Supreme Court overturns physical presence rule for state taxation

June 21, 2018

In brief

In the highly anticipated case of *South Dakota v. Wayfair*, the US Supreme Court on June 21, 2018, in a 5 to 4 opinion, overturned the *Quill* physical presence standard, finding it "unsound and incorrect." Justice Anthony Kennedy delivered the opinion of the Court, stating that *Quill* imposes the sort of arbitrary, formalistic distinction that modern Commerce Clause precedents disavow in favor of a sensitive case-by-case analysis of purposes and effects.

The Court concluded that the doctrine of *stare decisis* no longer can support the prohibition of a valid exercise of the state's sovereign power. The Court noted that South Dakota law includes several features intended to prevent undue burdens on interstate commerce, which include no obligation to retroactively remit the sales tax. The case was remanded for proceedings not inconsistent with the opinion.

This PwC Insight provides a brief summary of the *Wayfair* decision. A more detailed Insight will be issued in the near future. [South Dakota v. Wayfair, Inc. Et. Al. No. 17-494]

In detail

In *Wayfair*, South Dakota asked the Court to reconsider its decision in *Quill v. North Dakota*, which precluded states from requiring interstate retailers to collect and remit sales and use tax on sales made to in-state customers unless the retailer had a 'physical presence' in the state.

South Dakota has no state income tax and relies on sales and use taxes for much of its revenue. In 2016, the South Dakota legislature passed legislation directly challenging the *Quill* physical presence standard. Senate Bill 106 instituted an economic presence standard that requires sales tax collection and remittance for any entity exceeding an annual sales threshold of $100,000 or engaging in 200 or more separate transactions in South Dakota. The law contains a provision that allowed the state to quickly seek a court ruling to address the constitutional validity of the collection and remittance requirements, while blocking the state from enforcing the provisions until the legal issue was resolved.

Shortly after SB 106 was enacted, South Dakota commenced a declaratory judgment action in circuit court seeking a declaration that Wayfair, a company with no physical presence in the state, but one that met the sales and transaction requirements, must collect and remit sales and use tax to the state. Wayfair moved for summary judgment, which the lower court granted based solely on undisputed statements of fact and the parties' briefs. The state appealed directly to the South Dakota Supreme Court, which affirmed the judgment.

On April 17, 2018, two years after SB 106 was enacted, the US Supreme Court heard oral arguments addressing *Quill's*

26-year-old physical presence rule. Several key themes emerged during the arguments, including the Court's uncertainty as to whether the physical presence requirement is a diminishing issue, how burdensome tax collection and remittance would be under an economic nexus standard, and whether this issue remains one Congress is better suited to address.

Approximately 15 states have existing laws or regulations providing an out-of-state seller is considered doing business in the state based on economic factors.

The takeaway

This historic ruling changes the landscape of sales tax collection for remote sellers and has far-reaching implications. The ruling may influence Congressional action on the issue.

Let's talk

If you have any questions about economic nexus provisions and the impact of the *Wayfair* decision, please contact one of the following PwC state and local tax professionals:

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