No. 17-494

In the Supreme Court of the United States

SOUTH DAKOTA,

Petitioner,

v.

WAYFAIR, INC., OVERSTOCK.COM, INC., AND NEWEGG, INC.,

Respondents.

On Writ of Certiorari to the Supreme Court of South Dakota

BRIEF FOR MONTANA AS *AMICUS CURIAE* SUPPORTING RESPONDENTS

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INTEREST OF *AMICUS CURIAE*

This Court held over 50 years ago that allowing every state, municipality, school district, or other political subdivision to impose sales tax burdens on remote sellers without a physical presence in the taxing jurisdiction would entangle business in "a virtual welter of complicated obligations." *National Bellas Hess, Inc. v. Department of Revenue of Ill.*, 386 U.S. 753, 760 (1967). "The very purpose of the Commerce Clause was to ensure a national economy free from such unjustifiable local entanglements," including "the many variations in rates of tax, in allowable exemptions, and in administrative and record-keeping requirements." *Id.* at 759-60. The Court reaffirmed that holding in *Quill Corp. v. North Dakota*, 504 U.S. 298, 316 (1992), recognizing that "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." Those animating principles of *Bellas Hess* and *Quill* remain every bit as valid today.

The State of Montana has a compelling interest in supporting *Quill's* physical-presence rule, and the precedent that has evolved around it. Montana has never had a sales tax.[1] If the Court abrogates *Quill*, small businesses in states that do not impose a sales tax, such as Montana, will face significant burdens, in part because of past reliance on *Quill*. The sovereignty of the State is also threatened by the due process

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[1] Montana voters twice rejected proposals for a sales tax, once in 1971 by 70 percent of the vote, and again in 1993 by 75 percent of the vote.

implications of foreign jurisdictions increasing the reach of their sales-tax authority. Additionally, the State will be adversely affected should this Court abrogate the physical-presence rule without addressing what level of contact is sufficient under both the Commerce and Due Process Clauses.

SUMMARY OF THE ARGUMENT

1. This Court should retain Quill under *stare decisis*. The reliance interest in *Quill's* physical-presence rule is most important to small or medium-sized "brick and click" businesses engaged in remote commerce. The burden is even more acute in non-sales tax states where businesses do not have experience collecting sales tax. Were this Court to strike the physical-presence rule, many of these businesses likely will no longer be able to offer online sales. South Dakota's assumption that advances in technology have eliminated these burdens may apply to internet staples like Amazon.com, which likely tracks the necessary information anyway, or to companies within Streamlined Sales and Use Tax Agreement (SST) jurisdictions, but it is not the case with small to medium-sized businesses in non-sales tax states.

Even if an e-commerce retailer is presumed to be able to handle the burden of deciphering rules and collecting sales tax in various jurisdictions once it has a sufficient amount of sales, there is no way to determine whether a retailer has met the threshold amount of commerce in a taxing state without tracking all sales. All businesses that engage in e-commerce, therefore, will have to invest in software and staffing to track sales and tax regulations in all taxing jurisdictions just to determine whether they even

qualify to collect tax. Worse they will have to collect tax all along in case they do quality. In other words, the burden will necessarily apply to *all* businesses that conduct e-commerce in *all* taxing jurisdictions, regardless of size or sales or whether they meet a jurisdiction's threshold.

There is also a real risk of taxing jurisdictions retroactively applying a decision overruling *Quill*. Ordinarily a constitutional ruling is retroactive, *Harper v. Virginia Dep't of Taxation*, 509 U.S. 86, 94 (1993), and at least one jurisdiction has already sent notice that it intends to apply their use tax retroactively. In addition, there is no guarantee that other jurisdictions will implement any thresholds prior to imposing a sales tax. The difficulty in assessing what 12,000 or so jurisdictions will do is why this question is best left to Congress.

2. The failure of South Dakota to show, or even litigate, whether its law meets due process concerns counsels against overruling *Quill's* physical-presence rule in this case. As *Quill* made clear, the constraints of the Due Process Clause and the Commerce Clause are different and should be addressed separately. Due process is a bulwark for state sovereignty, and should be considered in tandem with the Commerce Clause requirements, as this Court did in *Quill*. To address the physical-presence aspect of the Commerce Clause in isolation, without also addressing due process, risks undercutting the very fairness that due process protects.

Here, for many small businesses engaged in remote commerce, due process is unlikely to be met due to the lack of a minimum connection resulting from isolated

online sales. In contrast, though ignored by Petitioner, the contacts found sufficient for due process in *Quill* were substantial.

3. Likewise, even if *Quill's* physical-presence rule is abandoned, this Court should not presume South Dakota's law meets the "substantial nexus" test. First, it is not within the question presented. Second, even if not required, the lack of a physical presence should necessitate a greater showing of other contacts for a substantial nexus to be met. On the other side of the ledger, the burden on commerce is likely to be significant. Finally, the isolated, random nature of many online sales means that a sales tax will often not be "fairly related to the services provided by the State," because the tax is out of "proportion" to the activities "within the State." *Commonwealth Edison v. Montana*, 453 U.S. 609, 625-26 (1981).

ARGUMENT

I. Small and Medium Sized Businesses, Especially In States Like Montana That Do Not Have Sales Tax, Depend On *Quill's* Bright Line Physical-Presence Rule.

Stare decisis is critical to fostering respect for this Court's decisions and for "the integrity of our constitutional system of government, both in appearance and in fact." *Vasquez v. Hillery*, 474 U.S. 254, 265 (1986). That is why the Court has described *stare decisis* as "a foundation stone of the rule of law." *Michigan v. Bay Mills Indian Community*, 134 S. Ct. 2024, 2036 (2014). Consequently, there must be some "special justification" for this Court to abrogate its precedent. *Id.* The bar is even higher in this case

because it involves well-settled principles in a delicate balance of economic forces that do not react well to unpredictability. The national economy has developed around the physical-presence rule over the past 51 years, and that rule has served as a workable and predictable bright-line test that has been consistently relied upon.

These reliance interests are most important to, and most relied on by, small and medium-sized businesses, especially those that reside in non-sales tax states where the businesses have no experience collecting sales tax, like Montana. Contrary to South Dakota's assumptions, *see* Pet. Br. at 44-47, tracking and remitting sales tax will impose a significant, and ongoing, burden on small and medium-sized businesses.

No small business, by itself, can keep up with the multitude of tax requirements for 12,000 or so taxing jurisdictions.[2] Instead these businesses must use sophisticated tax software to disentangle the "virtual welter of complicated obligations." *Bellas Hess*, 386 U.S. at 760 (recognizing that "many variations in rates of tax, in allowable exemptions, and in administrative and record-keeping requirements" would have a significantly adverse impact on interstate business); *see* Pet. Br. at 14-15 (discussing software). This software may be provided for free to businesses that choose to

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[2] https://www1.avalara.com/us/en/community/small-business/sales-tax-calculator-smb.html (Software provider Avalara touting sales-tax calculator as a tool to help with determining tax "for over 12,000 jurisdictions in the U.S. alone" and explaining that a "single ZIP code can have multiple sales tax rates").

register with the SST, but many states are not members of the SST, including the six largest states.[3] Even assuming the software is free and usable for all jurisdictions, it is estimated that setup and integration will cost a mid-sized business $80,000 to $290,000, along with a cost of $57,500 to $260,000 each following year for maintenance, updates, and audits.[4] These are significant costs for small and medium-sized businesses and may force these businesses to abandon their online sales, which would undercut the Commerce Clause's goal of a "national market." *C&A Carbone v. Town of Clarkstown*, 511 U.S. 383, 393 (1994). What is more, many of these small and medium-sized businesses are primarily brick-and-mortar stores. They engage in internet sales to make ends meet; in other words to address the challenges to local stores discussed by Petitioner and amici. *See, e.g.*, Br. of Colorado, *et al.* at 9.

South Dakota is correct that internet giants, like Amazon, already track more than enough information, and have sufficiently sophisticated software to easily collect and remit taxes. Pet. Br. at 39, 44 (focusing on "large-scale internet retailers" with a "nationwide scale."). But it is far from true of most businesses that have a more limited internet presence. Small and medium-sized businesses will face significant economic burdens should the physical-presence rule be abandoned. Though Petitioner focuses on what it

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[3] http://www.streamlinedsalestax.org/ (nonmembers include California, Texas, New York, Florida, Illinois, and Pennsylvania).

[4] http://truesimplification.org/wp-content/uploads/Final_TruST-COI-Paper-.pdf.

perceives as an unfair tax advantage, *id.* at 5, the true burden is not the tax, or the price difference, but the difficulty and expense of tracking and collecting the tax in far-flung jurisdictions.

As a recent GAO report confirmed, small to medium-sized businesses often lack the technology and infrastructure to comply with the manifold requirements of thousands of taxing jurisdictions that remote sales tax burdens would entail. United States Government Accountability Office, *SALES TAXES: States Could Gain Revenue from Expanded Authority, but Businesses Are Likely to Experience Compliance Costs* 17-19 (November 2017) ("GAO Report").[5] For many businesses, the significant costs of building and maintaining systems for complicated multi-jurisdictional tax collection, and the risks associated with making mistakes, will simply not be worth continuing to make online sales.

Although South Dakota ignores the GAO report entirely, it argues that they bear the extent of the burden because of lost tax revenue. Pet. Br. at 34-35. It estimates, for example, that in 2012 state and local governments lost "$23 billion in sales-tax revenues" due to *Quill*. *Id.* This estimate appears to be greatly exaggerated. The GAO Report estimated a total loss for 2017 of only $8.5 to $13.4 billion for state and local governments, or about 2 to 4 percent of total 2016 general sales and gross receipts tax revenues. GAO Report at 11-12.

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[5] Available at https://www.gao.gov/assets/690/688437.pdf.

Petitioner's focus on tax revenue also ignores that the burdens of collection will fall on each business, no matter how small and no matter the size of its internet presence. Even assuming each taxing jurisdiction imposes a threshold similar to South Dakota's (and there is no guarantee they will), each retailer with an internet presence will have to track and record all of its sales by taxing jurisdiction from day one, just to determine whether they meet the threshold of a particular jurisdiction in the first place. And from day one each retailer will have to collect tax from each sale in case they ultimately do meet a jurisdiction's threshold. This means that all internet retailers, in all taxing jurisdictions, regardless of size or sales, will have to invest in software and staffing to track sales and tax regulations in all taxing jurisdictions should the physical-presence test be overruled.

This burden, moreover, is prospective only. Though South Dakota dismisses it, Pet. Br. at 48-50, taxing jurisdictions may well apply an opinion overruling *Quill* retroactively. South Dakota enacted its law specifically to challenge *Quill*. SDCL § 10-64-1. As part of the test case, the State declared that it would not seek to collect taxes retroactively. SDCL § 10-64-6. But if this Court abrogates the physical-presence rule, there is no reason to believe other states will do the same. The "general rule" is one "of retrospective effect for the constitutional decisions of this Court." *Harper*, 509 U.S. at 94 (quoting *Robinson v. Neil*, 409 U.S. 505, 507, 35 L. Ed. 2d 29, 93 S. Ct. 876 (1973)). The Court thus resists "selective application of new rules" according to a claim of "actual reliance on an old rule and of harm from a retroactive application of the new rule." *Id.* at 97 (citing *James B. Beam Distilling Co. v.*

Georgia, 501 U.S. 529, 543 (1991)). In fact, one state has already notified businesses of its intent to apply sales tax to prior sales, on the theory that they should have been collecting taxes as a use tax. *See* Connecticut DRS Media Release.[6] As Colorado and other states admit, "certain States" may choose "to apply their laws retroactively" should this Court abrogate the physical-presence rule. Br. of Colorado, *et al*. at 19.

The inability of this Court to dictate whether states will attempt to apply sales taxes retroactively, and the possibility that many taxing jurisdictions may impose low, or no, economic thresholds, are reasons to uphold the physical-presence rule and leave it to Congress to address the issue. It is Congress, acting within the restraints imposed by due process, that is in the best position to balance the burdens of tax collection for remote businesses without a physical-presence with the desire for sales-tax revenue.

Upholding the physical-presence rule would also further this Court's goal of maintaining "bright line standards in the context of tax administration." *Wagnon v. Prairie Band Potawatomi Nation*, 546 U.S. 95, 113-14 (2005) (quoting *Arizona Dep't of Revenue v. Blaze Constr. Co.*, 526 U.S. 32, 37 (1999)); *see also Quill*, 504 U.S. at 315-16 ("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."). For all these reasons, the principles of *stare decisis* strongly favor maintaining the physical-presence rule.

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[6] http://www.ct.gov/drs/cwp/view.asp?Q=591496&A=1436.

II. Due Process Concerns Also Support Retaining *Quill's* Physical-Presence Rule.

Abandoning *Quill*'s physical-presence rule will create another layer of uncertainty because it will trigger a whole new set of questions about what level of activity satisfies the Due Process Clause. South Dakota has only focused on the Commerce Clause, but this Court in *Quill* conscientiously analyzed due process prior to addressing the Commerce Clause. *Quill*, 504 U.S. at 306-08. This is because each clause reflects "different constitutional concerns" and thus the Court considered "each constitutional limit in turn." *Id.* at 305. It is doubtful that South Dakota's threshold of $100,000 or 200 sales meets due process concerns because that threshold lacks any requirement that the seller actually target the State in any regard.

This Court has made clear that for due process to be met, a defendant must "be said to have targeted the forum." *J. McIntyre Mach., Ltd. v. Nicastro*, 564 U.S. 873, 881-82 (2011). "[I]t is not enough that the defendant might have predicted that its goods will reach the forum state." *Id; Quill*, 504 U.S. at 307. (a seller must "purposely avail[] itself of the benefits of an economic market in the forum State" with contacts sufficiently strong that a state's exercise of jurisdiction comports with "traditional notions of fair play and substantial justice.") *Id.* at 307 (quoting *International Shoe v. Washington*, 326 U.S. 310, 316 (1945)). "[R]andom, isolated, or fortuitous" contacts will not suffice. *Keeton v. Hustler Magazine*, 465 U.S. 770, 774 (1984). For that reason, neither the mere formation of a contract, without continuing relationships and obligations, nor "a single sale of a product in a State"

constitutes "an adequate basis" for regulation under due process. *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 478 (1985); *J. McIntyre*, 564 U.S. at 888 (Breyer, J., concurring). And importantly, it is not just the quantity, but also "the nature and quality" of the affiliation that controls. *Burger King*, 471 U.S. at 475 n.18.

Quill determined that due process was met due to Quill's "continuous and widespread *solicitation* of business" in North Dakota, including "almost $1 million" in annual sales (equivalent to $1.79 million in today's dollars) "to about 3,000 customers" in the State, making Quill the sixth largest vendor of office supplies in North Dakota. *Id.*, 504 U.S. at 302, 308 (emphasis added). While the Court in *Quill* overruled previous holdings requiring a physical presence in the forum state under the Due Process Clause, it held that the business must have "purposefully directed its activities" at the forum state to such an extent that it had fair warning that it could be subject to its jurisdiction. *Id.* at 308. Nothing in South Dakota's trigger of $100,000 or 200 sales requires that a Montana business that happens to sell products on the internet do anything whatsoever to target consumers in South Dakota or otherwise purposefully direct its activities toward the State.

The South Dakota threshold may be met, for example, without any solicitation by an internet retailer, other than creating a website. A retailer thus may make 200 sales "for delivery into South Dakota"[7]

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[7] Under South Dakota's law, neither the purchaser nor the recipient need be a South Dakota resident. SDCL § 10-64-2.

by "random, isolated, or fortuitous" contacts. As an example, a person in South Dakota may, after searching for "huckleberry products" online, order a huckleberry lollipop for $1 from The Huckleberry Patch, a small business located in Hungry Horse, Montana.[8] If this process is repeated 200 times (or if a single buyer, or a few, purchases multiple lollipops) the threshold would be met with no solicitation, much less "continuous and widespread solicitation."

South Dakota's trigger goes well beyond *Quill* or anything else this Court has approved as sufficient "purposeful availment" to satisfy due process. And there is no guarantee other states will impose even these low limits before taxing nonresident companies. At the least, more facts are needed prior to a decision from the Court as to whether due process is met. And without sufficient contacts to meet due process, the Commerce Clause analysis is a moot point.

The Due Process Clause, and indeed our constitutional system, ensures that "each State has a sovereignty that is not subject to unlawful intrusion by other States." *J. McIntyre Mach. v. Nicastro*, 564 U.S. 873, 884 (2011). When a state acts outside its territory, it potentially "upset[s] the federal balance" by intruding upon the sovereignty of other states. *Id.* Beyond due process, one of the central purposes of the Privileges and Immunities Clause is to guard against the possibility that states might exploit nonresidents' lack of representation to pass laws that specifically disadvantage them. *See, e.g., Travis v. Yale & Town*,

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[8] https://the-huckleberry-patch.myshopify.com/collections/sweetshop.

22 U.S. 60, 80 (1920). Whether a state may tax a nonresident, then, turns on a "broad inquiry" into "whether the state has given anything for which it can ask return." *MeadWestvaco Corp. v. Ill. Dep't of Revenue*, 553 U.S. 16, 24-25 (2008). To that end, Congress "may authorize state actions that burden interstate commerce," but it "does not similarly have the power to authorize violations of the Due Process Clause." *Quill*, 504 U.S. at 305.

In contrast to *Quill*'s careful analysis of contacts with the state, Petitioner urges this Court to simply assume due process is met and proceed to consider the physical-presence rule absent a factual record. To do so, however, would sacrifice the "traditional notions of fair play and substantial justice" protected by due process.

III. Even If Not A Complete Bar, The Lack Of Physical Presence Should Continue To Be A Factor Under The *Complete Auto* Test.

Petitioner asks this Court to "bless" South Dakota's law and "affirm South Dakota's economic-nexus approach." Pet. Br. at 48, 58. But that is beyond the question presented, which only asks whether *Quill's* physical-presence requirement should be abrogated. As pointed out in detail by Respondents, and several *amici*, there were no facts, or very limited facts, developed below in this strict legal-question case. Indeed, the South Dakota Supreme Court was reviewing the grant of summary judgment for Respondents based on *Quill's* prohibition; a motion in which South Dakota *agreed* its law was unconstitutional under *Quill*. App. 14a to Pet. for Cert. The state Supreme Court merely affirmed this ruling,

recognizing it is required to follow this Court's precedent where directly applicable. *Id.*

If the Court were to reverse course and overrule *Quill*'s physical- presence rule, the question remains as to what level of contact would be sufficient to impose a tax on a nonresident seller. Under *Complete Auto Transit v. Brady*, a tax may only be applied to an activity with "a substantial nexus with the taxing State," and where the tax "is fairly related to the services provided by the State." 430 U.S. 274, 279 (1977). A tax may even have "sufficient factual connections," to meet due process, but fail under the Commerce Clause "because of its burdening effect upon the commerce." *Quill*, 504 U.S. at 305-06 (quoting *International Harvester v. Dep't of Treasury*, 322 U.S. 340, 353 (1944)).

The lack of physical presence should require a heightened amount of other contacts under this test. Because of the *Quill* rule, however, this Court has not had the chance to determine what quantity and quality of contacts are sufficient as to a nonresident seller.[9] The Court should not do so on this bare record, but should remand with suggestions as to what level of contact is sufficient and other factors to consider.

The "burdening effect upon the commerce" of medium and small retailers, especially those in non-sales tax states like Montana, is likely to be significant, as discussed above. *See Raymond Motor Transp. v.*

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[9] This Court has concluded that licensing of software in a state is insufficient to meet the "substantial nexus" requirement. *Quill*, 504 U.S. at 315 n.8.

Rice, 434 U.S. 429, 441 (1978) (inquiry involves "consideration of the weight and nature of the state regulatory concern in light of the extent of the burden imposed on the course of interstate commerce."). These retailers are not equipped to collect tax, are not able to direct who sees their website, and do not have the staffing or funding to keep up with changes in tax law in 12,000 plus jurisdictions. Those factors should be considered before imposing taxing obligations on businesses without a physical presence in the taxing jurisdiction.

Moreover, any tax of a nonresident business must be "fairly related to the services provided by the State." *Complete Auto Transit*, 430 U.S. at 279. Under this additional requirement "the question is whether the State has exerted its power in proper proportion to appellant's activities within the State and to appellant's consequent enjoyment of the opportunities and protections which the State has afforded." *Commonwealth Edison*, 453 U.S. at 625-26.

The "fairly related" prong is clearly met when a business has an on-the-ground presence in a state. *Id.* at 626 (noting "little difficulty concluding that the Montana tax satisfies" this prong where the "operating incidence" of the tax is mining coal in Montana). But the "operating incidence" of one sale over the internet, or even 200, does not meet this threshold, especially where the nonresident retailer does not target the taxing state. What, or where, the "operating incidence" would be with an online sale is also unclear. Where is it, for example, if an online sale is completed on a website hosted on a server in state A, by a customer residing in state B but logged on in state C, for delivery

to an address in state D? It is patently unfair to require the retailer to determine where the taxing nexus lies on pain of a tax penalty with interest for a wrong decision.

In short, even if this Court were to overrule *Quill*, it should remand the case for full consideration of the substantial questions that remain and are unresolved by the bare factual record in this case.

CONCLUSION

This Court should affirm the South Dakota Supreme Court's decision.

Respectfully submitted,

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