Dear Client:

On June 21, 2018, the U.S. Supreme Court issued its opinion in *South Dakota v. Wayfair*, a landmark sales and use tax nexus case that will have implications for many online sellers and multistate businesses. The Court ruled, in a 5-4 decision, that a state can require an out-of-state seller to collect sales or use tax on sales to customers in that state, even though the seller lacks an in-state physical presence. Under certain circumstances, an economic or virtual presence can create nexus (a sufficient connection with the state), subjecting a seller to tax collection and remittance requirements in a state. In some cases, a company's electronic apps or website tracking "cookies" may be considered a nexus-creating presence in a state.

Background

In *Wayfair*, the U.S. Supreme Court considered the constitutionality of a South Dakota law (S.D. Codified Laws § 10-64-1, et al.) that requires certain remote sellers to register for, collect, and remit South Dakota sales tax. Under the law, a remote seller has sales tax nexus with South Dakota if the seller, in the current or previous calendar year:

- had gross revenue from sales of taxable goods and services delivered into the state exceeding $100,000; or
- sold taxable goods and services for delivery into the state in 200 or more separate transactions.[1]

The Commerce Clause of the U.S. Constitution requires that a seller have "substantial nexus" with a state before the state can require the seller to collect and remit sales and use taxes. Historically, under a precedent affirmed in the 1992 case of *Quill Corp. v. North Dakota*, this nexus depended on whether the seller had a physical presence in the state. The presence could be through the company's activities or property, or through the activities of its agents in the state. Over time, states have stretched the boundary of this standard by asserting "click through" nexus and affiliate nexus. Now "economic" nexus policies, like the South Dakota law in *Wayfair*, stretch it further still, with states asserting jurisdiction to impose sales tax collection responsibilities on companies that meet certain sales thresholds. In some states, the use of a company's apps or website tracking "cookies" by in-state customers may create nexus.

Considerations for Sellers

Sales and Use Tax Obligations

The *Wayfair* decision affects companies doing business in thousands of state and local tax-collecting jurisdictions across the country. The most immediate impact will be on sellers with a significant virtual or economic presence in a state that asserts economic nexus. Sellers delivering taxable products or services into South Dakota (and other economic nexus states) will need to determine if they surpassed

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[1] S.D. Codified Laws § 10-64-2.

the dollar amount or transaction volume thresholds for establishing nexus with the state. Sellers will need to do this analysis for each state that has adopted an economic nexus threshold policy, including determining whether each product sold is taxable or nontaxable. Some of these economic nexus policies may be vulnerable to attack under the Court's analysis in *Wayfair*, and companies may wish to consult with tax advisors who can help them make the decision whether to comply with or challenge the rules.

In addition, some states are beginning to enact laws targeting so-called "marketplace facilitators" and requiring that they collect tax on sales made by third-party sellers on the facilitator's platform if the gross receipts from those transactions exceeds an annual threshold and other conditions are met.

Sellers should be prepared for states to adopt and aggressively enforce expanded nexus provisions, although future legal challenges or Congressional action could limit the scope of the Court's decision.

Notice and Reporting Requirements

A growing number of states, led by Colorado, recently enacted complex use tax notice and reporting requirements for remote sellers. Under these laws, remote sellers must provide information to customers about potential use tax liability and report transaction data to the state. Noncompliance can result in stiff per-occurrence penalties. A few states, such as Pennsylvania, explicitly provide an election between the notice and reporting regime and voluntary sales tax registration.

Other Considerations

Expanded sales tax nexus may have far-reaching effects for businesses, beyond collection and remittance of the sales tax itself.

In the realm of business acquisitions, state "successor liability" laws typically impose notice, withholding, and tax clearance requirements that limit the purchaser's liability for unpaid sales tax liabilities of the seller in certain business asset acquisitions. As states begin to more aggressively assert sales tax nexus, companies contemplating business acquisitions should consult with a tax professional for assistance in navigating complex successor liability laws.

Companies should also consider potential financial statement impacts related to sales tax nexus issues.

Next Steps

We expect state revenue departments to issue guidance regarding the *South Dakota v. Wayfair* decision in the coming weeks and months, and we will be following those developments closely. In the meantime, if you would like to discuss how the decision may impact your business, please do not hesitate to contact me at the number or email below.

Sincerely,