

## **Sales Tax Implications of South Dakota v. Wayfair, Inc.**

On June 21, 2018, the Supreme Court issued its much anticipated opinion in the landmark case of *South Dakota v. Wayfair, Inc.*, fundamentally changing the sales tax landscape in the United States. Due to the changes in buying patterns to the internet and away from brick and mortar businesses over the last decade, there has been a growing discontent among the states that they are losing significant sales tax revenue. Thus, enters this recent decision. This case could and most likely will lead to the largest changes in how sales tax was administered in the last 50 years.

### **The Case**

South Dakota enacted a law requiring out-of-state sellers to collect and remit sales tax as if the seller had a physical presence in the state. The law only applies to sellers, who, on an annual basis, delivered more than \$100,000 of goods or services into the state or engaged in more than 200 separate transactions for the delivery of goods or services into the state.

South Dakota sought to enforce the law against Wayfair, Inc. and other online retailers who exceeded the limits of the law. Each of the retailers had no employees nor owned any real estate in the state.

Based on prior precedents (*National Bellas Hess, Inc. v. Department of Revenue of Illinois*, 386 U.S. 753, and *Quill Corp. v. North Dakota*, 504 U.S. 29), the lower courts ruled that the law was not enforceable due to the lack of substantial nexus with the state under the “Physical Presence” test outlined in these cases. That test allowed states to require retailers to collect and remit sales tax only if the retailer had a physical presence (e.g., employees or operating an office) in that state. The mere shipment of goods into the state did not satisfy the physical presence test.

### **The Result**

In a 5-4 verdict, the Supreme Court explicitly overruled the prior cases and held that, while physical presence provided substantial nexus, such nexus also included a certain level of business activities (delivery of goods or services) conducted within the state. Instead, this Supreme Court case is based on an “economic nexus” versus a physical presence standard.

The Court found that, in this case, the nexus is clearly sufficient based on both the economic and virtual contacts the retailers have with the South Dakota. The state law applies only to sellers that deliver more than \$100,000 of goods or services into South Dakota or engage in 200 or more separate transactions for the delivery of goods and services into the state on an annual basis. This quantity of business could not have occurred unless the seller availed itself of the substantial privilege of carrying on business in South Dakota. The retailers here are typically large, national companies that undoubtedly maintain an extensive virtual presence and perform significant marketing activities in the state. Thus, the substantial economic nexus requirement is satisfied.

## **The Implications**

Will you now be required to collect and remit sales taxes in states to which you deliver goods or services? That is the current question you need to address today.

South Dakota v. Wayfair, Inc. allows all states to enact laws requiring out-of-state sellers to collect and remit sales taxes on sales to customers in that state provided the law applies a safe harbor to those who transact only limited business in the state. While South Dakota chose an annual \$100,000/200 transaction limit that the Court found sufficient, the Court created a level of uncertainty by leaving it up to the states to decide what safe harbors might be sufficient. There are already several states that have joined South Dakota and have begun to implement their own thresholds for collecting sales and use tax. Such states currently include Alabama, Colorado, Indiana, Massachusetts, Maine, Mississippi, North Dakota, Ohio, Pennsylvania, Rhode Island, Tennessee, Vermont, Wyoming and Washington. This will have a profound effect on several taxpayers who sell tangible products thru the internet even though they have no physical presence in the states they sell into.

Given that sales tax laws are established on a state-by-state basis, all businesses making sales of goods or services to customers in multiple states should evaluate the impact of the Court's holding. It is very possible this could put an end to "tax free" shipping. Out of state retailers will have a new set of obligations and challenges ahead of them. Rest assured, we are available to provide guidance based on your specific situation.