicate a de minimis physical presence.[264] Even though the *Wayfair* Court reversed the physical presence rule, Congress, of course, still has the authority to re-impose it.[265]

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255. Remote Transactions Parity Act of 2017, H.R. 2193, 115th Cong. (2017).

256. *Id.* § 2(a)-(b).

257. *Id.* § 2(c).

258. *Id.* § 2(c)(1)(A)-(C).

259. *Id.*

260. No Regulation Without Representation Act of 2017, H.R. 2887, 115th Cong. (2017).

261. *Id.* § 2(a).

262. *Id.*

263. The following activities constitute a physical presence under the No Regulation Without Representation Act: (1) maintaining a commercial or legal domicile in the State; (2) owning, holding a leasehold interest in, or maintaining real property such as an office, retail store, warehouse, distribution center, manufacturing operation, or assembly facility in the State; (3) leasing or owning tangible personal property (other than computer software) of more than de minimis value in the State; (4) having one or more employees, agents, or independent contractors present in the State who provide on-site design, installation, or repair services on behalf of the remote seller; (5) having one or more employees, exclusive agents or exclusive independent contractors present in the State who engage in activities that substantially assist the person to establish or maintain a market in the State; (6) or regularly employing in the State three or more employees for any purpose. *Id.* § 2(b)(1).

264. *Id.* § 2(b)(2).

265. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2096 (2018); Quill Corp v. North Dakota, 504 U.S. 298, 318 (1992); Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 760 (1967).

Congress should take a good look at enacting legislation consistent with the Marketplace Fairness Act or the Remote Transactions Parity Act. A combination of these bills would create uniformity and deter any burden that may result because of *Wayfair*. Federal legislation would also eliminate any potential for states to discriminate against out-of-state retailers because protection is provided through the simplification requirements. Imposing simplification requirements and carving out exceptions for small sellers is likely the best way that Congress can ensure that state-imposed sales taxes on remote sellers will not burden interstate commerce.

The one downfall with the Remote Parity Act is that it exempts a substantial number of large retailers for a period of two years. Sellers that exceed $5 million in gross receipts certainly have the ability to collect and remit state-imposed sales and use taxes. Many sellers of this size likely already have a physical presence in multiple tax jurisdictions, thus subjecting them to multiple sales taxes. Having to account for additional tax jurisdictions would not be unduly burdensome for sellers of this size. Another sticking point is that there is no small-seller exception if the seller sells his products via an electronic marketplace. This would essentially eliminate the small-seller exception for anyone doing business online. If Congress decides to act, it should adopt a small-seller exception no larger than $1 million as put forth in the Marketplace Fairness Act, rather than the phased approach provided for in the Remote Transactions Parity Act. A minimum of $1 million is large enough to alleviate any concerns of burdensome compliance costs for small retailers, yet small enough to allow states to collect taxes from large companies who are not burdened by compliance.

Rather than resurrecting an unfair, Court-created rule, Congress should govern by promoting fairness and providing guidance for states that wish to impose sales taxes on out-of-state sellers. But no matter what approach Congress takes, it will likely have to take some type of action in light of *Wayfair*. After all, under the Constitution, "this is a domain where Congress alone has the power of regulation and control."[266]

VII. CONCLUSION

In the half-century since the physical presence test was established in *Bellas Hess*, e-commerce has grown to a size that some may have never thought possible. State tax revenues have continually declined over the past two decades because of their inability to collect sales tax from purchases made online from out-of-state retailers. To combat this problem, states began implementing alternative ways to collect sales tax from out-of-state retailers.

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266. *Bellas Hess*, 386 U.S. at 760.

In 2015, realizing this ever-growing problem, Justice Kennedy invited states to pose a challenge to *Bellas Hess'* and *Quill's* legacy. Capitalizing on this invitation, South Dakota, in 2016, passed legislation directly challenging *Quill's* rationale. And finally, the Court, in *South Dakota v. Wayfair*, reversed *Bellas Hess'* and *Quill's* physical presence rule. It is now up to Congress to decide if it will finally enact legislation that establishes standards for fairness for states, retailers, and consumers.

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