South Dakota: State Supreme Court hears oral arguments in nexus lawsuit

David M. Kall | Thursday, September 7, 2017

In the ongoing legal saga between internet retailers Wayfair, Overstock.Com, and Newegg, and South Dakota, the Supreme Court of South Dakota heard oral arguments last week on the familiar question of how much leeway states have to impose sales and use taxes on out of state internet retailers who arguably have no physical presence in the taxing jurisdiction.

South Dakota asserts that the main issue presented is whether precedent prevents "South Dakota from imposing an otherwise valid sales tax collection on retailers who lack a 'physical presence' within the state." In addition, the State also presented a second issue on the court, "whether the United States Supreme Court should reconsider its decision in [the 1992 case] *Quill Corp. v. North Dakota*…" *Quill* prohibits states from imposing sales and use tax obligations on remote retailers in the absence of a physical presence in the taxing state, pursuant to the dormant commerce clause.

Here is the crux of each party's arguments, as set forth in the briefs:

Appellant/State of South Dakota

The state characterized the proceeding as "an unusual case about an unusual statute." It explained that the legislature passed its tax-imposition statute, An Act to Provide for the Collection of Sales Taxes from Certain Remote Sellers" (Act), on retailers that have a "substantial connection to the State (defined by a minimum of $100,000 in sales or two hundred individual sales to in-state residents)." South Dakota explained that the legislature passed the law in response to Justice Kennedy's invitation in an opinion

from a separate case regarding notice and reporting obligations that Colorado imposed upon remote sellers, 2015's *Direct Marketing Ass'n v. Brohl.*

In his concurrence in *Brohl*, Justice Kennedy declared that in light of the "far-reaching systemic and structural changes in the economy… [and] 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."

South Dakota initiated the litigation when it sued the Internet retailer-defendants for failing to register with the Department of Revenue for sales tax collection, as required by the Act, even though they satisfied its conditions for registration. The State acknowledged that "[t]he Act itself recognizes that applying [its] rule to out-of-state retailers is in tension with existing decisions of the U.S. Supreme Court," including *Quill.*

To bolster its stance, South Dakota highlights the newest Supreme Court Appointee's take on the matter, Justice Gorsuch, who heard the *Brohl* case when he was on the Tenth Circuit, and wrote a concurring opinion, "likewise recogniz[ing] that *Quill* is an unusually vulnerable precedent that invites its own, eventual overruling."

The state ultimately justifies its desire to see Supreme Court precedent overturned by the damage *Quill's* hand-tying precedent is doing to the state's fiscal health.

Appellees/internet retailers Wayfair Inc., Overstock.Com. Inc., and Newegg Inc.

The appellees' case theory is equally straightforward. They assert that the Act, "requiring sales tax collection by retailers with no physical presence in South Dakota[, is] invalid as a matter of law under *Quill* and [accordingly,] this Court cannot, under existing constitutional doctrine, grant the State any relief, but must simply affirm the ruling below."

They say that even the plaintiff, South Dakota, acknowledges that the Act mandates "admittedly unlawful conditions for imposing a sales tax collection obligation on out-of-state retailers."

To support its side, the Internet retailers argue that just three facts have been established in the record, and that any other assertions that the state deploys are "drawn from external, non-record sources that are hotly contested and refuted by other sources… [and that serve] only to highlight the inappropriateness of the State's…action…and real goal of advancing a policy agenda."

The three facts are these:

1. Each of the Defendants has a principal place of business outside of South Dakota and lacks a physical presence in the state.
2. In 2015, each of the Defendants had gross revenue from the sale of tangible personal property delivered into South Dakota in excess of $100,000 and/or sold tangible personal property for delivery into South Dakota in 200 or more separate transactions.
3. None of the Defendants are registered to collect South Dakota sales tax.

In the end, appellees declare that "the State's appeal does not present any genuine and justiciable controversy for resolution by this Court, because both parties request the same outcome – affirmation of the lower court's order of summary judgment."

New nexus lawsuits

American Catalog Mailers Association and Netchoice, two plaintiffs who are suing many states for their nexus tax laws, filed a lawsuit against the Indiana Department of Revenue and related officials on June 30, 2017. This suit's basis is like the others, and seeks a declaration that Indiana's recently enacted legislation is unconstitutional. The legislation requires a retailer without a physical presence in the state to collect sales

taxes if (1) the retail merchant's gross revenue from sales into Indiana in a calendar year exceeds $100,000; or (2) the retail merchant makes sales into Indiana in more than 200 separate transactions.

According to Bloomberg, Indiana's Gov. Holcomb "said he signed the [nexus legislation] 'with full awareness' that *Quill* prohibits states from collecting sales and use taxes from out-of-state retailers."

These plaintiffs filed a similar suit in Wyoming on June 28, 2017, and in addition to the South Dakota action, have cases pending in Massachusetts and Tennessee.

David M. Kall

Team member bio