The Way Forward After *Wayfair*: Sorting Through the Constitutional Limits on State Sales and Use Taxes

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I. INTRODUCTION

Arriving amid a field of groundbreaking and attention-catching decisions, the recent Supreme Court case *South Dakota v. Wayfair, Inc.* garnered little public attention relative to how important the decision was. The Court in *Wayfair*, over a four-justice dissent, eliminated the 50-year-old physical presence rule established in *National Bellas Hess, Inc. v. Department of Revenue of Illinois*.[1] This physical presence rule prevented states from requiring sellers to collect and remit state sales and use taxes unless those sellers had some kind of physical presence in-state.[2] In the absence of the physical presence rule,

1. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2099 (2018).
2. *Id.* at 2091–92.

there is a noteworthy amount of uncertainty regarding the constitutional limits of a state's power to require purely out of state sellers to collect sales taxes. This Note's aim is to sort out some of this uncertainty.

In Part II, this Note will examine the creation and development of the physical presence rule, outline and report some of the key language from *South Dakota v. Wayfair, Inc.*, and evaluate the background requirements that the Dormant Commerce Clause and the Due Process Clause of the 14th Amendment place on state sales and use tax laws. Then, in Part III, this Note will lay out the restrictions on the states' power to require a seller to collect sales and use taxes for them in a more detailed fashion, first focusing on the constitutional restrictions and then evaluating the policy arguments surrounding sales and use taxation. Finally, in Part IV, this Note will present and attempt to answer the question of whether states ought to try to make their tax laws reach as many transactions as possible, then lay out what states should do to create their new tax laws within the bounds of these constitutional limits.

II. BACKGROUND

A. The Physical Presence Rule

A historian could trace the story of *South Dakota v. Wayfair*, *Inc.* back centuries before the actual ruling. One could begin the story with *McCulloch v. Maryland*, the Supreme Court's well-remembered early foray into the limits on the States' power to tax.[3] Another option is to begin this tale with the imperial crisis and the American Revolutionary War.[4] One could even choose to look back as far as Magna Carta.[5] However, the most direct starting point for this story, and the most appropriate for the limited scope of this Note, is the original pronouncement of the physical presence rule: the Supreme Court's decision in *National Bellas Hess, Inc. v. Department of Revenue of Illinois*.

A brief restatement of the facts in *Bellas Hess* is useful to understand the origins of the physical presence rule. National Bellas Hess, Inc. was a mail order sales company, incorporated in Delaware, which maintained a single operation center in North Kansas City, Missouri.[6] The company was not licensed to do business in Illinois, maintained no property in Illinois, did not advertise its products through any business operations (such as newspapers, television or radio stations, or billboard lessors) in Illinois, and did not support any agents or employees in Illinois.[7] The only connection Bellas Hess had with

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3. *See* McCulloch v. Maryland, 17 U.S. 316, 326–30 (1819) (discussing a limit on the states' power to tax the property and activities of the national government).

4. The idea that a government could only levy a tax against citizens which were adequately represented in the decision-making of that government was a central pillar in the political philosophy of the American revolutionary movement. *See* JACK P. GREENE, THE CONSTITUTIONAL ORIGINS OF THE AMERICAN REVOLUTION 71 (2010) (noting that the central assertion of protests against the British Parliament's proposed stamp tax was the fact that none of the British Colonies were represented in Parliament and, since it was a right of all British citizens to be free from taxation without representation, the tax was facially unjust).

5. After the passage of Magna Carta Libertatum, the British monarchy, with a few limited exceptions, could not levy a tax ("scutage or aid") "except by the common counsel of our kingdom." Magna Carta 1215, 17 John § 12, http://magnacarta.cmp.uea.ac.uk/read/magna_carta_1215/Clause_12.

6. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 753–54 (1967).

7. *Id.* at 754.

Illinois was the company routinely sending its advertisements and catalogues to Illinois residents through the United States Postal Service or other common carriers (Bellas Hess filled their orders through the same distribution methods).[8]

In Illinois, at the time, the use tax applied to all sellers which advertised in the state for the purposes of soliciting orders.[9] The law also allowed for service of process on and through the Illinois Secretary of State for tax claims brought against out-of-state sellers.[10] Illinois sued Bellas Hess under this law to require the company to collect use taxes on their sales to Illinois customers.[11] Bellas Hess in turn challenged the law on the basis that applying the tax against an out-of-state seller in their position violated the United States Constitution under the Commerce Clause of Article I, Section 8 and the Due Process Clause of the 14th Amendment.[12]

The Supreme Court ruled in favor of Bellas Hess.[13] In doing so, the Court first noted that the Commerce Clause and Due Process Clause considerations limiting the states' power to tax are similar.[14] Specifically, the Court announced that the Commerce Clause prohibits a state from taxing interstate commerce unless the tax is "designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys."[15] Meanwhile, the Due Process Clause limits a state to only taxing interstate commerce if "the state has given anything for which it can ask return."[16]

The Court further elaborated that "the Constitution requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax."[17] With these standards in mind, the Court noted there was a sharp distinction between foreign sellers employing agents or representatives in the taxing state or maintaining offices or warehouses in the taxing state and sellers who only interact with a state by advertising within the state.[18] Thus, the Court established that any state sales or use tax collection obligation applied to an interstate seller "who do[es] no more than communicate with customers in the State by mail or common carrier as part of a general interstate business" is a per se violation of the Commerce Clause.[19]

In the years following the Supreme Court's ruling in *Bellas Hess*, various courts wrestled with the meaning of the physical presence rule. Perhaps most prominent among these rulings during this formative period was *National Geographic Society v. California Board of Equalization*. This case established that a company with multiple, distinct

8. *Id.* at 754–55.
9. *Id.* at 755.
10. *Id.* at 755–56.
11. *Nat'l Bellas Hess, Inc.*, 386 U.S. at 754.
12. *Id.* at 756.
13. *Id.* at 758.
14. *Id.* at 756.
15. *Id.* (quoting Freeman v. Hewitt, 329 U.S. 249, 253 (1946)).
16. *Nat'l Bellas Hess, Inc.*, 386 U.S. at 756 (quoting Wisconsin v J.C. Penney Co., 311 U.S. 435, 444 (1940)).
17. *Id.* (quoting Miller Bros. Co. v. Maryland, 347 U.S. 340, 344–45 (1954)) (internal quotation marks omitted).
18. *Id.* at 758.
19. *Id.* at 758–60. While the Court specifically noted the Commerce Clause as the basis of this distinction, the prior discussion that the two standards were similar led to a general understanding that the physical presence rule extended to the Due Process analysis. *See, e.g.*, Quill Corp. v. North Dakota, 504 U.S. 298, 301 (1992) ("In *Bellas Hess* we held that a similar Illinois statute violated the Due Process Clause of the Fourteenth Amendment.").

operations and offices in a state devoted to one operation—but not to a separate sales operation—would still be subject to sales and use taxation in that state.[20] Another important development was courts not applying the rule when an otherwise exclusively out-of-state company used its own delivery trucks to fulfill orders in the taxing state.[21] However, the physical presence rule was generally straightforward and easy to apply—if the seller had any physical connection with the taxing state, the rule had no effect.[22]

Twenty-five years after the Court handed down its decision in *Bellas Hess*, the Court revisited the physical presence rule in *Quill Corp. v. North Dakota*. North Dakota sought to require an out-of-state mail-order seller with no agents or property in the state to collect and remit a use tax on goods sold in that state.[23] The seller relied only on common carriers to deliver its goods to customers in North Dakota.[24] The similarities between the facts of *Bellas Hess* and *Quill* are readily apparent; thus, *Quill* rose as a direct challenge to the continued application of the physical presence rule from *Bellas Hess*.[25] The North Dakota Supreme Court determined that the *Bellas Hess* rule was no longer correct in light of significant legal and societal changes.[26] Specifically, North Dakota pointed to the explosive growth of the mail-order business, the innovations of computer technology reducing compliance costs for businesses facing taxation in multiple states, the Court's ruling in *Complete Auto Transit, Inc. v. Brady*, and the change in Due Process analysis generally, no longer requiring a company's physical presence in a state before that state could exercise power over a company.[27]

The United States Supreme Court reviewing North Dakota's decision in *Quill* first established that there is an essential difference between the constitutional analysis of a state tax under the Due Process Clause and the analysis under the Commerce Clause.[28] After doing this, the Court reconsidered *Bellas Hess* under each branch of the analysis individually.[29] First, the Court ruled that *Bellas Hess* was wrongly decided with regard to the Due Process Clause.[30] The Court pointed to the changes in Due Process analysis concerning personal jurisdiction over corporations which had developed since *International Shoe Co. v. Washington* to justify overruling *Bellas Hess* on this point.[31] The Court then went on to explain that despite the fact they overruled *Bellas Hess* on the Due Process question—and despite any changes to how the Commerce Clause analysis was conducted after *Complete Auto*—the physical presence rule would remain in effect

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20. Nat'l Geographic Soc'y v. Cal. Bd. of Equalization, 430 U.S. 551, 552–54 (1977).

21. *See, e.g.*, Rowe-Genereux, Inc. v. Vt. Dep't. of Taxes, 411 A.2d 1345, 1350 (Vt. 1980) (upholding a Vermont sales tax levied on a company that "availed itself of the use of Vermont roads in its deliveries, Vermont media in its advertising, and the Vermont court system and a Vermont county sheriff's office in its business dealings").

22. D.H. Holmes Co. v. McNamara, 486 U.S. 24, 33 (1988).

23. *Quill Corp.*, 504 U.S. at 301–02.

24. *Id.*

25. *See id.* ("[W]e must either reverse the State Supreme Court or overrule *Bellas Hess*.").

26. *Id.* at 303–04.

27. *Id.* For a discussion of *Complete Auto* and its progeny, see *infra* Part II.C.

28. *Quill Corp.*, 504 U.S. at 305–06. This is a particularly important development, and the crux of an argument this Note adopts *infra* Part III: the Due Process and Dormant Commerce Clauses exist to protect fundamentally different interests and, in the absence of the physical presence rule, merit distinct analyses.

29. *Id.* at 306, 311.

30. *Id.* at 308.

31. *Id.* at 307–08. For further discussion of how jurisdictional Due Process analysis shapes the Due Process analysis for the validity of state taxes, see *infra* Part II.D.

for Commerce Clause purposes.[32]

B. Internet Retailers and the Court's Response in Wayfair

In the quarter century following the Court's decision in *Quill*, the country's economic landscape changed even more dramatically than it did in the years between *Bellas Hess* and *Quill*. This is primarily due to the enormous success and expansive reach of internet-based retailers.[33] These online sellers have the substantial advantage of reaching customers all over the country while maintaining incredibly few physical facilities relative to the amount of business they conduct. Because of the states' inability to tax internet sales, which were rapidly becoming a major element of the economy's retail sector, state governments frequently attempted to find creative ways around the physical presence rule in their efforts to tax internet commerce.[34] These methods were understandably complex and difficult to administer. All of these developments underscored the increasing desperation of state governments to obtain jurisdiction to tax these online sellers directly, eventually leading some states to blatantly disregard the rule and pass laws which would allow the state to set tax collection requirements on purely out-of-state sellers.[35]

One such state was South Dakota. In 2016, after declaring a state of emergency, South Dakota passed a law requiring "out-of-state sellers to collect and remit sales tax as if the seller had a physical presence in the state."[36] However, "[t]he Act applies only to sellers that, on an annual basis, deliver more than $100,000 of goods or services into the State or engage in 200 or more separate transactions for the delivery of goods or services into the State."[37] The tax did not apply retroactively.[38] Three companies, Wayfair, Inc., Overstock.com, Inc., and Newegg, Inc., challenged the constitutionality of the law when South Dakota attempted to force them to collect these taxes.[39]

When all was said and done, the *Wayfair* Court chose to overrule *Quill*.[40] The majority of the Court's opinion in *Wayfair* was devoted to its reasoning for doing so.[41] First, the Court explained the precedent underlying the Dormant Commerce Clause doctrine.[42] The Court concluded this section by noting the "two primary principles that mark the boundaries of a State's authority to regulate interstate commerce. First, state regulations may not discriminate against interstate commerce; and second, States may not

32. *See Quill Corp.*, 504 U.S. at 310–18 (explaining that *Complete Auto* did not overrule *Bellas Hess*).

33. *See* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2097 (2018) (noting the enormous changes in the national economy brought on by the internet era).

34. Such efforts included a Massachusetts regulation which defined physical presence as including a company placing "cookies" on the web browsers of state residents. 830 MASS. CODE REGS. 64H.1.7(1)(b)(2)(a) (2019). For some discussion of these state efforts to tax internet sellers in a world controlled by the physical presence rule, see *Wayfair*, 138 S. Ct. at 2097–98.

35. This desperation is further displayed by the fact that 41 states, two territories, and the District of Columbia collectively asked the Court to overrule *Quill*. *See generally* Brief for Colorado et al. as Amici Curiae Supporting Petitioner, South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018) (No. 17-494).

36. *Wayfair*, 138 S. Ct. at 2088–89 (internal quotation marks omitted).

37. *Id.* at 2089.

38. *Id.*

39. *Id.*

40. *Id.* at 2099.

41. *See generally Wayfair*, 138 S. Ct. 2080.

42. *Id.* at 2089–91.

impose undue burdens on interstate commerce."[43] The Court then briefly explained that these principles sit at the heart of Commerce Clause restrictions on state tax jurisdiction, and specifically outlined the analytical framework of these cases, drawing from *Complete Auto Transit, Inc. v. Brady*.[44]

Having articulated the analytical framework of the Commerce Clause's limits on states' ability to tax interstate sales, the Court's next endeavor was to explain its criticism of the physical presence rule.[45] First, the Court explained three reasons why it believed the decision in *Quill* was facially incorrect: (1) the physical presence rule is unnecessary to prevent undue burdens on interstate commerce because the framework for preventing these burdens works without the bright-line rule, (2) the physical presence rule created market distortions by unjustly favoring remote sellers, and (3) recent Commerce Clause decisions have favored case-by-case review over bright-line rules as a general policy matter.[46] In establishing these factors, the Court spent a great deal of time focusing on fairness concerns—how the physical presence rule treated like retailers differently purely on the basis of whether the retailer did its business online or in a physical store.[47] After this, the Court criticized how even the *Quill* Court noted "that the physical presence rule is artificial at its edges."[48] The Court further noted that the arbitrary nature of the *Quill* decision has only become more harmful as internet sellers rose to prominence.[49] The final criticism which the Court levied at the physical presence rule was that the rule was doing actual, significant harm to the states.[50]

Having firmly laid out why the *Quill* decision was wrong and the physical presence rule should fall, the Court next wrestled with *stare decisis*' demands.[51] In doing so, the Court stressed (1) the need to remedy a manifest injustice caused by the Court's own decisions, (2) the fact that the changing American economy made the physical presence rule far more egregiously harmful, (3) the increasingly unworkable nature of the physical presence standard in an economy dominated by e-commerce, and (4) the relative lack of any reliance by small businesses on the existence of the physical presence rule.[52]

Through this process, the Court put the physical presence rule to rest and remanded the case for further consideration.[53] Since the physical presence rule was in effect when the South Dakota Supreme Court ruled on the issue initially, there was no argument regarding whether the law failed the demands of the Commerce Clause in some other way.[54] But, the Court did provide the South Dakota courts with some guidance on the question. The Court determined that the minimum substantial nexus of contact standard from *Complete Auto* was definitively satisfied by the South Dakota law, because it applied only to sellers with more than $100,000 of sales in the state or more than 200

43. *Id.* at 2090–91.
44. *Id.* at 2091–92.
45. *Id.* at 2092.
46. *Wayfair*, 138 S. Ct. at 2092–95.
47. *Id.*
48. *Id.* at 2095 (quoting Quill Corp. v. North Dakota, 504 U.S. 298, 315 (1992)) (internal quotation marks omitted).
49. *Id.* at 2095.
50. *Id.* at 2095–96 ("In the name of federalism and free markets, *Quill* does harm to both.").
51. *Wayfair*, 138 S. Ct. at 2096–99.
52. *Id.*
53. *Id.* at 2099–100.
54. *Id.* at 2099.

individual sales in the state.[55] The Court also noted that these limits, designed so the tax would only apply to foreign sellers with a substantial amount of economic activity in the state, along with the fact that South Dakota is one of the states which passed the Streamlined Sales and Use Tax Agreement, tend to show that the tax was explicitly designed to prevent any undue burden on interstate commerce.[56]

C. The Dormant Commerce Clause

The main constitutional restriction on the states' tax power is the Commerce Clause. The Commerce Clause declares that "Congress shall have the power . . . [t]o regulate commerce with foreign nations, and among the several states, and with the Indian tribes."[57] The Supreme Court has long interpreted the Commerce Clause to not only vest the power to regulate interstate commerce with Congress, but also remove that power from the states.[58] This secondary effect, commonly referred to as the Dormant or Negative Commerce Clause, first appeared in *Gibbons v. Ogden*.[59] The Dormant Commerce Clause has developed along two distinct lines since *Ogden*. The first line of cases stands for the principle that states cannot pass laws which discriminate against interstate commerce.[60] The second line, which the physical presence rule was based on, prevents states from passing laws which impose an undue burden on interstate commerce.[61]

The Court succinctly stated the general rule for these undue burden cases in *Pike v. Bruce Church, Inc.*[62] The *Pike* balancing test, as it is generally referred to, sets the burden imposed by the state regulation against the benefit which the regulation provides to the state; then, the court upholds the law if the state benefit outweighs the burden on interstate commerce.[63] However, as the Court made clear in *Wayfair*, the *Pike* balancing test does not apply to state tax cases.[64] Instead, the Court follows the rule stated in *Complete Auto Transit, Inc. v. Brady*.[65] The *Complete Auto* rule says a state tax meets the requirements of the Dormant Commerce Clause—and therefore does not constitute an undue burden on interstate commerce—when it "is applied to an activity with a

55. *Id.*

56. *Wayfair*, 138 S. Ct. at 2099–100. The Streamlined Sales and Use Tax Agreement is a type of uniform law created to simplify and standardize state sales and use taxes and, by extension, significantly reduce tax compliance costs for businesses engaging in commerce between the member states. *About Us: The Streamlined Sales Tax Governing Board*, STREAMLINED SALES TAX GOVERNING BOARD, INC., https://www.streamlinedsalestax.org/index.php?page=About-Us (last visited Nov. 25, 2018).

57. U.S. CONST. art. I, § 8, cl. 3.

58. Gibbons v. Ogden, 22 U.S. 1, 13 (1824) ("We do not find . . . that any man speaks of a general *concurrent power*, in the regulation of foreign and domestic trade, as still residing in the States. The very object intended, more than any other, was to take away such power.") (emphasis in original).

59. *Id.*

60. *See, e.g.*, Bacchus Imps., Ltd. v. Dias, 468 U.S. 263, 268 (1984) (explaining that direct discrimination against interstate commerce violates the Commerce Clause).

61. *See, e.g.*, Huron Portland Cement Co. v. City of Detroit, 362 U.S. 440, 443 (1960) (explaining that even an "evenhanded" regulation promoting a "legitimate local public interest" will not stand if it burdens interstate commerce).

62. Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970).

63. *Id.*

64. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2099 (2018) (noting that the Court would not address the *amicus* argument that *Pike* balancing should apply to state tax collection cases).

65. Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977).

substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State."[66]

The physical presence rule existed to serve the first prong of the *Complete Auto* test—the requirement of a substantial nexus of contact.[67] As such, the rest of this Note will focus primarily on the nexus requirement when discussing the Commerce Clause requirements. However, for the sake of fully understanding the purposes of the Dormant Commerce Clause generally and the *Complete Auto* test specifically, this Note must briefly introduce the other three requirements. First, the fair apportionment requirement generally exists to prevent the problem of double-taxation and to support the nexus of contact requirement in ensuring states cannot tax extraterritorial activity.[68] Next, the non-discrimination prong reflects the other half of the Court's general Dormant Commerce Clause jurisprudence.[69] Lastly, the fair relation requirement of the *Complete Auto* test exists to ensure that the state is providing some benefit to the taxed entity by limiting the scope of any tax to the extent of the taxed entity's contacts with the state.[70] These three additional requirements are important for legislatures to keep in mind when shaping their new laws to take advantage of the space opened by *Wayfair*. Just as it is often all too easy to lose one's vision of the forest for the trees, it would be easy for legislatures to make the mistake of forgetting about these other Commerce Clause concerns when rushing to capitalize on the absence of the physical presence rule.

D. The Due Process Clause

The 14th Amendment's Due Process Clause declares that "[n]o state shall . . . deprive any person of life, liberty, or property, without due process of law."[71] This provision is a workhorse in the Constitution, serving a plethora of purposes in modern constitutional law. The most relevant of these purposes for this Note is the restriction on the states' power to reach outside of their territorial limits. As displayed by *Quill Corp. v. North Dakota*, the Due Process Clause imposes limits on the states' power to tax out-of-state entities essentially parallel to the states' power to exercise personal jurisdiction over out-of-state entities.[72]

The Supreme Court explicitly noted these personal jurisdiction limits in *International Shoe Co. v. Washington*.[73] The core concept at the heart of *International Shoe* is that Due Process prevents states from exercising personal jurisdiction over entities which "have certain minimum contacts with it such that the maintenance of the

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66. *Id.*

67. *Wayfair*, 138 S. Ct. at 2085 (2018).

68. Bradley W. Joondeph, *The Meaning of Fair Apportionment and the Prohibition on Extraterritorial State Taxation*, 71 FORDHAM L. REV. 149, 159 (2002). Professor Joondeph's article is also useful as a general overview of the fair apportionment requirement.

69. *See* Bacchus Imps., Ltd. v. Dias, 468 U.S. 263, 268 (1984) (explaining that non-discrimination is an essential element of the Dormant Commerce Clause doctrine).

70. Commonwealth Edison Co. v. Montana, 453 U.S. 609, 626 (1981) ("[T]he fourth prong of the *Complete Auto Transit* test imposes the additional limitation that the *measure* of the tax must be reasonably related to the extent of the contact.").

71. U.S. CONST. amend. XIV, § 1.

72. Quill Corp. v. North Dakota, 504 U.S. 298, 307–08 (1992).

73. *See generally* Int'l Shoe Co. v. Washington, 326 U.S. 310 (1945) (laying out the analytical framework for personal jurisdiction requirements).

suit does not offend traditional notions of fair play and substantial justice."[74] The Court then broke down two methods to achieve minimum contacts. The first method, commonly referred to as general *in personam* jurisdiction, allows a state to exercise jurisdiction over an entity for any purpose if the entity meets the nexus of contact requirement.[75] The second method, generally known as specific *in personam* jurisdiction, allows a state to exercise jurisdiction over an entity based on a relaxed nexus of contact if the exercise is based on the contacts the entity has with the state.[76]

While general *in personam* jurisdiction is an important concept for defining the limits on a state's power to tax generally, it is less important for defining the extent of the state's ability to require a foreign seller to collect and remit sales tax. This ought to be readily apparent because a sale is a specific activity—or exercise of privilege—which a seller conducts. Therefore, to use the Court's terminology, a tax on a sale is, by necessity, an obligation based on that exercise of privilege.[77] So, one needs to analyze developments in specific *in personam* jurisdiction to see the due process limits on a state's power to tax foreign sales.

In addition to the concerns of "traditional notions of fair play and substantial justice" articulated in *International Shoe*, the Court has referred to the due process requirements for the exercise of jurisdiction as a stand-in for notice.[78] This view was particularly favored by Justice Stevens in *Shaffer v. Heitner*.[79] A key concept of the Due Process Clause's notice conception is the requirement "in each case that there be some act by which the defendant purposefully avails itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws."[80] The Court later extrapolated on the purposeful availment requirement in *Burger King Corp. v. Rudzewicz*, stating that "[t]his purposeful availment requirement ensures that a defendant will not be haled into a jurisdiction solely as a result of random, fortuitous, or attenuated contacts . . . or of the unilateral activity of another party or a third person."[81] Thus, synthesizing a rule out of these principles, a state can only levy a sales or use tax collection responsibility on an entity when: (1) the entity purposefully directs its actions toward the state, (2) the tax is on the entities actions in that state, and (3) the tax does not offend traditional notions of fair play and substantial justice.

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74. *Id.* at 316 (quoting Milliken v. Meyer, 311 U.S. 457, 463 (1940)) (internal quotation marks omitted).

75. *See id.* at 318 (explaining that "there have been instances in which the continuous corporate operations within a state were thought so substantial and of such a nature as to justify suit against it on causes of action arising from dealings entirely distinct from those activities").

76. *Id.* at 319 ("But to the extent that a corporation exercises the privilege of conducting activities within a state, it enjoys the benefits and protection of the laws of that state. The exercise of that privilege may give rise to obligations; and . . . a suit brought to enforce them can, in most instances, hardly be said to be undue.").

77. This concept has not been formally recognized by the Supreme Court. The soundness of this logic is, however, supported by the fact that the Court in *Quill*, when initially developing the differing standards for the Commerce and Due Process Clauses, relied heavily on *Burger King Corp. v. Rudzewicz*. *Quill Corp.*, 504 U.S. at 306–08. *Burger King* is generally considered to be a highly important case for the development of specific *in personam* jurisdiction. *See* JOSEPH W. GLANNON ET AL., CIVIL PROCEDURE: A COURSEBOOK 205–12 (3d ed. 2017) (including *Burger King* as a case of note in a chapter devoted to specific *in personam* jurisdiction).

78. Shaffer v. Heitner, 433 U.S. 186, 217–19 (1977) ("The requirement of fair notice . . . includes fair warning that a particular activity may subject a person to the jurisdiction of a foreign sovereign.") (Stevens, J., concurring in judgment).

79. *Id.*

80. Hanson v. Denckla, 357 U.S. 235, 253 (1958).

81. Burger King Corp. v. Rudzewicz, 471 U.S. 462, 475 (1985) (internal quotation marks omitted).

III. ANALYSIS

A. The Requirements of the Commerce and Due Process Clauses

As previously discussed, the primary constitutional limits on a state's ability to require foreign corporations to collect and remit sales and use taxes come from the Commerce and Due Process Clauses. When the physical presence rule was first announced in *Bellas Hess*, the nexus of contact requirement for out-of-state sellers was identical under both clauses.[82] However, the Court in *Quill* divided the analysis of claims brought under the two clauses.[83] So, after *Wayfair*, one immediately apparent question is whether this divide between the two standards still exists.

The argument that the two standards have merged again following *Wayfair* is relatively straightforward. First, since *Quill* articulated the divide between the two standards and *Wayfair* overruled *Quill*, the origin of the divide is no longer good law.[84] Second, the Court in *Wayfair* said very little about the Due Process standard for state taxation of interstate sales, and instead looked only to the Commerce Clause standard articulated in *Complete Auto*.[85] Third, the language of the two requirements is substantially similar.[86] Finally, the Court has, in the past, explicitly stated that the Commerce Clause requirements tend to absorb due process demands.[87] Based on this argument, it is reasonable to believe that the requirements of the Commerce and Due Process Clauses have once again merged into a single nexus requirement.

However, as tempting as it is to look for a way to simplify these standards by applying a single analysis, the two standards are different at their core. The limits imposed by the Due Process and Dormant Commerce Clauses have fundamentally different objectives, and therefore must ask states to meet different demands.[88] The Dormant Commerce Clause is concerned with the free flow of commerce between the states.[89] By contrast, the Due Process Clause is concerned with the fairness of a state to requiring a foreign citizen to pay taxes in the state.[90] Further, while the Court in *Wayfair* noted there are "significant parallels" between the demands of the two clauses, they first prefaced the statement by acknowledging that the "standards may not be identical or coterminous."[91] Thus, in order to guarantee that the aims of both clauses are sufficiently protected, one needs to treat the two clauses differently—and articulate distinct tests for each.

But, if the two concepts are different, what are those differences? To determine this, one should, as a principal matter, identify what each standard demands in the first

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82. Nat'l Bellas Hess v. Dep't of Revenue of Ill., 386 U.S. 753, 756 (1967) (noting that claims under the Commerce Clause and claims under the Due Process Clause, with regard to the validity of a state sales or use tax levied on an out-of-state seller, are "closely related").

83. Quill Corp. v. North Dakota, 504 U.S. 298, 312 (1992) ("Despite the similarity in phrasing, the nexus requirements of the Due Process and Commerce Clauses are not identical.").

84. *Id.*; South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2099 (2018).

85. *Wayfair*, 138 S. Ct. at 2099–100.

86. *Quill Corp.*, 504 U.S. at 312.

87. *Id.* at 313 n.7.

88. *Id.* at 312.

89. *Id.*

90. *Id.*

91. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2093 (2018).

place.[92] The *Complete Auto* test still controls the demands of the Dormant Commerce Clause with regard to state taxation of interstate commerce.[93] The *Complete Auto* test requires a tax to be (1) "applied to an activity with a substantial nexus with the taxing state," (2) "fairly apportioned," (3) non-discriminatory against interstate commerce, and (4) "fairly related to the services provided by the State."[94] As noted above, a tax which meets the requirements of this four-part test will not impose an undue burden on interstate commerce.[95]

The precise demands of the Due Process Clause are somewhat more difficult to articulate.[96] The Due Process analysis in *Quill* was based entirely on parallels to corporate *in personam* jurisdiction.[97] These cases lead to some general principles which must be honored in the Due Process analysis. For one, it does not violate Due Process to subject a company to state action when said company has "certain minimum contacts with [the state] such that" doing so "does not offend traditional notions of fair play and substantial justice."[98] Additionally, Due Process requires the "commercial actor's efforts [to be] purposefully directed" into the taxing state.[99]

While the differences between these requirements in general are obvious, the differences between the Commerce Clause's substantial nexus requirement and the Due Process Clause's minimum contacts requirement are subtle. The similarities between the nexus and minimum contacts requirements are the primary focus of the merger debate. However, the reasons for dividing the two standards which the Court articulated in *Quill* remain valid. In *Quill*, the Court noted that the primary reason for acknowledging a difference between the two lies in the essential purposes of the two clauses.[100] Specifically, the Court said "the substantial nexus requirement is not, like due process' minimum contacts requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce."[101] This statement lies at the core of the distinction.

A couple of examples may help illustrate the point. First, consider Retailer, a corporation based entirely in State A. Retailer is incorporated in State A, has a number of administrative offices in State A, a number of warehouses in State A, and only hires employees who are residents of State A. Retailer makes its sales primarily through its website which does not leave any "cookies" on the computers of people visiting it. Then, Retailer packages its products at its warehouses and solicits a common carrier to deliver its products to its customers. Retailer engages in limited television advertising, but only purchases advertising time on local stations within State A. Those stations almost

92. What follows in this paragraph and the next is a summary of key points from Part II.

93. For discussion of the limits on state taxation imposed by the Commerce Clause, see *supra* Part II.C.; *Wayfair*, 138 S. Ct. at 2091.

94. Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977).

95. *See supra* Part II.C (explaining the requirements of the Dormant Commerce Clause in greater detail).

96. For a more thorough articulation of the Due Process Clause concerns in state taxation, see *supra* Part II.D.

97. *See* Quill Corp. v. North Dakota, 504 U.S. 298, 307–08 (tracing the development of corporate *in personam* jurisdiction through *International Shoe Co. v. Washington*, *Shaffer v. Heitner*, and *Burger King Corp. v. Rudzewicz* and applying the principles articulated in these cases to taxing interstate sales).

98. Int'l Shoe Co. v. Washington, 326 U.S. 310, 316 (1945) (citing Milliken v. Meyer, 311 U.S. 457, 463 (1940)) (internal quotation marks omitted).

99. Burger King Corp. v. Rudzewicz, 471 U.S. 462, 476 (1985) (internal quotation marks omitted).

100. *Quill Corp.*, 504 U.S. at 313.

101. *Id.* (internal quotation marks omitted).

exclusively serve viewers in State A. Because of this, Retailer's sales stem mostly from State A. Retailer makes some sales to customers in other states, including State B, but these sales are negligible.

Because Retailer is looking to expand its business, Retailer begins to purchase advertising time from a television station which primarily serves State B. However, due to an economic downturn, the quantity and value of the sales which Retailer makes in State B do not substantially change. In this case, if the two clauses' primary concerns are controlling on the matter, Retailer should have sufficient contacts with State B to satisfy the Due Process Clause, but it should not have the substantial nexus of contact required by the Commerce Clause. Retailer has minimum contacts with State B under the theory that Retailer took sufficient steps to avail itself of the benefits of doing business in State B, thus satisfying the notice and fairness demands of the Due Process Clause. But, Retailer does not have a substantial nexus of contact with State B because Retailer makes only minimal sales in State B. The general understanding of the substantial nexus requirement is that it is satisfied if the totally absent seller has a significant economic presence in the state, because the nexus requirement is based on the requirement that a state cannot place an undue burden on interstate commerce.[102]

Consider in the alternative the same Retailer. However, Retailer does not purchase additional advertising targeting State B. Instead, trends in societal taste cause Retailer's products to suddenly become immensely popular in State B, and both the value and quantity of their sales in State B skyrocket. Under these circumstances, it should be clear that, if the distinct purposes of the two separate clauses are to be honored, Retailer should not have minimum contacts with State B to satisfy Due Process demands but should have a substantial nexus of contact with the state to satisfy the Commerce Clause requirements. This result follows from the same reasoning as above: the Commerce Clause's nexus requirement is based on economic presence within the state, while the Due Process Clause's minimum contact requirement is based on deliberate action to participate in the state's markets.

In sum, the Dormant Commerce and Due Process Clauses ought to be considered as distinct, alternative limitations on the states' power to require extraterritorial sellers to collect and remit sales or use taxes. This argument lies in the idea, made apparent by the examples above, that extreme corner cases may exist where considering the two requirements as one would cause the fundamentally differing interests protected by those clauses to go unguarded. If the two requirements were merged into one standard by the *Wayfair* decision, the Due Process requirements would ostensibly disappear into the Dormant Commerce Clause.[103] This would cause the retailer in the second version of the hypothetical presented above, who makes a great deal of sales in a foreign jurisdiction without intentionally directing their conduct into that state, to become subject to the

102. This understanding is often referred to as the "economic nexus" principle. For a more thorough discussion of economic nexus, see generally Adam B. Thimmesch, *The Illusory Promise of Economic Nexus*, 13 FLA. TAX REV. 157 (2012).

103. This is displayed by the fact that *Wayfair* itself makes only minimal reference to the Due Process limits. *See generally* South Dakota v. Wayfair, Inc., 138 S. Ct. 2080 (2018). If one of the requirements were to fade into the other, it makes more sense for the dominant requirements to be those explicitly referenced as controlling by the Court in *Wayfair*: those of the Dormant Commerce Clause. *See id.* at 2099–100 (referencing *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), which articulated the Dormant Commerce Clause limits on states' power to tax generally, as controlling).

taxing power of the foreign state without the guarantee of essential fairness which the Due Process Clause entitles them to. Accordingly, in order to accurately provide for the interests guaranteed by both constitutional provisions, the Dormant Commerce and Due Process Clauses ought to be considered separately when evaluating whether a foreign seller should be subject to a foreign state's power to require sellers to collect and remit sales and use taxes to them.

B. Policies Coloring Taxation of Sales by Foreign Companies

The second set of limitations on the states' ability to tax interstate commerce come from general principles of public policy. These policy elements either manifest themselves laterally through the protections of the two constitutional clauses discussed previously or they are self-imposed by the states. Regardless, a proper understanding of how to move forward in the absence of the physical presence rule requires some understanding of the central policy arguments in these debates. Four elements of public policy tend to appear in discussions about how state taxation of interstate commerce ought to be treated more often than others: (1) the states' need to draw revenue from interstate commerce in a world where internet retailers are increasingly dominant, (2) the potential for businesses to be taxed by more than one state for the same transaction, (3) the high compliance costs for businesses subject to taxation in several jurisdictions, and (4) the importance of protecting small and startup businesses who seek to take advantage of the internet as a means for growth.

1. The States' Need for Revenue

The first key policy consideration lurking in the background of these discussions is the states' revenue needs. This is a relatively straightforward concern. States spend a great deal of money on everything from courthouses and police officers to utilities and construction projects. The states in turn, quite obviously, require a significant amount of money to afford these expenditures. This policy concern was one of the driving motivations in the Court's decision to abandon the physical presence rule in *Wayfair*.[104]

In fact, the Court estimated the states, in aggregate, lost "$8 to $38 billion" of sales tax revenue per year on account of the physical presence rule.[105] Professor Holderness also stressed the massive amount of revenue which states were losing, estimating states lost $11.4 billion in 2012.[106] Professor Holderness noted that this was, understandably, one of the driving forces behind the creation of a large, vocal group of policymakers commonly referred to as the "Kill *Quill*" movement.[107] The Court in *Wayfair* also noted that the rise to prominence of Internet sellers was another significant factor in this loss of revenue, and another motivating factor for abandoning the physical presence rule.[108] This shows the extreme weight which the Court places on the states' income needs, and for good reason.

104. *See Wayfair*, 138 S. Ct. at 2097 (discussing the importance of the states' lost income as a compelling factor for overcoming s*tare decisis*).

105. *Id.*

106. Hayes R. Holderness, *Questioning Quill*, 37 VA. TAX REV. 313, 322 (2018).

107. *Id.* at 322–23.

108. *Wayfair*, 138 S. Ct. at 2097.

2. The Double-Tax Issue

The double-tax issue refers to the idea that a seller could be liable for a tax twice for the same transaction. In general, the instance of a double-tax which tends to be the most troubling is the double-tax which could occur if two states apportion their sales and use taxes in such a way as to expose a seller to tax liability for the same sale in both states. For example, if State A taxes all sales made by businesses present in their state and State B levies a use tax on all sales to citizens of State B, then a seller based in State A selling to a customer in State B would be taxed in both states for the same transaction.

Double-taxation is a problem because it places sellers doing business across state lines at a severe disadvantage to wholly in-state sellers. As a matter of policy, states should take steps to avoid creating double-taxes for the businesses in their state to ensure that their businesses are competitive with businesses based in other states. After all, in a world where doing business across state lines is the norm, a state which imposes a double sales tax burden on its own sellers may dis-incentivize their businesses from participating in the ever-expanding interstate market, thereby reducing their own tax income. However, policy is not the only concern with creating a double-tax burden. The severe burden double-taxation places on interstate sellers is reflected by the fair apportionment requirement of the *Complete Auto* test, which is specifically aimed at preventing these problematic double taxes.[109] Thus, as a matter of constitutional law, states not only ought to avoid creating these burdens, but must do so.

3. The Compliance Burdens of Multi-State Taxation

Tax codes are complicated beasts. This is not a controversial assertion. Even dedicated accounting firms find it difficult to help businesses comply with sales and use taxation in multiple states.[110] Thus, it is unrealistic to think businesses, especially small and startup businesses which tend to be unsophisticated, could manage compliance on their own. This reality has a deterrent effect on business growth because being exposed to taxation in more than one jurisdiction will force the business to deal with more than one of these complex tax codes. A business may reasonably worry that any increase in compliance costs from managing more than one state's tax schemes, along with the general increase in expenses related to expanding, would outweigh the revenue gained from the new venture. Similarly, businesses may worry that using the Internet to expand and promote their business would push their business into additional states and expand their tax compliance costs beyond what the business could handle.

These concerns lie at the heart of the multistate tax compliance issue, and were even recognized by the Court in *Wayfair*.[111] However, the Court also noted that these costs may be decreasing due to the development of tax compliance software.[112] Despite this, such cost-saving software does not appear to exist yet in an effective and inexpensive

109. Joondeph, *supra* note 68, at 150.

110. *See* Peter J. Reilly, *Why Is Multi-State Tax Compliance So Hard?*, FORBES (June 12, 2015, 9:23 AM), https://www.forbes.com/sites/peterjreilly/2015/06/12/why-is-multi-state-tax-compliance-so-hard/#71d896446d99 (noting that it is difficult for accounting firms to comply with state sales and use taxes in general).

111. *Wayfair*, 138 S. Ct. at 2098 ("These burdens may pose legitimate concerns in some instances, particularly for small businesses that make a small volume of sales to customers in many States.").

112. *Id.*

form, so states should still be concerned with reducing the compliance costs of their own sales and use tax scheme to both benefit their own state's businesses and to attract expanding business from other states.

4. The Importance of Protecting Small and Startup Businesses

Supporting small business necessarily fosters innovation and competition central to the concept of capitalism, solidifying the support for small business as a central tenet of business tax policy.[113] Small businesses also tend to be more supportive of the rural and suburban communities they tend to grow out of, a key failure of larger companies which tend to focus on more populous urban areas.[114] It is especially important to protect small businesses in the tax context, due to the enormous pressure taxes and tax compliance place on small business bottom-lines.[115] For these reasons, and to protect the idyllic image of the "self-made person" in American society writ large, the protection and promotion of small business entrepreneurship is a fundamental element of the policy discussion surrounding taxation on foreign sellers.

IV. RECOMMENDATIONS

With a thorough understanding of the constitutional rules and policy arguments governing state sales and use taxation of foreign sellers, the central question of this Note arises: how should states craft their sales and use tax laws to best take advantage of the new power to tax interstate sales without offending these remaining demands? Drafting legislation is often difficult, especially when the limits on the states' power to do so are as nebulous as they are here. The Supreme Court provided some, albeit minimal, guidance at the end of the *Wayfair* decision on what, in addition to the factors already articulated, the Court will look for to determine whether a law violates the Constitution.[116] However, this guidance is specifically limited to meeting the nexus requirement under the Dormant Commerce Clause and the general requirement that the tax not create an undue burden on interstate commerce.[117] This Part will first question whether it is desirable for states to attempt to reach as many sales as possible with their sales and use taxes. Then, this Part will consider what steps the states can take to maximize their reach without violating the Constitution by looking to the constitutional demands set out above and the guidance the Court provided in *Wayfair*.

A. The Policy Debate: Should the States Attempt to Reach Every Sale?

Before this Note analyzes how the States can tax as many transactions as possible, it must first consider whether they ought to. Make no mistake, this is a very difficult

113. Jose Vasquez, *Why are Small Businesses So Important for the Economy?*, HUFFPOST (Apr. 18, 2017, 10:17 AM), https://www.huffingtonpost.com/entry/why-are-small-businesses-so-important-for-the-economy_us_58f61f9ae4b048372700db75.

114. *Id.*

115. For a discussion of how the federal tax code places a significant burden on small businesses, see Rafael Efrat, *The Tax Burden and the Propensity of Small-Business Entrepreneurs to File for Bankruptcy*, 4 HASTINGS BUS. L.J. 175, 180–85 (2008).

116. *Wayfair*, 138 S. Ct. at 2099–100 (2018).

117. *Id.*

question. The case for reaching as many sales as possible is very strong. State governments provide several essential services, many of which are aimed at providing for their neediest citizens, and these services require extensive funding. The need for government revenue is a venerable one. George Washington, in his farewell address, famously declared that "towards the payment of debts there must be revenue; that to have revenue there must be taxes; [and] that no taxes can be devised which are not more or less inconvenient and unpleasant."[118] The need for revenue was one of the issues which caused the founding generation to abandon the Articles of Confederation and adopt the Constitution.[119] Even sources as ancient as the Bible display the need for government funding, declaring that people should "[r]ender to Caesar the things that are Caesar's."[120]

But, ultimately, it seems the states should not attempt to reach every possible sale with their taxation schemes. Equally ancient as the concern for government revenue is the legal maxim *quod omnes tangit ab omnibus approbetur*, or "[w]hat touches all must be decided by all."[121] The concern that foreign sellers are being exposed to legal responsibilities which they had no say in establishing is an ever-present concern when discussing these sales tax regimes.[122] Now, fairness concerns like this are muted in the case of major national or international sellers who do a great deal of business in the state. A state may safely expose these sellers to sales tax liability without the need to worry about if it is just to do so. But, in the case of small to mid-sized businesses which deal in only a limited fashion with the taxing state, there is something distinctly unfair about requiring them to learn the nuances of a new tax regime just because a handful of that state's citizens wanted to purchase their products.[123]

Of course, the constitutional requirements for a state to lay a tax collection requirement on a seller, especially the Due Process Clause requirements, are primarily designed to prevent this fundamental injustice. Thus, states are capable of reaching most, if not all, sales by foreign entities within the constitutional limits of their power to do so without being unfair. Nonetheless, states ought to exercise some amount of restraint when taking advantage of the new space that *Wayfair* opened for them.

Of course, the extent to which states should exercise discretion in utilizing their new

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118. George Washington, *Washington's Farewell Address 1796*, THE AVALON PROJECT (1796), http://avalon.law.yale.edu/18th_century/washing.asp (last visited Nov. 24, 2018).

119. *See* THE FEDERALIST NO. 15 (Alexander Hamilton) (listing the shortcomings of the Articles of Confederation).

120. *Mark* 12:17 (King James).

121. *Roman Law*, *in* EUROPE, 1450 TO 1789: ENCYCLOPEDIA OF THE EARLY MODERN WORLD (2004), https://www.encyclopedia.com/social-sciences-and-law/law/law-divisions-and-codes/roman-law (last visited Nov. 24, 2018).

122. *See* Edward A. Zelinsky, *Rethinking Tax Nexus and Apportionment: Voice, Exit, and the Dormant Commerce Clause*, 28 VA. TAX REV. 1, 3–4 (2008) ("Taxation is an inherently and irreducibly political matter. . . . A physical presence test for tax nexus thereby protects, albeit imperfectly, against the modern version of taxation without effective representation.").

123. Note that the fairness concerns in taxation of foreign entities ultimately all return to the issue of taxation without adequate representation. *See id.* at 49–50. The larger the seller, the more muted this concern becomes due to the increase in political bargaining power of the foreign seller. As much of the commentary on *Citizens United v. F.E.C.* suggests, corporations have an "unnatural ability . . . to amass wealth," and this ability tends to lead to disparate bargaining power in the political process. *See, e.g.*, Samuel Issacharoff, *On Political Corruption*, 124 HARV. L. REV. 118, 122 (2010) (representing the larger commentary on *Citizens United*). As such, fairness concerns based on the inadequate representation of a foreign seller in the taxing state's political system are less relevant in the context of major sellers.

power to reach foreign sellers is ultimately unclear. Substantial size and quantity of sale limitations akin to those in South Dakota's law might act as a convenient starting point for these evaluations.[124] But, ultimately, each state's evaluation of the extent to which it wishes to protect these interests is one they are entitled to make. The purpose of this Part is not to suggest that states must forego significant portions of their otherwise-accessible revenue. This Note's purpose is merely to suggest that state legislatures ought to pause and think carefully about how, exactly, to balance these interests rather than rush to grab as much revenue as possible in the absence of the physical presence rule.

B. General Adherence to the Commerce and Due Process Clauses

For the states deciding they would like to tax as many transactions as possible within their state, the first thing to note is that the demands of the Dormant Commerce Clause have traditionally been more important when striking down state taxes than the demands of the Due Process Clause. For instance, the Court in *Quill* seemed to suggest the Due Process Clause limits were essentially irrelevant when determining the validity of a state sales or use tax.[125] While this is not, or should not be, a completely accurate statement of the relationship between the Commerce Clause and Due Process Clause limits on state sales and use taxation, it is illustrative of the fact that the Commerce Clause limits tend to be much more rigorous and, accordingly, receive the most attention.[126] It is also likely the most practical way of analyzing whether a state tax violates the demands of the Constitution.[127]

Another thing to keep in mind is that the Commerce Clause's demands are not set in stone. The nature and origin of the Dormant Commerce Clause doctrine allow Congress to, at any time, alter the Commerce Clause's requirements for a state to be able to tax interstate transactions.[128] This is because the Dormant Commerce Clause limits on state power are implied in an affirmative grant of power to Congress rather than explicitly declared as a limit on the powers of the states.[129] Of course, Congress actually making changes to what states need to do in order to satisfy Commerce Clause requirements when taxing interstate sales seems unlikely, given Congress' traditional refusal to do so.[130] However, it would be ideal if Congress were to articulate the limits on states' power to tax interstate sales. After all, Congress is better positioned than the courts to

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124. *See* S.D. CODIFIED LAWS § 10-64-2 (2018) (listing the criteria for an out-of-state seller to be required to collect and remit sales and use taxes to South Dakota).

125. Quill Corp. v. North Dakota, 504 U.S. 298, 313 n.7 (1992) ("We have sometimes stated that the *Complete Auto* test, while responsive to Commerce Clause dictates, encompasses as well . . . due process requirement[s].") (internal quotation marks omitted).

126. For a discussion of how the Commerce Clause and Due Process Clause requirements ought to interact, see *supra* Part III.A.

127. For a discussion outlining the impracticalities of legislating the Due Process Clause requirements and suggesting that the Due Process Clause limits should best be upheld through as-applied challenges to state tax laws, see *infra* Part IV.B.II.

128. White v. Mass. Council of Constr. Emp'rs, Inc., 460 U.S. 204, 213 (1983) ("Where state or local government action is specifically authorized by Congress, it is not subject to the Commerce Clause even if it interferes with interstate commerce.").

129. *Id.*

130. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2090 ("[T]his Court has observed that 'in general Congress has left it to the courts to formulate the rules' to preserve 'the free flow of interstate commerce.'") (quoting S. Pac. Co. v. Arizona, 325 U.S. 761, 770 (1945)).

make policy judgments about what level of protection from state taxation interstate businesses deserve. Additionally, the improved accountability of having these decisions made by an elected body is always a good thing. A Congressional statute articulating the Commerce Clause limits should help to make tax liabilities clearer for interstate businesses. Additionally, Congress doing so would solidify the line between the Commerce Clause limits—which are subject to Congressional alteration—and the Due Process Clause limits—which are immutable.

1. Adhering to the Dormant Commerce Clause

As it stands now, the single largest requirement for a state tax on foreign sales is that it not discriminate against interstate commerce. This requirement was explicitly noted in *Complete Auto*, and it lies at the heart of the Dormant Commerce Clause's requirements.[131] As important as this requirement is, it is equally easy to adhere to. States should simply avoid taxing foreign companies' sales at a higher rate than purely intrastate sales. States should also avoid taxing the sales of specific goods at particularly high rates when those goods are not produced by businesses in the state, since the Court may see such taxes as intentionally discriminatory against interstate commerce like in *Bacchus Imports, Ltd. v. Dias*.[132] So, adherence to this particular requirement of the Dormant Commerce Clause is as easy as setting a single rate for sales and use taxes and only setting excise taxes which do not intrinsically favor in-state businesses.

The next two requirements of the *Complete Auto* test—that a tax be fairly apportioned and fairly related to services rendered by the state—are also fairly easy to meet in the context of sales taxes.[133] A sales tax is, essentially, always "fairly related to the services provided by the State" because the services which the state provides are all related to providing the seller with a market for their product.[134] Additionally, the fair apportionment requirement is generally met by a sales or use tax so long as it avoids creating a double tax liability for a single transaction and the taxing state only levies a tax on the portion of the transaction that is "fairly attributable to economic activity within the taxing State."[135] These requirements are generally referred to as the requirement of internal consistency and the requirement of external consistency, respectively.[136]

Avoiding a double-tax issue is logically simple. Imagine a world where every state passed the same tax. If this would cause the seller to be liable for tax on a single transaction in more than one state, then there is a double-tax or internal consistency

131. Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977).

132. *See generally* Bacchus Imps., Ltd. v. Dias, 468 U.S. 263 (1984) (striking down a Hawaii excise tax which applied to all liquor except a specific type of brandy produced from a plant indigenous to Hawaii).

133. *Complete Auto*, 430 U.S. at 279.

134. No readily available authority states this proposition directly, as there is precious little discussion of the fair relation prong in general. However, following the analytic framework established in *Commonwealth Edison Co. v. Montana*, the conclusion follows logically from the rule. The "operating incidence" of a sales or use tax will always be the sale. When discussing a sales or use tax levied on a foreign seller, it is a sale to a citizen of the taxing state. Therefore, a tax levied on the sale is fairly related to the conduct of the seller within the taxing state. *See* Commonwealth Edison Co. v. Montana, 453 U.S. 609, 626–27 (1981) (laying out this framework).

135. Okla. Tax Comm'n v. Jefferson Lines, Inc., 514 U.S. 175, 185 (1995).

136. *Id.*

problem.[137] The concept of external consistency, on the other hand, reflects the traditional conception of fair apportionment prior to the ideas of internal and external consistency.[138] While external consistency is more complex than internal consistency at the conceptual level, it is even easier to achieve in the sales tax context. "[A]n internally consistent, conventional sales tax has long been held to be externally consistent as well."[139] Thus, in the context of sales taxes, fair apportionment is defined entirely by the internal consistency analysis.

That leaves only one piece of the *Complete Auto* test left for the state to satisfy: the nexus requirement.[140] Here, the Court's guidance in *Wayfair* becomes relevant. The Court determined that South Dakota's law unequivocally satisfies the Commerce Clause's nexus requirement.[141] In deciding this, the Court determined that the South Dakota law's provision by which it "applies only to sellers that deliver more than $100,000 of goods or services into South Dakota or engage in 200 or more separate transactions for the delivery of goods and services into the State on an annual basis" was determinative.[142] The Court decided this provision ensured a company had sufficient economic contacts with the taxing state.[143]

Of course, the next self-evident question is where is the line? We know that South Dakota's 200 sales or $100,000 in sales provision hits the mark. We also know that a threshold provision like this is probably necessary for a law to satisfy the Commerce Clause's nexus requirement, since the presence of the threshold was the only substantial fact which the Court cited in deciding to uphold South Dakota's law.[144] But, what about a provision requiring only 100 sales or $50,000 in sales? Ultimately, this is the single greatest ambiguity in the *Wayfair* decision. And, unfortunately, the answer to the question of lower thresholds is one of judicial line-drawing, left to be answered on a case-by-case basis in the future. Prudent states wishing to insulate their new taxes against challenge should simply adopt the threshold requirements from South Dakota's law, since they are proven to be acceptable. In order to sort out what is unacceptable, we need to wait for a state to push the issue by passing a law with a lower threshold; though, this would almost be inviting a challenge to the law.

While the Court in *Wayfair* withheld judgment on whether any other requirement of the Dormant Commerce Clause would invalidate the law, they strongly suggested the law met constitutional muster.[145] In deciding this, the Court pointed out three features of South Dakota's law which tended to prevent the law from imposing an undue burden on interstate commerce.[146] The first of these is that the threshold provision of South Dakota's law grants a "safe harbor to those who transact only limited business in" the state.[147] While this point is a bit redundant after establishing the need for such a threshold

137. *Id.*

138. WALTER HELLERSTEIN ET AL., STATE TAXATION ¶ 4.16[2] (3d ed. 2019) ("The external consistency test in substance is nothing more than another label for the fair apportionment requirement.").

139. *Jefferson Lines*, 514 U.S. at 188.

140. Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977).

141. South Dakota v. Wayfair, Inc., 138 S. Ct. 2080, 2099 (2018).

142. *Id.*

143. *Id.*

144. *Id.*

145. *Id.*

146. *Wayfair*, 138 S. Ct. at 2099.

147. *Id.*

provision in order to meet the nexus requirement of the Dormant Commerce Clause, it does reassert just how important these provisions are and serves as further evidence that these safe harbor provisions truly are necessary for the law to pass muster under the Dormant Commerce Clause.

The second aspect of South Dakota's law which the Court pointed out as burden defeating is that the law is forward-looking; and, the Court's focus on this point suggests that any tax on a foreign seller which applies retroactively probably constitutes an undue burden on interstate commerce.[148] The law applies only to sales which occurred after its effective date.[149] Essentially, by saying that this element of South Dakota's law proves the absence of an undue burden, the Court hinted that retroactive application of one of these laws probably would be an undue burden on interstate commerce. One can readily imagine why this would be. If companies had to constantly be ready to pay retroactive sales or use taxes, every seller would need to collect taxes on every transaction and be sophisticated enough to understand the sales and use tax codes of all 50 states simultaneously. This is clearly an undue burden on interstate commerce. So, we arrive at another general requirement for state sales or use taxes on an out-of-state seller: the tax must not apply retroactively.

The third point which the Court noted as burden-eliminating was the fact that South Dakota adopted the Streamlined Sales and Use Tax Agreement.[150] This point is relevant because it suggests that a reviewing court will look for any efforts made by a state to ease compliance burdens for interstate companies dealing with their tax system when deciding if the tax places an undue burden on interstate commerce. As such, a state looking to require a foreign seller to collect sales or use taxes will be well served by taking steps to make it easier for interstate companies to navigate its tax code. This may mean adopting the Streamlined Sales and Use Tax Agreement, as South Dakota did. Or, it may be a more involved process, such as delving into the state's tax code and making changes to simplify the code. In any case, every state should attempt to reduce compliance burdens for interstate sellers dealing with their respective tax codes as part of their efforts to take advantage of *Wayfair*.

2. Adhering to the Due Process Clause

Alongside these Commerce Clause requirements, each state needs to meet the requirements of the Due Process Clause. As previously noted, the Due Process Clause's demands have been stated several ways: as a demand that the state give some benefit for which it may fairly require compensation, as a demand that the state only tax sellers who made direct efforts toward engaging with the state, or as a simple requirement that the taxed seller have enough connections with the state so the seller is reasonably on notice that they could be taxed in the state.[151] These definitions all tend toward one requirement: A seller purposefully and successfully availed itself of the privileges of doing significant business in the taxing state.[152]

However, accounting for this requirement in the black letter law is very difficult and

148. *Id.*
149. *Id.*
150. *Id.*
151. *See supra* Part II.D (discussing these articulations).
152. *Id.*

could, ironically, lead to a great deal of confusion among companies as to whether they would have to collect sales or use taxes in any given state. After all, it seems an impossible task for a legislature to attempt to codify the full reach of their power to tax sales by out-of-state companies under the Due Process Clause. There are also concerns that attempts to do so might constitute an undue burden on interstate commerce, due to the intrinsic case-by-case nature of any Due Process analysis. To this end, the safest approach to meeting the Due Process requirements is also the simplest—adhere to the Commerce Clause requirements.

As discussed, the Dormant Commerce Clause dictates that states should have safe harbor provisions in their sales and use tax schemes. Essentially, the vast majority of, if not all, sellers will not realistically meet the threshold requirements under these safe harbor provisions unless the seller consciously directs their commercial actions into that state's markets. The Court in *Wayfair* stated that the "quantity of business" required by South Dakota's safe harbor provision "could not have occurred unless the seller availed itself of the substantial privilege of carrying on business in South Dakota."[153] Further, even in the incredibly unlikely event that a seller crosses the threshold without purposefully availing themselves of the benefits of the state's markets, a reviewing court could—and probably should, given the analysis suggested by this Note—allow the aggrieved seller to challenge the law as applied to them, rather than raising a facial constitutional challenge. It seems strange to say the safest and most practical method of meeting the demands of Due Process is to ignore those demands altogether. However, the reality is that the Due Process Clause creates an incredibly vague, nebulous standard which leaves no other readily apparent solution and, for the reasons just articulated, seems to come at little risk for the state.

V. CONCLUSION

Pulling all of this together, a tax which ought to meet the requirements of both the Dormant Commerce Clause and the Due Process Clause will not, directly or indirectly, favor intrastate commerce over interstate commerce or in-state sellers over out-of-state sellers. Further, this tax will not create a double tax liability for a single transaction or apply retroactively. Next, such a tax scheme will include an adequate safe harbor provision, likely modeled on South Dakota's law. Finally, the tax will take active steps toward eliminating the compliance burdens of foreign sellers.

With the physical presence rule's swan song behind us, we are entering the great unknown in the field of extraterritorial sales and use taxation. States looking to make use of the new authority opened by *Wayfair* need to keep in mind that there are still background rules under the Dormant Commerce Clause and Due Process Clause which they must adhere to. Beyond this, states should remember and carefully consider the policy concerns articulated earlier in Part III.B and Part IV.A. Only then can we find the best way forward after *Wayfair*.

153. *Wayfair*, 138 S. Ct. at 2099.