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 Petition for a Writ of Certiorari to the Supreme Court of South Dakota

BRIEF OF NETCHOICE AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENT

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QUESTION PRESENTED

Whether the Supreme Court should abrogate *Quill v. North Dakota's* sales-tax-only, physical presence requirement.

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INTEREST OF *AMICUS CURIAE*[1]

NetChoice is a trade association of leading e-commerce and online businesses promoting the value, convenience, and choice of the internet. NetChoice has been deeply engaged on internet sales and use tax issues for over a decade and is a founding member of the coalition for True Simplification of Taxation ("TruST"), a group whose association members include the American Catalog Mailers Association, the Direct Marketing Association, and the Electronic Retailing Association. NetChoice's core members are industry leaders in the online commerce economy.

NetChoice strongly believes that this Court should decline the State of South Dakota's petition for a writ of certiorari. NetChoice has an interest in this case because its members, e-commerce businesses both large and small, will be adversely affected if the physical presence standard set forth in *Quill. v. North Dakota*, 504 U.S. 298 (1992), is eliminated. The *Quill* standard, by preventing individual states from impeding commerce among the states, protects citizens of one state from regulation by foreign states.

In the years since *Quill* was decided, technology has improved retail commerce for the customer in many ways. But for the many small businesses whose customers reach them over the internet, the burden of compliance posed by divergent rules and regulations among 46 states and thousands of local jurisdictions

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[1] Pursuant to this Court's Rule 37.6, *amicus* states that this brief was not authored in whole or in part by counsel for any party, and that no person or entity other than *amicus*, its members, or its counsel made a monetary contribution intended to fund the preparation or submission of this brief. The parties have consented to the filing of this brief and were timely notified.

remains the same. There are still over twelve-thousand sales tax jurisdictions in the U.S.[2] *Quill's physical presence* standard wisely holds that forcing a small business located in one U.S. state to comply with the patchwork of rates and rules across these many jurisdictions, simply because they use the instrumentalities of interstate commerce, would amount to an unreasonable burden. Like all retailers, online merchants collect sales tax in every state where they are physically present. But abandoning *Quill's* standard of directly linking compliance with state and local sales tax collection regulations to the physical presence of retailers would create conditions ripe for abuse. States could use the unequal burden thus imposed on remote commerce to protect local retailers from out-of-state competition. Yet the out-of-state competitors neither benefit from in-state facilities nor impose burdens on local infrastructure.

Quill's physical presence standard has served to protect all businesses that maintain websites from overbearing tax compliance burdens imposed by foreign states where the business has no physical presence. At the same time, *Quill* requires every business, large or small, to collect and report sales tax in the same way in every state where the business does benefit from in-state facilities and does impose burdens on local infrastructure.

NetChoice members comply with the same regulatory demands as so-called brick-and-mortar merchants by paying applicable taxes and complying with regulations in the states they reside in. Abrogating *Quill* would open the door for multiple foreign states

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[2] *See* Avalara, Avalara Resource Center Sales Tax, *available at* https://www.avalara.com/learn/sales-tax/.

simultaneously to regulate an out-of-state merchant. This disproportionate regulatory burden, particularly on small business, will inherently discriminate in favor of in-state commerce.

For these reasons, NetChoice has a vital interest in whether the Court grants South Dakota's petition.

ARGUMENT

I. THE INTERNET SALES TAX DEBATE IS AN ISSUE OF VITAL IMPORTANCE TO MILLIONS OF AMERICANS AND SMALL BUSINESSES.

The internet sales tax debate is extremely important not only to NetChoice's membership, but also to millions of Americans who rely on the services provided by small businesses across the country. NetChoice is a trade association of businesses and trade associations who seek to promote convenience, choice, and commerce on the internet. Its members include many small providers of e-commerce goods and services, as well as online platforms that bring together buyers and small sellers from around the globe. We know from experience that internet commerce can expand the range of goods sold safely and legally in secondary markets, including when the internet enables these markets to reach across national borders.

The issue of sales and use tax collection on internet commerce impacts *every* small business with an online storefront, marketplace, or sales. That is because, were these small businesses required to comply not only with all of the government regulations where they are located, but also with the regulations of every distant state and its governmental subdivisions in

which it has a customer, many would irrevocably suffer.

The due process standard of purposefully availing oneself of the benefits of doing business in a particular jurisdiction should not be eviscerated for the internet era. Any business making use of a website is accessible by nearly all Americans and billions of citizens of foreign countries. This is not something a small business can opt out of. Imposing discriminatory regulatory burdens on a business simply because it takes web orders violates due process and inherently discriminates against interstate commerce.

The *Quill* standard allows internet start-ups, as well as small and medium-sized online and brick-and-mortar businesses, to exist. It protects them from regulatory burdens that would be both crippling and unfair, and allows them to grow. It provides them with consistency in understanding the tax regulatory framework they must follow.

As the Court noted in *Quill*, "the *Bellas Hess* rule has engendered substantial reliance and has become part of the basic framework of a sizeable industry."[3] That is even more true today because of the passage of time. E-commerce companies, particularly smaller and medium-sized retailers, rely on *Quill* today amid a tax and regulatory environment that has never been more complicated. At the same time, the *Quill* standard ensures that as online sellers expand their businesses and create physical presence in additional states, they accordingly submit to a broader scope of sales tax collection and regulatory burdens. Today, Amazon – not only the largest internet retailer but the ninth largest retailer of any kind in the United

[3] *Quill,* 504 U.S. at 317.

States – accounts for nearly half of all internet retail sales. It already collects sales tax in every U.S. jurisdiction that has such a tax. Wal-Mart, the nation's largest retailer, is the second-fastest growing retailer on the internet. *Quill's physical presence standard* ensures that all of this retail activity is already fully taxed in those states with sales and use taxes.

It is fundamentally at odds with a fair and efficient national marketplace to subject a local retailer, with only one place of business in a single state, to state tax compliance burdens – including the requirement to appear in person to defend a lawsuit brought by tax regulators – in each of the 46 states that have sales taxes. This is especially so if the only reason for the imposition of this enormous burden is the local retailer with only one place of business, engages in commerce via the internet.

A website, even one constructed in an hour by a small business using inexpensive online tools, immediately advertises that small business to the entire world. If a Vermont-based small business, for instance a bookseller, receives an order from a customer in a foreign state, fulfilling the order should not subject it to direct regulation and taxation by that foreign state. The wisdom of this is seen most easily if the customer placing the order is in a far-away country. Selling through a website should not automatically subject every small business to the regulation, taxation, and judicial reach of every foreign jurisdiction.

Because it is virtually impossible for the bookseller in Vermont to have a website that is accessible everywhere *except* a specific jurisdiction – say, South Dakota – it is specious to argue that the bookseller has purposefully availed itself of South Dakota's unique benefits in the way that concept has been developed in

this Court's prior cases. The owner of that small business in Vermont should not be required to refuse all sales via the internet from South Dakota. Likewise, the owner should not be automatically required to comply with complex sales or use tax requirements in a distant state just because it fulfills orders taken via the internet. If South Dakota audits the business or challenges its tax and regulatory filings, the owner should not be compelled to travel to South Dakota to defend herself in judicial and administrative proceedings.

This degree of burden and complexity rises to the level of fundamental unfairness, implicating not only the commerce clause but due process. The Supreme Court in *Quill* effectively has answered these questions correctly.

Bellas Hess created a bright line rule protecting merchants "whose only connection with customers in the [taxing] State is by common carrier or the United States mail."[4] From the standpoint of the interstate commerce clause, there is little meaningful distinction between a merchant who fulfills orders using the mail, telephone, telegraph, or internet. Such merchants are, according to *Quill*, properly "free from state imposed duties to collect sales and use taxes."[5] If this Court were to overrule *Quill*, tens of thousands of small businesses and tens of millions of customers who rely upon their staying in business will be adversely affected.

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[4] *National Bellas Hess v. Department of Revenue*, 386 U.S. 753, 758 (1967).

[5] *Quill,* 504 U.S. at 315.

II. IT IS AN UNDUE BURDEN FOR RETAILERS TO COMPLY WITH STATE SALES TAX AND USE REQUIREMENTS IN STATES WHERE THEY DO NOT HAVE A PHYSICAL PRESENCE.

A. South Dakota Has No Factual Record Upon Which to Base an Argument for Overturning Quill.

South Dakota has flouted Supreme Court precedent and urged the Court to reward it by ruling in a case that is fact free, by design. Petitioners present no facts regarding the burden (or lack thereof) of multistate sales and use tax collection on interstate commerce. The procedural origins of this case – a contrived and willful challenge to existing Supreme Court precedent by the state – has guaranteed that no evidentiary record exists. What's more, the case presents the legal construct of South Dakota's circumstances when a ruling by this Court would invariably apply to all 50 states. While petitioners freely make unproven assertions about how easy and inexpensive compliance with the rules of thousands of taxing jurisdictions will be, NetChoice's experience reveals a far different understanding of the continuing burdens of nationwide sales tax compliance.

South Dakota's "legal argument" consists largely of its own opinion, without factual evidence to support, that changes in computer technology, streamlined sales and use tax laws, and the evolution of the retail industry have made *Quill* obsolete. To the contrary, it is the experience of NetChoice members that states have neither simplified nor harmonized their sales and use tax rules; that the technology costs of complying with every state's often unique rules will be significant, and potentially fatal for small businesses;

and that the evolution of the retail industry, particularly among the largest participants, is to a model of brick-and-click, validating the wisdom of the *Quill* holding.

There is ample reason to reject petitioner's claims about the simplicity of compliance at face value. During a recent U.S. Senate hearing, a witness whose testimony was supposed to demonstrate the ease of online tax-collection was shown to be charging sales tax at the wrong rate and for the wrong tax jurisdiction.[6]

Quill's test and reasoning have well stood the test of time, and in particular it has well anticipated changes in technology. The reason is that *Quill* addressed a question that remains today: whether requiring far-away vendors to comply with the sales tax collection regimes and rules of every state's different framework has a burdensome effect on interstate commerce.

When *Quill* was decided, there were only 6,000 tax jurisdictions. On this record, the *Quill* Court found that subjecting out-of-state sellers to foreign tax collec-

[6] During a U.S. Senate Commerce Committee hearing on the Marketplace Fairness Act, witness Steven Bercu, CEO and Co-owner, BookPeople, Austin, TX, claimed it was easy to collect and remit sales taxes for out-of-state sales. He was shown to be incorrectly collecting sales taxes on purchases, including over-collecting the tax for some sales. U.S. Senate Committee on Commerce, Science & Transportation, *Marketplace Fairness: Leveling the Playing Field for Small Business* (Aug. 1, 2012).

tion and reporting requirements was unduly burdensome.[7] Today that number has ballooned to over 12,000.[8]

Quill protects local businesses from overbearing tax compliance burdens that include "many variations in rates of tax, in allowable exemptions, and in administrative and record-keeping requirements . . . a virtual welter of complicated obligations."[9] Such burdens on interstate commerce cannot be imposed without offense to the Commerce Clause, and to Congress' plenary authority to regulate in this area. As discussed fully below, Congress is currently working on alternative legislative approaches, some of which would tolerate increase and some of which would mitigate the burdens of foreign taxation and regulation upon merchants engaged in interstate commerce. For the Supreme Court now to obviate this legislative process in mid-stride, while making its decision upon a record lacking the evidence adduced in the many congressional hearings and debates on which currently contemplated legislation is based, would upend much so-called "dormant" Commerce Clause jurisprudence. Ironically, it would do so in order to upend Supreme Court precedent.

Entangling small businesses in a complicated framework of varying taxes, exemptions, administrative requirements, and audits would be unwise in all events. It is utterly unsupportable in a case lacking any developed factual record.

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[7] *Quill* 504 U.S. at 313.

[8] *See* Avalara, Avalara Resource Center Sales Tax, *available at* https://www.avalara.com/learn/sales-tax/.

[9] *Quill,* 504 U.S. at 313 n.6.

B. The 'Evolution of the Retail Industry' Has Not Mitigated the Inherent Burdens of Compliance with Multiple Foreign-State Tax and Regulatory Regimes.

Petitioner asserts without proof its opinion that changes in the volume and nature of e-commerce make *Quill* obsolete. This is at odds with the real-world experience of internet businesses.

There are over 12,000 tax jurisdictions in the United States, double the number of tax jurisdictions deemed unduly burdensome in *Quill*.[10] Software has made filing of taxes easier, and software license fees are a small part of the overall costs of compliance, but other costs necessitated by compliance with sales tax payment and reporting obligation in these thousands of state and local jurisdictions have risen. Overall compliance costs remain unduly burdensome on local merchants and on interstate commerce.

These costs include paying computer consultants to integrate new tax software into their existing systems for point-of-sale, web shopping cart, fulfillment, and accounting. Use of new tax software, in turn, requires training for customer support and back-office staff. Also excluded from South Dakota's appraisal of the actual cost burdens is the time and money spent answering customer questions about taxability of items. Businesses will be required to know, for example, the many different sales tax holidays in various remote jurisdictions. Every single business, large or small, will face audit questions from 46 states if *Quill* is

[10] *Id.* at 313.

overturned. Businesses will have to pay accountants and computer consultants to address all these issues.

As discussed more fully below, the Streamlined Sales Tax Project ("SSTP") was supposed to organize a uniform simplification of the many different tax rules, definitions, rates, and regulations across the country. It has not done so. Indeed, its own Cost of Collection study[11]—which has since been shown to grossly underestimate the costs[12]—found that the smallest businesses spend 17 cents in compliance for every tax dollar they collect for states. That is vastly more than their large-scale competitors.

Even if "free" tax software worked as advertised, that would help eliminate only two cents of the extra 17 cents in costs.[13] A small business with annual revenues of $1 million would still incur a new cost burden equal to 15 cents on every dollar it collects, for tasks such as:

- Computer consultants to integrate new tax software into their home-grown or customized systems for point-of-sale, web shopping cart, fulfillment, and accounting
- Training customer support and back-office staff

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[11] Pricewatershousecoopers, *Retail Sales Tax Compliance Costs: A National Estimate* (Apr. 6, 2006) *available at* http://www.netchoice.org/wp-content/uploads/cost-of-collection-study-sstp.pdf.

[12] *See* Larry Kavanagh and Al Bessin, *The Real-World Challenges in Collecting Multi-State Sales Tax*, September 2013, *available at* http://truesimplification.org/wp-content/uploads/Final_ TruST-COI-Paper-.pdf.

[13] Pricewatershousecoopers at E-4.

- Answering customer questions about entity and use exemptions and sales tax holidays
- Responding to audit demands from 46 states – plus potentially from up to 550 Indian Tribes
- Accountants and IT consultants to help with all of the above

These collection burdens will impose impossibly high costs on small catalog and online businesses.

The most significant of these costs is the expense of integrating tax rate lookup software into the business's in-house information systems. The cost is high not only because the software integration requires specialized skills, but also because it must be done at multiple integration points. In 2013, the True Simplification of Taxation (TruST) coalition commissioned a study to precisely measure both the upfront and ongoing software integration costs.[14] The study examined both catalog and online retailers in the mid-market bracket ($5 million to $50 million in annual sales). The study found that such mid-market online and catalog retailers would have to spend $80,000 to $290,000 in setup and integration costs in order to use the sales tax software discussed by petitioners.

Beyond the average $185,000 initial cost, *every year* these retailers would also have to spend between $57,500 and $260,000 on maintenance, updates,

[14] Larry Kavanagh and Al Bessin, *The Real-World Challenges in Collecting Multi-State Sales Tax*, September 2013, *available at* http://truesimplification.org/wp-content/uploads/Final_TruST-COI-Paper-.pdf.

audits, and service fees charged by tax software providers.

Most mid-market retailers have modified third-party order management and fulfillment software to fit their business processes, or have developed their own software. They use these order management systems for call center order entry, customer service, returns and refund processing, shipping, inventory management, and more. In many cases, these systems also integrate with separate accounting systems. In order to integrate with a CSP [Certified Software Provider], the retailer must make architectural modifications to map to the coding system of the CSP, establish real-time communication, and create error-handling code to process transactions when the real-time service fails to return a valid reply.

South Dakota's claim that the changing e-commerce landscape has made *Quill* obsolete fails to account for any of these factors. In reality, requiring taxation across all 12,000 United States state and local tax jurisdictions would today impose far greater burdens than Quill found unacceptably burdensome, and it would do so for *any* business that fills web orders. The burdens of compliance with multiple foreign-state tax and regulatory regimes inherently hinder interstate commerce.

C. South Dakota and Other States Have Not Sufficiently Simplified Tax Collection and Will Impose Undue Burdens on Collecting Businesses.

Petitioner's claim that nationwide, sales tax regimes have been simplified is unsubstantiated and, therefore, provides no basis for overturning *Quill*.

NetChoice has long been a supporter of the effort to streamline and simplify state sales taxes. But despite a decade of attempting to simplify tax codes, the actual simplifications achieved are few and far between. Unfortunately, for the SSTP, simplification has become just a slogan—not a standard. Across the country, states have not meaningfully simplified their tax systems, including through the SSTP – which has failed to come close to its stated objective.

Instead of simplifying taxes through the SSTP, we have witnessed the abandoning of most of the SSTP's original simplification requirements. For example, the SSTP originally promised one tax rate per state, uniform definitions, and a single audit on behalf of all states. Too many states were unwilling to undertake even these fundamental simplifications, and the simplifications were abandoned. The SSTP also abandoned its original aim to require states to compensate retailers for the cost of tax compliance. SSTP has no small seller exception. In an effort to attract states with origin sourcing, the SSTP abandoned a single sourcing rule, and now allows states to use *origin* sourcing for in-state shipments but requires *destination* sourcing for interstate sales. To entice Massachusetts to join SSTP, the Governing Board allowed thresholds for certain clothing items, even though thresholds were one of the extreme complexities that SSTP founders pledged to eliminate.

Perhaps the most glaring sign of failure is that despite the SSTP's many concessions to allow states to retain their complex systems, less than half of eligible states have become members of the SSTP. The Supreme Court should not overturn *Quill* on the basis of the negligible simplifications actually accomplished by the SSTP.

III. WHETHER TO REQUIRE TAX COLLECTION BY OUT-OF-STATE RETAILERS IS AN ISSUE OF INTERSTATE COMMERCE AND THEREFORE THE CONSTITUTIONAL RESPONSIBILITY OF CONGRESS.

A. Congress Has the Exclusive Authority to Regulate Interstate Commerce Under Article I.

This case presents an effort to leapfrog congressional action by purposefully violating clear Supreme Court precedent. Such a deliberate affront should not be rewarded. "After all, the Commerce Clause is found in Article I of the Constitution and it grants Congress the authority to adopt laws regulating interstate commerce."[15]

Quill observed that "the underlying issue is not only one that Congress may be better qualified to resolve, but also one that Congress has the ultimate power to resolve. No matter how we evaluate the burdens that use taxes impose on interstate commerce, Congress remains free to disagree with our conclusions." *Quill*, 504 U.S. at 318.

B. Congress Is Responsibly Exercising Its Legislative Powers with Respect to Internet Taxation.

Congress is currently deeply engaged in legislative debate, fact finding, hearings, and committee consideration of the issues raised by State efforts to require

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[15] *Direct Mktg. Ass'n v. Brohl*, 814 F.3d 1129, 1147–48 (10th Cir.), *cert. denied*, 137 S. Ct. 591, 196 L. Ed. 2d 473 (2016) (Gorsuch, J., concurring), and *cert. denied*, 137 S. Ct. 593, 196 L. Ed. 2d 473 (2016).

tax and regulatory compliance work by out-of-state online merchants. There is robust discussion and debate on a range of potential legislative approaches. While Congress has not yet acted in the way that petitioners desire, this hardly dispenses with the dormant Commerce Clause issue raised by petitioners' desire to overturn *Quill*. Indeed, Congress' power at the moment is anything but dormant. That Congress was engaged in the very process designed by the Founders to foster a deliberative and thoughtful approach to legislation[16] is an argument in favor of, not against, respecting Congress' authority in this area.

Contrary to petitioner's and some *amici*'s claim, Congress has demonstrated an abiding interest in legislating on this issue and has uninterruptedly sought ways to address it in recent years. In the past two years alone, Congress has considered, including through hearings, the following legislation: the Marketplace Fairness Act (MFA),[17] the Remote Transactions Parity Act (RTPA),[18] the No Regulation without Representation Act of 2017,[19] and the Online Sales

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[16] Newbold, Stephanie P., and David H. Rosenbloom. *Critical Reflections on Hamiltonian Perspectives on Rule-Making and Legislative Proposal Initiatives by the Chief Executive*, p. 1049-1056, Public Administration Review 67.6 (2007).

[17] Marketplace Fairness Act of 2015 (2015) S. 698, Marketplace Fairness Act of 2017 (2017) S. S.976.

[18] Remote Transactions Parity Act of 2015 (2015) H.R.2775, Remote Transactions Parity Act of 2017(2017) H.R.2193.

[19] No Regulation Without Representation Act of 2017 (2017) H.R. 2887.

Simplification Act (OSSA).[20] These proposals represent a range of approaches that seek to balance competing interests in differing ways. Resolving such differences based on policy inputs is exactly what legislatures are best at, and exactly what courts – charged with resolving cases and controversies – are least well equipped to handle. That the Constitution assigns the regulation of interstate commerce to Congress of course provides the ultimate reason for this Court to defer to the legislative branch, should any additional reason be required.

Further undermining petitioner's claim that Congress is not exercising its powers in the area of internet taxation is the fact that Congress recently enacted, and President Obama signed, the Permanent Internet Tax Freedom Act (PITFA).[21] This law makes permanent a federal ban on taxation of email, internet access, and other forms of internet-specific exactions, broadly prohibiting all multiple or discriminatory taxes on e-commerce. This legislation established an end date of June 30, 2020, for South Dakota's tax on internet access. It would seem not that Congress is abdicating legislating in the area of internet tax, but rather that petitioner does not like the policy choices that Congress is making.

Should this Court grant certiorari and overturn *Quill,* it would eliminate any incentive for States to

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[20] The Online Sales and Simplification Act of 2016 (2016), *available at* http://images.internetretailer.com/IR/2016/082516_DraftLanguage.pdf.

[21] Trade Facilitation and Trade Enforcement Act of 2015 (2015), H.R.644.

simplify their tax systems. It would cut off the opportunity for any national legislative solution from Congress. It would subject small businesses across the country to burdens of compliance with the reporting and collection regimes of thousands of state and local jurisdictions. It would undercut the stable and proven legal framework upon which the entire small business retail community has heretofore relied.

Justices have often warned about the Supreme Court usurping the role of Congress by legislating from the bench. As Justice Kennedy has eloquently noted, "Any society that relies on nine unelected judges to resolve the most serious issues of the day is not a functioning democracy."[22] This is not how things are supposed to work in our legal order, where, as Justice Gorsuch observed, "judges distinguish themselves from politicians by the oath they take to apply the law as it is, not to reshape the law as they wish it to be."[23]

We respectfully ask that the Supreme Court heed this wisdom, especially on an issue that directly implicates State usurpation of congressional authority over interstate commerce. The Court's established precedents recognize that Congress is the proper arbiter of this issue.

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[22] Brian Resnick, Anthony Kennedy: *The U.S. 'Is Not a Functioning Democracy'*, The Atlantic (Oct. 4, 2013).

[23] *Direct Mktg. Ass'n*, 814 F.3d at 1147–48.

CONCLUSION

The petition should be denied.

Respectfully submitted,

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