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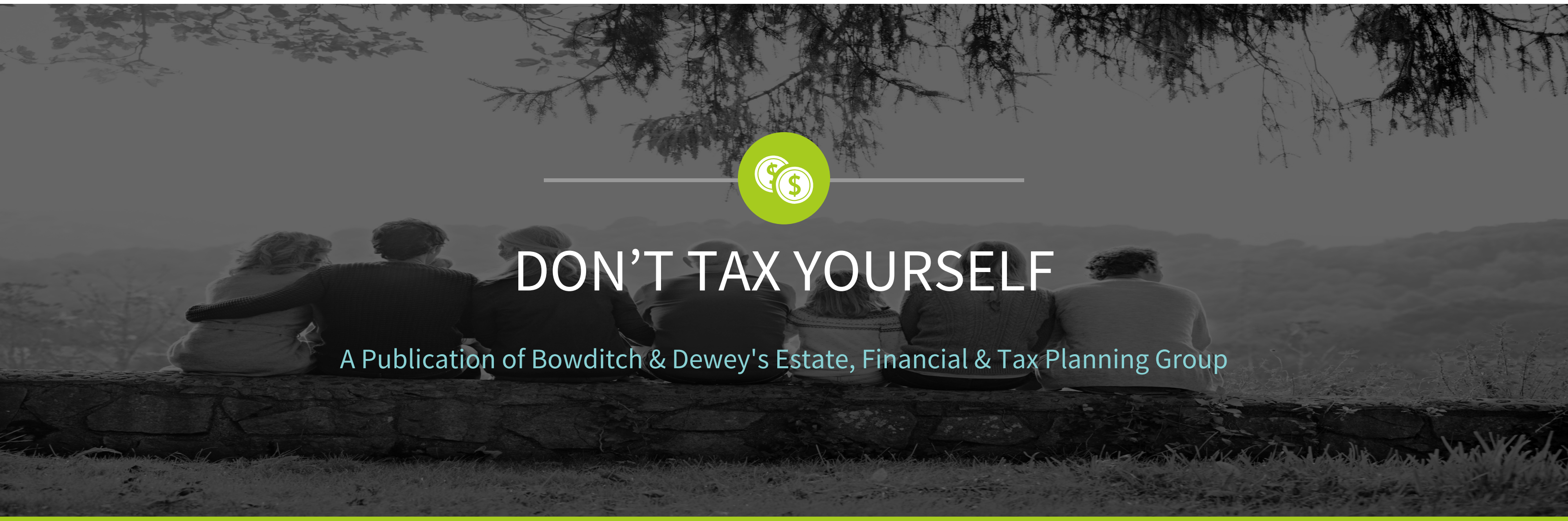

The Wayfair Decision: How Technology is Changing State Tax Laws

BY BOWDITCH & DEWEY • APRIL 13, 2022

The U.S. Supreme Court decision in *South Dakota v. Wayfair, Inc.* 138 S. Ct. 2080 (2018) upended how businesses think about state tax compliance. In *Wayfair*, the Court upheld a South Dakota sales tax law that taxed out-of-state online sellers on the sale of goods or services worth over $100,000 to South Dakota customers. By so holding, the Court overturned existing Supreme Court precedent that declared it unconstitutional (pursuant to the Commerce Clause and the Due Process Clause) for states to require a business to collect and remit a sales tax to the state, unless the business had a physical presence in the state. [See *National Bellas Hess, Inc. v. Department of Revenue of Illinois*, 386 U.S. 753 (1967) and *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).] In *Wayfair*, the Supreme Court acknowledged that with the development of the internet, an online seller “may be present in a State in a meaningful way without that presence being physical in the traditional sense of the term.” Since the Supreme Court decision, 45 states in addition to South Dakota have extended their sales tax reach to out-of-state sellers.

We have yet to see whether states will change their income tax laws to tax incomes (in addition to sales) of out-of-state businesses who sell to customers within a particular state. Congress passed Public Law 86-272 in 1959 to prohibit states from imposing a net income tax on business income derived within a state, if the only business activities within the state conducted by or on behalf of the business consist of soliciting orders for sales of tangible personal property (and the sales activities and shipment activities are out of state). This law applies, however, only to the sale of tangible personal property. Licensing, franchising, and other service agreements are not protected under Public Law 86-272.

With the advent of software as a service sold online through the internet, it is possible that states might change their income tax laws to tax revenue generated from such economic activity. The *Wayfair* decision paves the way for such a change in tax law. Talk with your tax advisor to help you establish a plan to deal effectively with state tax compliance. And stay-tuned, as states’ laws change to adapt to the rise of technology over industry as our economy’s main source of revenue.