The FAIR Coalition | Seeking Fair Access to Interstate Remedies

June 14, 2022

The Honorable Ron Wyden
Chairman
U.S. Senate Finance Committee
Washington, DC

The Honorable Mike Crapo
Ranking Member
U.S. Senate Finance Committee
Washington, DC

Re: Full Committee Hearing: Examining the Impact of *South Dakota v. Wayfair* on Small Businesses and Remote Sales

Introduction

The Fair Access to Interstate Remedies (FAIR) Coalition appreciates the opportunity to comment on the impact of the *Wayfair*[1] decision and the concomitant need to modernize the Tax Injunction Act (TIA)[2] to allow for expanded federal court jurisdiction in certain state and local tax cases.[3] The TIA was adopted in 1937 at a time when interstate commerce was far less prevalent and states were generally precluded from imposing taxes on interstate commerce. The Supreme Court in *Wayfair* found that the physical presence standard was anachronistic and "removed from economic reality."[4] The same can be said of the rationale for the TIA, particularly in light of the *Wayfair* decision. Businesses will be required to litigate common federal questions in multiple state and local jurisdictions, even where they have no physical presence. This will impose a particular financial strain on smaller businesses. Consequently, the FAIR Coalition believes the TIA should be amended to allow businesses access to federal courts in cases where state tax issues raise substantial federal questions—such as those requiring interpretation of either the U.S. Constitution or federal law.

Wayfair has expanded the need for access to federal courts in state tax matters

The Supreme Court's decision in *Wayfair* left open many questions, creating tremendous uncertainty for interstate businesses. The expansion of the definition of nexus due to *Wayfair* has caused the issues surrounding "burdens on interstate commerce" to reach a tipping point and access to a federal forum has never been more important.

Since 1937, the TIA has prevented access to federal courts to resolve state tax disputes. In 1937, the rationale for TIA was clear—taxpayers had used diversity jurisdiction to force states to litigate beyond their borders at a time when the state taxation of interstate commerce was extremely limited. Eighty-five years later, however, the landscape could not be more different. By and large, commerce today is interstate due to the internet and expansion of the global economy. Also, in 1977, the states' ability to impose taxes on interstate commerce was greatly expanded.[5]

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[1] 138 S. Ct. 2080 (2018).
[2] 28 U.S.C. §1341.
[3] For additional information about the FAIR Coalition, see https://www.thefaircoalition.com/.
[4] 138 S. Ct. 2080, 2092 (2018).
[5] *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977) (This case established the *Complete Auto* doctrine as the guiding principle for examining the validity of a state tax impacting interstate commerce. The *Complete Auto* doctrine provides that a state's taxation of interstate commerce may be upheld against a Commerce Clause challenge

In 1988, businesses lost the automatic right to U.S. Supreme Court review of state tax cases that involve a challenge based on federal law.[6] And, of course, most recently, *Wayfair* allowed states to tax businesses engaged in interstate commerce, even absent a physical presence in that state.

Businesses engaged in interstate commerce may now be faced with pursuing legal challenges to tax assessment regimes in 45 states,[7] resulting in a proliferation of state filings and increased administrative burdens, particularly for small businesses. Currently, because the TIA is outdated and does not reflect new "economic realities," businesses faced with state tax burdens that raise constitutional or other federal questions are required to litigate those disputes in many or all states in which the businesses' customers reside. And, under the new *Wayfair* nexus standard, this has already led to litigation in jurisdictions where a business has no physical presence.

The lack of federal court oversight of federal questions regarding state taxation has left a spiderweb of inconsistent state court rulings on federal law, which only further complicates the application of, and compliance with, various state tax laws. As a general matter, after *Wayfair,* a small business attempting to operate across the country will face the increased burden of being required to have an intimate working knowledge of each state's tax laws, including the specific nuances of each state's court cases, to properly comply. Because of the TIA, each state court is generally free to interpret federal law (including both the U.S. Constitution and federal statutes) as it sees proper, and, without greater oversight of the federal courts, we will continue to see state courts inconsistently apply federal law. Simple changes to the TIA could alleviate these issues and create greater uniformity for businesses throughout the country.

The *Wayfair* decision opens the door for states to further impose state sales tax collection and filing obligations (and possibly other direct state taxes) on businesses—making as few as $100,000 of sales into a state. Consequently, there has never been a time in which it was more imperative for taxpayers to have access to the federal courts. This access is needed in order to provide guidance and direction regarding the constitutional and other federal limitations on the ability of the states to require compliance with their tax laws.

In addition, states themselves are becoming increasingly frustrated when their constituents are taxed by out-of-state tax authorities with respect to in-state business activity. States have filed legal challenges with the Supreme Court, but, so far, the Court has declined to review such cases.[8]

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when the tax is applied to an activity with a 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. Prior to the decision in *Complete Auto*, the states ability to tax interstate commerce was much more limited.)

[6] The change to the Supreme Court's mandatory review was made by Congress as part of P.L. 100-352. Supreme Court Case Selections Act of 1988, Pub. L. No. 100-352, 102 Stat. 662 (codified at 28 U.S.C. §§1254, 1257-58, 2104 (1994)).

[7] Five states do not impose any sales tax: Alaska, Delaware, Montana, New Hampshire, and Oregon.

[8] *See, e.g., New Hampshire v. Massachusetts*, 141 S. Ct. 2848 (2021) (challenge to Massachusetts' regulation providing for taxation of employees of Massachusetts businesses working remotely in New Hampshire during pandemic)*; Arizona v. California*, 140 S. Ct. 684 (2020) (challenge to imposition of California minimum franchise tax on Arizona LLCs "doing business" in CA). The Supreme Court did not take either case and as a result, nexus and potential double taxation concerns remain unresolved.

States have also enacted legislation in an attempt to protect in-state businesses and individuals from taxation by other jurisdictions.[9]

Modernizing the TIA—Lets create a system that works for today's economy

Under the current system, barring federal courts from reviewing and ruling on state tax matters that involve federal questions creates inconsistent outcomes. A more efficient and equitable way to address the potential growing state conflicts would be to allow taxpayers access to federal court to resolve state tax issues that present federal questions.

Simply put, this is an issue of fairness. Federal courts are best situated to interpret Congressional intent regarding federal laws regulating state taxation. This would put tax issues on a parity with other issues. To our knowledge, all non-tax cases at the state level involving a federal question have access to federal courts. In contrast, challenges to state tax laws that potentially violate federal law are barred from federal court. Given the current economic realities, we see no reason for continuing this outdated distinction. Businesses with these types of federal issues at the state level should be allowed access to federal courts. This proposed change is also consistent with prior bipartisan laws that created exceptions to the TIA to expand access to federal courts to address federal questions.[10]

To increase certainty and consistency for both taxpayers and states and to help ensure that the states' expanded authority to tax interstate commerce does not unduly burden interstate and foreign commerce or violate taxpayers' Due Process and Fourteenth Amendment rights, taxpayers should be provided greater access to federal courts.

Conclusion

Businesses engaged in interstate commerce have long faced state taxes that raise Due Process and Commerce Clause concerns. Technological, legal, and economic changes in recent years have enabled taxpayers to expand their businesses across state and national boundaries. And the Supreme Court's decision in *Wayfair* has emboldened the states in their taxation of interstate commerce. As a result, businesses of all sizes engaged in interstate commerce now face the daunting burden of complying with complex and constantly-evolving tax laws across multiple jurisdictions, which may require litigation. Under the TIA, a business—regardless of its size—will be required to litigate the same federal issue in each state that has a taxing scheme or law regardless of whether that business has a physical presence in that state. Although the broad ambit of the TIA once made sense, that is no longer the case.

The FAIR Coalition thanks Chairman Wyden and Ranking Member Crapo for the opportunity to comment on the impact of *Wayfair* on interstate commerce and the need for expanded federal court jurisdiction in certain state and local tax cases. We strongly believe the

[9] *See, e.g.,* Idaho H.B. 677 (2022) (providing that no out-of-state taxing authorities may impose tax on an Idaho business for conducting sales or other business taking place within Idaho between an Idaho business and a nonresident who is physically present in Idaho while engaging in the business transaction).

[10] *See, e.g.*, Railroad Revitalization and Regulatory Reform Act ("4-R Act"), 49 U.S.C. § 11501(b), (c). Other federal statutes where Congress has provided for federal court jurisdiction for state tax disputes include motor carriers and wireless telecommunications providers.

time for relief is now and updating the TIA is the most simple and efficient way to achieve this goal. We look forward to working with the Committee and Congress on this vital issue.

Sincerely,

The FAIR Coalition