

## Another Online Sales Tax Update: SCOTUS Overrules Quill

On June 20, 2018 the United States Supreme Court held in *South Dakota v. Wayfair* that states can collect sales tax from online retailers. The decision overruled the “physical presence” rule articulated in *Quill Corp. v. North Dakota*, which held that states could only collect sales taxes from retailers with a “physical presence” in the state.

At issue in the case was South Dakota’s 2016 law that required all stores to collect a 4.5% sales tax if they had \$100,000 in annual sales or 200 transactions in the state, regardless of the retailer’s physical presence in South Dakota. State officials sued three online retailers—Wayfair, Overstock.com, and Newegg—for violating the law. The retailers argued that the law was unconstitutional under *Quill*. South Dakota’s highest court agreed with the retailers.

The Supreme Court disagreed. Writing for the 5-4 majority, Justice Anthony Kennedy explained that the *Quill* decision has caused states to lose annual sales tax revenues between \$8 and \$33 billion by allowing remote sellers to “avoid the regulatory burdens of tax collection and . . . offer de facto lower prices caused by the widespread failure of consumers to pay the tax on their own.”

Since the 1992 *Quill* decision, the retail industry has undergone massive changes, with more and more sellers focusing on e-commerce and online sales. As brick-and-mortar stores have long argued, the physical presence rule disadvantages local and interstate business with a physical presence against online-only retailers by requiring only the former to charge sales taxes. For years, under the *Quill* standard, online retailers’ sales were essentially tax-free. In theory, consumers have always been required to pay a “use tax” on these items, equivalent to the state’s sales tax, but in practice, few consumers did so. In 1992, only two percent of Americans had internet access. Today, 89% of Americans have internet access, and e-commerce sales alone total nearly \$434.5 billion, and when combined with traditional remote sellers, approximately half a trillion dollars in total remote seller sales. Given the ease with which today’s consumers can and do buy online, states risk losing substantial revenue if they are unable to tax e-commerce sales, especially largely rural states like South Dakota.

In dissent, Chief Justice Roberts, joined by Justices Breyer, Sotomayor and Kagan, agreed with the majority that *Quill* was wrongly decided

but that any change to the “backdrop of established rules, including the physical-presence rule . . . of such a critical segment of the economy should be undertaken by Congress. The Court should not act on this important question of current economic policy, solely to expiate a mistake it made over 50 years ago.”

The retailers involved in *South Dakota v. Wayfair* have said that the decision will have little impact on their businesses. Wayfair claims it already collected sales tax on 80% of its U.S. orders. Overstock said its business would largely be unaffected but noted that small on-line startups will face a compliance challenge as they navigate more than 12,000 different state and local taxing districts.

The impact on major online retailers will vary. Take Amazon, for example—while Amazon voluntarily collects sales tax in every state that assesses one, it does not require third-party sellers using its site to do the same, and these third-party sellers account for *half* of Amazon’s total sales. Wayfair has a similar model, charging sales tax on products it sells while not requiring third-party vendors on its site to do so. Big box stores with accompanying high online sales, such as Best Buy and Walmart, already have a physical presence in most states and accordingly have always collected sales taxes.

Consumers will likely see increased costs from smaller online-only sellers and third-party sellers on sites such as Amazon and Wayfair as states enact laws pursuant to the Court’s ruling requiring these remote sellers to collect sales taxes. And while online retailers and consumers will see changes moving forward, the Court declined to say whether the decision permits states to collect sales tax from these retailers retroactively.