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Looking Back at the *Quill* Oral Argument in Light of *Wayfair*

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In this article, Reed examines the oral arguments in *Quill* for hints at what the U.S. Supreme Court justices will likely focus on when they hear *South Dakota v. Wayfair Inc.* later this term.

The U.S. Supreme Court has announced that it will hear oral argument in *South Dakota v. Wayfair Inc.*[1] on April 17. A decision is expected in June.

Of the current justices, only Justices Anthony M. Kennedy and Clarence Thomas were on the U.S. Supreme Court in 1992 when the Court last considered use tax nexus in *Quill Corp. v. North Dakota.*[2] Accordingly, seven (or at least six[3]) of the justices are taking a fresh look at use tax nexus. Despite changes to the Court's membership, it is likely that its questions and concerns this time around will mirror those in *Quill*. In recognition of this likelihood, this article outlines, and offers brief commentary on, the major questions and concerns raised by the justices during the *Quill* oral argument and how those considerations may again factor in *Wayfair*.[4]

Rationale for the Physical Presence Nexus Standard

> I know what we've done [create a physical presence substantial nexus test in *National Bellas Hess*], but you're elevating it to a point of principle and not mere fact.[5]
>
> — Justice Antonin Scalia

At the *Quill* argument, the justices pressed for Quill's counsel to provide a rationale supporting the physical presence nexus standard. The rationale provided by Quill's counsel was that physical presence allows a free-flowing "national marketplace" of commerce. Because of the physical presence nexus standard, sellers can sell their products throughout the United States without having to register, file, and collect use tax in states in which they do not operate or have a physical presence.

Several justices, and especially Scalia, wanted clarification about the contours of the national marketplace concept. To Scalia, if the goal was to create a national marketplace in which sellers could sell nationwide without being taxed, it was hard to understand why the physical presence nexus rule was crafted so that it allowed a national marketplace for mail-order businesses but not other business models. "I want you to tell me why this is worse for somebody who operates by telephone or mail than it is for somebody who operates by sending

[1] *South Dakota v. Wayfair Inc.*, 2017 S.D. 56 (2017); U.S. Sup. Ct. Docket No. 17-494.

[2] 504 U.S. 298 (1992).

[3] Justice Neil M. Gorsuch's views on *Quill* and related use tax nexus issues can arguably be discerned from his concurrence in *Direct Marketing Association v. Brohl*, 814 F.3d 1129 (10th Cir. 2016).

[4] All quotes are taken from listening to the oral argument and reviewing the transcript offered by the Oyez Project.

[5] This quote, and all quotes from the *Quill* oral argument are from the Oyez Project transcript.

business representatives into all of the states," Scalia asked.

The answer was that the national marketplace was defined largely based on history. The appellant in *National Bellas Hess*[6] was a mail-order company, and in holding that the company could not be required to collect use tax, the Supreme Court accordingly enshrined a friendly nexus standard for the mail-order industry. An entire industry then grew up around that rule, which was sensible and easy to understand. As Quill's attorney put it, *National Bellas Hess* provides a simple "rule that businessmen [could] understand": so long as they send no one into the state and have no real or personal property in the state, they cannot be forced to collect use tax.

Economic and Technological Changes

> Have there been any changes in the national market? You mentioned computerized ability to calculate the tax. Have there been any changes in the nature of the market itself?
>
> — Justice Kennedy

Twenty-five years passed between *National Bellas Hess* and *Quill*. The justices wondered if this interval had changed the American economy in a way that cast a cloud on the national marketplace justification for physical presence. The Court asked North Dakota's counsel to address this point. He responded as follows:

> A lot has happened since then [1967] that . . . changes the view of the case from the standpoint of collectibility. You can buy computer software, and many direct marketers use it right now, that automatically calculate[s] the tax and add[s] it to a bill. That software's available. It takes into account the complexities of every jurisdiction in the country. It's not expensive. Quill could easily purchase it. . . . The combination of the changing marketplace, the ease of communication that goes on that facilitates this, and the fact that the collection burdens have gone down substantially because of technological developments, make the world a very different place in 1992 than it was in 1967 when *Bellas Hess* was decided.

Despite these changes from 1967-1992, the Court chose not to overrule *National Bellas Hess*. But nonetheless, the Court was interested in North Dakota's view on whether the passage of time undercut the arguments for a physical presence nexus rule and the national marketplace concept. Likewise, it is to be expected that the Court in *Wayfair* will ask both sides to address whether the passage of time since *Quill* has strengthened or weakened the basis for the physical presence nexus standard.

Stare Decisis

> Maybe we were wrong in 1967. Is there some reason why we would be more reluctant to change in this case than we ordinarily would be, or less reluctant? What kind of a case . . . this was a constitutional decision, right? And we have opinions that say that ordinarily where we think we've gotten it wrong there and are wrongly preventing the states here from doing something they ought to be able to do that we should 'fess up and . . . change our opinion.
>
> — Justice Kennedy

During oral argument, Quill's counsel repeatedly argued that the physical presence nexus standard represented the long-standing status quo and North Dakota was flouting that standard. That raised the common issue of how much deference to give a prior precedent. As seen above, Kennedy expressed willingness, at least during oral argument, to revisit physical presence anew.

In *Wayfair*, the Court again will have to decide whether to adhere to long-standing prior use tax nexus opinions. There is case law addressing the factors a court should consider in determining whether to overrule a prior opinion, including

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

At the *Wayfair* oral argument, it is likely that the justices will again press for an explanation of not only how the physical presence nexus rule originated, but also whether there is continued justification for it. Unlike in *Quill*, this time around the Court will need to evaluate whether a statute with specific dollar and transaction thresholds eases constitutional concerns.

whether the opinion: (1) was decided on constitutional or statutory grounds; (2) has engendered legitimate reliance interests; (3) has been undermined by changed circumstances; (4) has been consistently criticized, and is now seen as sufficiently inconsistent with other doctrines that it is a detriment to coherence in the law; and (5) has proven unworkable or outdated.

How each justice will weigh those factors is something to watch; some may be more inclined to tear down precedent than others. A cautious justice might need to be convinced that *National Bellas Hess* and *Quill* are disastrous before deciding to overrule them. Another justice might be willing to overrule those opinions if they merely seem ill-reasoned.

Retroactivity Concerns

> Would [overturning *National Bellas Hess*] involve potential retroactive liability covering several years and in a large number of the states? It would be very substantial in amount, would it not? — Justice Sandra Day O'Connor

During oral argument, O'Connor was concerned about the potential retroactive impact of reversing *National Bellas Hess*. At multiple points, she asked the attorneys to estimate the cumulative tax impact for remote sellers if the physical presence rule were overturned. She even tried to pin the attorneys down on precisely how many states could seek retroactive assessments: "Well, how many states? 36?"

The South Dakota statute at issue in *Wayfair* was specifically designed not to be retroactive.[7] However, consistent with O'Connor's questions in *Quill*, consideration will presumably need to be given to other states and the potential nationwide impact on multistate remote sellers if *Quill* is abrogated.

Separation of Powers and Federal Legislation

> Unlike a lot of our constitutional decisions, *Bellas Hess* is a decision which Congress can overrule. . . . If Congress wants to change the result in *Bellas Hess*, it can do so, and it's been asked to do so by the state.
>
> — Chief Justice William H. Rehnquist

From the questions and asides at oral argument, clearly the justices thought that Congress was better positioned than the U.S. Supreme Court to replace physical presence with an alternative jurisdictional standard for use tax collection. This sentiment figures clearly into the *Quill* opinion:

> The underlying issue is not only one that Congress may be better qualified to resolve, but also one that Congress has the ultimate power to resolve. No matter how we evaluate the burdens that use taxes impose on interstate commerce, Congress remains free to disagree with our conclusions. . . . Congress is now free to decide whether, when, and to what extent the states may burden interstate mail-order concerns with a duty to collect use taxes.[8]

Now, as in 1992, there is proposed federal legislation that would override the physical presence substantial nexus standard. Some of the justices might prefer punting to Congress rather than crafting an alternative to physical presence. On the other hand, some justices might reason that the Court has no choice but to fill the void, since Congress has chosen not to do anything in the 25-plus years since *Quill*.

Jurisdictional Consistency

> I would have thought you might want to rest your argument just on the commerce clause and say it is better left to Congress to change.
>
> — Justice O'Connor

> It seems to me that our due process jurisprudence has progressed to the point where it's very clear that your clients could be held liable for products liability, etc.,

[7]"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." S.D. Codified Laws section 10-64-7.

[8]*Quill*, 504 U.S. at 318.

> and that if *Bellas Hess* rested on due process at one point . . . if it did, and I'm not sure that it did . . . that that has been superseded by our jurisprudence.
>
> — Justice Kennedy

At the *Quill* oral argument, the justices made it clear that it was critical to determine whether the physical presence nexus standard derives from the due process clause or the commerce clause. They gave two reasons for this. One was that due process clause jurisdictional case law had changed since *National Bellas Hess*. In particular, case law in the products liability area granted jurisdiction over companies merely releasing products into a "stream of commerce" resulting in the products terminating in the state[9] (a standard not requiring physical presence). Therefore the justices suggested that there might be inconsistency if a more strict use tax due process clause jurisdictional standard was used relative to due process clause jurisdictional standards in other contexts.

Second, the justices did not want to create a constitutional right irreversible by Congress, which is what would have happened if *Quill* rested on due process clause grounds. A fundamental right would have then been created that Congress could not override. In the alternative, deciding the case on dormant commerce clause grounds still allowed Congress to enact contrary legislation. In O'Connor's words, "If *National Bellas Hess* rests on the dormant commerce clause, certainly Congress can take care of this problem . . . and it could rightfully weight the really massive concerns here for retroactive liability and try to sort it out in a fair and reasonable way."

Presumably, *Wayfair*, however it is decided, will again rest on the dormant commerce clause, consistent with *Quill*. Therefore, this consideration is unlikely to figure as heavily as it did in *Quill*. However, it is possible that the justices might give some consideration to jurisdictional standards outside the use tax context as they did in *Quill* — potentially including due process clause cases — as a jurisdictional reference point. They then could consider whether those reference points offer anything as far as whether physical presence should be retained as the use tax nexus standard.

Conclusion

Wayfair is perhaps the most important state tax case that the Court will hear in a generation. Seven of the nine justices were not on the Court when *Quill* was decided, and it is difficult to predict not only what the Court will decide to do, but also how they will decide to do it — it is anyone's guess what a decision in favor of either party might look like. In making its decision, the Court will likely consider many of the things that were crucial the last time around in *Quill*. This article has summarized the Court's main questions and concerns from the *Quill* oral argument with the goal of shedding some light on what some of the key considerations for the Court will likely be in deciding *Wayfair*. ■

[9] *See, e.g., Asahi Metal Industry Co. v. Superior Court*, 480 U.S. 102 (1987).