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***To Tax or Not To Tax? That's Not the Question:
The Role of Tax Within the Maturing World of e-Commerce***

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TO TAX OR NOT TO TAX? THAT'S NOT THE QUESTION: THE ROLE OF TAX WITHIN THE MATURING WORLD OF E-COMMERCE

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Tax moratoriums¹ and internet growth have paved a path for garage-style e-commerce start-ups to mature into retail titans. As states struggle with reduced budgets, the market gap widens between these internet retailers and their “brick and mortar” competitors. Initially, tax moratoriums on internet commerce were created to protect budding internet companies and to encourage growth.² Today, e-commerce is a dominant means of purchasing for many consumers.³ As consumers move rapidly from the physical to the virtual world, the law has attempted to impose a physical presence standard on e-commerce.

This Note discusses the question of *how* to tax e-commerce, focusing specifically on use taxes and sales taxes. One example of the online tax requirement, and the controversy surrounding it, was recently addressed in *Amazon.com v. New York State Department of Taxation & Finance*.⁴ This lawsuit occurred after the state of New York attempted to impose a sales tax requirement on out-of-state internet retailers.⁵ Amazon attacked New York’s sales tax law as “unconstitutional” and, as a result, chose to remove a substantial amount of its business from the state.⁶ Because the New York Supreme Court upheld the sales tax requirement as constitutional, the

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1. In 1998, President Clinton signed the Internet Tax Freedom Act into law, which barred certain taxes on electronic commerce transactions. See *Statement by the President*, The White House Office of the Press Secretary (Oct. 8, 1998), available at <http://govinfo.library.unt.edu/npr/library/news/100898.html>.

2. See Christopher J. Schafer, *Federal Legislation Regarding Taxation of Internet Sales Transactions*, 16 BERKELEY TECH. L.J. 415 (2001).

3. Michelle Kessler, *More Shoppers Proceed to Checkout Online*, USA Today (November 18, 2011, 11:49 am), http://www.usatoday.com/tech/news/2003-12-22-shoppers_x.htm.

4. *Amazon.com, LLC v. N.Y. State Dep’t of Taxation & Fin.*, 877 N.Y.S.2d 842 (N.Y. Sup. Ct. 2010).

5. *Id.* at 846.

6. *Id.*

Amazon case has ignited debate about fair business and a state's constitutional ability to impose a sales tax requirement on internet retailers.⁷

This Note will provide an overview of the debate surrounding internet taxation. Part I provides the background and the historical jurisdictional issues of U.S. tax law. Part II explains the *Amazon* case, highlighting the constitutional arguments regarding e-commerce taxation. Part III discusses proposals and legislation involving internet taxation. Also, in Part III, this Note will argue that legislation created to address tax collection on internet transactions should meet four requirements. The legislation (1) should clarify the tax landscape for internet retailers and consumers; (2) it must be constitutional;⁸ (3) it should promote virtual business equally and foster e-commerce growth,⁹ and (4) it should be forward thinking, addressing developments in technology and e-commerce.¹⁰

I. BACKGROUND

A. UNITED STATES APPROACH TO JURISDICTION OF OUT-OF-STATE RETAILERS

When discussing the United States's approach to the jurisdiction of out-of-state retailers, it is important to understand three things. First, although there are two types of taxes involved in the discussion of internet transactions taxation—use tax and sales tax—this discussion is primarily concerned with the latter type. Second, a state's ability to tax is determined by its ability to assert personal jurisdiction over a particular entity.¹¹ Once a state establishes personal jurisdiction, however, the question is not *whether to tax* internet transactions, but instead *how to tax* internet transactions. Third, courts are primarily concerned with analyzing Dormant Commerce Clause issues because the Dormant Commerce Clause focuses on state actions that might abuse power in a way that discriminates against interstate commerce, and internet retailers typically engage in interstate commerce.¹² The rest of Section I.A will explore these three considerations in greater detail.

7. *Id.* at 850.

8. *See* Quill Corp. v. North Dakota, 504 U.S. 298 (1992).

9. *See* Forst, *Old and New Issues in the Taxation of Electronic Commerce*, 14 BERKELEY TECH. L.J. 711 (1999).

10. *See* Megan Groves, *Tolling the Information Superhighway: State Sales and Use Taxation of Electronic Commerce*, 13 HARV. J.L. & TECH. 619 (2000).

11. *Quill*, 504 U.S. at 306–09.

12. *Gibbons v. Ogden*, 22 U.S. 1 (1824).

1. *Types of Tax Involved in Internet Transactions*

a) Use Tax

The Supreme Court in *McLeod v. J.E. Dilworth Co.* defined a use tax as “a tax on the enjoyment of that which was purchased.”¹³ Because use taxes are harder to enforce, lawmakers are more inclined to impose a sales tax collection requirement on internet retailers.¹⁴ Two primary issues are at the root of this enforcement problem.¹⁵ First, it is logistically challenging for states to educate consumers and to hold them responsible for collecting use taxes.¹⁶ Second, enforcement of use tax laws is administratively onerous, often impractical, and expensive.¹⁷ These issues will be addressed in turn below.

States generally find it too impractical and expensive to educate consumers about their obligations under the use tax laws. Typically, most states apply a use tax requirement to items that would be subject to a sales tax if they were purchased in that state.¹⁸ Most consumers are unaware they must pay a use tax on purchases ranging from television sets to tennis shoes.¹⁹ Furthermore, many who know of the use tax have no idea how to calculate what they owe.²⁰ The calculation percentage is usually the same as the state’s sales tax rate.²¹ For example, if a consumer buys a television online, she is required to record the price of the television, multiply this price by the standard use tax rate, and then insert the product of this calculation into a specifically delineated section of her income tax form for the year.²² This task may not be too challenging if all she purchased online that year was a television. The modern consumer, however, typically buys numerous things online that are subject to sales taxes.²³ Such consumers are technically required to keep track of these items and make calculations to input into

13. *McLeod v. J.E. Dilworth Co.*, 322 US 327, 330 (1944).

14. Eric Menhart, *Taxing the Internet: Analyzing the States’ Plan to Derive Online Sales Revenue*, J. OF ST. TAX’N, July–Aug. 2007, at 35, available at <http://www.cyberlaw.pro/docs/taxingtheinternet.pdf>.

15. *Id.* at 37.

16. *Id.*

17. *Id.*

18. Ronald J. Huefner & Arlene M. Hibscheiler, *Calculating and Reporting Use Tax in New York*, THE CPA JOURNAL (Nov. 14, 2011), <http://www.nysscpa.org/cpajournal/2004/704/essentials/p38.htm>.

19. *Id.*

20. Huefner & Hibscheiler, *supra* note 18.

21. Menhart, *supra* note 14.

22. Tonya Moreno, *What is Use Tax*, ABOUT.COM (Nov. 4, 2011), <http://taxes.about.com/od/statetaxes/a/use-tax.htm>.

23. See Kessler, *supra* note 3.

their annual tax returns.²⁴ Because many consumers are unaware of these obligations, states would be required to spend a significant amount of time and money educating millions of people.²⁵ Such a task would take a serious bite out of any possible revenue the states would hope to gain from use taxes. Consumers are also unlikely to take the time to record, calculate, and file their use tax forms because of the low chance of being prosecuted for failing to do so.²⁶ On average, the IRS audits 1.5% of individual taxpayers each year.²⁷ As such, the functioning of the tax system generally, and the use tax specifically, depends on voluntary compliance.²⁸

Second, strict use tax enforcement imposes abundant administrative and economic challenges on a state.²⁹ States would be required to keep detailed records of individual consumer spending patterns over the course of each tax year.³⁰ As with the problem of educating consumers, the cost of monitoring their behavior would likely exceed the revenues gained from use tax collection.³¹

b) Sales Tax

Unlike a use tax, a sales tax is “a tax levied on the retail price of merchandise and collected by the retailer or entity selling the good.”³² Contrary to use taxes that hold the consumer responsible for the tax activity, sales taxes impose the tax collection burden on the retailer.³³

Because of use tax challenges, legislators have determined that sales taxes are the more realistic method of collecting tax from internet sales.³⁴ States often have greater opportunities to create legislation incentivizing internet retailers to collect sales taxes on merchandise.³⁵ Additionally, internet businesses are likely better positioned than the individual consumer to develop methods to collect taxes that can be implemented throughout the

24. *Use Tax Basics*, CALIFORNIA STATE BOARD OF EQUALIZATION (Sept. 1, 2011), <http://www.boe.ca.gov/taxprograms/usetax/index.html>.

25. Huefner & Hibscheiler, *supra* note 18, at 37.

26. *Id.*

27. *How to Avoid an IRS Audit?*, WORLDWIDEWEB TAX (Nov. 14, 2011), http://www.wwwwebtax.com/audits/audit_avoiding.htm.

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.*

32. *Sales Tax Definition*, MERRIAM-WEBSTER.COM (Sept. 1, 2011), <http://www.merriam-webster.com/dictionary/sales%20tax>.

33. Menhart, *supra* note 14.

34. *Id.* at 37.

35. *Id.*

course of business.³⁶ Lawmakers can create strict business requirements, holding internet retailers accountable for collecting sales taxes, thus facilitating a logistically possible method of enforcement.³⁷

2. *Personal Jurisdiction*

Whether a state can require an out-of-state retailer to remit a sales tax depends upon whether that state can assert personal jurisdiction over that retailer.³⁸ The Supreme Court has established a physical presence nexus requirement that determines proper jurisdiction and when a state can constitutionally require an out-of-state retailer to pay taxes or collect sales taxes from consumer transactions.³⁹ Traditionally, taxation was constitutional when an out-of-state retailer made minimum contacts with a state and that state was not trying to hinder interstate commerce by that taxation.⁴⁰ Courts determined whether a state constitutionally had jurisdiction to tax an entity by using the *International Shoe* standard of minimum contacts.⁴¹ This analysis, however, evolved into a “more flexible inquiry” with courts typically looking past a physical presence requirement and determining whether the entity has “purposefully availed” itself enough to satisfy minimum contacts under the Due Process Clause.⁴² Judges typically engage in this “flexible inquiry” by addressing the constitutionality of personal jurisdiction through a bifurcated analysis incorporating both the Due Process Clause and the Commerce Clause.⁴³

The Due Process Clause, under the Fourteenth Amendment of the Constitution of the United States, holds that no state shall “deprive any person of life, liberty, or property, without due process of law”⁴⁴ For a court to assert tax law jurisdiction, judges must use a personal jurisdiction analysis and first determine if the parties involved have minimum contacts with the forum “such that the maintenance of the suit does not offend ‘traditional notions of fair play and substantial justice.’”⁴⁵ Judges usually

36. *Id.*

37. *See id.*

38. *Quill Corp. v. North Dakota*, 504 U.S. 298, 307 (1992).

39. *Id.*

40. *Id.*

41. *Int'l Shoe Co. v. Washington*, 326 U.S. 310 (1945). In *International Shoe*, the Court explained that due process requires that a defendant have minimum contacts with the forum “such that the maintenance of the suit does not offend traditional notions of fair play and substantial justice.” *Id.* at 316.

42. *Quill*, 504 U.S. at 307.

43. *Id.* at 305–07.

44. U.S. CONST. amend. XIV, § 1.

45. *Int'l Shoe*, 326 U.S. at 316 (quoting *Milliken v. Meyer*, 311 U.S. 457, 463 (1940)).

expand this analysis by determining whether a defendant was able to foresee that his “conduct and connection with the forum State were such that he should [have] reasonably anticipate[d] being haled into court there.”⁴⁶ The “conduct or connection,” however, need not be physical. The Court has determined that “it is an inescapable fact of modern commercial life that a substantial amount of business is transacted solely by mail and wire communications across state lines, thus obviating the need for [a] physical presence within a State in which business is conducted.”⁴⁷ Therefore, to constitutionally assert personal jurisdiction, a court usually determines whether the out-of-state defendant has “purposefully directed” his conduct or connection to the residents of the forum state.⁴⁸

3. *The Commerce Clause and the Dormant Commerce Clause*

The second part of the jurisdictional analysis involves the Commerce Clause, where judges typically consider whether a state’s nexus or physical requirement laws prohibit interstate commerce.⁴⁹ Judges divide this physical presence element into two inquiries involving the Commerce Clause and the Dormant Commerce Clause, which, in different ways, attempt to regulate the relationship between federal and state power.⁵⁰

The Commerce Clause expressly grants Congress the power to regulate commerce with “foreign Nations, and among the several States.”⁵¹ Essentially, the Constitution has specifically detailed certain powers listed for the federal government and those that are not specifically listed are reserved for the states.⁵² The Commerce Clause grants power to Congress and restricts states’ ability to regulate.⁵³

By contrast, the Dormant Commerce Clause is not expressly inscribed in the Constitution, but instead is a power that the Supreme Court has read into the Commerce Clause.⁵⁴ The Dormant Commerce Clause attempts to limit state and local governments from impeding interstate commerce by imposing “an implicit restraint on state authority, even in the absence of a conflicting

46. *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 297 (1980).

47. *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 476 (1985).

48. *Id.* at 472.

49. Julie M. Buechler, *Virtual Reality: Quill’s “Physical Presence” Requirement Obsolete When Cogitating Use Tax: Collection in Cyberspace*, 74 N.D. L. REV. 479, 487 (1998).

50. *Quill Corp. v. North Dakota*, 504 U.S. 298, 305 (1992).

51. *United States v. Lopez*, 514 U.S. 549, 554 (1995).

52. *Commerce Clause*, CORNELL UNIVERSITY LAW SCHOOL (Nov. 1, 2011), http://www.law.cornell.edu/wex/commerce_clause.

53. *Id.*

54. *Gibbons v. Ogden*, 22 U.S. 1, 189 (1824).

federal statute.”⁵⁵ Essentially, the Dormant Commerce Clause is concerned with state actions that might abuse power over particular areas of commerce in ways that discriminate against interstate commerce.⁵⁶ For instance, if a state created a tax that effectively bars foreign state businesses from competing in the state, a court would likely view that state’s act as economic protectionism, and Congress would have the ability to restrict that state from enacting such a tax.⁵⁷

Because internet retailers typically engage in interstate commerce, laws that tax out-of-state retailers implicate Dormant Commerce Clause issues. States, however, can typically overcome a Dormant Commerce Clause challenge to an imposed tax if 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.”⁵⁸

B. HISTORICAL GUIDELINES FOR TAXATION OF REMOTE SALES: THE PHYSICAL PRESENCE STANDARD

Personal jurisdiction challenges the constitutionality of a state tax on an internet retailer. Increasingly, however, courts are reading into a state’s constitutional powers the ability to tax out-of-state retailers.⁵⁹ Section I.B. will explain the historical guidelines for determining personal jurisdiction for taxation purposes through two foundational cases, *National Bellas Hess, Inc. v. Department of Revenue of Illinois*⁶⁰ and *Quill Corp. v. North Dakota*.⁶¹

In *National Bellas Hess*, the Supreme Court established a bright-line limitation on state taxation powers.⁶² The Court determined—by the Dormant Commerce Clause—that for taxation purposes, an appropriate nexus between an out-of-state retailer and the desired forum required a physical presence.⁶³ Subsequently, in *Quill Corp.*, the Court reaffirmed its position in *National Bellas Hess* that the Dormant Commerce Clause requires

55. *United Haulers, Inc. v. Oneida-Herkimer Solid Waste Management Authority*, 550 U.S. 330, 338 (2007).

56. *Gibbons*, 22 U.S. at 189.

57. *See id.*

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

59. *See Amazon.com, LLC v. N.Y. State Dep’t of Taxation and Fin.*, 877 N.Y.S.2d 842 (N.Y. Sup. Ct. 2010).

60. *Nat’l Bellas Hess v. Dep’t of Revenue*, 386 U.S. 753 (1967).

61. *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

62. *Nat’l Bellas Hess*, 386 U.S. at 758–60; *see also Quill*, 504 U.S. at 311.

63. *See Nat’l Bellas Hess*, 386 U.S. at 758–60.

some physical presence in the taxing state for that state to assert taxation jurisdiction over out-of-state retailers.⁶⁴

1. National Bellas Hess

In *National Bellas Hess*, a use tax case, the Court created a bright-line rule that requires states to establish a physical presence nexus between an out-of-state retailer and the desired forum before asserting personal jurisdiction:

[the] State of Illinois had no power to impose liability on out-of-state mail order firm to collect use taxes imposed by Illinois Use Tax Act, where mail order firm maintained no office, had no agents or solicitors, owned no property, and had no telephone listing in Illinois, and where all contacts which firm had with state were via United States mail or common carrier.⁶⁵

In *National Bellas Hess*, the state of Illinois attempted to require National Bellas Hess, a mail-order company located in Missouri, to remit taxes on mail-order purchases.⁶⁶ The primary issue was whether the state could constitutionally require an out-of-state company to remit a tax, even though the company had no physical location within the state.⁶⁷ Although mail-order catalogues were a new advancement at the time that affected interstate commerce, the Court required a physical nexus to exist before the state could override the Dormant Commerce Clause.⁶⁸ Courts used this physical presence requirement to determine whether or not a state could tax an out-of-state entity.⁶⁹ The Supreme Court later upheld the requirement in a subsequent case, *Quill Corp. v. North Dakota*.⁷⁰

2. Quill Corp.

In 1992, the Supreme Court reaffirmed the physical presence requirement in *Quill Corp. v. North Dakota*, holding that “a vendor whose only contacts with the taxing State are by mail or common carrier lack[ed] the ‘substantial nexus’ required by the Commerce Clause.”⁷¹ Quill was a Delaware corporation with offices in California, Georgia, and Illinois, but the company solicited business in other states, including North Dakota.⁷² Quill

64. *Quill*, 504 U.S. at 331.

65. *Nat'l Bellas Hess*, 386 U.S. at 753.

66. *Id.* at 753–54.

67. *Id.*

68. *Id.* at 758.

69. *Id.*

70. *Quill Corp. v. North Dakota*, 504 U.S. 298, 310 (1992).

71. *Id.* at 311.

72. *Id.* at 302.

conducted most of its out-of-state business “through catalogs and flyers, advertisements in national periodicals, and telephone calls.”⁷³ Prior to 1987, North Dakota had a statute that required “every ‘retailer maintaining a place of business in the State to collect the tax from the consumer and remit it to the State.’”⁷⁴ In 1987, North Dakota expanded its definition of “retailer” to include “every person who engages in regular or systematic solicitation of a consumer market in the state.”⁷⁵ The new definition mandated that Quill collect a tax on all of the orders it received from North Dakota residents. Quill objected to this requirement and challenged the state’s mandate.⁷⁶

Quill attacked North Dakota’s tax requirement by asserting that the tax was unconstitutional on Due Process Clause and Commerce Clause grounds.⁷⁷ When considering Quill’s claims that the state could not constitutionally assert personal jurisdiction to impose a tax requirement, the Court shifted its focus from the historical jurisdiction standard in *International Shoe Co. v. Washington*⁷⁸ to a “more flexible inquiry”⁷⁹ to determine whether Quill had “purposefully avail[ed] itself of the benefits of an economic market in the forum State.”⁸⁰ Using this flexible inquiry, the Court determined that the state had personal jurisdiction over Quill because Quill had purposefully availed itself enough to satisfy minimum contacts under the Due Process Clause.⁸¹

The Court then addressed Quill’s argument that the tax requirement violated the Dormant Commerce Clause. The Court applied a four-part test from *Complete Auto Transit, Inc. v. Brady*, stating that when addressing taxes facing Dormant Commerce Clause challenges, courts should uphold the tax if it “(1) is applied to an activity with a substantial nexus with the taxing State,

73. *Id.*

74. *Id.* (quoting N.D. CENT. CODE § 57-40.2-07 (Supp. 1991)).

75. *Id.* at 302–03 (quoting N.D. CENT. CODE § 57-40.2-01(6) (Supp. 1991)). “Regular or systematic solicitation” meant “three or more advertisements within a 12-month period.” *Id.* at 303 (quoting N.D. ADMIN. CODE 81-04.1-01-03.1 (1988)).

76. *Quill*, 504 U.S. at 303.

77. *See id.* at 303–04.

78. *Int’l Shoe Co. v. Washington*, 326 U.S. 310 (1945). In *International Shoe*, the Court explained that due process requires that a defendant have minimum contacts with the forum “such that the maintenance of the suit does not offend ‘traditional notions of fair play and substantial justice.’” *Id.* at 316; *see also Quill*, 504 U.S. 298 at 307 (quoting *Milliken v. Meyer*, 311 U.S. 457, 463 (1940)).

79. *Quill*, 504 U.S. at 307.

80. *Id.*; *see also Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 476 (1985) (“So long as a commercial actor’s efforts are ‘purposefully directed’ toward residents of another State, we have consistently rejected the notion that an absence of physical contacts can defeat personal jurisdiction there.”).

81. *Quill*, 504 U.S. at 308.

(2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to the services provided by the State.”⁸² In *Quill*, the Court was primarily concerned whether the mail-order business had an adequate nexus to justify taxation under the first prong of *Complete Auto*.⁸³ The Court found no substantial nexus, and thus upheld the bright-line rule that the Dormant Commerce Clause requires some physical presence in the taxing state for that state to assert taxation jurisdiction over out-of-state retailers.⁸⁴

Since *National Bellas Hess* and *Quill*, the Court has engaged in case-by-case determinations of what constitutes a substantial nexus, with no clear standard prevailing.⁸⁵ The determination is muddled by a fact-specific analysis and, as such, courts have not found a predictable answer in many cases.⁸⁶

It is important to understand, however, that the decision in *Quill Corp.* does not prevent states from collecting taxes for items sold online. Instead, it only provides that the state must have some type of substantial nexus to justify a state’s exercise of personal jurisdiction.⁸⁷ Therefore, the characterization of the debate surrounding the taxation of internet transactions as pro-tax versus anti-tax is inaccurate. Instead, the debate focuses on whether a state has justified personal jurisdiction that allows the state to constitutionally require out of state retailers to remit a tax on transactions.

82. *Id.* at 311 (quoting *Complete Auto Transit v. Brady*, 430 U.S. 274, 279 (1977)).

83. *See id.* at 311.

84. *Id.*

85. *See Standard Pressed Steel Co. v. Dep’t of Revenue*, 419 U.S. 560, 564 (1975) (stating the presence of an employee of a corporation within a state in which the corporation owned no property was sufficient to sustain a tax on sales); *see also Tyler Pipe Indus., Inc. v. Washington State Dep’t of Revenue*, 483 U.S. 232 (1987) (finding a substantial nexus where the out-of-state retailer used independent contractors to solicit sales).

86. *See Scholastic Book Clubs, Inc. v. State Bd. of Equalization*, 207 Cal. App. 3d 734 (Ct. App. 1989) (labeling teachers ‘agents’ of Scholastic who “obtain[ed] sales within California from local customers for a foreign corporation and such a nexus was substantial enough to make Scholastic liable for taxes.); *see also Orvis Co. v. Tax Appeals Tribunal*, 654 N.E.2d 954 (N.Y. 1995) (holding that (1) in order to impose duty on out-of-state vendors to collect compensating use taxes from their in-state customers, physical presence of vendors was required, which did not have to be substantial but had to be demonstrably more than “slightest presence,” and (2) activity of out-of-state vendors was sufficient to the impose obligation on vendors to collect sales and use taxes); *see also St. Tammany Parish Tax Collector v. Barnesandnoble.com*, 481 F. Supp. 2d 575, 577 n.1 (E.D. La. 2007) (holding that an out-of-state internet bookseller did not have substantial nexus to be required to remit a sales tax to the foreign state).

87. *See Quill*, 504 U.S. at 311.

C. APPLYING THE PHYSICAL PRESENCE REQUIREMENT FOR ASSERTING PERSONAL JURISDICTION TO THE INTERNET

E-commerce challenges laws that use geographic location or nexus as a fulcrum for determining jurisdiction.⁸⁸ Tax law jurisdiction has traditionally focused on the physical location where the transaction occurred.⁸⁹ Individuals, however, conduct internet transactions over a network and, as a result, such transactions are difficult to attribute to a single geographic location.⁹⁰ The decentralized nature of the Internet also makes it difficult to determine whether an e-business meets the constitutional requirement of establishing a substantial nexus with a state to remit a tax there. Moreover, as discussed in Section I.B, *supra*, a court's determination on this issue typically hinges on facts about the specific transaction.

Despite the ambiguity surrounding how states can tax internet transactions, states are nevertheless eager to access the potential revenue from these transactions.⁹¹ As such, state governments have become more creative in finding ways to establish a substantial nexus between internet retailers and their state's geographic borders in order to access this source of revenue.⁹² New York was the first state to statutorily create a nexus between the state of New York and out-of-state retailers and to impose a sales tax and use tax on companies like Amazon and Overstock.⁹³ Since New York took the first leap, numerous other states passed or are considering passing a similar tax on internet retailers.⁹⁴ These states include California,⁹⁵

88. Buechler, *supra* note 49, at 483.

89. *See id.* Many states, however, have attempted to draft around the *Quill* holding. *See* Mark Alan McGinnis, Comment, *Marching to the Beat of the Itinerant Drummer: States Increasingly Refuse to Get Physical Before Finding Nexus*, 32 CAP. U.L. REV. 149, 185–86 (2003).

90. *See* Buechler, *supra* note 49, at 479, 479–80, 483.

91. In Part III, *infra*, Table 1 depicts the states that proposed or enacted bills that create a tax requirement on internet retailers.

92. *See* *Amazon.com, LLC v. N.Y. State Dep't of Taxation and Fin.*, 877 N.Y.S.2d 842 (N.Y. Sup. Ct. 2010).

93. *Internet Sales Tax Fairness*, NEW RULES PROJECT (Oct. 1, 2011), <http://www.newrules.org/retail/rules/internet-sales-tax-fairness>.

94. *See* Table 1 in Part III, *infra*, for a state-by-state discussion.

95. ABx1 28, proposed by Assembly member Bob Blumenfield (D-San Fernando Valley), specifies the obligations under existing law for out-of-state retailers to collect and remit use tax on sales of tangible personal property to California residents. This bill was passed into law in on June 29, 2011. *Governor Brown Signs Legislation*, CA.GOV (Oct. 3, 2011), <http://gov.ca.gov/news.php?id=17101>.

Colorado,⁹⁶ Connecticut,⁹⁷ Florida,⁹⁸ Hawaii,⁹⁹ Illinois,¹⁰⁰ Indiana,¹⁰¹ Maryland,¹⁰² Minnesota,¹⁰³ Mississippi,¹⁰⁴ New Mexico,¹⁰⁵ Rhode Island,¹⁰⁶ Vermont,¹⁰⁷ Virginia,¹⁰⁸ Washington,¹⁰⁹ and Wyoming.¹¹⁰ Nevertheless, some internet retailers have not readily accepted these state tax requirements.¹¹¹ For example, when New York enacted its sales tax and use tax statute, internet retailers like Amazon responded with a lawsuit.¹¹²

II. *AMAZON.COM, LLC V. NEW YORK STATE DEPARTMENT OF TAXATION & FINANCE*

In 2008, the state of New York attempted to clarify through legislation what constituted a substantial nexus for purposes of taxation jurisdiction. The New York state legislature addressed the issue of e-commerce taxation

96. H.B. 10-1193, 112 Leg., 2nd Sess. (Colo. 2011).

97. S.B. 1239, 112 Leg., 1st Sess. (Conn. 2011).

98. *SB 204: Streamlined Sales and Use Tax Agreement*, FLORIDA HOUSE OF REPRESENTATIVES (Oct. 3, 2011), http://www.myfloridahouse.gov/Sections/Bills/bills_detail.aspx?BillId=42322&BillText=specified+digital+good&HouseChamber=H&SessionId=64&.

99. H.B. 1405, 25th Leg., Reg. Sess. (Haw. 2009). Although the Hawaii Legislature passed the bill, Hawaii Governor Linda Lingle vetoed it. *See* Mike Sachoff, *Hawaii Governor Vetoes Amazon Tax Law*, WEB PRO NEWS (July 2, 2009), <http://www.webpronews.com/topnews/2009/07/02/hawaii-governor-vetoes-amazon-tax-law>.

100. Janet Novak, *Illinois Governor Signs Amazon Internet Sales Tax Law*, FORBES.COM (Oct. 3, 2011), <http://www.forbes.com/sites/janetnovack/2011/03/10/illinois-governor-signs-amazon-internet-sales-tax-law/>.

101. S.B. 250, 111 Leg., (Ind. 2010).

102. *Maryland and Connecticut Updates*, AFFILIATE ADVOCACY (Oct. 3, 2011), <http://affiliateadvocacy.com/2010/maryland-and-connecticut-updates/>. The bill, however, failed to make it out of committee. *See* Missy Ward, *Maryland Advertising Tax SB 1071 Gets Squashed*, MISSYWARD.COM (Oct. 3, 2011), <http://www.missyward.com/2009/04/14/maryland-advertising-tax-sb-1071-gets-squashed/>.

103. S.F. No. 2074, 110 Leg., 2nd Engrossment (Minn. 2009).

104. S.B. 2927, 111 Leg., 54 Reg. Sess. (Miss. 2010).

105. Ken Garcia, *New Mexico HB 50-New Internet Tax Bill*, GTOMANAGEMENT (Oct. 3, 2011), <http://gtomanagement.com/new-mexico-hb-50-new-internet-tax-bill/>.

106. H. 7071, 111 Leg., 1st Sess. (R.I. 2010).

107. H. 661, 111 Leg., 2nd Gen. Assembly (Vt. 2010).

108. S.B. 660, 111 Leg., 1st Gen. Assembly (Va. 2010).

109. H.B. 2620, 111 Leg., 1st Sess. (Wash. 2010).

110. H.B. 0029, 111 Leg., 2nd Sess. (Wyo. 2010).

111. *See* Amazon.com, LLC v. N.Y. State Dep't of Taxation & Fin., 877 N.Y.S.2d 842 (N.Y. Sup. Ct. 2010).

112. *See id.*

when it passed § 1101(b)(8)(vi)¹¹³ of the New York Tax Law, more commonly known as the “Amazon Tax” because of one of the major internet retailers to which it applies.¹¹⁴ The statute creates a rebuttable presumption that an out-of-state online retailer has a nexus with the state of New York if the retailer enters into an agreement with a New York resident to refer customers to the retailer’s website for a commission, for example, through a link on the resident’s website.¹¹⁵

Predictably, internet retailers like Amazon responded negatively to this new obligation. Consequently, only a month after New York enacted the statute, Amazon filed a lawsuit against the state challenging the constitutionality of the statute. The New York Supreme Court¹¹⁶ ruled in favor of the state of New York, granting its motion for summary judgment.¹¹⁷

A. BACKGROUND OF THE CASE

At the time of the case, Amazon had operated its internet retail services for approximately fifteen years.¹¹⁸ Although many New York residents purchased products from Amazon, the company did not own any property in New York, maintain any New York offices, and none of its employees worked or resided in the state.¹¹⁹

113. N.Y. TAX LAW § 1101(b)(8)(vi) (McKinney 2012) provides that a person making sales of tangible personal property or services taxable under this article (“seller”) shall be presumed to be soliciting business through an independent contractor or other representative if the seller enters into an agreement with a resident of this state under which the resident, for a commission or other consideration, directly or indirectly refers potential customers, whether by a link on an internet website or otherwise, to the seller, if the cumulative gross receipts from sales by the seller to customers in the state who are referred to the seller by all residents with this type of an agreement with the seller is in excess of ten thousand dollars during the preceding four quarterly periods. . . . This presumption may be rebutted by proof that the resident with whom the seller has an agreement did not engage in any solicitation in the state on behalf of the seller that would satisfy the nexus requirement of the United States constitution during the four quarterly periods in question.

114. Joel West, *California May Never Collect the Amazon Tax*, SEEKINGALPHA (Nov. 2, 2011), <http://seekingalpha.com/article/277365-california-may-never-collect-the-amazon-tax>.

115. *Amazon*, 877 N.Y.S.2d at 846.

116. The New York Supreme Court is a court of original instance in the state. The New York Court of Appeals is the highest court.

117. *Amazon*, 877 N.Y.S.2d 842.

118. *Id.* at 846.

119. *Id.*

Amazon's presence in the state was limited to its "Associates Program" that allowed participants ("Associates") to maintain links to Amazon.com on their own websites.¹²⁰ In return for this link, Amazon would pay its Associates a percentage of its proceeds for any sale from a consumer who accessed Amazon.com through the link on the Associate's website.¹²¹ Furthermore, Amazon incentivized Associates to refer customers to the Amazon Prime program by compensating Associates twelve dollars for every new enrollee.¹²² Individuals who aspired to be an Associate for Amazon had to apply.¹²³ Once Amazon accepted her application, the Associate would sign an operating agreement that stated, "the relationship of the Parties [was] that of 'independent contractors.'" ¹²⁴ Amazon granted Associates "a revocable, non-exclusive, worldwide, royalty-free license . . . solely for purposes of facilitating referrals from their sites to the Amazon site."¹²⁵

Of the hundreds of thousands Amazon Associates, only a small percentage resided in New York.¹²⁶ Amazon stated, "sales to New York customers originating from New York based Associate referrals constituted less than 1.5% of Amazon's New York sales."¹²⁷

On April 23, 2008, New York ratified N.Y. Tax Law § 1101(b)(8)(vi) that requires out-of-state sellers to collect sales tax when these sellers pay commissions to New York residents for referring potential customers.¹²⁸ The new law essentially expanded the nexus requirement a state needed to collect sales taxes from an out-of-state retailer.¹²⁹ Under the new law, an out-of-state seller is exempt from the sales tax only if it could establish its commissioned New York residents "did not engage in any solicitation . . . that would satisfy the nexus requirement of the U.S. Constitution."¹³⁰

B. THE NEW YORK SUPREME COURT DECISION

About two weeks after New York passed the statute, Amazon filed a complaint against the state, alleging three primary issues.¹³¹ First, Amazon argued that the state statute violated "the Commerce Clause of the United

120. *Id.* at 845.

121. *Id.*

122. *Id.*

123. *Id.*

124. *Id.*

125. *Id.*

126. *Id.*

127. *Id.*

128. *Id.* at 846.

129. *Id.*

130. *Id.*

131. *Id.*

States Constitution, both facially and as applied to Amazon, because it impose[d] tax collection obligations on out-of-state entities who [had] no substantial nexus with New York.”¹³² Second, Amazon contended that “the provision violate[d] the Federal and State constitutions’ Due Process Clauses, both facially and as applied, because ‘it effectively create[d] an irrebuttable presumption of solicitation’ and [was] overly broad and vague.”¹³³ Third, Amazon alleged the statute “violate[d] the constitutions’ Equal Protection Clauses because ‘it intentionally target[ed] Amazon.’”¹³⁴

The New York Supreme Court did not accept Amazon’s arguments that the statute violated the Constitution and conflicted with U.S. Supreme Court precedent.¹³⁵ The court ruled in favor of the state, granting its motion for summary judgment and holding that the statute was “not facially invalid as violative of the Commerce Clause, did not violate the Commerce Clause as applied to the retailer, did not employ improper statutory presumption in violation of the Due Process Clause and was not targeted at the retailer alone.”¹³⁶ The court supported its holding on four grounds, determining that (1) Amazon had a substantial nexus to the state of New York, (2) the New York statute did not violate the Commerce Clause, (3) there was no Due Process Clause violation, and (4) the statute did not solely target Amazon’s program in New York.¹³⁷

The New York Supreme Court dismissed Amazon’s allegation that the statute was facially invalid because of a lack of a substantial nexus.¹³⁸ The court cited *National Geographic Society v. California Board of Equalization* stating, “so long as there is a ‘substantial nexus’ with the taxing State, the taxes that must be collected need not derive from the seller’s in-state activity.”¹³⁹ The court emphasized that the statute required collecting taxes if a seller enters into a contract with a New York resident, that the New York resident refer potential customers to the seller, and that the seller receive in excess of \$10,000 from New York customers referred through this contractual

132. *Id.*

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.* at 851.

137. *Id.*

138. *See id.* at 848.

139. *Id.* at 847 (citing *Nat’l Geographic Soc’y v. California Bd. of Equalization*, 430 U.S. 551, 560 (1977)).

arrangement.¹⁴⁰ The court found that all three of these elements were present in Amazon's Operating Agreement with its Associates.¹⁴¹

The New York Supreme Court also rejected Amazon's second argument, that the statute violated the Commerce Clause.¹⁴² The court based its analysis on the U.S. Supreme Court's decision in *Scripto v. Carson*.¹⁴³ In *Scripto*, the Supreme Court held that "a state could require tax collection by an out-of-state company that had contracts with ten in-state residents—deemed 'independent contractors'—who solicit orders for products on its behalf."¹⁴⁴ Following *Scripto*, the New York court stated that Amazon was benefiting from its New York Associates who were labeled "independent contractors" in the Operating Agreement.¹⁴⁵ Thus, the court determined that these Associates who encouraged Amazon sales reasonably fell within the statute.¹⁴⁶

Rejecting Amazon's allegations of due process violations, the New York Supreme Court stated that a legislative presumption—here, the presumption of solicitation—will withstand constitutional challenge if "there is some rational connection between the fact proved and the ultimate fact presumed, and . . . the inference of one fact from proof of another shall not be so unreasonable as to be a purely arbitrary mandate."¹⁴⁷ Consequently, the court determined that there was a "reasonably high degree of probability" that Amazon would want to encourage its Associates to solicit sales through the click-through links.¹⁴⁸ The court determined that Amazon was incorrect in stating that the presumption was "irrebuttable" by finding that out-of-state sellers could prevent tax collection by stopping all in-state solicitation activities.¹⁴⁹

Finally, the New York court dismissed Amazon's argument that the statute targeted Amazon specifically because it failed to state in its complaint that it was treated differently from other internet retailers. To state a valid claim under the Equal Protection Clause, a plaintiff "must allege that it was

140. *Id.* at 848.

141. *Id.*

142. *Id.* at 849.

143. *Id.*

144. *Id.* at 847 (quoting *Scripto v. Carson*, 362 U.S. 207, 209 (1960)).

145. *Id.*

146. *Id.*

147. *Id.* at 850 (quoting *Mobile, Jackson & Kansas City R.R. Co. v. Turnipseed*, 219 U.S. 35, 43 (1910)).

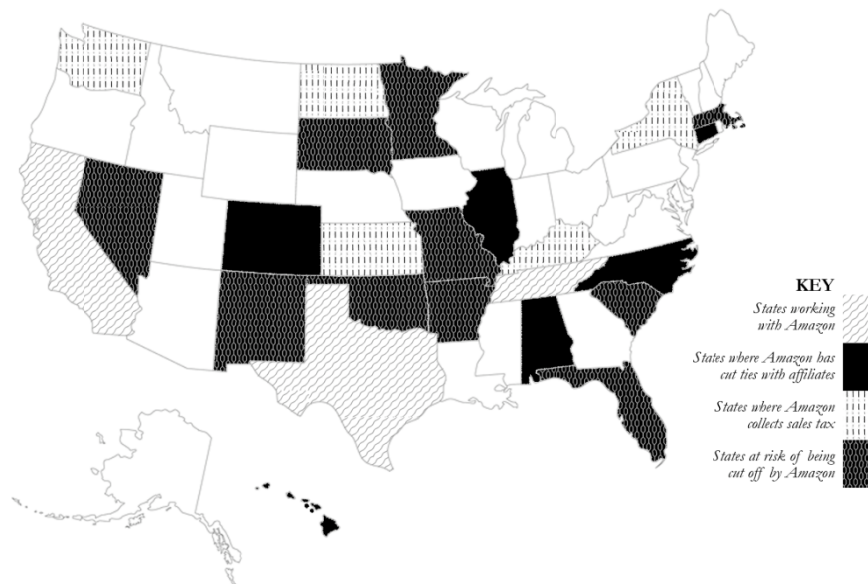
148. *Id.* at 849.

149. *Id.* at 846.

intentionally treated differently from similarly situated individuals.”¹⁵⁰ Had Amazon distinguished itself as being treated differently from other internet retailers in its complaint, it may have had a viable Equal Protection claim.¹⁵¹

Having rejected all of Amazon’s constitutional arguments, the court upheld the New York statute. Because of this decision, the New York statute and the similar statutes enacted by other states have affected the relationship between those states and Amazon.¹⁵²

Figure 1: Amazon Sales Tax Battle in the United States¹⁵³



III. TAX’S ROLE IN THE WORLD OF E-COMMERCE

As e-commerce evolves, so too does the discussion about its appropriate taxation. Events following the Amazon case reveal some of the primary arguments at play regarding the taxation of internet transactions. This Part will briefly summarize the main arguments for and against sales tax collection on internet transactions. Next, this Part will explain the national proposals aimed at addressing this issue. Then, this Part will examine what courts are likely to decide in light of state and national legislation on the subject. Finally,

150. *Id.* at 851 (quoting *Seabrook v. City of New York*, 509 F. Supp. 2d 393, 400 (S.D.N.Y. 2007)).

151. *Id.*

152. Jeanine Poggi, *Amazon Sales Tax: The Battle, State By State*, THE STREET (Nov. 14, 2011), <http://www.thestreet.com/story/11052898/amazon-sales-tax-the-battle-state-by-state.html>.

153. *Id.* This figure was re-created by the author.

this Part will suggest four requirements legislation should meet with regard to the taxation of internet transactions.

A. TWO SIDES OF THE DEBATE

1. *Pro-Sales Tax Collection*

There are four primary arguments for imposing a sales tax on internet transactions.¹⁵⁴ These arguments revolve around preferential treatment by bureaucrats toward internet retailers, unfair advantage of e-commerce against brick-and-mortar establishments, antiquated need to incubate and protect internet retailers, and suffering state economies needing additional revenue sources.

Advocates of sales taxation on internet transactions argue that lobbying organizations and political pandering inappropriately discourage lawmakers from imposing sales taxes on e-commerce.¹⁵⁵ Many on this side of the debate argue that this preferential treatment of e-commerce distorts economic decision-making because such treatment may lead consumers to choose e-commerce over traditional forms of commerce.¹⁵⁶

Second, proponents for the sales tax argue that lack of such taxation increases the digital divide, favoring consumers with internet access and retailers in the digital space.¹⁵⁷ They suggest that the only way to even the playing field is to tax both e-commerce and brick-and-mortar commerce transactions equally.¹⁵⁸

Third, the argument that internet retailers are small and in need of protection to survive in the marketplace is no longer as viable as it was in the 1990s.¹⁵⁹ Giants like Amazon, eBay, and Overstock.com account for significant portion of consumer purchases today.¹⁶⁰ Consequently,

154. Charles McLure, *The Taxation of Electronic Commerce: Background and Proposal*, in PUBLIC POLICY AND THE INTERNET: TAXATION AND PRIVACY (Nicholas Imparato, ed. forthcoming), available at <http://www.egov.ufsc.br/portal/sites/default/files/anexos/20477-20478-1-PB.pdf>.

155. *Id.* at 3.

156. *Id.*

157. *Id.*

158. *Id.*

159. See Stefany Moore, *Barnes & Noble's e-Commerce Site Is No Longer Just About Books*, INTERNET RETAILER (Oct. 19, 2011), <http://www.internetretailer.com/2011/10/19/barnes-nobles-e-commerce-site-no-longer-just-about-books>. (discussing the growth of internet retailers).

160. According to Internet Retailer's Top 100 Guide, Amazon.com is number 1 in the industry. *Id.*

proponents for the internet tax argue that it is no longer necessary to shield such companies from a sales tax requirement to support growth.¹⁶¹

Finally, proponents for the sales tax highlight the struggling economy and the reality that states could use internet taxes as a source of revenue for state coffers.¹⁶² These individuals argue that as e-commerce continues to grow, the inability of states to collect taxes on consumer purchases will lead to serious negative economic consequences.¹⁶³

2. *Anti-Sales Tax Collection*

Those against requiring internet retailers to collect sales tax from internet transactions assert that the tax is unconstitutional and unfair to e-commerce. The anti-sales taxation position is buttressed by three primary arguments.

First, sales tax opponents argue that an e-commerce sales tax will lead to loss of jobs by harming small businesses.¹⁶⁴ Many of the Amazon affiliates were small businesses and, because of state “affiliate” statutes, Amazon simply cut ties with these individuals, negatively affecting their businesses.¹⁶⁵ Furthermore, many small e-businesses have stated that they lack the capability to collect taxes on consumer purchases in numerous states, thus affecting their ability to do business in multiple areas.¹⁶⁶

Second, those against internet sales taxation argue that legislation—like that at issue in the *Amazon* case—violates the Commerce Clause.¹⁶⁷ Because Supreme Court precedent prohibits a state from requiring an out-of-state retailer to collect and remit a tax unless the retailer has a “substantial nexus” with the taxing state, and because this nexus is arguably lacking in the relationship between internet retailers and the taxing state, laws that impose a sales tax on internet transactions run afoul of the Commerce Clause.¹⁶⁸

161. See Moore, *supra* note 159.

162. See Laura Gordon-Murnane, *E-Commerce and Internet Taxation, Issues, Organizations, and Findings*, KNOWLEDGE NET UNLIMITED (Dec. 1, 2011), <http://www.infotoday.com/searcher/jun00/gordon-murnane.htm>.

163. *Id.*

164. *Tax Collection Laws Could Harm Small e-Commerce Business*, PATRICIA WEBER CONSULTING (Feb. 3, 2012), <http://www.patriciaweberconsulting.com/online-payment-processing-blog/benefits-of-accepting-online-payments/tax-collection-laws-could-harm-small-e-commerce-businesses/>.

165. Katy Grimes, *Amazon Tax Would Kill 25K CA Businesses*, CAL WATCHDOG, 3 (Nov. 14, 2011), <http://www.calwatchdog.com/2011/06/21/>.

166. *Tax Collection Laws Could Harm Small e-Commerce Business*, *supra* note 164.

167. Daniel Cowan, *New York's Unconstitutional Tax on the Internet: Amazon.com v. New York State Dep't of Taxation & Finance and the Dormant Commerce Clause*, 88 N.C. L. REV. 1423 (2010).

168. *Tax Collection Laws Could Harm Small e-Commerce Business*, *supra* note 164.

Third, those against the sales tax argue that its imposition is unfair to e-commerce because, even today, internet retailers need protection from taxes to thrive in the marketplace.¹⁶⁹ Opponents of the tax primarily rest their argument on the effect of such a tax on small businesses.¹⁷⁰ For example, over 17,000 small businesses in California submitted letters to their legislators to oppose laws that impose a tax collection obligation on internet retailers.¹⁷¹ These small businesses primarily oppose this tax collection because many of these businesses earn revenue by placing advertisements from out-of-state retailers on their websites and, “[t]he bill states that if someone has advertisements on California Web sites, then there is a nexus in California, and the business needs to pay taxes on all revenue collected in the state.”¹⁷² This portion of the argument primarily rests on the need to foster the growth of e-commerce as it continues to develop.

B. STATUTES AND PROPOSALS

The inconsistent laws and the complexity of state-by-state legislation have compelled lawmakers to attempt to create uniform tax acts to regulate e-commerce taxation. Most of the legislation attempts to address arguments from both sides of the debate. One example is the Streamlined Use Tax and Sales Agreement, enacted in 2002.¹⁷³ Lawmakers have drafted other national proposals, such as the Main Street Fairness Act and the Marketplace Fairness Act.¹⁷⁴ This Section will explain the details of each of these acts and how they attempt to mitigate the constitutional, logistical, and policy challenges facing sales tax collection on internet transactions.

1. *Streamlined Sales and Use Tax Agreement*

Congress adopted the Streamlined Sales and Use Tax Agreement (“SSUTA”) on November 12, 2002.¹⁷⁵ The fundamental purpose of the act was to “simplify and modernize sales and use tax administration in order to

169. *Id.*

170. *Id.*

171. Grimes, *supra* note 165.

172. *Id.*

173. *Streamlined Sales and Use Tax Agreement*, STREAMLINED SALES TAX GOVERNING BOARD, INC. (Nov. 14, 2011), <http://www.streamlinedsalestax.org/index.php?page=modules>.

174. *The Main Street Fairness Act*, THE NEW RULES PROJECT (Nov. 15, 2011), [http://www.newrules.org/retail/rules/internet-sales-tax-fairness/main-street-fairness-act](http://www.newrules.org/retail/rules/internet-sales-tax-fairness/main-street-fairness-act;); *see also* Jason Hamilton, *Bi-Partisan Marketplace Fairness Act Introduced in the Senate Today*, 404 TECH SUPPORT (Nov. 9, 2011), <http://www.404techsupport.com/2011/11/bi-partisan-marketplace-fairness-act-introduced-to-senate-today/>.

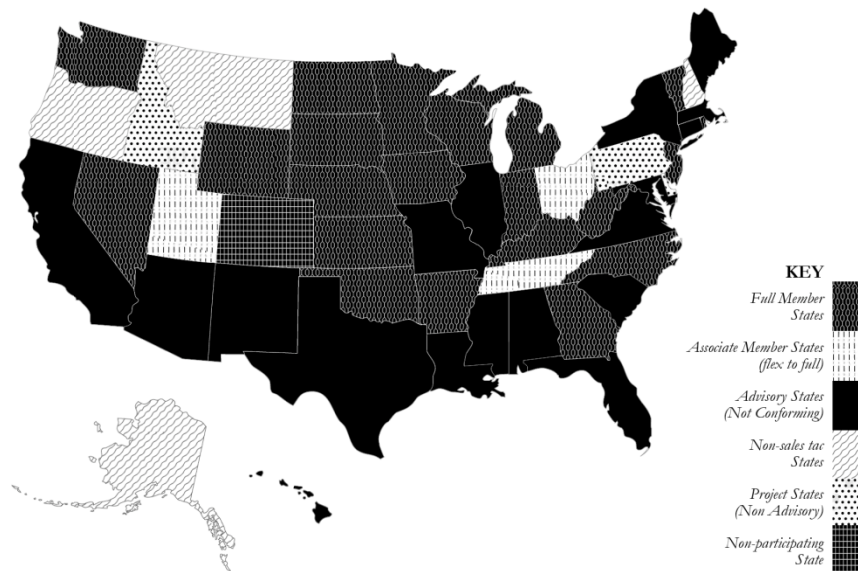
175. *Streamlined Sales and Use Tax Agreement*, *supra* note 173.

substantially reduce the burden of tax compliance.”¹⁷⁶ The Streamlined Sales Tax Governing Board, responsible for drafting the act, stated that

the goal of [the] effort is to find solutions for the complexity in state sales tax systems that resulted in the U.S. Supreme Court holding (*Bellas Hess v. Illinois and Quill Corp. v. North Dakota*) that a state may not require a seller that does not have a physical presence in the state to collect tax on sales into that state.¹⁷⁷

The SSUTA sets standards by which states can create legislation that encourages internet retailers and other remote sellers to collect tax on sales to consumers living in the participating states.¹⁷⁸ States participating in the SSUTA typically work within their own borders to pass legislation that follows the SSUTA and requires sales tax collection.¹⁷⁹ Figure 2, *infra*, illustrates state participation in the SSUTA.

Figure 2: Streamlined State Status as of August 8, 2011¹⁸⁰



2. Main Street Fairness Act

Senator Dick Durbin sponsored the Main Street Fairness Act in August 2011.¹⁸¹ The Main Street Fairness Act attempts to create consistency and to

176. *Id.*

177. *Id.*

178. *Frequently Asked Questions*, STREAMLINED SALES TAX GOVERNING BOARD, INC. (Nov. 14, 2011), <http://www.streamlinedsalestax.org/index.php?page=faqs>.

179. *Id.*

180. Poggi, *supra* note 152. This figure was re-created by the author.

level the competition for all businesses. The legislation would require states to “adhere to uniform product definitions, adopt uniform requirements for filing sales tax returns, administer both state and local sales tax collection through a single state office, and allow retailers to register through a centralized, one-stop multistate registration system.”¹⁸²

The passing of the Main Street Fairness Act would impose a national tax standard but allow states abiding by the SSUTA to force internet sellers to collect tax based on their own state’s legislation.¹⁸³ Traditional retailers such as Target, Wal-Mart, Best Buy, Home Depot, and Sears all support the Main Street Fairness Act.¹⁸⁴ Most large retailers support the passage of a national tax, arguing that it would level the playing field between them and large internet retailers.¹⁸⁵

Advocates for the Main Street Fairness Act argue that it would eliminate some of the negative, unintended consequences of nexus legislation such as New York’s “Amazon Tax.” For example, under the “Amazon Tax,” small businesses suffer a disproportionate amount of the adverse consequences, as Amazon has terminated its relationship with some of these businesses when states have passed these laws.¹⁸⁶ This type of legislation has also harmed many brick-and-mortar businesses, as customers price shop in their stores and subsequently purchase the item online to save on sales tax.¹⁸⁷ By allowing states to require all online retailers, not just those with affiliate programs or substantial nexus, to collect sales tax, the Main Street Fairness Act could purportedly eliminate these harms to small businesses and brick-and-mortar stores.¹⁸⁸

Nevertheless, not everyone is pleased with the Main Street Fairness Act. Some internet businesses argue that it is brick-and-mortar retailers who have the competitive advantage. This argument follows from the observation that brick-and-mortar businesses have the tangible advantages of community

181. *The Main Street Fairness Act*, THE NEW RULES PROJECT (Nov. 15, 2011), <http://www.newrules.org/retail/rules/internet-sales-tax-fairness/main-street-fairness-act>.

182. *Id.*

183. *Id.*

184. *Wall Street Journal: Retailers Support the Main Street Fairness Act*, BLOG.FEDTAX.NET (Nov. 28, 2011), <http://blog.fedtax.net/2011/03/17/wall-street-journal-retailers-support-main-street-fairness-act/>.

185. *Id.*

186. See Zak Stambor, *Amazon Cuts Affiliate Ties Over Sales Tax, and Retail Chain Rivals Try to Take its Place*, INTERNET RETAILER (Mar. 31, 2011), <http://www.internetretailer.com/2011/03/31/amazon-cuts-affiliate-ties-over-sales-tax>.

187. Gordon-Murphy, *supra* note 162.

188. *Main Street Fairness Act*, New Rules Project, (Dec. 1, 2011), <http://www.newrules.org/retail/rules/internet-sales-tax-fairness/main-street-fairness-act>.

involvement, ease of returns, and customer satisfaction, as the customer can see and hold a product prior to purchase.¹⁸⁹ Many small online businesses also oppose the Main Street Fairness Act. These businesses argue that the tax imposition will stifle growth on budding e-businesses, especially in the tough economic climate.¹⁹⁰

3. *Marketplace Fairness Act*

In response to some of the concerns about the Main Street Fairness Act, Senators Mike Enzi (Republican of Wyoming), Dick Durbin (Democrat of Illinois), Lamar Alexander (Republican of Tennessee), and Tim Johnson (Democrat of South Dakota) introduced the Marketplace Fairness Act, also referred to as the Enzi-Durbin-Alexander bill.¹⁹¹ If enacted, the Act will create a constitutional framework for collecting sales tax online; it will “allow states to require out of state retailers to collect sales tax at the time of purchase[,] . . . remit those taxes on behalf of customers, and . . . facilitate collection on behalf of third party sellers.”¹⁹²

The support for the bill is mixed. Amazon has expressed strong support for the bill’s passage, stating that it “strongly supports enactment of the Enzi-Durbin-Alexander bill and will work with Congress, retailers, and the states to get this bi-partisan legislation passed.”¹⁹³ Amazon argues that, unlike other bills addressing national taxation that target its affiliate program, the Marketplace Fairness Act is simplified and applies broadly so as to not only target Amazon.¹⁹⁴

By contrast, eBay does not support the Marketplace Fairness Act. A trade group that represents the company, the Computer and Communications Industry Association, responded to the bill and those fighting against it. The Association stated that “it is extremely heartening to know that there are

189. Ken Berry, *Will Congress Green Light the Main Street Fairness Act?*, ACCOUNTINGWEB TAX, SALES & USE TAX (Nov. 16, 2011), <http://www.accountingweb.com/topic/tax/will-congress-green-light-main-street-fairness-act>.

190. *Lungren Introduces Resolution to Protect Small Business and Entrepreneurs from New Sales Taxes*, CONGRESSMAN DAN LUNGREN (Nov. 14, 2011), <http://lungren.house.gov/index.cfm?sectionid=39§iontree=6,39&itemid=759>.

191. Jason Hamilton, *Bi-Partisan Marketplace Fairness Act Introduced in the Senate Today*, 404 TECH SUPPORT (Nov. 9, 2011), <http://www.404techsupport.com/2011/11/bi-partisan-marketplace-fairness-act-introduced-to-senate-today/>.

192. *Id.*

193. *Amazon Strongly Supports Enactment of Enzi-Durbin-Alexander Federal Online Sales Tax Bill*, AMAZON.COM (Nov. 14, 2011), <http://phx.corporate-ir.net/phoenix.zhtml?c=176060&p=irol-newsArticle&ID=1628503&highlight=>.

194. See Nate Anderson, *Surprise: Amazon “Strongly Supports” New Sales Tax Bill*, ARSTECHNICA (Dec. 1, 2011), <http://arstechnica.com/tech-policy/news/2011/11/surprise-amazon-strongly-supports-new-sales-tax-bill.ars>.

those in the Senate, as well as the House, who are willing to stand up in support of innovation and entrepreneurship against retrogressive measures that would draft online vendors into service as remote sales tax collectors.¹⁹⁵ Furthermore, Tod Cohen, the vice president for government relations at eBay, argued “it does not make sense to expand Internet sales tax burdens on small businesses at a time when we want entrepreneurs to create jobs and economic activity.”¹⁹⁶

In response, opponents to eBay’s position contend that the Marketplace Fairness Act exempts small e-businesses whose gross sales are less than \$500,000 annually from sales tax collection.¹⁹⁷ Such a provision takes into consideration the concerns expressed by small businesses that argue that a sales tax collection would disproportionately harm them.

C. THE POTENTIAL EFFECTS OF INTERNET TRANSACTIONS SALES TAX LEGISLATION ON CONSUMERS, RETAILERS, AND STATES

A sales tax on online purchases would affect consumers, internet retailers, and state governments in a variety of ways. Consumers would no longer have the option to avoid sales taxes by purchasing online.¹⁹⁸ Consequently, those consumers who would have purchased online for this reason will likely resort to physical establishments, which would promote brick-and-mortar commerce. Internet retailers may lower prices to maintain an advantage over their brick-and-mortar competitors.¹⁹⁹ The Act may also force internet retailers to develop the logistical systems necessary to collect sales taxes on all transactions. State governments may benefit from streamlined national proposals, as the sales tax collected from internet retailers could go into state budgets, potentially increasing collective state revenue by “23 billion a year in uncollected taxes.”²⁰⁰

D. JUDICIAL RESPONSE TO INTERNET TRANSACTIONS SALES TAX LEGISLATION

The divergent nexus requirements detailed on a case-by-case basis reveal an already growing new problem: lack of predictability. Proposals like the

195. Hamilton, *supra* note 191.

196. Jan Norman, *U.S. Senate Moves To Allow Internet Sales Tax*, THE ORANGE COUNTY REGISTER (Nov. 14, 2011), <http://m.ocregister.com/articles/tax-326546-states-sales.html>.

197. *Small Businesses Applaud Introduction of Marketplace Fairness Act*, THE KITSAP PENINSULA BUSINESS JOURNAL (Nov. 14, 2011), http://kpbj.com/business_weekly/2011-11-14/small_businesses_applaud_introduction_of_marketplace_fairness_act.

198. Hamilton, *supra* note 191.

199. *See* Gordon-Murname, *supra* note 162.

200. Kyung M. Song, *Tax Free Shopping Doomed?*, CHICAGO SUN-TIMES (Nov. 14, 2011), <http://www.suntimes.com/8747010-417/tax-free-shopping-doomed.html>.

Main Street Fairness Act, the Marketplace Fairness Act, and a pending decision in the New York Supreme Court reveal the effort legislators and courts are making to address the proper method of taxing internet transactions. Furthermore, courts will likely continue to decide questions of constitutionality and jurisdiction of internet transactions taxation. This Section will discuss how courts will likely decide when faced with state statutes and the pending national proposals.

1. *State Statutes*

Table 1, *infra*, provides a list of states that either proposed or enacted bills that would require internet retailers to collect and remit a sales tax. One likely concern for the Courts is whether or not such statutes contain an “affiliate” requirement. As noted by the New York Supreme Court in *Amazon*, such individualized tactics can possibly violate the Constitution.²⁰¹ Another primary concern will be the “intentionality requirement,” which requires the plaintiff to “allege that [she] was intentionally treated differently from similarly situated individuals” under the Equal Protection Clause.²⁰² If a court finds that a statute unjustly targets only one type of retailer, it will likely deem such a law unconstitutional as impeding interstate commerce.²⁰³ However, the plaintiff will typically bear this high burden of alleging the intentionality of the defendant.²⁰⁴ Furthermore, if Congress passes the Marketplace Fairness Act into law, most of these states will have to simplify their nexus legislation to conform with the law.²⁰⁵

201. *See* *Amazon.com, LLC v. N.Y. State Dep’t. of Taxation & Fin.*, 877 N.Y.S.2d 842, 850–51 (N.Y. Sup. Ct. 2010).

202. *Id.* at 851.

203. *See id.*; *see also* *Quill Corp. v. North Dakota*, 504 U.S. 298, 310 (1992).

204. *See* *Village of Willowbrook v. Olech*, 528 U.S. 562, 564 (2000).

205. *Small Businesses Applaud Introduction of Marketplace Fairness Act*, Market Watch, THE WALL STREET JOURNAL (Nov. 14, 2011), <http://www.marketwatch.com/story/small-businesses-applaud-introduction-of-marketplace-fairness-act-2011-11-09>.

Table 1: Selected/Implemented E-Commerce Tax Statutes by State²⁰⁶

STATE	STATUTE	AFFILIATE AS NEXUS?
California ²⁰⁷	AB 28 1x 28: Enacted. However, Governor Jerry Brown signed AB 155 into law, which repealed the affiliate nexus tax for one year from September 2011.	Yes, included in the Democrats' 2010 budget proposal and would impose an "affiliate nexus tax" on all purchases made online from out-of-state retailers
Colorado ²⁰⁸	H.B. 10-1193: Enacted	Yes
Connecticut ²⁰⁹	Senate Bill 239: Enacted	Yes, "affiliate nexus tax" on all purchases made online
Florida ²¹⁰	Senate Bill 204: Died in committee on April 30, 2010	Not specifically, would have established Streamlined Sales Tax in Florida with the goal of extending the sales tax to out-of-state online purchases
Hawaii ²¹¹	H.B.1405: Vetoed by governor	Yes, would have imposed "affiliate nexus" on all online purchases
Illinois ²¹²	House Bill 3659: Enacted	Yes, imposes an "affiliate nexus tax" on all internet purchases

206. This table was created by the author.

207. *Governor Brown Signs Legislation*, CA.GOV (June 29, 2011), <http://gov.ca.gov/news.php?id=17101>. *But see* Shelly Sullivan, *Governor Signs Legislation That Will Help 25,000 California Companies Get Back in Business*, PERFORMANCE MARKETING ASSOCIATION (Sept. 23, 2011), <http://performancemarketingassociation.com/california-repeals-the-affiliate-nexus-tax-law>.

208. H.B. 10-1193, 112 Leg., 2nd Sess. (Colo. 2011).

209. S.B. 1239, 112 Leg., 1st Sess. (Conn. 2011).

210. *SB 204: Streamlined Sales and Use Tax Agreement*, FLORIDA HOUSE OF REPRESENTATIVES (Oct. 3, 2011), http://www.myfloridahouse.gov/Sections/Bills/bills_detail.aspx?BillId=42322&BillText=specified+digital+good&HouseChamber=H&SessionId=64&.

211. H.B. 1405, 25th Leg., Reg. Sess. (Haw. 2009). Although the Hawaii Legislature passed the bill, Hawaii Governor Linda Lingle vetoed it. *See* Mike Sachoff, *Hawaii Governor Vetoes Amazon Tax Law*, WEB PRO NEWS (July 2, 2009), <http://www.webpronews.com/topnews/2009/07/02/hawaii-governor-vetoes-amazon-tax-law>.

212. Janet Novak, *Illinois Governor Signs Amazon Internet Sales Tax Law*, FORBES.COM (Oct. 3, 2011), <http://www.forbes.com/sites/janetnovack/2011/03/10/illinois-governor-signs-amazon-internet-sales-tax-law/>.

STATE	STATUTE	AFFILIATE AS NEXUS?
Indiana ²¹³	House Bill 250; In committee	Not specifically, would apply the sales tax to sales of digital goods and also conforms the state's tax code to the Streamlined Sales Tax
Maryland ²¹⁴	Senate Bill 824: Bill never made it out of committee	Not specifically, would apply the sales tax to all products purchased online from out-of-state retailers
Minnesota ²¹⁵	Minnesota Senate omnibus tax bill, SF2074: Abandoned without legislative action	Yes
Mississippi ²¹⁶	Senate Bill 2927: Died in committee on February 2, 2010	Yes, would have enacted an "affiliate nexus tax" on all online sales made by in-state consumers and out-of-state retailers would have been required to collect the tax and remit it back to the state
New Mexico ²¹⁷	House Bill 50: Tabled	Yes, would establish an "affiliate nexus tax" and would require out-of-state retailers to collect tax on state consumers and remit it to the state
Nevada ²¹⁸	Governor has proposed a nexus tax in budget	Yes, proposal included "affiliate nexus tax" provision
North Carolina ²¹⁹	HB 867: Enacted	Yes, "Click through nexus" sufficient for sales tax collection

213. S.B. 250, 111 Leg., (Ind. 2010).

214. *Maryland and Connecticut Updates*, AFFILIATE ADVOCACY (Oct. 3, 2011), <http://affiliateadvocacy.com/2010/maryland-and-connecticut-updates/>. The bill, however, failed to make it out of committee. See Missy Ward, *Maryland Advertising Tax SB 1071 Gets Squashed*, MISSYWARD.COM (Oct. 3, 2011), <http://www.missyward.com/2009/04/14/maryland-advertising-tax-sb-1071-gets-squashed/>.

215. S.F. No. 2074, 110 Leg., 2nd Engrossment (Minn. 2009).

216. S.B. 2927, 111 Leg., 54 Reg. Sess. (Miss. 2010).

217. Ken Garcia, *New Mexico HB 50-New Internet Tax Bill*, GTOMANAGEMENT (Oct. 3, 2011), <http://gtomanagement.com/new-mexico-hb-50-new-internet-tax-bill/>.

218. Cy Ryan, *Gibbons' Budget Plan Calls for Higher Taxes, Fees*, THE LAS VEGAS SUN (Nov. 14, 2011), <http://www.lasvegassun.com/news/2010/feb/17/gibbons-budget-plan-calls-higher-taxes-fees/>.

219. H.B. S.715, 112th Leg., 2nd Sess. (N.C. 2011).

STATE	STATUTE	AFFILIATE AS NEXUS?
Rhode Island ²²⁰	HB 7071: Pending committee	Not specifically, but would require online retailers and catalogue sellers to collect sales tax like other local businesses
Vermont ²²¹	House Bill 661: In committee	Yes; proposal includes "affiliate nexus tax" provision
Virginia ²²²	Senate Bill 660: Tabled in finance by voice vote in 2010.	Yes; language included affiliate tax provision
Washington ²²³	House Bill 2620: Enacted	Not specifically, clarifies prior legislation that enacted a digital goods tax on consumers.
Wyoming ²²⁴	House Bill 29: Enacted	Not specifically, enacts a digital goods tax on digital goods

2. Federal Proposals

Courts will likely look at the federal proposals and analyze whether they provide states with excessive power in a way that obstructs interstate commerce.²²⁵ The primary concern of the Supreme Court in *National Bellas Hess* and *Quill Corp.* was whether states had the power to enforce tax burdens on out-of-state retailers in a way that effectively prohibited interstate commerce and thus violated the Constitution.²²⁶ The *Amazon* case reveals how some courts are moving away from the strict physical presence requirement in *Quill Corp.* and questioning whether a streamlined proposal might be more appropriate.²²⁷

E. REQUIREMENTS INTERNET TRANSACTION TAXATION LEGISLATION SHOULD MEET

The legal landscape surrounding e-commerce taxation, both statutorily and within case law, is ambiguous and difficult to predict. This Note argues

220. H. 7071, 111 Leg., 1st Sess. (R.I. 2010).

221. H. 661, 111 Leg., 2nd Gen. Assembly (Vt. 2010).

222. S.B. 660, 111 Leg., 1st Gen. Assembly (Va. 2010).

223. H.B. 2620, 111 Leg., 1st Sess. (Wash. 2010).

224. H.B. 0029, 111 Leg., 2nd Sess. (Wyo. 2010).

225. *See Quill Corp. v. North Dakota*, 504 U.S. 298, 310 (1992); *see, e.g., Nat'l Bellas Hess v. Dep't of Revenue*, 386 U.S. 753, 760 (1967); *Amazon.com, LLC v. N.Y. State Dept. of Taxation & Fin.*, 877 N.Y.S.2d 842, 847 (N.Y. Sup. Ct. 2010).

226. *Quill*, 504 U.S. at 310.

227. *See, e.g., Amazon*, 877 N.Y.S.2d 842.

that lawmakers should aim to meet the following four requirements when drafting such legislation: (1) the legislation should clarify the tax landscape not only for internet retailers but for consumers as well;²²⁸ (2) the legislation must be constitutional;²²⁹ (3) the legislation should promote virtual business equally and foster e-commerce growth;²³⁰ and (4) the legislation should be forward thinking, addressing developments in technology and in e-commerce.²³¹

First, the law must be clear and consistent for consumers and businesses alike. As one commentator has explained:

Anyone doing business in cyberspace needs to know what laws to obey, whether it be a question of what taxes are due and where, or what consumer protections apply to the sale of their products and services. . . . [A] legal infrastructure that can provide the requisite elements of certainty and predictability . . . will allow electronic commerce to flourish as efficiently as market forces dictate.²³²

By having a clear standard, both consumers and businesses will know what to expect. This would create a predictable foundation upon which e-commerce would thrive. Predictability is a crucial point in both the pro-sales taxation and anti-sales taxation debates.²³³ Small and large businesses will benefit from the ability to incorporate tax issues into their accounting methods, and consumers will benefit from having a better understanding of when they must calculate taxes into their purchase prices.

The law may affect various types of businesses differently, but a consistent standard will promote efficiency the most effectively. For example, if each state had a different set of accounting laws and reporting requirements, a business would need to research each state's laws when doing business there. Such a process, through both research and compliance, could require substantial efforts and resources from a business. Some small business might be indirectly prevented from participating because of such an impediment. This type of inconsistency is at play in the current online sales tax landscape. Instead, legislators should draft a clear requirement that could better manage expectations, facilitate planning for businesses and consumers, and thus help to ensure greater diversification in the market.

228. Dan Stempel, *Who Has Jurisdiction over the Internet?*, 39 FAIRFIELD COUNTY BUS. J., no. 41, 2000, at 10.

229. See, e.g., *Quill*, 504 U.S. 298.

230. See Gordon-Murname, *supra* note 162.

231. See Groves, *supra* note 10, at 619.

232. Stempel, *supra* note 228, at 10.

233. *Id.*

Second, legislation around internet taxation must be constitutional. The Framers designated the Commerce Clause and the Due Process Clause as a means to promote the economy and sustain interstate commerce, and courts will likely address constitutional concerns after the enactment of the aforementioned statutes.²³⁴ The new law should be uniform so as to allow states access to the potential revenue sources while promoting virtual business across state lines.²³⁵

Internet retailers will likely argue that sales tax collection on online transactions is unconstitutional.²³⁶ Internet retailers, however, seem analogous to mail-order catalogues.²³⁷ Since the laws that require mail-order catalogues to collect sales taxes are constitutional, legislators have the opportunity to create something similar and constitutional for internet retailers. Legislators, however, must take care that such a provision does not target only one particular type of business.

Third, the new law should not be overly burdensome on small retailers. Although some internet retailers are large enterprises, there are still several small e-business that are trying to survive.²³⁸ In order to maintain a diversified marketplace and greater options for consumers, it is necessary that more than a few large businesses dominate the space. As such, legislators should consider whether taxation would limit small businesses from adequately competing.²³⁹

Fourth, the legislation should be timely. New developments should take into account how the e-commerce landscape will evolve by attempting to create legislation that anticipates further e-commerce evolution. Lawmakers should take into account other issues involved in online transactions—such as privacy or new business technology—and create legislation that is encompassing, but not outdated. E-commerce is essentially an evolution of the mail-order catalogue. Accordingly, lawmakers should analyze what new technological developments are and will be part of the consumer landscape. As technology evolves, so too does consumer mobility. Perhaps the physical nexus and state sales tax is no longer the proper means to determine tax responsibility. It is possible that lawmakers may need to create an entirely

234. See, e.g., *Quill*, 504 U.S. 298.

235. See Stempel, *supra* note 228, at 10.

236. See, e.g., *Amazon.com, LLC v. N.Y. State Dep't of Taxation & Fin.*, 877 N.Y.S.2d 842 (N.Y. Sup. Ct. 2010).

237. See *Quill*, 504 U.S. 298.

238. See Grimes, *supra* note 165.

239. *What Is the eTax?*, STOP ETAXES.COM (Dec. 15, 2011), <http://stopetaxes.com/what-is-etax>.

new type of tax that addresses online shopping and develops an equitable model to distribute tax revenue to states.

IV. CONCLUSION

A state's ability to tax an out-of-state entity is not a new discussion. When analogized to mail-order catalogues, the question of how to tax e-commerce transactions is not a completely new discussion either. Initially, legislatures decided issues of taxation in a way to ensure that e-commerce continued to thrive and to protect budding internet retailers. Today, however, many internet retailers are large enterprises, and although the growth of e-commerce has changed many components of the discussion, some elements remain the same. Courts are still fundamentally concerned with the constitutionality of taxes. Although the physical nexus requirement has evolved, courts are primarily interested in whether an entity has "purposefully availed"²⁴⁰ itself of a particular state as a way to determine whether taxation requirements are proper. One particular case, *Amazon v. New York Department of Taxation & Finance*, lays out the constitutional debate and the elements a court considers when facing a taxation constitutionality question.²⁴¹

As the discussion evolves, legislators should consider legislation that clarifies the tax landscape, not only for internet retailers, but for consumers as well.²⁴² Any new laws should promote virtual business equally and foster e-commerce growth.²⁴³ As such, new laws should be forward thinking, addressing developments in technology and e-commerce. As this discussion reveals, the controversy is not about *whether* to tax, but instead about *how* to tax. Accordingly, legislators should consider the multifaceted nature of the issue so as to impose tax requirements effectively and within constitutional limits.

240. *Quill*, 504 U.S. at 307.

241. *See Amazon*, 877 N.Y.S.2d 842.

242. *See Strempel*, *supra* note 228, at 10.

243. *Id.*

