IN THE SUPREME COURT
STATE OF SOUTH DAKOTA

No. 28160

STATE OF SOUTH DAKOTA,

Plaintiff and Appellant,

v.

WAYFAIR INC.,
OVERSTOCK.COM. INC., and
NEWEGG INC.

Defendants and Appellees.

APPEAL FROM THE CIRCUIT COURT
SIXTH JUDICIAL CIRCUIT
HUGHES COUNTY, SOUTH DAKOTA

THE HONORABLE MARK W. BARNETT
Circuit Court Judge

APPELLANT'S BRIEF

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Notice of Appeal filed March 8, 2017

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PRELIMINARY STATEMENT

Throughout this brief, Defendants and Appellees, Wayfair Inc., Overstock.Com. Inc., and Newegg Inc., will be referred to as "Defendants." Plaintiff and Appellant, State of South Dakota, will be referred to as "State." Senate Bill 106, 91st Session, South Dakota Legislature, 2016, "An Act to Provide for the Collection of Sales Taxes from Certain Remote Sellers," codified at SDCL chapter 10-64, will be referred to as "the Act." General references to the South Dakota Legislature will be shortened to "the Legislature." The settled record in the underlying civil case, *State of South Dakota v. Wayfair Inc., Overstock.Com. Inc., and Newegg Inc.,* Hughes County Civil File No. 16-0092, will be referred to as "SR," followed by the appropriate page number(s). References to materials in the appendix to this brief will be signified by "App." followed by the appropriate page number(s).

JURISDICTIONAL STATEMENT

The Honorable Mark W. Barnett issued an Order Granting Defendants' Motion for Summary Judgment on March 6, 2017. SR 390-92. Defendants filed the Notice of Entry of Order Granting Defendants' Motion for Summary Judgment on March 7, 2017. SR 393-94. The State filed its Notice of Appeal on March 8, 2017. SR 398-99. This Court has jurisdiction over this matter pursuant to the Act, App. 15 (§ 4), and SDCL § 15-26A-3.

STATEMENT OF THE ISSUES AND AUTHORITIES

I

WHETHER *QUILL CORP. V. NORTH DAKOTA*, 504 U.S. 298, 112 S.CT. 1904 (1992) PROHIBITS SOUTH DAKOTA FROM IMPOSING AN OTHERWISE VALID SALES TAX COLLECTION ON RETAILERS WHO LACK A "PHYSICAL PRESENCE" WITHIN THE STATE.

The lower court found that Defendants lack a physical presence in South Dakota and therefore, the State is "prohibited from imposing sales tax collection and remittance obligations on the Defendants" citing to *Quill*. SR 391 ¶¶ 3-4.

Quill Corp. v. North Dakota, 504 U.S. 298, 112 S.Ct. 1904 (1992)

Nat'l Bellas Hess Inc. v. Dept. of Rev. of Ill., 386 U.S. 753, 87 S.Ct. 1389 (1967)

II

WHETHER THE SUPREME COURT OF THE UNITED STATES SHOULD RECONSIDER ITS DECISION IN *QUILL CORP. V. NORTH DAKOTA*, 504 U.S. 298, 112 S.CT. 1904 (1992).

The lower court did not directly address this issue, but stated it was "duty bound to follow applicable precedent of the United States Supreme Court […] even when changing times and events clearly suggest a different outcome" and concluded "it is simply not the role of

a state circuit court to disregard a ruling from the United States Supreme Court." SR 391-92, ¶ 5.

Direct Marketing Ass'n v. Brohl, 135 S.Ct. 1124 (2015)

Comptroller of Treasury of Maryland v. Wynne, 135 S.Ct. 1787 (2015)

Direct Marketing Ass'n v. Brohl, 814 F.3d 1129 (10th Cir. 2016)

Complete Auto Transit v. Brady, 430 U.S. 2174, 97 S.Ct. 1076 (1997)

STATEMENT OF THE CASE

This is an unusual case about an unusual statute. In 2016, responding to an invitation from U.S. Supreme Court Justice Anthony Kennedy, the Legislature passed the Act, which requires out-of-state retailers who 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) to collect and remit the state sales tax. SR 23-28; App. 14 (§ 1). In so doing, it recognized that this effort was contrary to the decision of the Supreme Court of the United States in *Quill Corp. v. North Dakota*, 504 U.S. 298, 112 S.Ct. 1904 (1992), the case Justice Kennedy thought the U.S. Supreme Court should reconsider. *See Direct Marketing Ass'n v. Brohl*, 135 S.Ct. 1124, 1134-35 (2015) (hereinafter "DMA")(Kennedy, J. concurring). The Act included an emergency clause allowing the legislation to go into effect early. SR 27; App. 18 (§ 9). The Legislature also provided that judicial proceedings should move "as expeditiously as possible." SR 23; App. 14-15 (§ 2).

On April 28, 2016, the State filed a complaint alleging that Defendants and an additional company called Systemax, Inc., met the provisions of the Act but had failed to register to collect state sales tax. SR 1-20. The State's complaint sought a declaratory judgment that Defendants were validly required to collect and remit sales tax under the Act. SR 1-20. On May 5, 2016, the day after being served, Systemax voluntarily registered for and received a sales tax license and began calculating and collecting sales tax on all sales for delivery within South Dakota. SR 91, 94. The State then dismissed Systemax from this litigation. SR 94-96.

On May 25, 2016, Defendants submitted a Notice of Filing of Notice of Removal intending to remove the matter to the federal court, rather than filing an answer with the lower court. SR 97-99. On January 19, 2017, the Honorable Roberto A. Lange's January 17, 2017 Order and Opinion Granting Plaintiff's Motion to Remand to State Court was filed, returning this matter to the circuit court after finding the federal district court lacked jurisdiction. SR 247-67. Following the remand order, Defendants then filed a joint answer on February 21, 2017. SR 287-300.

On February 21, 2017, the parties filed a Parties' Joint Statement Regarding Proceedings Following Remand, in which the parties agreed to rely on the summary judgment briefing previously submitted to the federal court. SR 301-3. The parties also agreed that summary judgment in Defendants' favor was appropriate in light of *Quill*: There was no dispute that Defendants met the thresholds in the Act, but lacked the physical presence required by

Quill's sales-tax-specific exception to the dormant commerce clause's ordinary test. SR 301-3; *see also* SR 390; App. 1-3. The parties further agreed to simply re-caption and file with the circuit court all "respective pleadings concerning the Defendants' Motion for Summary Judgment." SR 304. Defendants' then filed their motion for summary judgment, statement of material facts, and brief in support of motion on February 22, 2017. SR 333-34, 335-38, 339-65. In turn, on February 23, 2017, the State filed the response to Defendants' motion for summary judgment and response to Defendants' statement of material facts. SR 366-82, 383-86. The Defendants filed their reply brief on February 24, 2017. SR 387-89.

The trial court issued the Order Granting Defendants' Motion for Summary Judgment on March 6, 2017, recognizing that it was bound by U.S. Supreme Court precedent "even when changing times and events clearly suggest a different outcome." SR 391-92; App. 2-3. The circuit court's order noted that the State had been (and remained) enjoined from imposing the requirements of the Act since the initiation of this suit. SR 392; App. 3. Recognizing that the Legislature had directed the circuit court to act "as expeditiously as possible," the court filed its order in a matter of days after the parties submitted their briefing. SR 391; App. 2 (quoting SDCL § 10-64-3).

STATEMENT OF THE FACTS

Through the Act, the Legislature required out-of-state sellers to collect the state sales tax as though they had a physical presence in South Dakota,

but only if they transact a specified volume of business with South Dakota citizens by delivering goods or services to them in the State. SR 10, ¶ 29; App. 14 (§ 1). The Act itself recognizes that applying this rule to out-of-state retailers is in tension with existing decisions of the U.S. Supreme Court, and would likely require at least partial abrogation of the holdings in *National Bellas Hess, Inc. v. Dept. of Rev. of Ill.*, 386 U.S. 753, 875, S.Ct. 1389 (1967), and *Quill*. These cases held, respectively, that catalog mailers lacking physical presence within a state could not be required to collect the state sales tax under the dormant commerce clause (*Bellas Hess*) and, later, that while this rule might well be incorrect, and no longer had any basis in doctrines of due process, it would still be retained as a matter of stare decisis (*Quill*). Echoing that recognition, the State has consistently taken the position in this case that it cannot prevail absent at least partial abrogation of the U.S. Supreme Court's decision in *Quill*. *See* SR 390.

Quill was decided in 1992, shortly before the Internet revolution that reshaped the face of consumer retail and the way that "remote" sellers interact with their customers. Indeed, in 1992, Amazon.com was not yet a place to buy books. Kayla Webley, *A Brief History of Online Shopping*, Time Magazine (July 16, 2010), https://goo.gl/Cmu38u ("When Amazon.com opened for business on July 16, 1995, it was nothing more than a few people packing and shipping boxes of books from a two-car garage in Bellevue, Wash"). *Quill* was considering retaining a rule *first* created in 1967, when retailers would not have had access to anything like modern computers.

Accordingly, at the time *Quill* was decided, the U.S. Supreme Court faced a very different factual environment, in terms of both the relative "presence" of out-of-state, Internet-based retailers within the state and its consumers' homes, and the technological tools available to retailers to comply with the sales-tax obligations imposed by multiple states.

Meanwhile, given the extensive growth of Internet retail, the U.S. Supreme Court also confronted a very different set of stakes regarding the harms caused to state treasuries by preventing states from imposing a sales tax collection obligation on out-of-state sellers. Recent studies confirm that, even as the burden of compliance on retailers has precipitously fallen, the harms on states from non-compliance have grown. For example, last month the National Conference of State Legislatures estimated that $29.6 billion went uncollected in 2015 (the most recent year for which data is available) on account of non-collection by *Quill*-exempt Internet retailers. Nat'l Conference of State Legislatures, *Uncollected Sales & Use Tax from Remote Sales: Revised Figures* (March 2017), http://www.thecenterofshopping.com/news/updated-estimate-of-26-billion-annual-loss-due-to-uncollected-sales-taxes.

Recognizing these realities, Justice Kennedy identified an "urgent" need for the U.S. Supreme Court to reconsider *Bellas Hess* and *Quill*—stressing, in particular, the increasing harm to state treasuries. *DMA*, 135 S.Ct. at 1134-35 (Kennedy, J. concurring). In fact, he expressly asked states to create vehicles for *Quill*'s reconsideration. *Id.* Notably, Justice Kennedy is

one of two justices remaining from the *Quill* Court, neither of whom joined that Court's principal opinion because they refused to endorse the *Quill* rule in any respect on the merits. *Quill*, 504 U.S. at 319-21 (Scalia, J., joined by Thomas and Kennedy, JJ., concurring only in the judgment). The other remaining member of the *Quill* Court, Justice Clarence Thomas, has expressly called on the U.S. Supreme Court to reject this line of constitutional doctrine entirely. *Comptroller of Treasury of Maryland v. Wynne*, 135 S.Ct. 1787, 1811 (2015) (Thomas, J. dissenting) ("I continue to adhere to my view that the negative Commerce Clause has no basis in the text of the Constitution, makes little sense, and has proved virtually unworkable in application, and, consequently, cannot serve as a basis for striking down a state statute"). Meanwhile, then-Judge Neil Gorsuch of the Tenth Circuit Court of Appeals—who was recently sworn in as an Associate Justice of the United States Supreme Court—has likewise recognized that *Quill* is an unusually vulnerable precedent that invites its own, eventual overruling. *Direct Marketing Ass'n v. Brohl*, 814 F.3d 1129, 1151 (10th Cir. 2016) (hereinafter "Brohl") (Gorsuch, J. concurring) ("*Quill*'s very reasoning — its *ratio decidendi* — seems deliberately designed to ensure that *Bellas Hess*'s precedential island would never expand but would, if anything, wash away with the tides of time").

Taking up Justice Kennedy's explicit invitation, the Legislature passed the Act. App. 12-19. In so doing, it noted that *Quill*'s refusal to overrule *Bellas Hess* was now causing greater harm to the State because of the

growth of Internet retail. SR 14, ¶ 43; App. 16-18 (§ 8). To address this urgent harm, the Act created not only the obligation at issue in this case, but also a cause of action allowing the matter to quickly reach both this Court and, ultimately, the U.S. Supreme Court. App. 14-15. In fact, the Act's unique structure not only answers Justice Kennedy's call for expedition but also protects remote sellers, like Defendants, from the challenging compliance choices that such legislation might create. *See* App.14-15 (§ 2). To protect the State treasury and to promote the U.S. Supreme Court's ability to quickly determine *Quill*'s continuing vitality free from any confounding, collateral questions, the Act creates a declaratory judgment action that the State was allowed to immediately bring against retailers who did not comply. App. 14-15. This provision obviates the need for an audit, and the law asks both the circuit court and this Court to adjudicate the declaratory action as quickly as possible. App. 14-15 (§§ 2, 4). But to protect Defendants, who face a difficult compliance decision (if they collect the tax, they have to remit it; if they don't, they may be personally liable for it), the Legislature provided an automatic injunction against enforcement of the Act until completion of any litigation. App. 15 (§ 3) .

STANDARD OF REVIEW

This Court reviews the lower court's order granting summary judgment de novo. *AMCO Ins. Co. v. Employers Mut. Cas. Co.*, 2014 S.D. 20, ¶ 6, n.2, 845 N.W.2d 918, 902, n.2.

ARGUMENTS

While the State concedes the operative legal issue in this Court in light of *Quill*, there remains an important question at the heart of this case. That question is whether the U.S. Supreme Court should reconsider *Quill* so that obligations like those imposed in the Act can be upheld, and it is a question this Court should answer in the affirmative. It is both appropriate and important for this Court to do so, precisely because it lacks the independent power to revise the U.S. Supreme Court's decisions, no matter how problematic or conflicting they may become over time.

Below, the State elaborates on three key reasons why, having decided to stay its hand 25 years ago, "the time has come [for the U.S. Supreme Court] to renounce the bright-line test of *Bellas Hess*." *Quill*, 504 U.S. at 318. In light of these reasons, and others, it asks this Court to issue an opinion affirming the decision and yet advocating to the U.S. Supreme Court to grant certiorari and reverse its decision by overturning *Bellas Hess* and *Quill*, finally relieving the states from the harms caused by the outdated rule. Such an opinion from this Court would weigh heavily in the U.S. Supreme Court's decision whether to grant certiorari, and is most appropriate in circumstances, like these, where the underlying precedent remains in force but both is out of step with contemporary legal doctrine and has been questioned by members of the U.S. Supreme Court, itself.

In addition to asking this Court to flag the importance of this case for the U.S. Supreme Court, the State also seeks to resolve this matter quickly.

In passing the Act, the Legislature explicitly asked the courts to act "as expeditiously as possible." App. 14-15 (§§ 2, 4). Heeding that call, the State has worked diligently to expedite the judicial process by quickly conceding the conflict between the Act and *Quill* in the lower court, by noticing its appeal immediately, and by filing this brief before the statutory deadline. The U.S. Supreme Court will only be able to decide this case during its October Term 2017 (that is, by June 2018) if this Court enters a decision relatively soon—by approximately August of this year. Accordingly, given the Legislature's directive, the agreement of the parties on an affirmance, and the delays related to the unsuccessful removal of this matter to federal court, the State respectfully asks this Court to dispense with oral argument and prepare an opinion on this matter at the earliest opportunity.

I

WHETHER *QUILL CORP. V. NORTH DAKOTA*, 504 U.S. 298, 112 S.CT. 1904 (1992) PROHIBITS SOUTH DAKOTA FROM IMPOSING AN OTHERWISE VALID SALES TAX COLLECTION ON RETAILERS WHO LACK A "PHYSICAL PRESENCE" WITHIN THE STATE.

The question whether this Court should affirm or reverse the judgment is easily resolved: The State has consistently agreed throughout this litigation that, unless and until the U.S. Supreme Court reconsiders its decision in *Quill*, this Court must affirm the circuit court's holding that the Act is invalid as applied to Defendants. *See* SR 390; App. 1-3.

The Act itself recognizes that the test of "substantial nexus" it imposes does not match the "physical presence" requirement the U.S. Supreme Court

imposed regarding sales tax collection by out-of-state mail-order catalogs in *Bellas Hess*, and retained in *Quill*. The Act accordingly facilitates the creation of a case, like this one, to test whether the U.S. Supreme Court will continue to apply that outdated physical-presence rule to the modern problems of Internet retail. But *that* ultimate question is one that only the U.S. Supreme Court can answer: Because this Court is obligated to follow the precedent of the U.S. Supreme Court—no matter how inconsistent with contemporary factual realities and even if it "appears to rest on reasons rejected in some other line of decisions"—the State agrees that, for now, Defendants must inevitably prevail in this Court as a matter of law. *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 484, 109 S.Ct. 1917, 1921 (1989). Summary judgment was thus appropriately granted to Defendants, and this Court should affirm.

II

WHETHER THE SUPREME COURT OF THE UNITED STATES SHOULD RECONSIDER ITS DECISION IN *QUILL CORP. V. NORTH DAKOTA*, 504 U.S. 298, 112 S.CT. 1904 (1992).

As explained below, there are many reasons why the U.S. Supreme Court should reconsider *Quill*. There are, likewise, many reasons the State asks this Court to issue an opinion encouraging the U.S. Supreme Court to do so. At the outset, however, the State notes that this is an ordinary and appropriate role for a state's highest court or federal Court of Appeals to take in the rare case where U.S. Supreme Court precedent appears to be faltering and yet still controls the outcome. *See, e.g.*, *Kahn v. State Oil*, 93 F.3d 1358,

1363-64 (7th Cir. 1996) (strictly applying U.S. Supreme Court's *per se* rule against vertical maximum price fixing while calling on U.S. Supreme Court to overrule it), *certiorari granted*, *State Oil Co. v. Khan*, 522 U.S. 3, 118 S.Ct. 275 (1997) (overruling relevant precedent); *Allapattah Servs., Inc. v. Exxon Corp.*, 362 F.3d 739, 745 (11th Cir. 2004) ("The [U.S.] Supreme Court should grant certiorari in this case to resolve the controversy[.]"), *certiorari granted,* in part*, Exxon Corp. v. Allapattah Services, Inc.*, 543 U.S. 924 (2004). In fact, it is clear from *Quill* itself this is what the U.S. Supreme Court wanted North Dakota's Supreme Court to have done—to have flagged the tension in the precedent and the case for *Bellas Hess*'s senescence, while leaving to the U.S. Supreme Court "the prerogative of overruling its own decisions." *Quill*, 504 U.S. at 321 (Scalia, J. concurring) (quoting *Rodriguez de Quijas*, 490 U.S. at 484). The only way for a state's highest court to avoid repeating the approach from North Dakota that the U.S. Supreme Court criticized, and yet to encourage the reconsideration *Quill* demands, is to both speedily affirm and, in so doing, to "add [this Court's voice] to the others that have urged the [U.S.] Supreme Court to revisit [*Quill*]." *See Arizona v. Gant*, 556 U.S. 332, 338, 129 S.Ct. 1710, 1716 (2009) (noting Arizona Justices' encouragement to revisit *New York v. Belton,* 453 U.S. 454, 101 S.Ct. 2860 (1981) in case granting certiorari and overruling it).

In this regard, the State asks this Court to consider at least three arguments in an opinion affirming the judgment below, as the reasons the U.S. Supreme Court should nonetheless grant certiorari and reverse.

First, there is *Quill*'s dissonance with the rest of the doctrine, which muddies the analysis courts face in applying the dormant commerce clause, and leads to incompatible outcomes in closely analogous cases. Despite *Quill*, laws that impose similar or even heavier burdens on interstate commerce are upheld because they do not technically require tax collection, while tax obligations having a practically identical structure are likewise approved because they are not called "sales taxes." And that is so even though the U.S. Supreme Court has expressly rejected "formalistic" versions of the dormant commerce clause that depend for their outcome on how a tax is characterized by its drafters, rather than its substance. Meanwhile, *Quill*'s supposedly bright and straight line rule has become opaque and squiggly, as multiple states have obtained approval for looser conceptions of "physical presence" that sellers might unknowingly transgress—leading to potentially catastrophic and unforeseen tax liability. In other words, this "*ad hoc*" "sales-taxes-on-mail-orders exception" to the ordinary "substantial nexus" test, *see Wynne*, 135 S.Ct. at 1809 (Scalia, J. dissenting), is making the law hard for courts to interpret rationally, which is a compelling reason for the U.S. Supreme Court to reconsider *Quill* and harmonize its doctrine.

Second, there are the marked changes in critical constitutional facts since *Quill*. "A case questionable even when decided, *Quill* now harms states to a degree far greater than could have been anticipated earlier," and as Justice Kennedy explained, should thus "be left in place only if a powerful showing can be made that its rationale is still correct." *DMA*, 135 S.Ct. at

1135 (Kennedy, J., concurring). But while the harms visited on states like South Dakota have grown, the grounds for a rule like *Quill* have actually shrunk. Technology has made sales tax compliance a relatively easy matter for large masters of interstate logistics like Defendants, and states like South Dakota have enacted policies that streamline the process even further. Meanwhile, the ubiquity and intrusiveness of Internet storefronts has further eroded any distinction between sellers that are "physically" present and those that are equally present through the all-day, everyday access provided to the State's consumers by computers, tablets, and smart phones. *Quill*'s rule reflects nothing about contemporary realities.

Finally, there are the strengths of this case as a vehicle for reconsidering *Quill*: It frames the problems created by *Quill* with precision, and indicates that the time for review is now. South Dakota's law, which has become a model for legislation in other states, replaces the now murky concept of physical presence with a new, easily perceptible bright line requiring a substantial economic nexus between the seller and the State. The facts of this case, including South Dakota's heavy reliance on its sales tax, its adoption of streamlined sales tax compliance provisions, and even Systemax's ability to instantly comply with its collection obligations, starkly frame the stakes of the legal issue.

A. Quill is doctrinally anomalous and its uncertain force makes dormant commerce clause law incomprehensible.

As Defendants acknowledged in their motion for summary judgment (SR 347), "[u]nder contemporary dormant Commerce Clause analysis," a state tax can constitutionally be applied to interstate commerce if it satisfies the four requirements of *Complete Auto Transit v. Brady*: It must be (1) "applied to an activity with a substantial nexus with the taxing State," (2) "fairly apportioned," (3) "not discriminat[ory] against interstate commerce," and (4) "fairly related to the services provided by the State." 430 U.S. 274, 279, 97 S.Ct. 1076, 1079 (1977). And as Defendants likewise acknowledged only the first prong is at issue here (Defendants' Brief in Support of Motion for Summary Judgment, SR 347) rendering the question presented by cases like this one whether companies doing at least $100,000 of business in South Dakota's relatively small economy have "a substantial nexus" with the State. The obvious answer to that question is: Yes.

It is thus already recognized that *Quill*'s insistence on physical presence when it comes to sales tax collection by out-of-state retailers is in substantial tension with the existing doctrine. *Quill* itself acknowledged that "contemporary Commerce Clause jurisprudence might not dictate the same result [the Court adopted in *Bellas Hess*] were the issue to arise for the first time today." 504 U.S. at 311. Indeed, even at that time, the Court acknowledged that it had not followed *Bellas Hess* in its "review of other types of taxes." *Quill*, 504 U.S. at 314. This has led U.S. Supreme Court

Justices and federal judges to identify *Quill* not as a rule, but as an *ad hoc* exception to the rule—one that contributes to an increasingly chaotic set of dormant commerce clause doctrines. *See, e.g.*, *DMA*, 135 S.Ct. at 1135 (Kennedy, J., concurring) (calling *Quill* "questionable even when decided"); *Wynne*, 135 S.Ct. at 1808-9 (Scalia, J. dissenting) (criticizing *Quill*'s "sales-taxes-on-mail-orders exception" as among the "bestiary of ad hoc tests and ad hoc exceptions" now governing this doctrine); *Brohl*, 814 F.3d at 1150 (Gorsuch, J. concurring) (describing *Quill* as "an analytical oddity" that essentially "guarantees a competitive benefit to certain firms" that avoid physical presence, even though "the mainstream of dormant commerce clause jurisprudence . . . is all about preventing discrimination between firms").

As a prominent exception to an already malleable standard, *Quill* makes a lot of doctrinal trouble. For example, in a recent case in Ohio, Defendant Newegg itself argued that Ohio could not apply its "Commercial Activity Tax" (or CAT) to Newegg because Newegg lacked a physical presence within the state—analogizing to *Quill*. *Crutchfield Corp. v. Testa*, No. 2015-0386 (Ohio 2016), 2016 WL 6775765 at ¶ 1, Slip Op. at 2.[*] The CAT was assessed much like a sales tax: that is, on the basis of the amount of

[*] While Newegg was not a named defendant in *Crutchfield Corp.*, it was a defendant in a companion case which was consolidated with *Crutchfield Corp*. "for purposes of oral argument." *Newegg, Inc., v. Testa*, 2016 WL 6775839, ¶ 1. The Ohio Supreme Court stated "[t]he circumstances of the present case being no different from those in Crutchfield, we resolve [this matter] on the authority of *Crutchfield*." *Newegg,* at ¶ 3.

revenue Newegg derived from sales of products it shipped into Ohio. *Crutchfield Corp.,* 2016 WL 6775765 at ¶ 1, Slip Op. at 2. But the Ohio Supreme Court nonetheless rejected Newegg's argument and held that, because *Quill* by its terms applied only to sales taxes, the ordinary "substantial nexus" standard applied, rather than the physical presence requirement adopted in *Bellas Hess* and retained in *Quill*. *Crutchfield Corp.,* 2016 WL 6775765 at ¶¶ 42-43, Slip Op. at 17.

In other words, what seemed to make the difference was the name associated with the tax. But that only sows further confusion into the doctrine. The whole point of the U.S. Supreme Court's last forty years of dormant commerce clause jurisprudence has been to reject formalistic distinctions that make it a "trap for the unwary draftsman," and look instead to the substance of the tax under *Complete Auto*'s four-factor test, rather than what the state had "called its tax." *Complete Auto*, 430 U.S. at 279, 288. Thus, not only is *Quill*'s physical-presence requirement an exception to the doctrine, but *Quill* also requires an exception to the ordinary mode of analysis just to determine whether a state has enacted the kind of tax to which the exception applies.

Accordingly, none of the Ohio Supreme Court's reasoning regarding *Quill* in Newegg's case touched the fundamental inquiries associated with the dormant commerce clause, including concerns about placing undue burdens upon interstate commerce. That was so despite the fact that, as the dissenting justices pointed out, the *Bellas Hess* rule was expressly rooted in

such concerns, and the CAT imposed burdens of the same form and weight as sales taxes on non-Ohio retailers shipping into Ohio. *Crutchfield Corp.,* 2016 WL 6775765 at ¶ 73, Slip Op. at 31 (Judges Kennedy and Lanzinger, dissenting).

The simple point is that, from the perspective of a state legislature considering a new tax provision or a state supreme court attempting to implement the U.S. Supreme Court's current dormant commerce clause doctrine, that doctrine is adrift. If, rather than calling its tax a "sales tax" and forthrightly acknowledging *Quill,* the state had called it a "business tax" and argued for application of *Complete Auto*, there would be no logically sound way to determine whether *Quill* should apply. The question whether *Quill* is "limited to sales and use taxes," or rather applies more broadly to "commercial activity involving companies without a physical presence in the taxing state," *Crutchfield Corp.,* 2016 WL 6775765 at ¶ 73, Slip Op. at 31 (Judges Kennedy and Lanzinger, dissenting), appears to require attention to otherwise arbitrary facts, and is entirely disconnected from the rationales underlying the doctrine. This is, of course, a product of the fact that *Quill* is itself an "artificial" and "formalistic" exception to a functional rule, which makes it exceedingly hard to tell where the rule ends and the exception begins. Nonetheless, there are countless cases over the last two decades where state and federal courts have enforced against out-of-state companies various state taxes that look a lot like—and impose burdens quite similar

to—state sales taxes, *Quill* notwithstanding. *See, e.g.*, *Am. Target Advert., Inc. v. Giani*, 199 F.3d 1241, 1255 (10th Cir. 2000), *cert. denied*, 531 U.S. 811, 121 S.Ct. 34 (2000); *KFC Corp. v. Iowa Dep't of Revenue*, 792 N.W.2d 308, 323 (Iowa 2010), *cert. denied*, 565 U.S. 817, 132 S.Ct. 97 (2011); *Capital One Bank v. Comm'r of Revenue*, 899 N.E.2d 76 (Mass. 2009), *cert. denied*, 557 U.S. 919, 129 S.Ct. 2827 (2009); *Tax Comm'r of State v. MBNA Am. Bank, N.A.*, 640 S.E.2d 226, 232-34 (W.Va. 2006), *cert. denied sub nom FIA Card Servs., NA. v. Tax Comm'r of West Virginia*, 551 U.S. 1141, 127 S.Ct. 2997 (2007); *Couchot v. State Lottery Comm'n*, 659 N.E.2d 1225 (Ohio 1996), *cert. denied*, 519 U.S. 810, 117 S.Ct. 55 (1996); *Geoffrey, Inc. v. S.C. Tax Comm'n*, 437 S.E.2d 13 (S.C. 1993), *cert. denied*, 510 U.S. 992, 114 S.Ct. 550 (1993).

Put otherwise, this Court could explain to the U.S. Supreme Court that, essentially, the State of South Dakota should not be punished for accepting Justice Kennedy's invitation and confronting *Quill* head on, rather than trying to accomplish the same result through other means. The latter effort could well succeed because of the disharmony in that law. That is particularly so because, even though this Court would apply *Quill* to any improper effort to circumvent it, it is just impossible to tell what makes an effort to circumvent *Quill* improper, given that it is a "precedential island" incompatible with the case law that surrounds it. *Brohl*, 814 F.3d at 1151 (Gorsuch, J. concurring).

Indeed, a perfect example is found in *DMA* and *Brohl*—the situation that gave rise to both Justice Kennedy's and Judge Gorsuch's concurrences doubting the continued vitality of *Quill*. There Colorado imposed a burden on out-of-state sellers to track and report all substantial sales to in-state residents, rather than requiring them to actually collect and remit the tax due. *Brohl,* 814 F.3d at 1131-32. The Tenth Circuit held that burden compatible with the dormant commerce clause and with *Quill*, even though the burden at issue could hardly have been that different from collecting and remitting the tax—indeed, may have been heavier. *Brohl*, at 1146-47. As Judge Gorsuch explained, *Quill*'s own reasoning suggests that it should be artificially cabined to its facts, even when the laws under review create "burdens comparable in their severity to those associated with collecting the underlying taxes." *Brohl* at 1149 (Gorsuch, J., concurring). But, again, the problem with arbitrarily cabining an exception to its facts is that it is hard for courts to identify what the operative facts might be: If it is not the burden created on interstate commerce by the law, where else should the courts look?

What makes this even more complicated is that *Quill*'s potentially limiting facts include not only the type of tax at issue (a sales tax), but also the kind of "presence" that might or might not be "physical" for purposes of its "bright-line" test. *Bellas Hess* and *Quill* held that a state cannot apply its sales tax collection requirement to out-of-state *mail order* catalog companies that deliver their goods by common carrier, but the U.S. Supreme Court has

never fleshed out how a "physical presence" requirement would apply in any other context—including Internet retail. Accordingly, forty states have enacted laws that expand the concept of physical presence to embrace situations where, for example, a purchaser in the state "clicks through" an in-state advertising affiliate to reach the retailer, and in the remaining five sales tax states, the department of revenue (or equivalent agency) takes the position that these affiliate relationships create nexus. *See, e.g.*, MultiState Insider, Liz Malm, "A Three-Map Overview of State Sales Tax Compliance for Remote Sellers," (Feb. 14, 2017), https://www.multistate.us/blog/a-three-map-overview-of-state-sales-tax-compliance-for-remote-sellers. Other states have recently argued that the installation of "cookies" and other software or applications on state residents' devices suffices for a company to create physical presence. *See Crutchfield Corp.,* 2016 WL 6775765 at ¶¶ 2, 78, Slip Op. at 24, 34 (refusing to consider Ohio's alternative argument that "computerized connections" satisfied physical presence, having already affirmed). *Quill* itself acknowledges that the basic concept of physical presence can be arbitrary and "artificial." 504 U.S. at 315. For example, a seller is right now constitutionally required to comply with California's sales tax requirements throughout the entire state of California and across all of that seller's product lines, even if it ships all of its consumer goods from out of state, so long as it has a single office near the Nevada border whose sole purpose is to supply human resource support to the seller's main facilities in other states. *Quill* thus supplies no principled way to distinguish allegedly

"physical" presence on citizens' computers from, for example, non-retail-related presence in one corner of a state. Courts are forced to guess at what the U.S. Supreme Court meant by "physical" when it created this carve out from the doctrine, and have no tether to the doctrine's underlying principles with which to do that analysis.

This has three related implications for dormant commerce clause doctrine, all of which recommend in favor of *Quill*'s reconsideration. First, courts attempting to implement the U.S. Supreme Court's cases are left with no compass to guide them. If the State had chosen to argue here that *Quill* did not apply because Internet retailers are "present" in a way that catalog mailers were not, there would be no principles with which to test that distinction—*Quill* cannot supply them, because it is an acknowledged *exception* to the principles that usually apply. Second, retailers are deprived of the sole benefit *Quill* supposedly supplies: In place of a bright-line rule, they must consult the physical-presence standards of fifty different states, and if they cross any of those lines in even a hyper-technical sense, they face liability for uncollected sales taxes. Finally, the reliance interests that typically support adhering to precedent necessarily erode given the *multiple* ways that *Quill* itself invites states to impose burdens on out-of-state retailers that are comparable to a simple collection requirement. "*Quill* might be said to have attached a sort of expiration date for mail order and internet vendors' reliance interests on *Bellas Hess*'s rule by perpetuating its rule for the time being while also encouraging states over time to find ways

of achieving comparable results through different means." *Brohl*, 814 F.3d at 1151 (Gorsuch, J. concurring).

In the end, it is clear that *Quill* no longer fits within dormant commerce clause doctrine, and the result of trying to jam its square peg into the round hole of the "substantial nexus" test is to either warp the test or shave *Quill* down to a narrow and arbitrary set of operative facts. Meanwhile, there is no offsetting benefit to this, because uncertainty about the minimum content of "physical presence" in the Internet age—and exceptions to *Quill*'s exception for laws like Colorado's reporting requirement—leave retailers with burdens at least as heavy as the ones *Quill* allegedly prevents. As a court tasked with trying to implement the U.S. Supreme Court's conflicting doctrine in this area, this Court plays an important role in highlighting that those cases no longer provide effective guidance to state supreme courts seeking to determine which kinds of state tax obligations are governed by a physical-presence test, and why.

B. Changed circumstances recommend a reconsideration of Quill.

Quill is not only doctrinally anomalous but also out of step with contemporary conditions. As compared to when the *Quill* Court decided to retain the *Bellas Hess* rule, *Quill* now causes greater harm to states, lifts only a smaller and ever-shrinking compliance burden for out-of-state retailers, and provides an increasingly unfair and inefficient tax subsidy to retailers that in no way need it to compete effectively.

1. *Quill* harms state treasuries.

The harms that *Quill* causes to state treasuries were recognized by Justice Kennedy in *DMA*, and contemporary scholarship continues to validate this point. Justice Kennedy relied on a study by Professor William Fox of the University of Tennessee and others to conclude that Colorado alone lost around $170 million in 2012 due to its inability to collect taxes on purchases the state's residents made from out-of-state retailers. *See DMA*, 135 S.Ct. at 1135 (Kennedy, J. concurring) (citing D. Bruce, W. Fox, & L. Luna, *State and Local Government Sales Tax Revenue Losses from Electronic Commerce* 11 (2009) (Table 5)). As a whole, states and local governments now have $23 billion in annual sales tax revenue that they are unable to force out-of-state retailers to collect. *See id.*; Estimated Uncollected Use Tax From All Remote Sales in 2012, NCSL, http://www.ncsl.org/research/fiscalpolicy/collecting-ecommerce-taxes-an-interactive-map.aspx#2. The present estimate for South Dakota is that approximately 50 million in sales-tax revenue is attributable to out-of-state sellers that are shielded from sales tax collection by *Quill*. *See* Transcript, Budget Address of Governor Dennis Daugaard, Fiscal Year 2018, http://sd.gov/governor/docs/FY2018%20Budget%20Address%20Transcript.pdf.

This is not just a big problem for state treasuries today, it is also a growing one that will continue to expand with time. Uncollected tax on remote sales grew nationally from $16.1 billion in 2003 to $23 billion in

2012, of which $11.4 billion was due solely to Internet sales. *See* State to the House Judiciary Committee on the Marketplace Equity Act, NCSL, (July, 24, 2012), http://www.ncsl.org/research/telecommunications-and-information-technology/hr-3179-statement.aspx. Internet retail continues to flourish every year—for example, while overall retail grew only 1.9 percent from 2014 to 2015, Internet retail grew by 14 percent. *See* United States Census, Estimated Annual United States Retail Trade Sales – Total and E-commerce|: 1998-2015, http://www2.census.gov/retail/releases/current/arts/ecommerce.xls. It is common knowledge that "Black Friday" now competes with "Cyber Monday" for the biggest sales day of the year. Particularly given the squeeze on State budgets currently being contemplated, the growing revenue shortfalls caused by *Quill* require urgent attention. *See* FY 2018 Budget Address, http://sd.gov/governor/docs/FY2018%20Budget%20Address%20Transcript.pdf.

Indeed, the problem is particularly bad in states like South Dakota, for two reasons. First, given the largely rural and dispersed population, there is a greater incentive to rely on Internet retail rather than travel potentially long distances to retail hubs to buy goods. And second, because South Dakota has no income tax, it relies on its sales tax to fund critical state infrastructure and services. For example, at the same time the Legislature passed the Act, it also increased the sales tax to fund teacher pay in the State. House Bill 1182, 91st Session, South Dakota Legislature, 2016 "An Act to increase the state sales tax, the state use tax, the excise tax on farm

machinery, and amusement device tax for the purpose of increasing education funding and reducing property taxes, to provide for certain school district reporting and penalties, and to declare an emergency." The inability to require sales tax collection by Internet retailers thus poses a grave and immediate threat to the State, as the Legislature itself found in the Act.

One reason the threat is so grave is that raising the sales tax rate in response to the erosion in the sales tax base caused by *Quill* can actually exacerbate the problem. Studies show that consumers are particularly sensitive to the sales tax in choosing to divert their sales online—"customers are much more sensitive to $0.01 of sales tax than they are to $0.01 of item price even though both values have the same effect on the total price." Michael D. Smith & Erik Brynjolfsson, *Consumer Decision-Making at an Internet Shopbot: Brand Still Matters*, 49 J. Indus. Econ. 541, 549-50 (2001). So if the State increases its tax rate to make up for the shortfall, this may only tend to make the shortfall bigger. At a minimum, the gap will be much harder to close, meanwhile, aggressively raising the rate to address the eroding base further punishes in-state retailers and those who rely on them relative to out-of-state retailers and their customers.

In fact, *Quill* not only harms the State's treasury and retailers, but also its most vulnerable consumers. Put otherwise, *Quill* essentially creates a regressive tax subsidy system that transfers value from poorer communities to wealthier ones. Wealthier consumers with lucrative rewards credit cards and consistent, easy access to broadband Internet get a five to ten percent

discount on an ever-growing set of purchases by avoiding sales tax through Internet sales, while cash-dependent families living paycheck to paycheck and who purchase locally, pay ever-higher sales taxes on daily necessities.

Finally, it is not just the immediate tax shortfall created by *Quill* that bears attention, but the follow-on effects as well. The tax advantage *Quill* provides to out-of-state retail costs local jobs. Studies in some states have estimated that gains on the order of 10,000 jobs could follow from requiring online retailers to collect sales taxes, because of the diversion of sales back to stores that employ local citizens. *See* AngelouEconomics, *Economic Impact Analysis: The Economic Benefits Achieved in Texas as a Result of Collecting Sales Taxes from Online-Only Retailers* (Mar. 2011), https://goo.gl/4pK1C9; Elliott D. Pollack & Co., *Economic and Fiscal Impact of Uncollected Taxes on E-Commerce in Arizona* (Jan. 2012), https://goo.gl/tMEdle. Lost local jobs further stunt the local economy, leading to even more lost tax revenue through a multiplier effect. Justice Kennedy was clearly correct that the harms caused by *Quill* require "urgent" attention.

2. The benefits of the *Quill* exception have nearly vanished given advances in technology and State efforts to ease collection.

While the costs of the anomalous *Quill* exception have grown, whatever benefits it might provide have conversely fallen to near the vanishing point. As explained above, *Quill* does not provide the certainty that supposedly justified its bright-line physical presence rule because of shifting disagreements among states regarding the baseline for such presence. And

at the same time, *Quill* is less and less necessary to alleviate any "burden" associated with complying with the tax laws of multiple jurisdictions, given the increasing power of network computing and the efforts of states, like South Dakota, to simplify their sales tax regimes. Today, the same forces that allow companies like Defendants to deliver virtually anything to virtually anywhere within a matter of days—or hours—likewise makes it easy for them to calculate and collect the sales taxes applicable to those locations.

This case itself provides the perfect example. When the State sued Systemax, Systemax chose to instead voluntarily comply with the Act's collection obligations rather than litigate. SR 94-96. Systemax was able to begin collecting South Dakota sales tax through its online shopping portal *the very next day*. *See* SR 91, 94-96. When *Quill* was decided, it was only speculated that modern advances in computing would reduce the burdens placed on multi-state retailers to sort out variations in tax rules and rates around the country. *See Quill*, 504 U.S. at 303 (describing discussion by the North Dakota Supreme Court). Now, however, it is beyond dispute that the incredible progress in cloud-based computing and software design, that has occurred over the 25 years since *Quill*, has made this a problem companies (like those who would meet South Dakota's statutory thresholds) can easily solve.

This is especially true for two reasons. The advent of large, third-party companies that supply ready-made tax compliance software that retailers can integrate into their online shopping carts is the first. In 1996—more

than twenty years ago, but still four years after Quill was decided—Taxware released the first software program that provided sales and use tax compliance for Internet merchants. And, unsurprisingly, the progress in this (and every other) field of Internet logistics software over the intervening 20 years has been dramatic. Tax integration software is now hosted in "cloud-based" models where major providers almost instantaneously update the software with the latest changes to state rates and rules. And tax calculation functionality can be built right in to retailers' online "shopping carts," enabling retailers to calculate and collect the applicable tax with the same information that allows them to ship the product. A steadily growing number of sales tax compliance vendors provide these already simple and ever-simpler solutions, leading to consistently better products at consistently better prices, even for smaller scale retailers of the kind South Dakota crafted the Act around. http://www.salestaxinstitute.com/resources/links/tax-software (listing of fourteen sale tax compliance software providers).

The second is the effort by states like South Dakota to simplify the burdens of tax compliance through the Streamlined Sales Tax (SST) project, which was initiated in 1999 by the National Governor's Association (NGA) and the National Conference of State Legislatures (NCSL). *See* http://www.streamlinedsalestax.org/index.php?page=gen4. The SST project established common definitions and administrative procedures for the participating states, along with certification models for sales tax compliance software. It also protects retailers that use certified providers from liability

for errors in tax collection. Seven certified companies now offer software for compliance in the 24 states that have adopted the SST agreement. *See* http://www.streamlinedsalestax.org/index.php?page=Certified-Service-Providers; http://www.streamlinedsalestax.org/index.php?page=gen6. And all of this is available *at no charge* to remote sellers who collect sales tax for the participating states through SST.

These facts highlight how anomalous *Quill* has become. At this point, it does not matter how light the burdens might be on an individual retailer—in fact, the marginal cost of compliance could be *zero* because SST is footing the bill, and *Quill* would still prohibit a state from requiring the out-of-state retailer to collect the tax. It would appear, that what motivates companies to resist collecting and remitting sales tax is not the cost of compliance, but their lost ability to offer their customers a tax-avoidance discount for choosing them over their local competitors. This is why such retailers frequently advertise their interstate sales as "no tax" even though the purchaser is supposed to pay the state use tax if a sales tax was not collected. *See Black Hills Truck & Trailer, Inc. v. S. Dakota Dep't of Revenue*, 2016 S.D. 47, ¶ 17, 881 N.W.2d 669, 674 ("If sales tax was not included in the price of a transaction involving taxable property, the user of such property is then required to pay use tax.") (citing SDCL 10–46–2; SDCL 10-46-4; *Sioux Falls Newspapers, Inc. v. Sec'y of Revenue,* 423 N.W.2d 806, 810 (S.D.1988)). For example, enter "furniture" into Google's shopping page, https://goo.gl/ObTX0a (last visited April 11, 2017), and click on any item

available from Wayfair to see the following displayed, just below the price: "Free shipping. No tax." As Judge Gorsuch recognized in *Brohl*, what is really going on here is a bizarrely backwards situation in which a dormant commerce clause doctrine meant to prevent discrimination among businesses has been perverted into a unilateral tax preference for out-of-state retailers. *Brohl*, 814 F.3d at 1147-1151 (Gorsuch, J., concurring).

3. Contemporary conditions call strongly for *Quill*'s reconsideration.

When *Quill* was decided, the U.S. Supreme Court was considering only the catalog-mailer industry, which was perhaps a relatively small corner of the retail world that had, arguably, grown up in partial reliance on the *Bellas Hess* regime. In multiple respects, however, the world of contemporary Internet retail bears no resemblance to what the U.S. Supreme Court had in mind 25 years ago when it decided, "at least for now," to retain that regime. *Quill*, 504 U.S. at 318. Under current conditions, *Quill* disrupts the efficient functioning of free market competition far more dramatically than it did before.

First, the unfairness and inefficiencies created by *Quill* are manifest. Respected economists from across the political spectrum have concluded that the tax subsidy provided to online retailers by *Quill* substantially harms local retailers who must compete with cheaper online goods. *See, e.g.*, Austan Goolsbee, *In a World Without Borders: The Impact of Taxes on Internet Commerce,* 115 Q.J. Econ. 561 (2000); Arthur B. Laffer and Donna Arduin,

Pro-Growth Tax Reform and E-Fairness (July 2013), http://www.efairness.org/files/dr-art-laffer-sudy.pdf. This is best shown by "natural experiments" where online retailers who were not collecting in a given state either agree to voluntarily collect or establish a physical presence and must begin compliance. An Ohio State University study showed that in states where online retailers have started collecting sales taxes, their sales have been diverted back to local stores, falling 11% overall, 25% for purchases greater than $250, and fully 32.5% for big-ticket purchases (where customers are, predictably, most willing to search for savings). Brian Baugh et al., *Can Taxes Shape an Industry? Evidence from the Implementation of the "Amazon Tax"* (Fisher Coll. of Bus. Working Paper No. 2014-03-05, Mar. 2015), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2422403 ("We document strong evidence that the effect of the Amazon Tax increases with the size of the purchase, suggesting that households are particularly likely to engage in Internet shopping to avoid sales tax for large purchases").

This is just unfair. Proponents of the *Quill* regime like to point to the burdens that would fall on small businesses trying to figure out the tax laws applicable to their businesses in all 50 states. But, of course, *small* businesses neither ship to all 50 states nor come close to satisfying the Act's statutory thresholds. The real small businesses who are disadvantaged by this rule are local, family owned, brick-and-mortar retailers who are forced to comply with state sales tax laws while their competitors do not. So a

doctrine designed to prevent discrimination now has the opposite effect, harming state citizens as a result.

In fact, the resulting inefficiencies hurt not only local retailers, but the retail industry and national economy as a whole. *Quill* distorts the price signals that make the economy function smoothly: It results in too much patronage to online retail, and too little to local stores, relative to the benefits these different parts of the industry provide. For example, one recognized problem with *Quill*'s preference for online retail is that—given how easy it now is to find cheaper online prices for products found in stores—consumers treat local retailers like "showrooms" for products before turning to online retailers to consummate the purchase and reap the tax subsidy *Quill* provides. As the U.S. Supreme Court has itself recognized, forces like these can lead to the retail industry investing too little in customer service, because the local stores who provided it cannot reliably reap the benefit. *See, e.g.*, *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877, 127 S.Ct. 2705 (2007) (noting that "the retail services that enhance interbrand competition might be underprovided" when "discounting retailers can free ride on retailers who furnish services and then capture some of the increased demand those services generate").

Again, non-partisan economic literature focused on Internet retail bears out the concern: "In a market with a strong Internet presence and a high degree of free riding, the merchant's incentive to provide services can essentially collapse. The provision of services is vital to channel profits, and

dependence on [brick-and-mortar] retailers to perform this traditional role, in the presence of E-commerce and free riding, may be disastrous for channel profits." Steven Strauss, *The Impact of Free Riding on Price and Service Competition in the Presence of E-Commerce Retailers 50* (Yale Sch. of Mgmt. Working Paper Series PHD, No. 2, Jan. 14, 2002), http://papers.ssrn.com/sol3/papers.cfm ?abstract_id=296851; *see also* Dennis W. Carlton and Judith A. Chevalier, *Free Riding and Sales Strategies for the Internet*, 49 J. Indus. Econ. 441, 442-43 (2001) (explaining that showrooming effects harm both traditional retailers and manufacturers because such free riding "erodes the incentive of any retail store to promote the product," resulting in lower total sales); S. Umit Kucuk and Robert C. Maddux, The Role of the Internet on Free-Riding: An Exploratory Study of the Wallpaper Industry, 17 J. Retailing & Consumer Services 313, 318 (2010). Thus, in the unique context of modern Internet commerce, *Quill* doesn't just create winners and losers, it harms the competitiveness of the U.S. economy as well.

Meanwhile, these same forces have made the *physical* presence requirement of *Quill* increasingly obsolete. The reason "showrooming" is such a serious issue for retailers in the smartphone era is that, in every meaningful sense, the Internet competitor is just as "present" in a state as the local storefront—indeed, it is so omnipresent as to be inside the local retailer's own store, not to mention the consumer's home. Moreover, given the kind of targeted, user-specific advertising that can now be achieved

online, there is no disputing that Internet retailers operate just as intentionally within a state as a company that chooses to locate a brick and mortar store there. A rule like *Quill*'s perhaps made sense when "location, location, location" was the defining factor governing how most of the retail industry did business. But now that the industry itself values digital ubiquity over physical location, it makes even less sense to impose a tax disadvantage on local, physical retailers.

Simply put, *Quill* is increasingly harmful to states, decreasingly helpful in avoiding burdens on interstate commerce, and an increasingly bad fit for the retail industry and the U.S. economy as a whole. The U.S. Supreme Court decided to stay its hand, "at least for now," when it reconsidered *Bellas Hess* 25 years ago. But the radical changes of the past 25 years show that now *Quill*'s time has come.

C. This matter deserves the United States Supreme Court's urgent attention.

Finally, the State respectfully asks this Court to expeditiously resolve this case and, in so doing advocate to the U.S. Supreme Court to take up this "urgent" issue by granting certiorari.

There are three reasons why this case should reach the U.S. Supreme Court. First, by staying enforcement during the pendency of this action, the State has strengthened the case for both expedition and an immediate grant of certiorari. In order to prevent harm to taxpayers and keep this case free of confounding issues, the State chose not to enforce the collection obligation

against Defendants until this purely legal dispute was finally resolved. In addition, the State's acknowledgement of *Quill*'s applicability means that the U.S. Supreme Court can cleanly consider the question whether *Quill* should be overruled. But that same decision prevents the State from enforcing the Act until after review by the U.S. Supreme Court, which strengthens the case for that Court to intervene as soon as possible.

Next, the unique facts of this case help to isolate the stakes of *Quill*. Because South Dakota has no income tax and is heavily reliant on state sales tax, this case shows more vividly than most the large and growing harms that *Quill* visits on state treasuries. And because Systemax was able to comply instantaneously with S.B. 106, this case shows more vividly than most how little weight the alleged burden on interstate commerce actually has. South Dakota's participation in Streamline also vividly demonstrates that *Quill* has the perverse effect of advantaging out-of-state retailers in their competition with local businesses even if the State works hard to minimize the compliance burdens—even to the point of picking up most or all of them itself (a benefit it does not provide to in-state retailers). This Court's opinion can, accordingly, clarify for the U.S. Supreme Court that results as extreme as these are the cost of keeping *Quill*, making this an ideal opportunity to reconsider it.

Finally, South Dakota's experience over the last 25 years makes this a uniquely appropriate case to highlight for the U.S. Supreme Court how *Quill* is not only doctrinally anomalous, but fundamentally incompatible with the

federal system created and enshrined in the Tenth Amendment. In *Quill*, the Court decided to stay its hand, "at least for now," out of the hope that Congress would intervene and create a legislative solution. That was newly possible because *Quill* found that there was no due process clause barrier to requiring out-of-state retailers to collect sales taxes, and Congress could empower states to impose that requirement where the dormant commerce clause would otherwise prohibit it. *See* 504 U.S. at 318. South Dakota did its part: It simplified its tax code, worked with other states, set up the SST project, and enacted its provisions into law—provisions which would come into effect whenever Congress provided the legislation that *Quill* had suggested. But that day never came: Despite 25 years of hard work and political leadership from South Dakota and others, the many barriers to congressional action in our system have made these efforts increasingly futile.

This is not the separation of powers the Founders had in mind. Under the Tenth Amendment, the powers not affirmatively granted to the federal government are reserved to states. The commerce clause means that Congress can *take away* states' powers to tax goods moving in interstate commerce, but nothing in the Constitution supports a change in the default rule, where states lose their traditional powers to enact equal, non-discriminatory taxes unless and until they can convince both houses of Congress and the President to give their powers back. The U.S. Supreme Court may have thought that Congress could "fix" this problem, but the

reality is that the shape of any legislation that emerges—including the absence of any legislation for 25 years—is entirely a product of what happens if Congress does nothing at all. Furthermore, because the U.S. Supreme Court's dormant commerce clause jurisprudence changes the default rule, and the default rule is often determinative, it is the U.S. Supreme Court and not Congress that must fix the upset balance of power between the federal government and the states. South Dakota's experience makes clear that *Quill* makes a supplicant out of a constitutional sovereign, and that this is a problem only the Supreme Court of the United States can fix by restoring states to the role contemplated by the Tenth Amendment and the actual text of the commerce clause.

CONCLUSION

The State askes this Court to affirm the decision below as expeditiously as possible. The State also respectfully asserts this case presents an opportunity for this Court to advocate that *Quill Corp. v. North Dakota,* 504 U.S. 298, 112 S.Ct. 1904 (1992), be reconsidered by the Supreme Court of the United States.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

1. I certify that the Appellant's Brief is within the limitation provided for in SDCL 15-26A-66(b) using Bookman Old Style typeface in 14 point type. Appellant's Brief contains 9,438 words.

2. I certify that the word processing software used to prepare this brief is Microsoft Word 2010.

Dated this 13th day of April 2017.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this 13th day of April, 2017, a true and correct copy of Appellant's Brief in the matter of *State of South Dakota v. Wayfair Inc., Overstock.com. Inc. and Newegg Inc.* was served via electronic mail upon

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APPENDIX

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STATE OF SOUTH DAKOTA	)	IN CIRCUIT COURT
	:	
COUNTY OF HUGHES	)	SIXTH JUDICIAL CIRCUIT

STATE OF SOUTH DAKOTA, Plaintiff, vs. WAYFAIR INC., OVERSTOCK.COM, INC., and NEWEGG INC., Defendants.	32CIV16-000092 **ORDER GRANTING DEFENDANTS' MOTION FOR SUMMARY JUDGMENT**

This matter came before me on the Defendants' Motion for Summary Judgment regarding the Complaint for declaratory relief filed by the Plaintiff pursuant to Senate Bill 106, "An Act to provide for the collection of sales taxes from certain remote sellers," 91st Sess., S.D. Legis. (2016) ("S.B. 106"), which has been codified as SDCL Chapter 10-64 "Collection of Sales Taxes From Out-of-State Sellers."

Upon a review of the record and the filings made by the parties, the Court rules in favor of the Defendants in granting them summary judgment. In reaching this decision, the Court finds as follows:

1. The Parties agree that no material issue of fact exists and this action may be decided as a matter of law. Defendants' Brief in Support of Summary Judgment at 7-8 (noting that the parties agree that this case "presents no genuine dispute of fact" and "turns on pure questions of law"); Plaintiff's Response to Defendants' Motion for Summary Judgment at 2 ("the State agrees that there are no disputes of material fact");

see also Defendants' Statement of Material Facts, ¶¶ 1-9; Plaintiff's Response to Defendants' Statement of Material Facts, ¶¶ 1-9.

2. The parties further agree that no hearing on the Defendants' Motion is necessary. In accordance with SDCL 10-64-3, this Court is directed to act on this matter "as expeditiously as possible" with the presumption that "the matter may be fully resolved through a motion to dismiss or a motion for summary judgment."

3. Because each of the Defendants lacks a physical presence in South Dakota, *see* Plaintiff's Response to Defendants' Statement of Material Facts, ¶¶ 1-3, the State acknowledges that under *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), the State of South Dakota is prohibited from imposing sales tax collection and remittance obligations on the Defendants. The State further admits that this Court is required to grant summary judgment in Defendants' favor, because of the *Quill* ruling. Parties' Joint Statement of Proceedings Following Remand at 4.

4. SDCL 10-64-2, by requiring remittance of sales tax by sellers who "do[] not have a physical presence in the state," fails as a matter of law to satisfy the physical presence requirement that remains applicable to state sales and use taxes under *Quill* and its application of the Commerce Clause (U.S. Const., Art. I, s.8, cl. 3).

5. This Court is duty bound to follow applicable precedent of the United States Supreme Court. *James v. Boise*, -- U.S. --, 136 S.Ct. 685, 686 (2016) (state court is required to follow U.S Supreme Court precedent interpreting federal law); *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477, 484 (1989) (where precedent of the Supreme Court has direct application in a case, lower courts must follow the decision which directly controls). This is true even when changing times and events clearly

suggest a different outcome; it is simply not the role of a state circuit court to disregard a ruling from the United States Supreme Court.

6. The initiation of this action by the Plaintiff on April 27, 2016, resulted in the injunction of its enforcement as a matter of law under SDCL 10-64-4.

NOW, THEREFORE, after due consideration of the parties' submissions, the terms of SDCL Chapter 10-64, and controlling precedent, the Court hereby ORDERS that:

Defendants' Motion for Summary Judgment is GRANTED;

Judgment on the Plaintiff's Complaint shall enter for the Defendants;

The Plaintiff is enjoined from enforcing SDCL 10-64-2, in accordance with SDCL 10-64-4; and

Each party shall bear its own costs, disbursements, and fees.

Dated this 6th day of March, 2017.

BY THE COURT:

Mark Barnett

Mark W. Barnett
Circuit Court Judge
Sixth Judicial Circuit

ATTEST:

KELLI SITZMAN, Clerk of Court

By: _____
Deputy Clerk

STATE OF SOUTH DAKOTA
CIRCUIT COURT, HUGHES CO
FILED
MAR 06 2017
Kelli Sitzman Clerk
By _____ Deputy

STATE OF SOUTH DAKOTA) : COUNTY OF HUGHES)	IN CIRCUIT COURT SIXTH JUDICIAL CIRCUIT
STATE OF SOUTH DAKOTA, Plaintiff, vs. WAYFAIR INC., OVERSTOCK.COM, INC., and NEWEGG INC., Defendants.	32CIV16-000092 **DEFENDANTS' STATEMENT OF MATERIAL FACTS**

Pursuant to SDCL § 15-6-56(c)(1), Defendants Wayfair Inc., Overstock.com, Inc. and Newegg Inc. submit this statement of material facts as to which there is no genuine issue to be tried:

1. Defendant Wayfair Inc. ("Wayfair") has its principal place of business in the Commonwealth of Massachusetts and lacks a physical presence in South Dakota. Complaint ¶¶ 18, 19; Joint Answer ¶¶ 18, 19.

2. Defendant Overstock.com, Inc. ("Overstock.com") has its principal place of business in the State of Utah lacks a physical presence in South Dakota. Complaint ¶¶ 16, 19; Joint Answer ¶¶ 16, 19.

3. Defendant Newegg Inc. ("Newegg") has its principal place of business in the State of California and lacks a physical presence in South Dakota. Complaint ¶¶ 15, 19; Joint Answer ¶¶ 15, 19.

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4. In the previous calendar year (2015), Defendant Wayfair 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 two hundred or more separate transactions. Complaint ¶ 41; Joint Answer ¶ 41.

5. In the previous calendar year (2015), Defendant Overstock.com 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 two hundred or more separate transactions. Complaint ¶ 41; Joint Answer ¶ 41.

6. In the previous calendar year (2015), Defendant Newegg 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 two hundred or more separate transactions. Complaint ¶ 41; Joint Answer ¶ 41.

7. Defendant Wayfair is not registered to collect South Dakota sales tax. Complaint ¶ 40; Joint Answer ¶ 40.

8. Defendant Overstock.com is not registered to collect South Dakota sales tax. Complaint ¶ 40; Joint Answer ¶ 40.

9. Defendant Newegg is not registered to collect South Dakota sales tax. Complaint ¶ 40; Joint Answer ¶ 40.

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Dated this 22nd day of February, 2017.

BANGS, MCCULLEN, BUTLER, FOYE & SIMMONS, LLP

By: /s/ Jeff Bratkiewicz

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CERTIFICATE OF SERVICE

I hereby certify that on February 22, 2017, a true and correct copy of the foregoing Defendants' Statement of Material Facts was served electronically via the Odyssey system, via e-mail, and/or via U.S. Mail, postage prepaid, upon the following attorneys of record for Plaintiff, the State of South Dakota:

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One of the Attorneys for the Defendants

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STATE OF SOUTH DAKOTA) :SS COUNTY OF HUGHES)	IN CIRCUIT COURT SIXTH JUDICIAL CIRCUIT
STATE OF SOUTH DAKOTA, Plaintiff, v. WAYFAIR INC OVERSTOCK.COM INC NEWEGG INC Defendants.	32 Civ. 16-92 PLAINTIFF'S RESPONSE TO DEFENDANTS' STATEMENT OF MATERIAL FACTS

The State of South Dakota hereby submits its Response to the Defendants' Statement of Material Facts, pursuant to SDCL 15-6-56(c)(2). The State's responses below are specifically limited to and for the purposes of this litigation alone and shall not be used or interpreted for any other purpose.

The following numbered paragraphs correspond to the same numbered paragraphs from the Defendants' Statement of Material Facts.

1. Defendant Wayfair Inc. ("Wayfair") has its principal place of business in the Commonwealth of Massachusetts and lacks a physical presence in South Dakota.

   ADMIT that Wayfair's principal place of business in the Commonwealth of Massachusetts and that Wayfair lacks a "physical presence" in the traditional sense.

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2. Defendant Overstock.com, Inc. ("Overstock") has its principal place of business in the State of Utah and lacks a physical presence in South Dakota.

ADMIT that Overstock.com's principal place of business in the State of Utah and that Overstock.com lacks a "physical presence" in the traditional sense.

3. Defendant Newegg Inc. ("Newegg") has its principal place of business in the State of California and lacks a physical presence in South Dakota.

ADMIT that Newegg's principal place of business in the State of California and that Newegg lacks a "physical presence" in the traditional sense.

4. In the previous calendar year (2015), Defendant Wayfair 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 two hundred or more separate transactions.

ADMIT

5. In the previous calendar year (2015), Defendant Overstock.com 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 two hundred or more separate transactions.

ADMIT

6. In the previous calendar year (2015), Defendant Newegg had gross revenue from the sale of tangible personal property delivered into South Dakota in

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excess of $100,000, and/or sold tangible personal property for delivery into South Dakota in two hundred or more separate transactions.

ADMIT

7. Defendant Wayfair is not registered to collect South Dakota sales tax.

ADMIT

8. Defendant Overstock.com is not registered to collect South Dakota sales tax.

ADMIT

9. Defendant Newegg is not registered to collect South Dakota sales tax.

ADMIT

Dated this 23rd day of February, 2017.

/s/ Kirsten E. Jasper

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CERTIFICATE OF SERVICE

On this 23rd day of February, 2017, the undersigned hereby certifies that a true and correct copy of the *Plaintiff's Response to Defendants' Statement of Material Facts* in the above-entitled matter was served electronically through the Odyssey File and Serve system, upon the following:

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/s/ Kirsten E. Jasper
Kirsten E. Jasper
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State of South Dakota

OFFICE OF THE SECRETARY OF STATE

Department of State

United States of America, ☐
☐ **Secretary's Office**
State of South Dakota ☐

This is to certify that the attached instrument of writing is a true, correct and examined copy of Senate Bill 0106 in our office as filed March 22, 2016;

IN TESTIMONY WHEREOF, I have hereunto set my hand and caused to be affixed the Great Seal of the state of South Dakota at the city of Pierre, the capital, this day April 18, 2016.

Shantel Krebs

Shantel Krebs
Secretary of State

Appendix A

State of South Dakota

OFFICE OF THE SECRETARY OF STATE

Department of State

United States of America,
State of South Dakota

SECRETARY'S OFFICE

This is to certify that the attached instrument of writing is a true, correct and examined copy of SB 0106 duly passed in the Legislature of the State of South Dakota, as an Emergency Act, and has been carefully compared with the original now on file in this office and found correct.

IN TESTIMONY WHEREOF, I have hereunto set my hand and caused to be affixed the Great Seal of the State of South Dakota at the City of Pierre, the Capital, on March 22, 2016.

Shantel Krebs

Shantel Krebs, Secretary of State

AN ACT

ENTITLED, An Act to provide for the collection of sales taxes from certain remote sellers, to establish certain Legislative findings, and to declare an emergency.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF SOUTH DAKOTA:

Section 1. That the code be amended by adding a NEW SECTION to read:

Notwithstanding any other provision of law, any seller selling tangible personal property, products transferred electronically, or services for delivery into South Dakota, who does not have a physical presence in the state, is subject to chapters 10-45 and 10-52, shall remit the sales tax and shall follow all applicable procedures and requirements of law as if the seller had a physical presence in the state, provided the seller meets either of the following criteria in the previous calendar year or the current calendar year:

(1) The seller's gross revenue from the sale of tangible personal property, any product transferred electronically, or services delivered into South Dakota exceeds one hundred thousand dollars; or

(2) The seller sold tangible personal property, any product transferred electronically, or services for delivery into South Dakota in two hundred or more separate transactions.

Section 2. That the code be amended by adding a NEW SECTION to read:

Notwithstanding any other provision of law, and whether or not the state initiates an audit or other tax collection procedure, the state may bring a declaratory judgment action under chapter 21-24 in any circuit court against any person the state believes meets the criteria of section 1 of this Act to establish that the obligation to remit sales tax is applicable and valid under state and federal law. The circuit court shall act on this declaratory judgment action as expeditiously as possible and this action shall proceed with priority over any other action presenting the same question in any other venue.

In this action, the court shall presume that the matter may be fully resolved through a motion to

dismiss or a motion for summary judgment. However, if these motions do not resolve the action, any discovery allowed by the court may not exceed the provisions of subdivisions 15-6-73(2) and (4).

The provisions of § 10-59-34, along with any other provisions authorizing attorney's fees, do not apply to any action brought pursuant to this Act or any appeal from any action brought pursuant to this Act.

Section 3. That the code be amended by adding a NEW SECTION to read:

The filing of the declaratory judgment action established in this Act by the state operates as an injunction during the pendency of the action, applicable to each state entity, prohibiting any state entity from enforcing the obligation in section 1 of this Act against any taxpayer who does not affirmatively consent or otherwise remit the sales tax on a voluntary basis. The injunction does not apply if there is a previous judgment from a court establishing the validity of the obligation in section 1 of this Act with respect to the particular taxpayer.

Section 4. That the code be amended by adding a NEW SECTION to read:

Any appeal from the decision with respect to the cause of action established by this Act may only be made to the state Supreme Court. The appeal shall be heard as expeditiously as possible.

Section 5. That the code be amended by adding a NEW SECTION to read:

No obligation to remit the sales tax required by this Act may be applied retroactively.

Section 6. That the code be amended by adding a NEW SECTION to read:

If an injunction provided by this Act is lifted or dissolved, in general or with respect to a specific taxpayer, the state shall assess and apply the obligation established in section 1 of this Act from that date forward with respect to any taxpayer covered by the injunction.

Section 7. That the code be amended by adding a NEW SECTION to read:

A taxpayer complying with this Act, voluntarily or otherwise, may only seek a recovery of taxes,

penalties, or interest by following the recovery procedures established pursuant to chapter 10-59. However, no claim may be granted on the basis that the taxpayer lacked a physical presence in the state and complied with this Act voluntarily while covered by the injunction provided in section 3 of this Act.

Nothing in this Act limits the ability of any taxpayer to obtain a refund for any other reason, including a mistake of fact or mathematical miscalculation of the applicable tax.

No seller who remits sales tax voluntarily or otherwise under this Act is liable to a purchaser who claims that the sales tax has been over-collected because a provision of this Act is later deemed unlawful.

Nothing in this Act affects the obligation of any purchaser from this state to remit use tax as to any applicable transaction in which the seller does not collect and remit or remit an offsetting sales tax.

Section 8. That the code be amended by adding a NEW SECTION to read:

The Legislature finds that:

(1) The inability to effectively collect the sales or use tax from remote sellers who deliver tangible personal property, products transferred electronically, or services directly into South Dakota is seriously eroding the sales tax base of this state, causing revenue losses and imminent harm to this state through the loss of critical funding for state and local services;

(2) The harm from the loss of revenue is especially serious in South Dakota because the state has no income tax, and sales and use tax revenues are essential in funding state and local services;

(3) Despite the fact that a use tax is owed on tangible personal property, any product transferred electronically, or services delivered for use in this state, many remote sellers

actively market sales as tax free or no sales tax transactions;

(4) The structural advantages of remote sellers, including the absence of point-of-sale tax collection, along with the general growth of online retail, make clear that further erosion of this state's sales tax base is likely in the near future;

(5) Remote sellers who make a substantial number of deliveries into or have large gross revenues from South Dakota benefit extensively from this state's market, including the economy generally, as well as state infrastructure;

(6) In contrast with the expanding harms caused to the state from this exemption of sales tax collection duties for remote sellers, the costs of that collection have fallen. Given modern computing and software options, it is neither unusually difficult nor burdensome for remote sellers to collect and remit sales taxes associated with sales into South Dakota;

(7) As Justice Kennedy recently recognized in his concurrence in *Direct Marketing Association v. Brohl*, the Supreme Court of the United States should reconsider its doctrine that prevents states from requiring remote sellers to collect sales tax, and as the foregoing findings make clear, this argument has grown stronger, and the cause more urgent, with time;

(8) Given the urgent need for the Supreme Court of the United States to reconsider this doctrine, it is necessary for this state to pass this law clarifying its immediate intent to require collection of sales taxes by remote sellers, and permitting the most expeditious possible review of the constitutionality of this law;

(9) Expeditious review is necessary and appropriate because, while it may be reasonable notwithstanding this law for remote sellers to continue to refuse to collect the sales tax in light of existing federal constitutional doctrine, any such refusal causes imminent harm to this state;

RP

(10) At the same time, the Legislature recognizes that the enactment of this law places remote sellers in a complicated position, precisely because existing constitutional doctrine calls this law into question. Accordingly, the Legislature intends to clarify that the obligations created by this law would be appropriately stayed by the courts until the constitutionality of this law has been clearly established by a binding judgment, including, for example, a decision from the Supreme Court of the United States abrogating its existing doctrine, or a final judgment applicable to a particular taxpayer; and

(11) It is the intent of the Legislature to apply South Dakota's sales and use tax obligations to the limit of federal and state constitutional doctrines, and to thereby clarify that South Dakota law permits the state to immediately argue in any litigation that such constitutional doctrine should be changed to permit the collection obligations of this Act.

Section 9. Whereas, this Act is necessary for the support of the state government and its existing public institutions, an emergency is hereby declared to exist. This Act shall be in full force and effect on the first day of the first month that is at least fifteen calendar days from the date this Act is signed by the Governor.

An Act to provide for the collection of sales taxes from certain remote sellers, to establish certain Legislative findings, and to declare an emergency.

I certify that the attached Act originated in the

SENATE as Bill No. 106

Secretary of the Senate

President of the Senate

Attest:

Secretary of the Senate

Speaker of the House

Attest:

Chief Clerk

Received at this Executive Office this 8th day of March, 2016 at 9:20 A M.

By for the Governor

The attached Act is hereby approved this 22nd day of March, A.D., 2016

Governor

STATE OF SOUTH DAKOTA, ss.

Office of the Secretary of State

Filed March 22nd, 2016 at 11:45 o'clock A M.

Secretary of State

By Asst. Secretary of State

Senate Bill No. 106
File No. ____
Chapter No. ____

IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

No. 28160

STATE OF SOUTH DAKOTA,

Plaintiff/Appellant,

v.

WAYFAIR INC.,
OVERSTOCK.COM, INC., and
NEWEGG INC.,

Defendants/Appellees.

Appeal from the Circuit Court
Sixth Judicial Circuit
Hughes County, South Dakota
The Honorable Mark W. Barnett, Presiding Judge

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Notice of Appeal filed March 8, 2017

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PRELIMINARY STATEMENT

The Defendants and Appellees, Wayfair Inc., Overstock.com, Inc., and Newegg Inc., are referred to throughout this brief as "the Defendants." The Plaintiff and Appellant, State of South Dakota, is referred to as "the State." Senate Bill 106, 91st Session, South Dakota Legislature (2016), "An act to provide for the collection of sales taxes from certain remote sellers," codified at SDCL chapter 10-64, is referred to as "the Act." General references to the South Dakota Legislature are shortened to "the Legislature."

References to the Appellant's Brief are cited as "Applnt. Br. __." References to materials contained in the appendix to the Appellant's Brief are cited as "App.__." Citations to materials contained in the Settled Record of the proceedings below are cited as "SR __."

JURISDICTIONAL STATEMENT

The Honorable Mark W. Barnett issued an Order Granting Defendants' Motion for Summary Judgment on March 6, 2017. App. 001-003. The Defendants filed the Notice of Entry of Order Granting Defendants' Motion for Summary Judgment on March 7, 2017. SR 393-94. The State filed its Notice of Appeal on March 8, 2017. SR 398-99. The Court has jurisdiction pursuant to the Act, SDCL § 10-64-5, and SDCL § 15-26A-3.

STATEMENT OF THE ISSUE

WHETHER THE CIRCUIT COURT'S ENTRY OF SUMMARY JUDGMENT IN FAVOR OF THE DEFENDANTS MUST BE AFFIRMED.

The Circuit Court granted the Defendants' Motion for Summary Judgment because the provisions of the Act that require an out-of-state retailer with no physical presence in the state to collect and remit South Dakota sales tax, SDCL § 10-64-2, are in direct and undisputed conflict with existing Supreme Court precedent. As stated by the

Circuit Court, the Act "fails as a matter of law to satisfy the physical presence requirement that remains applicable to state sales and use taxes under *Quill* [*Corp. v. North Dakota*, 504 U.S. 298 (1992)] and its application of the Commerce Clause." App. 002 (brackets added). The State concedes that this Court must affirm the entry of summary judgment by the Circuit Court. Applnt. Br. at 11, 12. As a result, the State presents no actually disputed issue on which this Court can afford the State relief, nor has the State made any factual record that would support its request for what would amount to an advisory opinion by the Court regarding the continuing viability of the *Quill* standard. The Court should simply issue a decision affirming the lower court's entry of summary judgment, as both the State and the Defendants agree is required.

Quill Corp. v. North Dakota, 504 U.S. 298, 112 S.Ct. 1904 (1992)

Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 87 S.Ct. 1389 (1967)

Rodriguez de Quijas v. Shearson/Am. Express, Inc., 490 U.S. 477, 109 S.Ct. 1917 (1989)

STATEMENT OF THE CASE

The State's appeal from the entry of summary judgment by the Circuit Court suffers from fundamental infirmities. It is undisputed that the Act's provisions requiring sales tax collection by retailers with no physical presence in South Dakota are invalid as a matter of law under *Quill* and that this Court cannot, under existing constitutional doctrine, grant the State *any* relief, but must simply affirm the ruling below. Applnt. Br. at 11. Furthermore, the State has failed to make a factual record on which this Court might, in a properly presented case, such as an appeal from a tax assessment, undertake a thoughtful analysis of relevant facts as they pertain to the important constitutional issues underlying (and invalidating) the Act's tax collection provisions. The only facts of record in this case simply confirm that the Defendants satisfy the Act's admittedly unlawful conditions for imposing a sales tax collection obligation on out-of-state retailers. *See* App. 008-010. Indeed, 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.

Rather than asking this Court to uphold an admittedly unconstitutional law, the State advances an elaborate policy argument on which this Court lacks the power to grant relief. Moreover, that policy argument is grounded in factual assertions outside of the record which are disputed and have been shown to be false by respected authorities. The unprecedented statutory scheme contrived by the Legislature (enacting a law whose "findings" acknowledge its unconstitutionality) should not be condoned by this Court. The Act simply treats this Court as a waystation on the State's quest to reverse established precedent of the United States Supreme Court. The Defendants respectfully suggest that such a gambit is not a proper use of the state's judicial system.

The State's underlying cause of action arises directly from the Act, which was enacted in March 2016 with the Legislature's express acknowledgement that "existing constitutional doctrine calls this law into question." App. at 018. The Act requires any seller that "does not have a physical presence in the state" to collect and remit sales tax if the seller meets either of two criteria during the previous or current calendar year:

> (1) the seller's gross revenue from the sales of tangible personal property, any products transferred electronically, or services delivered into South Dakota exceeds $100,000; or
>
> (2) the seller sold tangible personal property, any product transferred electronically, or services for delivery into South Dakota in 200 or more separate transactions.

SDCL 10-64-2; *see* App. at 014. The Act further authorizes the State to initiate a declaratory judgment action under SDCL chapter 21-24 against any person the State believes meets these criteria. SDCL § 10-64-3. In devising these standards, however, the

Legislature expressly found that: (a) established constitutional doctrine "prevents states from requiring remote sellers to collect sales tax;" (b) the Supreme Court's substantial nexus doctrine would need to be changed "to permit the collection obligations of this Act;" and (c) "a decision from the Supreme Court of the United States abrogating its existing doctrine" would be necessary for the Act to be enforced. *Id.* § 10-64-1(7), (10), (11).

On March 25, 2016, three days after the Act was signed into law, the South Dakota Department of Revenue ("Department") sent notices to the Defendants and over 200 other companies that the Department believed met the requirements of the Act but lacked physical presence in South Dakota and were not collecting sales tax. *See* SR 12 (Complaint, ¶¶ 35, 37). The notices directed the Defendants to register with the Department by April 25, 2016, or face possible suit under the Act. SR 13 (Complaint ¶ 38). In other words, the Department sent out hundreds of demand notices informing recipients that they were compelled to comply—under the threat of suit—with a set of burdensome tax obligations, even though the very legislation giving rise to the requirements acknowledges the unconstitutionality of such demands.

The Defendants did not register to collect sales tax, because of their awareness that the Act's requirement of sales tax collection by retailers with no physical presence in the State plainly violates the limitation on the State's taxing power under the Commerce Clause, as reaffirmed in *Quill*. Significantly, the Department's demand letters did not inform the recipients that the Act was admittedly unconstitutional under existing Supreme Court precedent. *See* SR 29-34.

The State subsequently filed its Complaint against the Defendants on April 28, 2016, seeking a declaration that the collection requirements of SDCL 10-64-2 were valid as applied to the Defendants under state and federal law (although the Act itself acknowledges the contrary), and a declaration that the Defendants are required to register for, collect, and remit South Dakota sales tax. SR 1-20. Despite this prayer for relief, in its Complaint, the State again acknowledged that "a change in federal constitutional doctrine will be necessary for the State to prevail in this case" and that "a declaration in its favor will require the abrogation of the United States Supreme Court's decision in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992)." SR 1, 19 (Complaint ¶¶ 1, 51).

The Defendants on May 25, 2016, removed the action to the federal District Court for the District of South Dakota because of the federal constitutional question presented. SR 97-99. The Defendants filed a motion for summary judgment, and the State filed a motion to remand the action to Circuit Court. *See* SR 302. In its briefs filed with the federal court, the State acknowledged that the Act's provisions requiring the Defendants, as retailers that have no physical presence in South Dakota, to collect and remit South Dakota sales tax are directly at odds with the Supreme Court's decision in *Quill*. *See* SR 250, 303. At oral argument, the State informed the federal District Court that, if the matter were remanded to state court, the State would agree that summary judgment in favor of the Defendants is compelled by controlling Supreme Court precedent. SR 303.

Following that acknowledgement, on January 17, 2017, the federal District Court entered an Order and Opinion Granting Plaintiff's Motion to Remand, which was filed with the Circuit Court on January 19, 2017. SR 247-67, 303. On February 21, 2017, the

parties filed the Parties' Joint Statement Regarding Proceedings Following Remand. SR 301-04. The Defendants also filed a joint answer on February 21. SR 287-300.

The parties re-captioned and refiled in Circuit Court the summary judgment pleadings each had submitted in federal court. *See* SR 304. Defendants filed their motion for summary judgment on February 22, 2017. SR 333-65. The State filed its response to the motion on February 23, 2017. SR 366-86. In its response, the State again conceded that, because *Quill* is controlling and can only be modified by the United States Supreme Court, the Circuit Court "must therefore grant summary judgment to the Defendants." SR 369. The Defendants filed their reply brief on February 24, 2017. SR 387-89.

On March 6, 2017, The Honorable Mark W. Barnett entered the Order Granting Defendants' Motion for Summary Judgment. App. 001-003. In the Order, the Circuit Court ruled that "SDCL 10-64-2 by requiring remittance of sales tax by sellers who 'do[] not have a physical presence in the state,' fails as a matter of law to satisfy the physical presence requirement that remains applicable to state sales and use taxes under *Quill* and its application of the Commerce Clause (U.S. Const., Art. I, s.8, cl. 3)." App. 002. The Circuit Court granted the Defendants' motion for summary judgment and enjoined the State from enforcing the Act's sales tax collection provisions in accordance with SDCL § 10-64-4. App. 003.

STATEMENT OF FACTS

The only facts of record before the Court are the following:

- Each of the Defendants has a principal place of business outside of South Dakota and lacks a physical presence in the state. App. 008-009.

- 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. App. 009-010.

- None of the Defendants is registered to collect South Dakota sales tax. App. 010.

No other facts are established by the proceedings below. As detailed herein, the assertions of "fact" contained in the State's brief have no basis in the record, but rather are drawn from external, non-record sources that are hotly contested and refuted by other sources. The State's recitation of such disputed, extra-record "facts" serves only to highlight the inappropriateness of the State's declaratory judgment action and the State's real goal of advancing a policy agenda by enlisting this Court to take sides in a debate which most properly belongs in the U.S. Congress. In fact, Congress is actively considering legislation that would balance state revenue enhancement objectives with the need to protect interstate commerce from overreaching extraterritorial state impositions. *See* infra, Argument § II.E. This Court should simply affirm summary judgment—as requested by both parties—and not be drawn into a complex policy debate.

STANDARD OF REVIEW

Summary judgment is appropriate when there is no issue as to any material fact and the moving party is entitled to judgment as a matter of law. SDCL § 15-6-56(c). Review of a lower court order granting summary judgment is de novo. *Heitmann v. Am. Family Mut. Ins. Co.*, 2016 SD 51, ¶ 8, 883 N.W.2d 506, 508. In this case, the State does not contest the Circuit Court's order granting the Defendants summary judgment, but instead insists upon its affirmance. Applnt. Br. at 12.

ARGUMENT

It has been established by the United States Supreme Court for at least 50 years in successive cases that a state lacks the power under the Commerce Clause to impose a sales or use tax collection obligation on a company located outside its borders that has no "physical presence" in the taxing state and communicates with its customers there solely via the instrumentalities of interstate commerce (*e.g.*, United States mail, common carrier, and, today, the Internet). *See Nat'l Bellas Hess, Inc. v. Ill. Dep't of Revenue*, 386 U.S. 753, 758-60, 87 S.Ct. 1389, 1392-93 (1967). In 1992, the Supreme Court reaffirmed the physical presence, substantial nexus requirement for sales and use taxes in *Quill*. 504 U.S. at 313-19. The Court has never held, or even suggested, that any different or lesser standard applies for determining the validity of a state sales tax. To the contrary, as recently as 2015, the Court reaffirmed *Quill's* basic principles regarding limits on state taxing power under the Commerce Clause, in contrast with the Due Process Clause. *See Comptroller of the Treasury v. Wynne*, 135 S.Ct. 1787, 1793 (2015).

Under these principles, as the State concedes, the Act violates *Quill* by imposing sales tax collection and reporting obligations upon any remote seller "who does not have a physical presence in the state," so long as the seller meets one of two different economic thresholds during the prior or current calendar year: realizing at least $100,000 of gross revenue from, or completing at least 200 separate transactions with, customers in South Dakota. SDCL § 10-64-2. Accordingly, the Circuit Court properly awarded summary judgment to the Defendants. *See id.* at 12.

The State seeks to justify the Act's express violation of established constitutional doctrine with reference to the concurring opinion of Justice Kennedy in *Direct Mrkt'g*

Ass'n v. Brohl, 135 S.Ct. 1124, 1134-35 (2015) (Kennedy, J., concurring). *See* Applnt. Br. at 3, 7-9. Justice Kennedy wrote that "[t]he legal system should find an appropriate case for this Court to reexamine *Quill* and *Bellas Hess*." *Id.* at 1135. No other Justice joined Justice Kennedy's concurrence, although the decision in *DMA v. Brohl* was unanimous.

Nevertheless, the South Dakota Legislature chose to treat Justice Kennedy's concurring comments as an "invitation" to action, Applnt's Br. at 3, 8-9, *not by the legal system* in its ordinary workings, but by enacting an awkward, unprecedented, and unfair manipulation of the court system. Justice Kennedy's call for "an appropriate case" would be one in which there is an ample record for the Court's full consideration of the competing claims regarding such factors as the Act's impact on the parties, its restrictions on commercial activity, the complexity of state tax systems, and a host of other relevant facts. Indeed, the ordinary legal process of audit, tax assessment, protest, and appeal, followed by all states in the regular course of tax administration, provides courts with a complete record and, perhaps, presents the type of "appropriate case" to which Justice Kennedy was referring.

By contrast, the Act's *sui generis* cause of action for which the courts of South Dakota can offer no redress and which is supported by no factual record or expert witness reports is not an "appropriate case" for the U.S. Supreme Court to review. Furthermore, every "factual" premise on which the State bases its demand for Supreme Court review (other than the Defendants meeting the economic thresholds of the Act) derives from non-record sources and is, moreover, controverted by competing studies, information, and commentary concerning the modern economy, as the Defendants demonstrate below.

Even for a skeptic of the continuing vitality of the physical presence standard for state sales taxes reaffirmed by an 8-1 majority of the Supreme Court in *Quill* (an even greater majority than the prior and consistent 6-3 *Bellas Hess* decision), it would be difficult to conceive of a more *inappropriate* case than this for review of the long-standing constitutional principles challenged by the State. This is certainly not the type of "reexamination" even Justice Kennedy had in mind.

Alarmingly, the *Quill* physical presence standard is not the sole objective of the State's suit, or its plea to this Court. The State also hunts bigger game, and its "ask" of this Court is much more expansive than just a critique of *Quill*, as the closing paragraphs of its brief make clear.

This case, the State believes, is its opportunity to undo the hundreds of decisions over two centuries of jurisprudence that recognize the "dormant" or "negative" aspect of the Constitution's Commerce Clause. The State insists that "nothing in the Constitution supports a change in the default rule, where states lose their traditional powers to enact equal, non-discriminatory taxes unless and until they can convince both houses of Congress and the President to give their powers back." Applnt. Br. at 38. This perceived injustice, the State concludes, "is a problem only the Supreme Court of the United States can fix by restoring states to the role contemplated by the Tenth Amendment and the *actual text of the commerce clause.*" *Id.* at 39 (emphasis added). Never mind that a majority of the Supreme Court recently reiterated, in an opinion authored by Justice Alito, that there is " 'great force' in the argument that the Commerce Clause by itself limits the power of the States to enact laws regulating interstate commerce," a doctrine that "has been applied in dozens of our opinions, joined by dozens of Justices." *Wynne*,

135 S.Ct. at 1806.

For all of these reasons, this Court should decline the State's entreaty to advance its far reaching—indeed overreaching—constitutional reform agenda. The proper role of this Court is clear. The Court should affirm the entry of judgment as a matter of law against the State on the bare record now before it.

I. THE CIRCUIT COURT PROPERLY GRANTED THE DEFENDANTS' MOTION FOR SUMMARY JUDGMENT.

Because the parties agree that under current Commerce Clause doctrine the Act is unconstitutional, an exhaustive discussion of existing Supreme Court jurisprudence is not necessary. Nonetheless, a summary of fundamental Commerce Clause principles may be helpful to the Court.

The Commerce Clause delegates to Congress the power "[t]o regulate commerce ... among the several States." U.S. Const., Art. 1, Sec. 8, Cl. 3. It is well-established that the Commerce Clause has a corresponding "negative" or "dormant" aspect that expressly restricts the authority of a state to impose undue burdens on interstate commerce. *Wynne*, 135 S.Ct. at 1806; *Oregon Waste Sys., Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 98, 114 S.Ct. 1345, 1349 (1994). Under contemporary dormant Commerce Clause analysis, a state tax must satisfy the four-part test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279, 97 S.Ct. 1076, 1079 (1977), to withstand a challenge that the tax is unconstitutional. *E.g., Wynne*, 135 S.Ct. at 1793 (citing *Complete Auto*, 430 U.S. at 279). The Act runs afoul of the first prong of the *Complete Auto* test—"substantial nexus"—which is designed to "limit the reach of state taxing authority so as to ensure that state taxation does not unduly burden interstate commerce." *Quill*, 504 U.S. at 313. Pursuant to this test, an interstate business "must have a substantial nexus with the State

before *any* tax may be levied on it." *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 626, 101S.Ct. 2946, 2958 (1981) (italics in original).

Consistent with the substantial nexus requirement for state taxes recognized in *Complete Auto*, it has been established at least since the Supreme Court decided *Bellas Hess* that a state lacks the power to impose a sales or use tax collection obligation on a company located outside the state that has no "physical presence" in the taxing state and communicates with its customers there solely via the instrumentalities of interstate commerce. *See Bellas Hess*, 386 U.S. at 758-60. In *Bellas Hess,* decided in 1967, the Supreme Court held that the State of Illinois lacked the power to impose a sales/use tax collection obligation on a company located outside the state whose only connection to the taxing state was communications with customers in the state via mail and common carrier. *See id*. The Supreme Court upheld the "sharp distinction" established in prior cases between sellers with a physical presence in the state, and those without a presence who reach customers only via interstate commerce. *Id.* at 758.

Twenty-five years later, in *Quill*, the Supreme Court reaffirmed the physical presence requirement of *Bellas Hess* and again held that, under the Commerce Clause, a retailer with no physical presence in the state cannot be obligated to collect a state's use tax. *Quill*, 504 U.S. at 313-19. Like the retailer in *Bellas Hess,* the remote seller in *Quill* had no outlets or salespeople in the taxing state, but sent catalogs and flyers to customers in the state via mail. The Supreme Court reaffirmed that a vendor whose only connection with the taxing state is via the instrumentalities of interstate commerce lacks a physical presence in the state for purposes of the "substantial nexus" test. *Id.* at 315.

In reaching its decision, the Supreme Court emphasized that the "bright line" physical presence rule of *Bellas Hess* furthers the ends of the dormant Commerce Clause:

> Undue burdens on interstate commerce may be avoided not only by a case-by-case evaluation of the actual burdens imposed by particular regulations or taxes, but also, in some situations, by the demarcation of a discrete realm of commercial activity that is free from interstate taxation. *Bellas Hess* followed the latter approach and created a safe harbor for vendors "whose only connection with customers in the [taxing] State is by common carrier or United States mail."

Id. at 314-15 (brackets added). The Court further noted that any "artificiality" at the edges of the physical presence test is more than offset by a rule that "firmly establishes the boundaries of legitimate state authority to impose a duty to collect sales and use taxes." *Id.* at 315.

Quill has never been called into question by any decision of the Supreme Court. To the contrary, the Court has continued to cite *Quill* favorably with regard to the limitations on state taxing authority under the Commerce Clause. For example, in *Hemi Group, LLC v. City of New York*, 559 U.S. 1, 130 S.Ct. 983 (2010), the Court rejected an effort by the City to find a creative way to "end-run its lack of authority" under *Quill*. *Hemi*, 559 U.S. at 17 (Roberts, J., majority) (City improperly sought to impose civil liability on company for lost taxes "it had no obligation to collect, remit, or pay") and 18 (Ginsburg, J., concurring) (noting that the Commerce Clause prohibits the imposition of a use tax collection obligation on an out-of-state seller with no physical presence in the jurisdiction, citing *Quill* and *Bellas Hess*); *see also Wynne*, 135 S.Ct. at 1798-99 (citing *Quill* for the proposition that "while a State may, consistent with the Due Process Clause, have the authority to tax a particular taxpayer, imposition of the tax may nonetheless

violate the Commerce Clause"). The economic nexus provisions of the Act clearly overstep these fundamental limitations on state taxing power under *Quill*.[1]

II. THIS IS NOT AN APPROPRIATE CASE FOR THE REVIEW OF THE *QUILL* PHYSICAL PRESENCE STANDARD.

Quill is a controversial precedent primarily because the States have never accepted that *any* limitation on their taxing power under the Commerce Clause is warranted, as the State's brief makes clear. Even for opponents of the *Quill* physical presence test for state sales taxes, however, this is an utterly inappropriate case in which to take-up review of the *Quill* standard.

A. There Is No Factual Record.

The most glaring shortcoming in the State's appeal is that there is no factual record on which a reviewing court can evaluate *any* issue significant to the continuing vitality of the *Quill* physical presence standard as applied to electronic commerce. The State's (and Justice Kennedy's) fundamental premise for why *Quill* should be revisited by the Supreme Court is that circumstances in the retail marketplace have so dramatically changed since *Quill* was decided that a standard relevant to the mail order era cannot possibly remain appropriate in the Internet era. Applnt. Br. at 7 ("at the time *Quill* was decided, the U.S. Supreme Court faced a very different factual environment"). The State, however, presented no facts in the proceedings below and readily agreed with the

[1] As the Supreme Court has made clear, if the "precedent of this Court has direct application in a case," lower courts "should follow the case which directly controls, leaving to this Court the prerogative of overruling its own decisions." *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477, 484, 109 S.Ct. 1917, 1921-22 (1989); *see also James v. Boise*, 136 S.Ct. 685, 686 (2016) (*per curiam*) (State Supreme Court bound to follow U.S. Supreme Court precedent interpreting federal law).

Defendants that summary judgment for the Defendants was required. *See* SR 369; App. 002.

Review by this Court is "restricted to facts contained within the settled record." *Toben v. Jenske*, 2006 SD 57, ¶ 11, 718 N.W.2d 32, 35-36. Even sworn evidence that the parties agree should be considered by the Court "cannot be considered on appeal" where it is not part of the settled record. *Id.* Moreover, "the ultimate responsibility for presenting an adequate record on appeal falls upon the appellant." *Id.* (citing *Caneva v. Miners & Merchants Bank*, 335 N.W.2d 339, 342 (S.D. 1983)). The State has made no record, at all.[2]

In considering the dearth of evidence, it is important to recognize that this action was brought by the State against specific retailers, seeking a declaration that the requirements of Act "are valid and applicable *with respect to the defendants*." SR 20 (italics added). The State has made no effort to develop any facts about the Defendants and how they do business; nothing about the nature of their purported "'presence' . . . within the state and its consumers' homes," Applnt. Br. at 7; nothing about the

[2] Nor can the State respond that the necessary facts are embedded in the findings of the Legislature contained in the Act. *See* SDCL § 10-64-1. Such findings serve principally to show that the Legislature knew it was enacting requirements at odds with existing constitutional doctrine. *See id.* § 10-64-1(7), (10), (11). None of the findings reflect anything more than conclusory statements and few are even quasi-factual in nature. The Legislature received no written or live testimony regarding the Act, conducted no substantive committee hearings (approving the bill on a roll call vote each time), had no floor discussion or debate in either the Senate or the House, attached no fiscal note to the bill, and gave no supporting references or citations for any of the findings contained in the bill as originally introduced and later adopted as part of the Act. *See* Legislative Research Council, Action List for S.B. 106, S.D. Legis. (2016), http://sdlegislature.gov/legislative_session/bills/Bill.aspx?Bill=106&Session=2016. Nor are findings of the Legislature conclusive as to a factual issue they address. *See State v. Howell*, 95 N.W.2d 36, 39 (S.D. 1959) (determination on an issue addressed in a legislative finding is "a fact to be determined from the evidence.")

technology, systems and personnel they use to comply with sales tax obligations in their home state and in every other state where they have a physical presence; indeed, nothing about any other matter concerning the Defendants. Such facts specific to each Defendant are likely to be germane as to whether the *Quill* physical presence standard of substantial nexus retains its vitality in the Internet age. The State's "no-record-fast-track" approach demonstrates contempt for any careful and considered review of such crucial factual issues.[3]

The State engages in an extended discussion, based on non-record materials—most of which are themselves disputed, out-of-date, based on unsupported conjecture, and erroneous—concerning the "changed circumstances" that it contends warrant a reconsideration of *Quill*. *See generally* Applnt. Br. at 24-36. These arguments are debunked below, but what they show (especially in light of the contrary materials cited herein) is that "fast tracking" a case through the court system is an ill-conceived and inappropriate way to seek review of long-established constitutional doctrine.

B. The State Had a Means For Challenging *Quill* That It Could Easily Have Pursued to Bring Forward an Appropriate Case For Review.

In contrast to its "fact-track" approach on a totally barren record, the State had a straightforward option for contesting the continuing viability of the *Quill* standard. The Department could have initiated an audit of one or more of the Defendants, gathered relevant facts regarding its business and operations, reached a conclusion regarding whether its activities would support a case for nexus under *Quill* or even under a claim

[3] The State cannot request that the Court take judicial notice of its broad assertions about Internet sellers as support for its claims against the Defendants. Judicial notice is only appropriate as to a matter that "(1) is generally known within the trial court's territorial jurisdiction; or (2) can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned." SDCL § 19–19–201(b).

based on a modification in existing law, and issued an assessment to the retailer. This is the standard means by which the State, and every other state that has a sales tax, pursues tax administration and enforcement. *See generally* SDCL chapter 10-59. Indeed, the Act expressly gave the Department the option to use that established procedure. *See* SDCL § 10-64-3 (authorizing declaratory judgment action "whether or not the state initiates an audit or other tax collection procedure").

Under this time-honored process, after the Department issued an assessment, a putative taxpayer, such as an out-of-state retailer relying on *Quill*, would have the option of paying the assessment and electing to register, or contesting the assessment by requesting a hearing with the Department. SDCL § 10-59-8. At the hearing, evidence and expert testimony could be presented by both parties, and the hearing officer would be required to make findings of fact and present conclusions of law. SDCL § 10-59-9. The putative taxpayer could then appeal the matter to the Circuit Court. *Id.* After the Circuit Court ruled, either party could take a further appeal to this Court. *See, e.g., Paul Nelson Farm v. S.D. Dep't of Revenue*, 2014 SD 31, ¶ 6, 847 NW.2d 550, 553.

The foregoing process is the manner in which the legal system would generate a potentially "appropriate case" for review of the *Quill* physical presence standard, with a factual record and expert testimony pertinent to the important legal issues presented. Rather than pursuing such a procedure, the Legislature and the State have devised a precipitous and fundamentally inadequate process, which treats the state court system as little more than a procedural waystation, and generates a case barren of any record.[4] This

[4] It is worth noting that *Quill* itself, while resulting from a declaratory judgment action filed by the state, was presented to the U.S. Supreme Court on a detailed record. *See Quill*, 504 U.S. at 302-04 and n.1.

Court must, of course, affirm summary judgment on such a deficient appeal, but it should do nothing more that would endorse the State's approach.

C. The External "Facts" Relied Upon by the State Are Contested, Outdated, and Wrong.

Having failed to establish a record in the Circuit Court, the State resorts to citing secondary sources from outside the record. Its assertions are inaccurate and refuted by other reliable information.

1. The State's Estimates of Uncollected Sales Tax Are Greatly Inflated.

The State claims that South Dakota fails to collect $50 million annually on remote sales, and that the national total for "uncollected tax" are in excess of $20 billion. Applnt. Br. at 7, 25-26. The exaggerated claims put forward in each of the State's sources, from Governor Daugaard's assertion in his fiscal year 2018 budget address to a recent press release by the National Conference of State Legislatures, all derive from a single, unreliable source: a study done in 2009 by professors at the University of Tennessee. *See* Applnt. Br. at 25; Donald Bruce, William Fox, & LeAnn Luna, *State and Local Government Sales Tax Revenue Losses from Electronic Commerce*, University of Tennessee (Apr. 13, 2009) ("Tennessee Study"). The Tennessee Study's inflated estimates, however, were discredited by competing analyses soon after they were issued. For example, a more recent study showed that the Tennessee Study overstated the uncollected use tax on Internet sales by approximately three-hundred percent (300%). *See* Jeffrey A. Eisenach and Robert E. Litan, "Uncollected Sales Tax on Electronic Commerce: A Reality Check," (Feb. 2010), available at https://netchoice.org/wp-content/uploads/eisenach-litan-e-commerce-taxes.pdf (estimating uncollected tax in South Dakota of $10 million, compared to an estimate of $29.8 million in the Tennessee

Study); *see also* Peter A. Johnson, *Setting the Record Straight: The Modest Effect of Ecommerce on State and Local Sales Tax Collections*, Direct Marketing Association (Jan. 31, 2008) (estimating uncollected taxes 30% lower than an earlier version of the Tennessee Study).

The Tennessee Study is also wildly out-of-date. The most recent economic data available when the Tennessee Study was performed was from 2006. *See* Tennessee Study at 1. There have been dramatic changes in the online marketplace with regard to sales tax collection since Tennessee Study was conducted. Most notably, Internet behemoth Amazon.com collected sales tax in only five states (KS, KY, NY, ND and WA) when the Tennessee study was published, but now collects sales tax in every state that imposes a sales tax, including South Dakota. Chris Isadore, *Amazon to start collecting state sales taxes everywhere*, CNN (Mar. 29, 2017), http://money.cnn.com/2017/03/29/technology/amazon-sales-tax/index.html. The Tennessee Study itself reveals a twenty to thirty percent increase in sales tax collection rates in states where Amazon collected sales tax, so its expansion to nationwide sales tax collection practices dramatically reduces the level of uncollected sales tax revenue. *See* Tennessee Study at 22 (Table 9). Moreover, Amazon alone accounts for sixty percent of all online sales growth, so its change in tax collection practices will have an even more dramatic effect in reducing estimates of "lost" sales tax revenue over time. *See* Tonya Garcia, "Amazon accounted for 60% of US online sales growth in 2015," MarketWatch (May 3, 2016), http://www.marketwatch.com/story/amazon-accounted-for-60-of-online-sales-growth-in-2015-2016-05-03.

In fact, current U.S. Census Bureau data quickly demonstrates that the problem of uncollected tax on electronic commerce has nowhere near the magnitude projected by the State. Retail online sales—those ecommerce sales that may actually be subject to sales tax[5]—are reported by the Commerce Department to have reached $341 billion nationally in 2015. *See* "Quarterly Retail E-Commerce Sales 4th Quarter 2015," U.S. Census Bureau News (Feb. 17, 2016), http://www2.census.gov/retail/releases/historical/ecomm/15q4.pdf. Of that, industry reports indicate that on the order of 45 percent, or about $155 billion in sales, were made by Amazon.com and the large "multi-channel" retailers (*i.e.*, store-based retailers that now sell online, such as Wal-Mart and Best Buy) that dominate the Internet marketplace and collect state and local sales taxes. *See* Arthur Zackiewicz, "Amazon, Wal-Mart Lead Top 25 E-commerce Retail List," WWD (Mar. 7, 2016), http://wwd.com/business-news/financial/amazon-walmart-top-ecommerce-retailers-10383750/.

Of the remaining $186 billion, sales tax is also collected on some portion, because many smaller online retailers also have stores, and because almost every retailer, including "pure" online retailers, are required to collect sales tax in their home states. (Only 5 smaller states—AK, DE, MT, NH, and OR—do not have a sales tax.) Assuming, conservatively, that sales tax is collected on only one-fifth of the remainder, or another $37 billion, that leaves $149 billion of sales as to which the retailer does not collect the tax. Even ignoring, entirely, the self-reporting of use tax by consumers, the remaining $149 billion in national sales, divided proportionally by population for South Dakota (at

[5] The over $3 trillion figure often cited by critics of *Quill* represents all ecommerce, including manufacturing and wholesaling amounts which are not subject to sales tax. *See, e.g.*, *Direct Mrkt'g Ass'n v. Brohl*, 135 S.Ct. at 1135 (Kennedy, J., concurring). Retail ecommerce is much lower, as U.S. Census Bureau data shows.

0.267% of the total U.S. population), would result in approximately $398 million in "untaxed" sales in the State annually. *See* "Quick Facts, South Dakota," U.S. Census Bureau (estimates of South Dakota and U.S. populations as of July 1, 2015), http://www.census.gov/quickfacts/table/PST045215/46,00. South Dakota's average state and local tax rate is 5.43%. *See* Sales Tax Handbook, South Dakota, Local Sales Tax Rates, https://www.salestaxhandbook.com/south-dakota/rates. Applying that average tax rate, the annual "lost" sales tax revenue in South Dakota would be on the order of $21 million, not the excessive $50 million annually claimed by the State. This is less than one-half of one percent of the South Dakota budget for 2016 of $4.4 billion. *See* Total State Government Budget (Revised Budgeted FY 2016), https://bfm.sd.gov/budget/rec17/SD_Total_Recommended_2017.pdf.

2. Multistate Sales Tax Collection Is Not Rendered Uncomplicated By Sales Tax Software.

The system of state and local sales taxes in the United States is highly complex. There are 45 states, plus the District of Columbia, and another 12,000 local taxing jurisdictions that impose a sales or use tax. Jaimy Ford, *Tracking Sales Tax Rates Across Thousands of Jurisdictions*, Avalara (June 25, 2015) https://trustfile.avalara.com/blog/tracking-sales-tax-rates-across-thousands-of-jurisdictions/. This dizzying array of jurisdictions results in thousands of different tax rates, taxable and exempt products and services, exempt purchasers, shipping tax treatment, specialized tax rules (such as sales tax "holidays" and "thresholds" for different products), statutory definitions, registration and reporting regimes, record keeping requirements, and filing systems. In addition to the compliance burdens of such a system, companies are exposed to potential audit by

every state and locality with a self-administered sales or use tax. Remote sellers are only shielded from such inordinate burdens by the substantial nexus requirement under *Quill*.

The number of state and local taxing jurisdictions has continued to mushroom since the Supreme Court first recognized the physical presence requirement in 1967. *See* Billy Hamilton, *Home Sweet Taxing Unit*, State Tax Notes (Apr. 19, 2010) at 220 ("on average, a new local government is created every day in the United States"). The Supreme Court noted in *Bellas Hess* that there were over 2,300 such jurisdictions in 1967. *Bellas Hess*, 386 U.S. at 759 n.12. At the time *Quill* was decided in 1992, there were over 6,000. *Quill*, 504 U.S at 313 n.6. In 2014, the number reached 10,000. *See* Joseph Henchman, "State Sales Tax Jurisdictions Approach 10,000," Tax Foundation (Mar. 24, 2014), http://taxfoundation.org/blog/state-sales-tax-jurisdictions-approach-10000. Today, there are over 12,000 state and local taxing jurisdictions. *See* Ford, *Tracking Sales Tax Rates Across Thousands of Jurisdictions*, Avalara (June 25, 2015). Moreover, the number and types of local tax jurisdictions is staggering, including not only thousands of cities and counties, but also stadium districts, transportation districts, water districts, hospital districts, scientific and cultural facilities districts, resort community districts, and police jurisdictions, among others. *See, e.g.*, Hamilton, State Tax Notes at 220.

South Dakota's sales tax regime contributes to the overall complexity of the United States tax system. South Dakota has 142 city, county, and special district taxes in addition to the state sales tax. *See* Tax Rates.org, 2016, South Dakota Sales Tax by Zip Code, available at http://www.tax-rates.org/south_dakota/sales-tax-by-county. A leading industry provider of sales tax software reports that "since South Dakota sales tax has

numerous local taxing levels that must be monitored and maintained on a regular basis, compliance is complex and time consuming." *See* Avalara TaxRates, South Dakota, available at http://www.taxrates.com/state-rates/south-dakota.

The State nevertheless asserts that retailers can "easily" implement nationwide sales tax collection in thousands of jurisdictions due to improvements in software, Applnt. Br. at 29, but the State fundamentally misunderstands the complexity. First, the State repeatedly points to the decision of Systemax, Inc., a named defendant in the original suit, to register commence sales tax collection, as evidence that compliance is simple. *See* Applnt. Br. at 15, 29, 37. The State's conclusions about Systemax, however, are nothing more than conjecture. There is nothing in the record that indicates whether Systemax's implementation of sales tax collection was costly, or not, time-consuming, or not, fraught with problems, or not.

Indeed, the State glosses over the fact that it notified Systemax on March 25, 2016, more than a month in advance of filing the action, that the State intended to sue the company if it failed to register. There is no evidence regarding how Systemax responded to that demand – for example, whether it spent the next month or more preparing to collect sales tax as demanded by the Department on May 1, 2016. Furthermore, the threat of costly litigation, which the State intends to take all the way to the U.S. Supreme Court, may have prompted Systemax to elect to incur substantial compliance expense The State, and more importantly the Court, simply has no idea what Systemax's experience says about the larger sales tax collection debate, except that when a State uses the full weight of its authority to threaten an unconstitutional action against parties who

are exercising their rights, some will elect to forego those rights to avoid suffering potentially even greater injury at the hands of the State.

The State next suggests that "the same forces that allow companies like Defendants to deliver virtually anything anywhere within a matter of days—or hours—likewise makes it easy for them to calculate and collect sales taxes applicable to those locations." Applnt. Br. at 29. The comparison is utterly inapt. While shipping goods to customers involves essentially one variable—location—sales tax collection and reporting depends on countless variables, including thousands of different taxability determinations for a company's products lines, different tax rates (sometimes from product to product within a jurisdiction), exemptions, and taxability thresholds, not to mention reporting and record keeping requirements.

The State further asserts that sales tax collection is just a matter of integrating software "into [retailers'] online shopping carts," Applnt. Br. at 29 (brackets added), ignoring the costly realities of tax software implementation with multiple systems, including a company's enterprise management and financial reporting systems. Larry Kavanagh and Al Bessin, "The Real World Challenges in Collecting Multi-State Sales Tax For Mid-Market Online and Catalog Retailers," TRuST, Sept. 2013 (estimating initial costs of implementing new sales tax collection systems at between $80,000 and $270,000, with annual compliance-related costs thereafter of between $47,500 and $160,000), http://truesimplification.org/wp-content/uploads/Final_Embargoed-TruST-COI-Paper-.pdf. Putting a sales tax line on a check-out screen is merely the tip of the ice berg of sales tax compliance.

The State also points to the purported simplification in state tax systems promoted through the Streamlined Sales and Use Tax Agreement ("SSUTA"), an agreement implemented by certain states, including South Dakota, in an effort to reduce the burdens of sales tax collection, which includes a provision purporting to offer sales tax collection software at "no charge" to participating retailers. Applnt. Br. at 31. The SSUTA's alleged simplification measures, however, have attracted the membership of only 24 smaller states, representing less than one-third of the nation's population. *About Us*, Streamlined Sales Tax Governing Board (last visited June 12, 2017), http://www.streamlinedsalestax.org/index.php?page=About-Us. The SSUTA has never satisfied its original objectives of significant multi-state uniformity and tax simplification. *See, e.g.*, George S. Isaacson, *A Promise Unfulfilled: How the Streamlined Sales Tax Project Failed to Meet Its Own Goals for Simplification of State Sales and Use Taxes*, State Tax Notes (Oct. 27, 2003). Indeed, the SSUTA has not added any new member states in several years and the group of states that have declined to become members includes each of the six largest, California, Texas, New York, Florida, Illinois, and Pennsylvania. As a national solution to the complexity of the U.S. sales tax systems, the SSUTA falls woefully short.

Furthermore, the State's claim that software available through the SST project comes at no cost to a retailer is patently incorrect. The SST pays retailers *nothing* for integration, implementation, testing, training employees, maintenance, and operation of the software. Nor does the SSUTA insulate companies from the burden and expense of being audited by revenue officials from 45 different states and numerous home-rule local jurisdictions. The complexity of the U.S. sales tax system that led to the adoption of the

Quill rule is about much more than the cost of a software license, and its ramifications for interstate commerce deserve careful consideration on a fully-developed factual record.

3. The State's Economic Policy Arguments Are Refuted by Other Sources.

The State makes numerous policy arguments about economics and competitiveness, all of which are erroneous. The State contends that the *Quill* standard is fundamentally unfair because it gives some companies a competitive advantage, but the Supreme Court has previously determined precisely the opposite is true. In *Quill*, the Court found that requiring nationwide sales tax collection by a multi-state retailer, without regard to physical presence, would unduly burden interstate commerce. In other words, such an "undue" burden would disadvantage multi-state sellers, *i.e.*, impose costs that would prevent them from effectively engaging in commerce and competing with intrastate retailers.

The State insists that the *Quill* rule gives remote sellers an unfair price advantage, because consumers are hyper-sensitive to sales taxes and divert sales away from companies that collect sales tax. Applnt. Br. at 27, 33. Although the State cites studies regarding Amazon for the proposition that collecting a state's sales taxes dramatically reduces a retailer's sales, Applnt. Br. at 33, Amazon is surely the best judge of whether collecting, or not collecting, sales tax will drive consumer purchasing decisions. In the last several months, Amazon has moved to implement sales tax collection in every state in the nation, apparently unconcerned that collecting sales tax will harm its sales. The reason for Amazon's apparent lack of concern about implementing sales tax collection is likely straightforward: consumers' online shopping decisions are driven primarily by other factors. For example, a comprehensive PwC study conducted in 2016 showed that

convenience was a far greater reason why consumers chose to shop online, outpacing the price of the product 58 percent to 32 percent. PwC, *Total Retail Survey, 2016* (Feb. 2016) at 9. Moreover, remote sellers have always operated at a fundamental cost disadvantage to local businesses, because remote sellers must charge (or absorb) shipping and handling fees in order to deliver their products to consumers. Such fees are almost invariably greater, as a percentage of the purchase price, than the amount of a state's sales tax. If the only issue driving consumer purchasing decisions between in-store and online retailers was total price, remote sellers would lose the price war (or give away much of their profit margin). *See* Janet Stilson, *Study Shows Prevalence 'Webrooming,'* Adweek (May 14, 2014) (47% of consumers say avoiding shipping costs is the primary reason they will go to a store to buy a product after researching it online), http://www.adweek.com/brand-marketing/study-shows-prevalence-consumer-webrooming-157576/.

The State decries in exaggerated terms the practice of so-called "showrooming," in which a customer goes to a local store to learn about a product, only to then purchase the product online free of sales tax. Applnt. Br. at 34-36. According to the State, the practice not only demonstrates the fundamental unfairness of the *Quill* rule, but also results in retailers refusing to invest in customer service and support, harming the U.S. economy as a whole. The State's misunderstanding of the modern marketplace is profound. Recent studies prove that instances of "showrooming" are dwarfed by precisely the opposite phenomenon of "webrooming," in which consumers use a website to research a product and then go to a local store to purchase it, incurring the sales tax in the process.

A study conducted in 2013 showed that sixty-nine percent of consumers had engaged in "webrooming" while fewer than fifty percent had engaged in showrooming. *See* Stilson, *Study Shows Prevalence 'Webrooming,'* Adweek (May 14, 2014). In fact, more recent studies show that webrooming is increasing. *Spotlight on Webrooming*, MEC Global (May 2016), at 4 (consumers are five times more likely to engage in webrooming than showrooming) http://www.mecglobal.com/assets/publications/2016-05/Spotlight-On-Webrooming.pdf; Michelle da Silva, *Webrooming in Retail: How Businesses Can Turn Online Browsing Into In-Store Buying*, Shopify (Sept. 7, 2016), https://www.shopify.com/retail/why-retailers-should-embrace-webrooming ("89% of shoppers born between 1980 and 2000 favor heading to a store to purchase items").

The effect of this trend is dramatic. First, Forester research estimated that by 2017, the volume of in-store retail purchases attributable to webrooming would be nearly five times the volume of *all* consumer electronic commerce. *See* Stilson, *Study Shows Prevalence 'Webrooming,'* Adweek (May 14, 2014) (citing Forester study). Furthermore, consumers prefer retailers who are able to offer them the opportunity to see a product in person before they buy, increasing the pressure for retailers to offer a multi-channel shopping experience, *i.e.*, both a store location and website. Sara Spivey, *Consumers have spoken: 2016 is the year of "webrooming,"* Marketing Land (July 29, 2016) http://marketingland.com/consumers-spoken-2016-year-webrooming-180125. Indeed, contrary to the State's unfounded concerns about declining customer service in retail stores, consumers expect retailers to provide enhanced services during their store visits. *Id.* These market pressures not only enhance customer experience, they necessarily result in greater sales tax collection—whether in-store, or online—by multi-

channel retailers. The net effect of these developments is that the so-called "problem" of uncollected sales tax is trending down and is largely self-correcting, as the marketplace is increasingly dominated by large multi-channel merchants.

Finally, the State is misleading in its depiction of electronic commerce through its focus only on Internet shopping for consumer goods. In truth, the change in constitutional doctrine the State seeks has ramifications that reach much farther. The Act imposes sales tax collection and reporting obligations not only on out-of-state retailers that sell tangible personal property, like the Defendants, but also on all out-of-state service providers and vendors of products transferred electronically whose South Dakota revenues or transactions exceed the Act's thresholds. The Act also implicates not only companies that sell to consumers, but also businesses that sell products for consumption by other businesses. Companies across the country of every size and description will be swept up in the law, with uncertain implications regarding such issues as "sourcing" for tax purposes, transactions occurring in the "cloud," and complex definitional problems resulting from inconsistent state regulations. The potential effects on the national economy are significant.

D. The State Mischaracterizes the Law.

To begin with, the State misrepresents *Quill* itself. The State asserts, with reference to *Complete Auto*'s four-prong test that "[i]t is thus already recognized that *Quill*'s insistence on physical presence when it comes to sales tax collection by out-of-state retailers is in substantial tension with existing doctrine." Applnt. Br. at 16. The State then quotes from *Quill* the statement that "'contemporary Commerce Clause jurisprudence might not dictate the same result [the Court adopted in *Bellas Hess*] were

the issue to arise for the first time today.'" *Id.* (citing *Quill*, 504 U.S. at 311). The State, however, *omits the immediately following clause* in which the Court concluded that "*Bellas Hess* is *not inconsistent* with *Complete Auto* and our recent cases." *Quill*, 504 U.S. at 311 (italics added). The Court then went on to explain its express disagreement with the assertions of the North Dakota Supreme Court that the physical presence rule is inconsistent with *Complete Auto* and with contemporary doctrine limiting a state's authority to impose tax obligations on companies engaged in interstate commerce. *Id.* at 311-12 (twice stating that "we disagree" with the state supreme court's conclusions of law). The State's reading of *Quill* is simply wrong.

As the Court recognized in *Quill*, the danger of inconsistent state laws across the many thousands of state and local taxing jurisdictions in the United States implicates fundamental principles of the Commerce Clause and justifies the "bright line" physical presence standard adopted by the Court. *Id.* at 313 n.6. The potential burdens on retailers doing business in multiple states with differing tax laws are enormous, from initial registration and determination of a company's taxable products and services, to rate tracking and tax collection, to determining the proper taxable "sales price" and accounting for exemptions/exclusions, to obtaining the proper documentation from purchasers and maintaining the proper records, to monthly tax reporting and responding to revenue department audits, to identify only some of the complexities involved. Absent a rule that places clear and meaningful limits on state taxing authority, interstate businesses are faced with the substantial and, for small and medium-sized business, potentially crippling burdens of tax reporting and administration across multiple jurisdictions.

Indeed, the very same "structural concerns" that support the physical presence requirement of *Quill* apply with equal force to the nexus thresholds of the Act. If South Dakota is free to impose tax obligations on remote sellers based on nothing more than making sales to customers in the state, then "so can every other State, and so, indeed, can every municipality, every school district, and every other political subdivision throughout the Nation with power to impose sales and use taxes," resulting in precisely the kinds of "local entanglements" and burdens on interstate commerce that the Commerce Clause is designed to prevent. *Bellas Hess*, 386 U.S. at 759-760.

The State further relies on cases from outside the sales and use tax context to try to illustrate that the *Quill* rule "makes a lot of doctrinal trouble." Applnt. Br. at 17. The State concocts confusion where there is none. To begin with, the State points to a recent Ohio case involving Newegg concerning the constitutionality of the Ohio Commercial Activity Tax ("CAT"), a tax on the privilege of doing business in Ohio measured by gross receipts. Applnt. Br. at 17 (citing *Crutchfield Corp. v. Testa*, No. 2016-Ohio-7760, 2016 WL 6775765). According to the State, the Ohio CAT is "much like a sales tax," but the Supreme Court of Ohio has expressly rejected the claim that the CAT is like a sales tax. *Ohio Grocers Ass'n v. Levin*, 2009-Ohio-4872, ¶¶ 14, 51, 916 N.E.2d 446, 450, 457 ("The notion that the CAT 'operates' as a sales tax ... is factually incorrect.") Amplifying on that conclusion in *Crutchfield*, the Ohio Supreme Court concluded that the CAT "should be viewed as occupying the same constitutional category as an income tax on that same seller—whereas the sales tax on the in-state purchaser *occupies a different category*." *Crutchfield*, 2016-Ohio-7760, ¶ 46 (italics added). As a result, the Ohio

Court followed a different line of cases concerning state income taxes in holding that the *Quill* physical presence test did not apply to the CAT. *Id.* ¶ 47.

The State further asserts that "there are countless cases" involving out-of-state companies in which courts have enforced taxes that "look a lot like—and impose burdens quite similar to—state sales taxes, *Quill* notwithstanding." Applnt. Br. at 19-20 (collecting cases). But a reading of those cases shows that the court in each case determined that *Quill* was not applicable precisely because the taxes in question (typically state income taxes) were, in fact, *not similar to state sales and use taxes*, particularly with regard to the burdens they imposed on companies doing business in interstate commerce. *See, e.g., KFC Corp. v. Iowa Dep't of Revenue*, 792 N.W.2d 308, 325 (Iowa 2010) ("*the burden of state income taxes is substantially less*" than the burden of collecting and remitting state sales and use taxes, because income taxes involve few jurisdictions, do not make the retailer the tax collector for the state from thousands of consumers, and involve fewer assessments) (italics added), *cert. denied*, 565 U.S. 817, 132 S.Ct. 97 (2011); *Capital One Bank v. Comm'r of Revenue*, 899 N.E.2d 76, 85 (Mass. 2009) ("the collection of franchise and income taxes *did not appear to cause similar compliance burdens*" as sales taxes) (italics added), *cert. denied*, 557 U.S. 919, 129 S.Ct. 2827 (2009); *Tax Comm'r of State v. MBNA Am. Bank, N.A.*, 640 S.E.2d 226, 233-34, (W.Va. 2006) (describing in detail how the burden of sales tax collection is much greater than for franchise/income taxes and "demands knowledge of a multitude of administrative regulations"), *cert. denied sub nom FIA Card Servs., N.A. v. Tax Comm'r of West Virginia*, 551 U.S. 1141, 127 S.Ct. 2997 (2007); *Cuchot v. State Lottery Comm'n*, 659 N.E.2d 1225 (Ohio 1996) (rejecting application of *Quill* to state income tax on

lottery winnings, but finding physical presence in any event), *cert. denied*, 519 U.S. 810, 117 S.Ct. 55 (1996); *Geoffrey, Inc. v. S.C. Tax Comm'n*, 437 S.E.2d 13 (S.C. 1993) (rejecting application of *Quill* to income tax on licensing royalties); *cert. denied*, 510 U.S. 992, 114 S.CT. 550 (1993); *see also Am. Target Advert., Inc. v. Gianni*, 199 F.3d 1241, 1255 (10th Cir. 2000) (not a tax case; court held that *Quill* did not apply to licensing requirement for out-of-state fundraising entity).

The State likewise mischaracterizes the conclusion of the Tenth Circuit in *Direct Mrkt'g Ass'n v. Brohl*, 814 F.3d 1129 (10th Cir. 2016) ("*Brohl II*") concerning another non-sales tax law. In rejecting the application of *Quill* to notice and reporting requirements specifically imposed on retailers that *did not* collect Colorado sales taxes, the Tenth Circuit noted that "the Colorado Law does not require out-of-state retailers to assess, levy, or collect use tax on behalf of Colorado," a conclusion that "could not be squared" with the district's court determination that *Quill's* undue burden analysis applied to the law. *Brohl II*, 814 F.3d at 1146-47.

The fact that states have repeatedly attempted to circumvent *Quill*'s limitation on their taxing authority is hardly surprising, but such efforts do not demonstrate that the core principles of the Commerce Clause that protect interstate commerce from an unduly burdensome state and local tax system are no longer applicable, workable, or appropriate.

E. The Constitution Assigns to Congress, not the States, or the Courts, the Responsibility for Regulating Interstate Commerce.

Striking the proper balance between a free-flowing national marketplace, on the one hand, and the interest of the States in burdening such commerce in order to secure the collection of revenue ultimately due from its residents, on the other hand, is a responsibility assigned by the Constitution to Congress, through the Commerce Clause,

and not to the States, let alone an individual State such as South Dakota. U.S. Const., Art. I, Sec. 8, Cl. 3 (Congress shall have the power "[t]o regulate commerce … among the several States"). As the Court concluded in *Quill*, in light of Congress' role in regulating interstate commerce, including whether to permit the imposition of sales/use tax collection obligations on remote sellers, "the better part of both wisdom and valor is to respect the judgment of the other branches of the Government." 504 U.S at 318-19. It is only Congress, and not the States or the courts, that has the institutional expertise to weigh the national implications of expanded state taxing authority and to craft legislation that will simplify and make more uniform state sales tax systems, to assure that state tax obligations do not unduly burden interstate commerce.

Indeed, the need to safeguard the national economic interests secured by the Commerce Clause and inherent to remote sales transactions has only increased in the years since *Quill* was decided, with the growth of electronic commerce conducted over the Internet. The physical presence requirement adopted in *Bellas Hess* and reaffirmed in *Quill* was based in part on the Supreme Court's conclusion that "it is difficult to conceive of commercial transactions more exclusively interstate in character than the mail order transactions here involved." *See Bellas Hess*, 386 U.S. at 759. Today, the majority of remote sales are conducted online, an even more intensely interstate environment.

To that end, Congress is actively considering bills that would determine the appropriate conditions under which states would be authorized to require retailers with no physical presence in a state to collect and remit sales and use taxes, including the necessary measures for simplification and uniformity of state sales and use tax laws. Now pending before Congress are three bills: (1) the Marketplace Fairness Act of 2017,

S. 976, 115th Cong. (2017-2018), https://www.congress.gov/bill/115th-congress/senate-bill/976, a version of which passed the Senate in an earlier session; (2) the Remote Transactions Parity Act of 2017, H.R. 2193, 115th Cong. (2017-2018), https://www.congress.gov/bill/115th-congress/house-bill/2193; and (3) the No Regulation Without Representation Act, H.R. 2887, 115th Cong. (2017-2018), https://www.congress.gov/bill/115th-congress/house-bill/2887/text, a bill sponsored by Representative Jim Sensenbrenner (R-WI), which would largely codify the *Quill* standard. In addition, Representative Bob Goodlatte (R.-VA), the Chairman of the House Judiciary Committee, the committee charged with the review of the various proposals in the House, plans to introduce the Online Sales and Simplification Act, a bill meant to streamline tax reporting on remote sales. *See* Allison Enright, *The online sales tax may see new life in Congress*, Digital Commerce 360 (Feb. 8, 2017), https://www.digitalcommerce360.com/2017/02/08/online-sales-tax-may-see-new-life-congress/. Since Congress is considering the issue, "the better part of both wisdom and valor is to respect the judgment of [Congress]" with regard to state taxation of interstate commerce generally, and remote sellers in particular. *Quill*, 504 U.S. at 318-19 (internal citation omitted).

CONCLUSION

The Defendants respectfully request that the Court affirm the decision below, without addressing the State's request for what amounts to an advisory ruling on the vitality of *Quill*, a policy matter for which the State's "no-record-fast-track" approach has not generated an appropriate case. The Defendants respectfully request oral argument.

Dated this ___ day of June, 2017.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

1. I certify that the Brief of Appellees is within the limitation provided for in SDCL 15-26A-66(b) using Times New Roman typeface in 12 point type. Brief of Appellees contains 9,992 words.

2. I certify that the word processing software used to prepare this brief is Microsoft Word 2010.

Dated this _____ day of June, 2017.

_____

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this _____ day of June, 2017, a true and correct copy of the Brief of Appellees in the matter of *State of South Dakota v. Wayfair Inc., Overstock.com, Inc. and Newegg Inc.* was served via electronic mail upon

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IN THE SUPREME COURT
STATE OF SOUTH DAKOTA

No. 28160

STATE OF SOUTH DAKOTA,

Plaintiff and Appellant,

v.

WAYFAIR INC.,
OVERSTOCK.COM. INC., and
NEWEGG INC.

Defendants and Appellees.

APPEAL FROM THE CIRCUIT COURT
SIXTH JUDICIAL CIRCUIT
HUGHES COUNTY, SOUTH DAKOTA

THE HONORABLE MARK W. BARNETT
Circuit Court Judge

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Notice of Appeal filed March 8, 2017

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IN THE SUPREME COURT
STATE OF SOUTH DAKOTA

No. 28160

STATE OF SOUTH DAKOTA,

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WAYFAIR INC.,
OVERSTOCK.COM. INC., and
NEWEGG INC.

Defendants and Appellees.

PRELIMINARY STATEMENT

This reply brief will use the same references as set forth in the Preliminary Statement of the State's initial brief. References to the Defendants' Brief of Appellees will be denoted by "DB" followed by the appropriate page number. References to the State's initial Appellant's Brief will be cited as "SB" followed by the appropriate page number.

The State relies on the Statement of the Issues and Authorities, Jurisdictional Statement, Statement of the Case, Statement of the Facts, and Standard of Review presented in its initial brief. SB 1-9.

ARGUMENT

The parties agree that the decision below must be affirmed in this Court because, at least in this forum, *National Bellas Hess, v. Department of Revenue of Illinois*, 386 U.S. 753, 87 S.Ct. 1389 (1967) and *Quill Corp. v. North Dakota*, 504 U.S. 298, 112 S.Ct. 1904 (1992)

remain binding precedent. The parties also apparently agree that, pursuant to the Legislature's directive, *see* App. 15 (§ 4), this appeal should be decided as speedily as possible; Defendants do not suggest otherwise, do not dispute the (quick) timetable necessary to allow the U.S. Supreme Court to consider this case during its October 2017 Term, or provide any ground for rejecting the statute's own call for expedition. The only thing they disagree about is whether the U.S. Supreme Court should overrule *Quill* in this case, and relatedly, whether this Court ought to encourage reconsideration of *Quill* as part of its decision to affirm. On the latter point, there are a few assertions in Defendants' brief that require clarification.

The first, and perhaps most important, is a passing suggestion that this appeal "does not present any genuine and justiciable controversy." DB 2. Defendants do not actually press this argument, but if they did, it would necessarily fail for the reasons explained below. Most importantly, Defendants acknowledge (DB 5) that the State ultimately seeks a very different judgment from the circuit court than the court entered below. *See* I, *infra*.

The second is Defendants' core complaint—namely, that the presentation of this case as an isolated legal question on summary judgment makes this "not an appropriate case for the review of the *Quill* physical presence standard." DB 14, II. Remarkably, Defendants fault the State for sparing them the expense of an audit and extensive

discovery, and then bemoan the shape of the record *they* created by moving for immediate summary judgment. *See* DB 9, 16-18. Given Defendants' control of the process below—and the many ways it benefitted them—these process objections lack any force.

Even if they did not, however, Defendants' underlying premise is decidedly backwards. The U.S. Supreme Court *prefers* that cases be presented as isolated legal questions, and will "usually deny certiorari when review is sought of a lower court decision that turns solely upon an analysis of the particular facts involved." Robert L. Stern et al., SUPREME COURT PRACTICE § 4.14, at 249 (8th ed. 2002). Indeed, the summary judgment posture only helps to clarify the stakes: Having successfully moved for summary judgment, Defendants must necessarily believe that *Quill* prevents the State from enforcing the Act *despite* the facts found by the Legislature, described in the State's Complaint (SR 1-20), and universally recognized by accomplished academic researchers. No matter how serious the harms to the State—and Defendants concede they are quite serious—*Quill* stands in the way. The question the U.S. Supreme Court must decide is thus ideally framed here for its review. *See* II, *infra.*

Finally, there is Defendants' newfound effort to contest both the legal analysis and the economic realities that motivated Justice Kennedy's call for *Quill*'s reexamination in *Direct Marketing Association v. Brohl*, 135 S. Ct. 1124, 1134 (2015) (Kennedy, J. concurring), then-

Judge Gorsuch's similar analysis in *Direct Marketing Association v. Brohl*, 814 F.3d 1129, 1147 (10th Cir. 2016) (Gorsuch, J. concurring) (hereinafter "*Brohl*"), and the Legislature's decision to pass the Act itself. Defendants' efforts in this regard rely almost entirely on "studies" by interested entities—including papers authored by Defendants' own counsel. *See* DB 22, 25, 27-28. But, ultimately, both the factual and legal arguments Defendants press only end up confirming the State's point that *Quill* is in urgent need of reconsideration. *See* III, *infra*.

I. This Case Presents A Justiciable Controversy.

Defendants suggest the absence of a controversy in passing (at DB 2), but do not actually press such an argument. Indeed, the relief they ask for—affirmance, rather than dismissal—confirms that they believe the Court has jurisdiction to decide this case. *See* DB 35; *State v. Texley*, 275 N.W.2d 872, 875 (S.D. 1979) (Henderson, J., concurring specially) (without jurisdiction, "this Court cannot affirm").

In any event, there is a live controversy here. If the State ultimately prevails, the Act will become immediately applicable to Defendants, and they will be required to collect and remit sales tax to the State. If Defendants prevail, they will not have to collect and remit. That is a prototypical legal case or controversy. *See, e.g.*, *FCC v. Sanders Bros. Radio Station*, 309 U.S. 470, 477, 60 S.Ct. 693, 698 (1940) (economic injuries to party provide standing and controversy for

appeal even if economic factors do not affect the legal basis for the decision appealed).

To be sure, the legal consequence of *Quill* is that—*for now*—the State cannot prevail, and the State has forthrightly acknowledged as much. That does not destroy the controversy between the parties, however, which concerns the State's effort to reverse the *judgment* below in the final analysis. *See Campbell v. Fritzsche*, 78 S.D. 593, 595, 105 N.W.2d 675, 676 (1960) (There is an "actual controversy . . . where the judgment appealed from, if left unreversed, will preclude an appellant as to a fact vital to its rights"). The circuit court can clearly provide the State with the relief it seeks if the State is successful in encouraging the courts to reconsider *Quill* and reverse the circuit court's judgment; at that point, the circuit court can enter a declaration for the State and require Defendants to collect and remit. *See* DB 5 (acknowledging that the State seeks "a declaration that the Defendants *are* required to register for, collect, and remit South Dakota sales tax") (emphasis added). And while binding precedent from the U.S. Supreme Court prevents this Court from providing reversal that only makes it *more* plain that this Court's role, in a case like this one, is to highlight the need for the U.S. Supreme Court to reconsider that precedent.

II. Defendants' Objections Regarding The Record Lack Merit.

The core of Defendants' brief involves a scattershot process complaint, which they believe undermines this case as a vehicle for

reconsidering *Quill*. Describing the Legislature's expeditious alternative of declaratory judgment litigation as somehow "unfair," DB 9, Defendants suggest that it would have been better for the State to audit Defendants, seek an assessment against them, require them to bear the expense of protest and appeal, and use the entire process for expensive discovery into the myriad details of Defendants' businesses. *See* DB 16-18. Rather than exhaustively addressing Defendants' misunderstandings regarding the development of the Act and this litigation,[1] the State will focus on three key problems with Defendants' suggestion.

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[1] Defendants' argumentative "Statement of the Case" involves some odd characterizations. For example, it faults the State for sending "demand" letters notifying potentially affected sellers of the change in the law and explaining that they may be sued for a declaratory judgment if they fail to register. *See* DB 4. But the real purpose of these letters was entirely benign: They were meant to provide *extra* notice beyond the sufficient notice provided by the Act's mere passage, and to ensure that the State did not bring this action against defendants who intended to comply with the law rather than invoke their constitutional defense. *See* SR 29-36. Notably, Defendants' apparently preferred alternative would be for the State to *not* send direct notice to potentially affected parties, and then put them through the substantially greater expense of an audit and assessment case if they failed to register.

Other inconsistencies abound. Defendants say it is "not a proper use of the state's judicial system" for the Legislature to acknowledge that *Quill* must be abrogated before the Act can be enforced, and, relatedly, that the State's forthright approach to this litigation "treats this Court as a waystation on the State's quest" for a U.S. Supreme Court reversal. *See* DB 3. But Defendants then argue that if a precedent—like *Quill* here—"has direct application in a case, lower courts should follow the case which directly controls, leaving to [the U.S. Supreme] Court the prerogative of overruling its cases." DB 14, n.1 (quoting U.S. Supreme

(continued . . .)

First, Defendants cannot credibly suggest that the State has acted "unfairly" or failed to create an adequate record by bringing this pre-enforcement, declaratory judgment action in lieu of an audit and assessment. Among other things, Defendants' own counsel has brought a pre-enforcement declaratory judgment challenge designed to cut off audits and assessments in this State, and in the several other states that have recently adopted similar sales tax collection measures. *See American Catalog Mailers Association and NetChoice, v. Gerlach,* Civil File No. 16-0096, Hughes County, S.D. Sixth Judicial Circuit; *see also American Catalog Mailers Association and NetChoice, v. Heffernan,* Commonwealth of Massachusetts, 1784-CV-01772, Superior Court, Suffolk County; *American Catalog Mailers Association and NetChoice, v. Tennessee Department of Revenue,* No. 17-307-IV, In the Chancery Court for the State of Tennessee, 20th Judicial District, Davidson County, Part IV, at Nashville. That is hardly surprising; companies like Defendants and the trade associations litigating such cases on their behalf would surely prefer that members be spared the expense and uncertainty of audits and assessments in favor of a highly simplified

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(. . . continued)
Court precedents) (internal quotation marks omitted). Defendants do not explain how their consternation regarding the State's approach to this litigation can be squared with their own statement of the law. Again, their apparently preferred alternative would be for the State *not* to acknowledge the Act's tension with *Quill*, and to put Defendants through the time and expense of trying claims raising a host of colorable distinctions between this case and the binding precedent.

legal vehicle for the State to obtain a final word from the U.S. Supreme Court on *Quill*'s continuing force. What *is* surprising is to see Defendants now suggest the State ought to have enforced the Act against them in the most onerous way possible—not only auditing them and calculating an assessment, but forcing them to develop and defend against a trial, replete with expert reports, regarding not only their own businesses, but the state of the entire American economy. DB 16-18. This process complaint amounts to nothing more than a debater's point; it is the kind of argument a party only makes when it is certain that it will not suffer the consequences of being right.

Moreover, an audit and assessment will not ordinarily develop *any* of the factual issues Defendants say are lacking on the record here. The point of the audit is to determine and assess the extent of any tax liability, not to inquire into facts that may potentially relate to the question of whether the U.S. Supreme Court should overturn its controlling precedent. Defendants' proposed "straightforward" alternative is anything but.

Perhaps more important, Defendants ignore their own complete control over the case's current posture. As Defendants acknowledge (DB 15, n.2), the Legislature made detailed findings describing both the State revenue concerns and the changes in the national economy that the Legislature believed called for *Quill* to be overturned. App. 17 (§§ 1-9). If Defendants wanted to challenge those findings, they could have

done so; they were not required to move for immediate summary judgment. But having moved for summary judgment and denied the existence of any material factual disputes, Defendants cannot now complain that what they really need is a chance to contest the Legislature's factual determinations. Defendants' legal position in this case is quite clear: In denying the existence of any *material* disputed facts, Defendants necessarily believe that *Quill* prevents the State from prevailing here *in spite of* the facts as found by the Legislature and recited at length in the State's Complaint. *See* SR 1-20. And that is correct—as the State has acknowledged—precisely because *Quill* sets up a "bright-line" rule that is "artificial," "formalistic," and wholly insensitive to these critical concerns. *See, e.g.*, *Brohl*, 814 F.3d at 1149 (Gorsuch, J., concurring). That is a vivid demonstration of just how out of step the *Quill* rule is with the modern economy, and how indifferent it is to the increasing harm it is visiting on States like South Dakota. The summary judgment posture thus ideally presents this case for the U.S. Supreme Court's review.

Indeed, apart from faulting the State for Defendants' own litigation strategy, Defendants also argue from a faulty premise: The lack of case-specific or defendant-specific facts is a *strength* of this case as a vehicle for U.S. Supreme Court review, not a weakness. As the leading treatise on U.S. Supreme Court practice explains, if the U.S. Supreme Court determines that the holding in the case may turn on

case-specific factors, it is "the kiss of death" for the petition. *See* Stern, *supra*; "Certiorari Practice: The Supreme Court's Shrinking Docket" (Mayer Brown, 1995), *https://www.mayerbrown.com/certiorari-practice-the-supreme-courts-shrinking-docket-06-12-1995* ("'Fact-bound' cases also fall quickly by the wayside"). In fact, because the U.S. Supreme Court sets rules of general applicability through the process of case-by-case adjudication, it strongly prefers that the petition isolate a legal issue in a way that is abstracted from the case's particular factual record, and will thus apply broadly to future disputes. This is especially so where the question presented asks the U.S. Supreme Court to consider overruling one of its own precedents—an issue of obviously generalized and national importance that should not depend on how the record of one particular case was developed between two particular litigants. Notably, on the most recent occasion that the U.S. Supreme Court granted such a question, it did so in precisely this posture: The petitioner acknowledged in the Ninth Circuit that it could not win unless the U.S. Supreme Court changed its rule. *See* Reply Brief, *Friedrichs v. Cal. Teachers Ass'n*, No. 13-57095 (9th Cir. Mar. 29, 2016) at 5 (appellant asking Ninth Circuit to "affirm the district court's judgment as quickly as is practicable . . . so that Appellants may take their claims to the [U.S.] Supreme Court"); *Friedrichs v. Cal. Teachers Ass'n*, 135 S. Ct. 2933 (June 30, 2015) (granting certiorari).

Finally, and relatedly, Defendants simply misunderstand the kind of "facts" that are supposedly at issue here. Defendants omit from their brief South Dakota's statutory standard, which clarifies that the *only* facts that must be of record to be considered—and which might require judicial notice if they are not—are "adjudicative fact[s]." *See* SDCL 19-19-201(a). These are precisely the kinds of facts the U.S. Supreme Court seeks to avoid in finding appropriate vehicles for certiorari: As this Court explained just this year "[a]djudicative facts are those which relate to the *immediate* parties involved—the who, what, when, where[,] and why *as between the parties*." *See Mendenhall v. Swanson*, 2017 S.D. 2, ¶ 9, 889 N.W.2d 416, 419 (emphasis added) (citations omitted). The facts about which Defendants now complain are classic *legislative* facts—indeed, they are materials that bear directly on the factual judgments reached by the Legislature itself. And as explained in the committee note to Federal Rule of Evidence 201, on which SDCL 19-19-201(a) was modeled verbatim:

> This is the view which should govern judicial access to legislative facts. It renders inappropriate any limitation in the form of indisputability, any formal requirements of notice other than those already inherent in affording opportunity to hear and be heard and exchanging briefs, and any requirement of formal findings at any level.

The legislative facts that bear on whether *Quill* should be reconsidered have been recited in the State's filings in this case going back to April 2016—and back to the Legislature's findings before that. Defendants

have had every opportunity they could possibly want to "hear and be heard" and to exchange briefing on these questions. They have simply chosen not to challenge the facts as Justice Kennedy described them and as the Legislature found here.

In fact, Defendants' real complaint boils down to a footnote where it casts aspersions on the Legislature for not conducting more extensive hearings on the Act, suggesting this makes its findings unreliable. *See* DB 15, n.2. As an initial matter, this footnote is simply incorrect: There were committee hearings on the bill, and live testimony was offered and received—all of it in favor of the Act. http://sdlegislature.gov/Legislative_Session/Bills/Bill.aspx?Bill=106&Session=2016. And, of course, the Legislature heard from every witness who came forward to testify: The lack of testimonial support for Defendants' position is certainly not the Legislature's fault.

Moreover, even if Defendants accurately describe the legislative process surrounding the Act (which they do not), their picture of the legislative process remains a distorted caricature. The Legislature passed the Act after years of studies by disinterested economists demonstrated the harms the *Quill* rule was causing, a Justice of the U.S. Supreme Court drew attention to that scholarship in calling for *Quill* to be overturned, and Congress worked to no avail to address the issue. *See, e.g.*, Marketplace Fairness Act of 2013, S.743, https://www.congress.gov/bill/113th-congress/senate-bill/743. It also

acted in light of *years* of deliberation in the State Capitol and at legislative conferences around the country about how best to address the harms that *Quill* has caused. The Legislature also passed the Streamlined Sales Tax project, and is familiar with the simplification it enables in filing South Dakota sales taxes. Accordingly, the Act met with near-unanimous support in both houses and the strong backing of the Governor, all of whom were informed by their extensive experience on this issue. The judgments of the State's political branches cannot be so cavalierly dismissed.

Ultimately, there is a rich irony in Defendants' position on the expedited and simplified litigation structure the State adopted here. As the State has consistently explained, *see* SB 9, 36-37, the design of the statute and of this litigation was carefully calculated to *minimize* the compliance burden on taxpayers and limit any dislocations caused by the unusual circumstances of this case—namely, that the State must take an action that conflicts with current precedent as the only possible means of obtaining reconsideration of that precedent. If Defendants wanted to develop the record further, notwithstanding the Legislature's effort to minimize the cost this litigation would impose upon them, they were free to do so. Indeed, they could have conducted extensive expert research or other record development during the delay occasioned by

their unsuccessful effort to remove this case to federal court.[2] Instead, *they* asked that it move forward without making any factual submissions or contesting the findings of the Legislature. The time for Defendants' complaints has passed and this case is ready to expeditiously move toward review by U.S. Supreme Court as requested by the Legislature.

III. Defendants' Efforts to Contest *Quill*'s Legal and Economic Infirmities Are Unavailing.

When Defendants do turn to contesting the propositions laid out by the Act, the Complaint, and the State's brief, their arguments prove empty. The plain, consensus view among disinterested academics and legal thinkers is that *Quill*'s "ad hoc," "artificial," and "formalistic" exception is both bad economics and bad law.

Regarding the law, the best Defendants can say is that, even as *Quill* took the very unusual step of calling its own result into question on the merits, a narrow majority of the U.S. Supreme Court was willing to describe the *Bellas Hess* rule as "not inconsistent" with *Complete Auto Transit v. Brady*, 430 U.S. 274, 97 S.Ct. 1076 (1977). DB 30 (quoting *Quill*). The U.S. Supreme Court chose its words carefully; this conspicuous double-negative does not help Defendants.

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[2] That effort *directly* conflicted with a unanimous holding of the United States Supreme Court. *See Franchise Tax Bd of Cal. v. Construction Laborers Vacation Trust*, 463 U.S. 1, 21-22, 103 S.Ct. 2841, 2852 (1983) ("[A] State's suit for a declaration of the validity of state law is . . . not within the original jurisdiction of the United States district courts," and "not removable either").

That is particularly true because time has proven *Quill* even more "artificial" and "formalistic" than predicted. *See Brohl*, 814 F.3d at 1149 (Gorsuch, J.) (describing it as already "a matter of precedent for this court and many others" to treat *Quill* as "pretty 'artificial' and 'formalistic'" and refuse to extend it even to "*comparable* tax and regulatory obligations") (emphasis added). Defendants attempt to explain recent cases minimizing the *Quill* rule by noting that courts put the taxes at issue in those cases in "a different category" from sales taxes. *See* DB 31-33. But Defendants cannot explain *why*, for example, a Commercial Activity Tax calculated by reference to gross receipts "occupies a different category" from sales taxes, and made no effort to do so. Notably, the courts do *not* look to the functional differences among various state taxes in the burdens they actually create on interstate commerce in determining which kinds of regimes pass muster, and which do not. *See Brohl*, 814 F.3d at 1149 (Gorsuch, J. so noting). Instead, they characterize the taxes as sales taxes or something else (like an income tax), and then apply *Quill*'s exception as narrowly as possible. Notably, that makes *Quill* not only an exception from *Complete Auto*'s general test of substantial nexus—a test that is surely satisfied by doing large amounts of business in a state—but also an exception to the function-over-form approach that *Complete Auto* expressly adopts. *See, e.g.*, *Complete Auto*, 430 U.S. at 279 (rejecting

rule that prefers the "formal language of the tax statute" to its "practical effect" and thus "stands only as a trap for the unwary draftsman").

Nor is there any force to Defendants' suggestion that the issue presented is for Congress rather than the courts. Not only has Congress failed to resolve this issue in the 25 years since *Quill*, this assertion also begs the very constitutional question presented: There is certainly a policy question for Congress to answer in this realm, but the issue in this case is what form that question takes. The State's view—reflected in the Tenth Amendment and the text of the commerce clause itself—is that the relevant policy question is not whether Congress should devolve to the states a power that the Constitution never vested exclusively with the federal government in the first place, but, rather, whether Congress should oust the states from the power to regulate sales to consumers within their borders. This in no way denies that commerce clause doctrine properly prohibits discriminatory laws or laws of protectionist intent, nor does it deny that the commerce clause may have some other negative force. *Contra* DB 10, 33-35. Instead, the simple point is that states regulating sales within their borders in an evenhanded and ordinary fashion are presumptively exercising the powers reserved to them by the Constitution, and that changing the default rule to require congressional action before states can exercise those powers has warped the very political forces on which Defendants ask the Court to rely.

Defendants remarkably fair even worse in attempting to controvert the existing economic consensus against *Quill*. Tellingly, many of the "studies" they cite come from interested parties: They cite an electronic tax preparer that profits by "simplifying" the allegedly "complicated" system for taxpayers for the proposition that sales tax compliance is too complicated. *See* DB 23. They cite an article published by sales tax collection opponent NetChoice for the proposition that the tax losses in the materials relied on *by Justice Kennedy himself* are overstated. *See* DB 18. To support the proposition that the Streamline Sales Tax project has insufficiently simplified state tax compliance, they cite a paper by their own counsel *in this case*, DB 25, and a study published by a group that "represents American businesses in the fight to keep interstate commerce and competition free from unfair tax burdens imposed by states where our businesses have no operations or representation." *See* DB 24; http://truesimplification.org/about/ (describing "TruST"). And in a marked contrast to the distinguished academics who have researched and published peer-reviewed articles respecting the economic dislocations and harms to State revenue caused by *Quill*, *see* SB 24-35, Defendants spend pages discussing a phenomenon called "webrooming" based on articles published in the advertising trade press. *See* DB 27-28 (citing Adweek and Marketing Land).

In any event, the questionable authorities Defendants do marshal typically hurt their case on inspection, rather than help it. For example, the expert Defendants cite to regarding "webrooming" says, in the very article quoted, "showrooming is a flight risk and *a bigger problem for retailers*." *See Adweek*, http://www.adweek.com/brand-marketing/study-shows-prevalence-consumer-webrooming-157576/ (emphasis added). And while Defendants spend several pages making assumptions in order to calculate the taxes lost to *Quill* at a lower number than the best estimate of the State's political branches, even they ultimately calculate the loss at over $20 million. *See* DB 21. The significance of such amounts to South Dakota's fiscal soundness is plain; Defendants' own best version of the facts proves the State's key point.

Moreover, as to this argument and others, Defendants trade incorrectly on the happenstance that Amazon.com recently agreed to begin collecting sales taxes throughout the Nation. *See, e.g.*, DB 20, 26. The fact that one of the largest players in the industry has abandoned *Quill*'s outdated tax advantage does prove that the sky will hardly fall on Internet retail if *Quill* is finally overturned. But it also cannot possibly support the proposition that sales tax avoidance by Internet retailers is unproblematic. Voluntary compliance can be abandoned; absent the relief sought in this case, jurisdictions like South Dakota could suffer immediate budgetary shortfalls if Amazon suddenly decided to reassert

its rights under *Quill*. In addition, this is simply not how public policy analysis works: No one would conclude that restaurants should not have to pass mandatory health inspections because the largest chain or franchise has decided to voluntarily welcome in health inspectors.

There are other problems in Defendants' "factual" arguments. For example, the State did not have to force Systemax to stay in the case and testify about how quickly it was able to comply with South Dakota's collection obligations in order for the ease of its very-next-day compliance to be patent. *See* DB 23. Occam's razor is sharp enough to do the work. Defendants suggest that perhaps Systemax was working furiously for a month to prepare for compliance, and yet (for some reason) failed to notify the State that it intended to register and comply, as the notice invited. *See* SR 30, 32, 34, 36 ("Because the State may file this declaratory judgment action without undertaking an audit . . . it is important that you notify us immediately if you intend to comply with the Act"). The facts regarding the ease of compliance were entirely within Defendants' control; if they wanted to contest them, they could have done so.

In the end, the balance of the scholarly and legal thought regarding *Quill* is a remarkable testament to its vulnerability. Celebrated economists from both the Reagan and Obama administrations are united in finding, through detailed research, that *Quill* harms state revenue, distorts economic efficiency, and undermines

the proper functioning of retail markets. Meanwhile leading legal scholars in both the state and federal courts bemoan its bad fit with contemporary commerce clause doctrine. This case provides this Court with an opportunity to lead the way for U.S. Supreme Court review by adding its voice to the chorus calling upon the U.S. Supreme Court to reconsider *Quill*'s outdated rule. It should take that opportunity here.

CONCLUSION

The State respectfully asks this Court to affirm the judgment below as expeditiously as possible, so as to facilitate review by the U.S. Supreme Court during its upcoming Term. *See* SB 11 (explaining that a decision by August 2017 is likely necessary for the U.S. Supreme Court to make a final determination by June 2018). Defendants do not contest this expedited timetable but do, inconsistently, ask for oral argument while also asserting there is nothing for the Court to address in this case. *See* DB 35. The State respectfully suggests that the briefing is sufficient for this Court to fully consider this appeal and to craft an opinion identifying this case as an appropriate vehicle for the U.S. Supreme Court to reconsider its holdings in *Bellas Hess* and *Quill*.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

1. I certify that the Appellee's Brief is within the limitation provided for in SDCL 15-26A-66(b) using Bookman Old Style typeface in 12 point type. Appellee's Brief contains 4,856 words.

2. I certify that the word processing software used to prepare this brief is Microsoft Word 2010.

Dated this 22nd day of June 2017.

Kirsten E. Jasper
Assistant Attorney General

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this 22nd day of June, 2017, a true and correct copy of Appellee's Reply Brief in the matter of *State of South Dakota v. WAYFAIR INC., OVERSTOCK.COM. INC., and NEWEGG INC.* was served via electronic mail upon:

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