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| To:      | Sales and Use Tax Nexus Model Statute Workgroup               |
| From:    | Roxanne Bland, MTC Counsel                                    |
| Date:    | June 21, 2013   |
| Subject: | Model Sales and Use Tax Nexus Statute –Draft Policy Checklist |

At its May 20, 2013 teleconference, the working group asked staff to illustrate the draft policy questions with existing state statutory language or draft language. Below are the policy questions with statutory and case law examples from several states.

In addition, the subcommittee asked the work group to determine whether the Internet Tax Freedom Act would have any impact on the associate nexus portion of the model statute. The MTC submitted a brief in the Illinois Supreme Court on this issue in *Performance Marketing Association v. Hamer*, and reproduces its argument below.

## I. POLICY QUESTIONS

1. How much or how little in-state activity will rise to the level of “establish[ing] and maintain[ing]” a market in a state so as to confer nexus on an out-of-state retailer? For non-internet sales, should the emphasis be on the quality of the contacts rather than the quantity of contacts?

*Arizona Department of Revenue v. O’Connor, Cavanagh, Killingsworth and Beshears, P.A.*, 963 P.2d 279 (1998)

Arizona Department of Revenue brought action against O’Connor for use tax owed on a now-defunct out-of-state office furniture retailer arguing that the retailer had insufficient nexus with Arizona to impose the transaction privilege tax. The retailer had entered into a contract with O’Connor to build a substantial amount of custom office furniture. O’Connor was the retailer’s only client in Arizona. Finding that the matter was governed by *Tyler Pipe Industries, Inc. v. Washington Department of Revenue*, 483 U.S. 232 (1987), after an examination of the retailer’s activities, the court concluded that those activities were substantial and helped the retailer to establish and maintain its market in the state. “[F]or the purpose of establishing nexus, the volume of local activity is less significant than the nature of its function[.]”

*Arizona Department of Revenue v. Care Computer Systems, Inc.*, 4 P.3d 169 (2000) “[T]he volume of local activity is less significant than the nature of its function on the out-of-state taxpayer’s behalf.”

2. Should the proposal specify that nexus is found in cases of an in-state person unrelated to the out-of-state retailer and with no formal agreement with the retailer, but who acts as a “*de facto* marketing and distribution” channel in the state for the retailer’s goods? For example:

An out of state seller is a retailer in this state regardless of the lack of a formal agency, independent contractor, or any other contractual relationship with an in state person if the in-state person’s activities are significantly associated with the seller’s ability to establish and maintain a market in this state.

3. Should the proposal specify that third-party independent contractors soliciting within a state on behalf of an out-of-state retailer results in nexus with the state?

**K.S. A. 79-3702(h)**

79-3702(h)(1) "Retailer doing business in this state" or any like term, means:

79-3702(h)(1)(B) any retailer having an employee, independent contractor, agent, representative, salesperson, canvasser or solicitor operating in this state either permanently or temporarily, under the authority of the retailer or its subsidiary, for the purpose of selling...soliciting sales or the taking of orders for tangible personal property.

This is the statutory equivalent of the U.S. Supreme Court decision in *Scripto v. Carson*.

4. Should the proposal specify that the unitary business may be the basis for analyzing nexus?

**K.S.A. 79-3702(h)(2)** A retailer shall be presumed to be doing business in this state if:

79-3702(h)(2)(A) Both of the following conditions exist:

79-3702(h)(2)(A)(i) The retailer holds a substantial ownership interest in, or is owned in whole substantial part by, a retailer maintaining a sales location in Kansas; and

79-3702(h)(2)(A)(ii) the retailer sells the same or a substantially similar line of products as the related Kansas retailer and does so under the same or a substantially similar business name, or the Kansas facilities or Kansas employees of the related Kansas retailer are used to advertise, promote or facilitate sales by the retailer to consumers.

**California Unitary Nexus Regulation 1684**

A retailer is engaged in business in this state as defined in section 6203 of the Revenue and Taxation Code if:

(A) The retailer is a member of a commonly controlled group, as defined in Revenue and Taxation Code section 25105; and

(B) The retailer is a member of a combined reporting group, as defined in California Code of Regulations, title 18, section 25106.5, subdivision (b)(3), that includes another member of the retailer's commonly controlled group that, pursuant to an agreement with or in cooperation with the retailer, performs services in California in connection with tangible personal property to be sold by the retailer, including, but not limited to, design and development of tangible personal property sold by the retailer, or the solicitation of sales of tangible personal property on behalf of the retailer. For purposes of this paragraph:

(i) Services are performed in connection with tangible personal property to be sold by a retailer if the services help the retailer establish or maintain a California market for sales of tangible personal property; and

(ii) Services are performed in cooperation with a retailer if the retailer and the member of the retailer's commonly controlled group performing the services are working or acting together for a common purpose or benefit.

## **Idaho**

63-3615A(1) Subject to the limitation in subsection (2) of section 63-3611, Idaho Code, a retailer has substantial nexus with this state if both of the following apply:

63-3615A(1)(a) The retailer and an in-state business maintaining one (1) or more locations within this state are related parties; and

63-3615A(1)(b) The retailer and the in-state business use an identical or substantially similar name, trade name, trademark or goodwill to develop, promote or maintain sales, or the in-state business provides services to, or that inure to the benefit of, the out-of-state business related to developing, promoting or maintaining the in-state market.

63-3615A(2) Two (2) entities are related parties under this section if they meet any one (1) of the following tests:

63-3615A(2)(a) Both entities are component members of the same controlled group of corporations under section 1563 of the Internal Revenue Code;

63-3615A(2)(b) One (1) entity is a related taxpayer to the other entity under the provisions of section 267 of the Internal Revenue Code;

63-3615A(2)(c) One (1) entity is a corporation and the other entity and any party, for which section 318 of the Internal Revenue Code requires an attribution of ownership of stock

from that party to the entity, own directly, indirectly, beneficially, or constructively at least fifty percent (50%) of the value of the outstanding stock of the corporation; or

63-3615A(2)(d) One (1) or both entities is a limited liability company, partnership, estate or trust, none of which is treated as a corporation for federal income tax purposes, and such limited liability company, partnership, estate or trust and its members, partners or beneficiaries own in the aggregate directly, indirectly, beneficially, or constructively at least fifty percent (50%) of the profits, capital, stock or value of the other entity or both entities.

63-3615A(3) The provisions of this section shall not apply to a retailer that had sales in this state in the previous year in an amount of less than one hundred thousand dollars (\$100,000).

63-3615A(4) The definition of "Internal Revenue Code" in section 63-3004, Idaho Code, shall apply to this section.

## **Alabama**

**40-23-190(a)** An out-of-state vendor has substantial nexus with this State for the collection of both state and local use tax if: (1) the out-of-state vendor and an in-state business maintaining one or more locations within this State are related parties; and (2) the out-of-state vendor and the in-state business use an identical or substantially similar name, tradename, trademark, or goodwill, to develop, promote, or maintain sales, or the in-state business and the out-of-state vendor pay for each other's services in whole or in part contingent upon the volume or value of sales, or the in-state business and the out-of-state vendor share a common business plan or substantially coordinate their business plans, or the in-state business provides services to, or that inure to the benefit of, the out-of-state business related to developing, promoting, or maintaining the in-state market.

**40-23-190(b)** Two entities are related parties under this section if one of the entities meets at least one of the following tests with respect to the other entity: (1) one or both entities is a corporation, and one entity and any party related to that entity in a manner that would require an attribution of stock from the corporation to the party or from the party to the corporation under the attribution rules of Section 318 of the Internal Revenue Code owns directly, indirectly, beneficially, or constructively at least 50 percent of the value of the corporation's outstanding stock; (2) one or both entities is a limited liability company, partnership, estate, or trust and any member, partner or beneficiary, and the limited liability company, partnership, estate, or trust and its members, partners or beneficiaries own directly, indirectly, beneficially, or constructively, in the aggregate, at least 50 percent of the profits, or capital, or stock, or value of the other entity or both entities; or (3) an individual stockholder and the members of the stockholder's family (as defined in Section 318 of the Internal Revenue Code) owns directly, indirectly, beneficially, or constructively, in the aggregate, at least 50 percent of the value of both entities' outstanding stock.

Note: Approximately 20 states have similar laws or regulations.

5. Should the proposal specify that nexus for an internet retailer arises if an in-state entity, through agreement with the internet retailer, solicits sales on behalf of the retailer?

**N.Y.S. 1101 (b)(8)(vi)**

(vi) For purposes of subclause (I) of clause (C) of subparagraph (i) of this paragraph, 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 (\$10,000) during the preceding four quarterly periods ending on the last day of February, May, August, and November. 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. Nothing in this subparagraph shall be construed to narrow the scope of the terms independent contractor or other representative for purposes of subclause (I) of clause (C) of subparagraph (i) of this paragraph.

**Draft MTC Associate Nexus Model Statute**

(1) A person who sells tangible personal property or services taxable under this Act to a purchaser in this state ("seller"), shall be presumed to have a presence sufficient for the state to require compliance with [cite state sales and use tax statute], through the in-state activities of a resident of this state, if the seller enters into an agreement, directly or indirectly, with the resident under which the resident, for a commission or other consideration based on completed sales, directly or indirectly refers potential customers, whether by a link on an internet website or otherwise, to the seller, and if during the preceding 12 months the cumulative gross receipts from sales by the seller to customers in the state who are referred to the seller by all residents with which seller has this type of an agreement is in excess of \$\_\_\_\_\_. [optional: and the cumulative gross receipts from sales by the seller to all customers in the state is in excess of \$\_\_\_\_\_.] 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 same preceding 12 months. An agreement under which a seller purchases advertisements from a resident of this state is not an agreement described in this section unless the advertisement revenue paid to the resident consists of commissions or other consideration that is based upon sales of tangible personal property or services. Nothing in this section shall limit or reduce this state's authority under other sections of this Act, agency regulations, or the United States Constitution, to require compliance with [cite state sales and use tax statute]. This Act shall become effective as of the date of enactment.

For purposes of this section, “cumulative gross receipts” includes receipts from sales made during the 12-month period before the effective date of this act.

(2) A. A person who sells tangible personal property or services taxable under this Act to a purchaser in this state ("seller"), shall be presumed to have a presence sufficient for the state to require compliance with [cite state sales and use tax statute] if both of the following apply:

(1) the seller and an in-state business maintaining one or more location within this State are related parties; and

(2) the seller and the in-state business use an identical or substantially similar name, tradename, trademark or goodwill to develop, promote, or maintain sales, or the in-state business provides services to, or that inure to the benefit of, the out-of-state business related to developing, promoting, or maintaining the in-state market.

B. Two entities are related parties under this subsection if they meet any one of the following tests:

(1) both entities are component members of the same controlled group of corporations under section 1563 of the Internal Revenue Code<sup>1</sup>;

(2) one entity is a related taxpayer to the other entity under the provisions of section 267 of the Internal Revenue Code<sup>2</sup>;

(3) one entity is a corporation and the other entity and any party, for which section 318 of the Internal Revenue Code<sup>3</sup> requires an attribution of ownership of stock from that party to the entity, own directly, indirectly, beneficially, or constructively at least 50 percent of the value of the outstanding stock of the corporation; or

(4) one or both entities is a limited liability company, partnership, estate, or trust, none of which is treated as a corporation for federal income tax purposes, and such limited liability company, partnership, estate, or trust and its members, partners or beneficiaries own in the aggregate directly, indirectly, beneficially, or constructively at least 50 percent of the profits, capital, stock, or value of the other entity or both entities.

### **Severability**

If any of the provisions of this Act are found invalid by a court of competent jurisdiction, the invalid portion of the statute shall be severed without affecting the remaining provisions of this Act.

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<sup>1</sup> <http://www.law.cornell.edu/uscode/text/26/1563>

<sup>2</sup> <http://codes.lp.findlaw.com/uscode/26/A/1/B/IX/267>

<sup>3</sup> <http://www.law.cornell.edu/uscode/text/26/318>

## **Definitions**

### Resident

Any individual who maintains a permanent place of abode in this state is a resident. Permanent place of abode is a dwelling place maintained by a person, or by another for him, whether or not owned by such person, on other than a temporary or transient basis. The dwelling may be a home, apartment or flat; a room including a room at a hotel, motel, boarding house or club; a room at a residence hall operated by an educational, charitable or other institution; housing provided by the Armed Forces of the United States, whether such housing is located on or off a military base or reservation; or a trailer, mobile home, houseboat or any other premises.

Any corporation incorporated under the laws of [insert your state]; and any corporation, association, partnership, or other pass-through entity, or other entity that maintains a place of business in the State, or otherwise has nexus in the State for purposes of this act, is a resident.

### Seller

A seller includes, but is not limited to, an entity, including a pass-through entity, affiliated with a seller within the meaning of Section 1504 of the Internal Revenue Code.<sup>4</sup>

## **Regulation**

If the written agreement between the seller and the resident specifies that the resident may not engage in solicitation, then this presumption may be rebutted for any prior 12 month period by providing to the [Department] a copy of the agreement signed by both parties and a statement signed by the resident attesting that he or she did not in fact engage in any solicitation during that 12 month period.

6. Should the proposal specify that a non-affiliated entity, contracted to perform in-state warranty, “installation, maintenance or repair” services for products sold by an out-of-state retailer, gives rise to nexus in the taxing state?

## **South Dakota Codified Laws**

10-45-2.9. Retailers having contractual relationship with entity for installation, maintenance, or repair of purchases

Any retailer making sales of tangible personal property to purchasers in this state by mail,

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<sup>4</sup> Section 1504 (26 U.S.C. §1504) defines an affiliated group.  
<http://www.law.cornell.edu/uscode/text/26/1504>

telephone, the internet, or other media which has a contractual relationship with an entity to provide and perform installation, maintenance, or repair services for the retailer's purchasers within this state shall be included within the definition of retailer under the provisions of [§§ 10-45-2.5](#) to 10-45-2.9, inclusive.

To remind you, during the April 22<sup>nd</sup> teleconference, a question was raised as to whether this section should include activities such as warehousing and drop shipping. The work group did not indicate whether such language was acceptable or not, so again, here is an example from Michigan as to what that provision might look like.

**House Bill 4202, Amendment to MCL 205.51 to 205.78, General Sales and Use Tax, New Section 2B (Michigan)**

(1) A person who sells tangible personal property to a customer in this state is presumed to be engaged in the business of making sales at retail in this state if an affiliated person . . . has a physical location in this state, conducts business activity in this state, or is otherwise subject to the tax under this Act or the Use Tax Act, 1937 PA 94, MCL 205.91 to 205.111, and that affiliated person, directly or indirectly, does any of the following:

(C) maintains an office, distribution facility, warehouse, storage place or similar place of business in his state to facilitate the delivery of tangible personal property sold by the seller to the seller's customers in the state.

(F) facilitates the sale of tangible personal property to customers in this state by allowing the seller's customers in this state to pick up or return tangible personal property sold by the seller at an office, distribution facility, warehouse, storage place or similar place of business maintained by that affiliated person in this state.

During the May 20<sup>th</sup> teleconference, a question was raised as to whether provisions like the ones above should apply to non-related entities as well. The workgroup felt that it should, but emphasized the need to differentiate between the activities of related and non-related entities that will confer nexus on the seller. In what way should they be differentiated? Should there be a higher standard for non-related entities, or a different standard altogether?

7. Should the model statute contain a rebuttable presumption for all areas of nexus as to whether a taxpayer is doing business in the state—i.e., agents or representatives as well as affiliates? Should the standard for agency and representational nexus be higher than for affiliates?

Below is an example of a rebuttable presumption from Kansas regarding affiliates:

**Kansas**

**79-3702(h)(2)** A retailer shall be presumed to be doing business in this state if any of the following occur:

**79-3702(h)(2)(A)** Any person, other than a common carrier acting in its capacity as such, that has nexus with the state sufficient to require such person to collect and remit taxes under the provisions of the constitution and laws of the United States if such person were making taxable retail sales of tangible personal property or services in this state:

**79-3702(h)(2)(A)(i)** Sells the same or a substantially similar line of products as the retailer and does so under the same or a substantially similar business name;

**79-3702(h)(2)(A)(ii)** maintains a distribution house, sales house, warehouse or similar place of business in Kansas that delivers or facilitates the sale or delivery of property sold by the retailer to consumers;

**79-3702(h)(2)(A)(iii)** uses trademarks, service marks, or trade names in the state that are the same or substantially similar to those used by the retailer;

**79-3702(h)(2)(A)(iv)** delivers, installs, assembles or performs maintenance services for the retailer's customers within the state;

**79-3702(h)(2)(A)(v)** facilitates the retailer's delivery of property to customers in the state by allowing the retailer's customers to pick up property sold by the retailer at an office, distribution facility, warehouse, storage place or similar place of business maintained by the person in the state;

**79-3702(h)(2)(A)(vi)** has a franchisee or licensee operating under its trade name if the franchisee or the licensee is required to collect the tax under the Kansas retailers' sales tax act; or

**79-3702(h)(2)(A)(vii)** conducts any other activities in the state that are significantly associated with the retailer's ability to establish and maintain a market in the state for the retailer's sales.

**79-3702(h)(2)(B)** Any affiliated person conducting activities in this state described in subparagraph (A) or (C) has nexus with this state sufficient to require such person to collect and remit taxes under the provisions of the constitution and laws of the United States if such person were making taxable retail sales of tangible personal property or services in this state.

**79-3702(h)(2)(C) [Associate Nexus (w/rebuttable presumption)]**

**79-3702(h)(2)(D)** The presumptions in subparagraphs (A) and (B) may be rebutted by demonstrating that the activities of the person or affiliated person in the state are not significantly associated with the retailer's ability to establish or maintain a market in this state for the retailer's sales.

## **II. Associate Nexus and the Internet Tax Freedom Act**

Another issue the subcommittee asked the work group to investigate is whether the N.Y.-style associate nexus statute runs afoul of the Internet Tax Freedom Act because one party is an internet retailer. The Internet Tax Freedom Act forbids states from imposing multiple and discriminatory taxes on transactions taking place over the Internet. In *Performance Marketing Association v. Hamer*, pending in the Illinois Supreme Court, the MTC filed an amicus brief arguing that the Internet Tax Freedom Act has no impact on associate nexus statutes. The MTC's argument is below:

**C. The Illinois Statute Does Not Violate the Internet Tax Freedom Act's Moratorium on Discriminatory Taxes.**

The circuit court ruled that Public Act 96-1544 is preempted by the Internet Tax Freedom Act, 47 U.S.C.A. § 151 (note) ("ITFA"), but the court's ruling did not specify which section or sections of ITFA are implicated. V.5, C. 1066. There has been very little litigation over the contours of ITFA to date. The Commission is vitally concerned that in this matter of first impression by a state's highest appellate court that ITFA's preemption provisions receive an appropriate and narrow construction, as required under long-established principles of federalism, in a manner that does not impinge on state interests in a way which Congress did not intend. Certainly, the question before this court should not be whether Public Act 96-1544 was "directed to" sales activities taking place over the Internet, which appears to be the core of PMA's complaint. Nothing in the ITFA prohibits the states from passing laws concerning, clarifying or "directed to" the subject of Internet sales; the law only prohibits *discriminatory* taxes on transactions conducted over the Internet (as well as taxes on Internet service providers, which are broadly preempted). As defined in ITFA, a "discriminatory tax" means:

(A) any tax imposed by a State or political subdivision thereof on electronic commerce that--

(i) is not generally imposed and legally collectible by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means;

(ii) is not generally imposed and legally collectible at the same rate by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means, unless the rate is lower as part of a phase-out of the tax over not more than a 5-year period;

(iii) imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or information accomplished through other means.

Presumably, the circuit court did not believe that subdivisions (i) or (ii) are violated by Illinois law. The obligation to collect sales and use tax is applicable to the same kinds of “property, goods, services and information” sold in Illinois regardless of the means used to carry out those sales, and the tax rate is the same for all such taxable transactions. PMA contends, and the circuit court apparently agreed, that Public Act 96-1544 imposes collection obligations on sellers having commission-based contractual relationships with residents using Internet solicitation that would not be imposed on vendors with commission-based contractual relationships with residents who do not use the Internet to solicit sales. V.2, C.302-02; V.4, C. 774-78.

Public Act 96-1544 specifies particular conduct and relationships with affiliates that will result in a seller being considered a “retailer maintaining a place of business in this state” (henceforth referred to as a “retailer”) who is obligated to collect use tax on purchases made by Illinois customers. 35 ILCS § 105/2. A law identifying certain kinds of relationships and activity which will create “retailer” status does not “discriminate” if non-Internet sellers maintaining the same kinds of relationships and activity will also be considered “retailers”. The definition of “retailer maintaining a place of business in this state” is quite broad, and includes sellers with in-state advertising contracts, with or without commission-based compensation, telephone solicitation and television shopping channels. It is clear, then, that 35 ILCS § 105/2 does not impose a different collection obligation on “retailers” using “electronic commerce” for selling than other forms of selling, such as telephone solicitations or television shopping programs.

Just as significantly, the list of persons who might be considered “retailers” is *inclusive*, not exclusive. Without a fully-developed factual record, PMA’s arguments as

to what activities undertaken by a seller which would or would not create "retailer" status are simply speculative. The partial listing of potential "retailers maintaining a place of business in this state" is long but worthy of review (the provision objected to by PMA is set forth in italics):

"Retailer maintaining a place of business in this State", or any like term, means and includes any of the following retailers:

1. A retailer having or maintaining within this State, directly or by a subsidiary, an office, distribution house, sales house, warehouse or other place of business, or any agent or other representative operating within this State under the authority of the retailer or its subsidiary, irrespective of whether such place of business or agent or other representative is located here permanently or temporarily, or whether such retailer or subsidiary is licensed to do business in this State. However, the ownership of property that is located at the premises of a printer with which the retailer has contracted for printing and that consists of the final printed product, property that becomes a part of the final printed product, or copy from which the printed product is produced shall not result in the retailer being deemed to have or maintain an office, distribution house, sales house, warehouse, or other place of business within this State.

*1.1. Beginning July 1, 2011, a retailer having a contract with a person located in this State under which the person, for a commission or other consideration based upon the sale of tangible personal property by the retailer, directly or indirectly refers potential customers to the retailer by a link on the person's Internet website. The provisions of this paragraph 1.1 shall apply only if the cumulative gross receipts from sales of tangible personal property by the retailer to customers who are referred to the retailer by all persons in this State under such contracts exceed \$10,000 during the preceding 4 quarterly periods ending on the last day of March, June, September, and December.*

1.2. Beginning July 1, 2011, a retailer having a contract with a person located in this State under which:

A. the retailer sells the same or substantially similar line of products as the person located in this State and does so using an identical or substantially similar name, trade name, or trademark as the person located in this State; and

B. the retailer provides a commission or other consideration to the person located in this State based upon the sale of tangible personal property by the retailer.

The provisions of this paragraph 1.2 shall apply only if the cumulative gross receipts from sales of tangible personal property by the retailer to customers in this State under all such contracts exceed \$10,000 during the preceding 4 quarterly periods ending on the last day of March, June, September, and December.

2. A retailer soliciting orders for tangible personal property by means of a telecommunication or television shopping system (which utilizes toll free numbers) which is intended by the retailer to be broadcast by cable television or other means of broadcasting, to consumers located in this State.

3. A retailer, pursuant to a contract with a broadcaster or publisher located in this State, soliciting orders for tangible personal property by means of advertising which is disseminated primarily to consumers located in this State and only secondarily to bordering jurisdictions.

4. A retailer soliciting orders for tangible personal property by mail if the solicitations are substantial and recurring and if the retailer benefits from any banking, financing, debt collection, telecommunication, or marketing activities occurring in this State or benefits from the location in this State of authorized installation, servicing, or repair facilities.

5. A retailer that is owned or controlled by the same interests that own or control any retailer engaging in business in the same or similar line of business in this State.

6. A retailer having a franchisee or licensee operating under its trade name if the franchisee or licensee is required to collect the tax under this Section.

7. A retailer, pursuant to a contract with a cable television operator located in this State, soliciting orders for tangible personal property by means of advertising which is transmitted or distributed over a cable television system in this State.

8. A retailer engaging in activities in Illinois, which activities in the state in which the retail business engaging in such activities is located would constitute maintaining a place of business in that state.

The circuit court appears to have agreed with PMA's argument that a retailer who is engaged in "performance marketing" with an in-state affiliate through print and broadcast "advertisers" would not be considered a "retailer", while an Internet seller engaged in the identical activity would be considered a "retailer". Again, the argument is speculative at best, since the state may well conclude that *any* seller with a commission-based representative in the state is a "retailer." The 2011 amendment merely identifies several

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The circuit court appears to have agreed with PMA's argument that a retailer who is engaged in "performance marketing" with an in-state affiliate through print and broadcast "advertisers" would not be considered a "retailer", while an Internet seller engaged in the identical activity would be considered a "retailer". Again, the argument is speculative at best, since the state may well conclude that *any* seller with a commission-based representative in the state is a "retailer." The 2011 amendment merely identifies several

types of in-state activity that do give rise to “retailer” status, including entering into commission-based Internet sales agreements with residents.

But in addition, PMA is comparing apples to oranges, since the particular form of solicitation activity addressed in Public Act 96-1544 is arguably unique to Internet website inter-connections (“click-throughs”). Since the activity is unique, there is no comparison class upon which to base a claim of discriminatory treatment. In contrast to what happens when a customer sees a “performance-based” advertisement in a magazine or other print media, in the case of Internet affiliate relationships a potential customer gains instant access to the “retailer’s” website through the affiliate’s website. The immediacy and directness of the connection between the in-state representative and the “retailer” is analogous to an out-of-state casino using a dedicated van service to bring gamers directly from a state’s airport to the entrance of the casino. The in-state representative has contractually arranged to be the means of communication not just for delivering a solicitation but for the transmission of the customer from one site to another. The casino has a taxable presence based on the van’s in-state pick-up and delivery. That the activity covered by Public Act 96-1544 which triggers a taxable nexus is made possible because of the Internet, does not mean that the resulting tax is discriminatory and preempted by ITFA, because there is no identical non-Internet activity which has been given preferential treatment. Thus, in *Village of Rosemont, Illinois v. Priceline.com, Inc.*, 2011 WL 4913262 (N.D. Ill. 2011), the federal district court rejected claims that ITFA barred collection of occupancy taxes on an on-line hotel reservation provider where traditional travel agents were not taxed on commissions, since travel agents operated

under different business practices. *Accord, Mayor and City of Baltimore v. Priceline.com, Inc.*, NO. CIV. A. MJG-08-3319, 2012 WL 3043062 (D. Md. 2012).

The Commission urges this court to analyze ITFA according to its terms and to reject PMA's attempt to give the preemption provisions of the statute an overly-expansive meaning. The Supreme Court has consistently recognized that the states' taxing powers provide a crucial component of sovereignty necessary to support our federal system. *See, e.g., National Private Truck Council, Inc., Oklahoma Tax Commission*, 515 U.S. 582, 586 (1995), *quoting, Dows v. City of Chicago*, 78 U.S. 108, 110 (1870) ("It is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments, and it is of the utmost importance to all of them that the modes adopted to enforce the taxes levied should be interfered with as little as possible.").

This court should interpret the provisions of ITFA with the understanding that Congress knows how to write preemptory language, and does not need the assistance of the judiciary to infer that purpose if it is beyond the clear wording of the statute. *See Department of Revenue of Oregon v. ACF Industries, Inc.*, 510 U.S. 332 (1994). In *ACF Industries*, the Court refused to apply the preemption provision in the "4R Act", 49 U.S.C.A. § 11501, which preempted "any other [state] tax which discriminates," to preclude the state from taxing railroad property despite the fact that some industrial property had been granted a property tax exemption. The Court wrote that, "We will interpret a statute to pre-empt the traditional state powers only if that result is the 'clear and manifest purpose of Congress'", *quoting from, Rice v. Santa Fe Elevator Corporation*, 331 U.S. 218, 230 (1947). And as the Court wrote in *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504 (1992):

The principles of federalism and respect for state sovereignty that underlie the Court's reluctance to find preemption where Congress has not spoken directly to the issue apply with equal force where Congress has spoken, though ambiguously. In such cases, the question is not *whether* Congress intended to pre-empt state regulation, but to what extent. We do not, absent unambiguous evidence, infer a scope of preemption beyond that which clearly is mandated by Congress' language.

505 U.S. at 553 (emphasis in original); *Accord, Gregory v. Ashcroft*, 501 U.S. 452 (1991).

In the present case, as in *Rosemont, Illinois v. Priceline.com, Inc.*, PMA's members have chosen a business model predicated on use of the Internet; that does not mean that Congress intended to provide them a safe harbor from state taxation; they must show actual discrimination, which they cannot do on these facts.

Under the circuit court's broad (if ill-defined) application of ITFA's preemption language, it is difficult to see how any sales carried out through the Internet would not eventually be preempted, since at least some sales carried out through other means—such as the door-to-door sale of Girl Scout cookies—will inevitably be subject to a state exemption, setting up the claim that Internet sales and solicitation have received disparate treatment. If that broad application of IFTA's preemption language were upheld as fulfilling congressional intent, it would raise the possibility that Congress had exceeded its powers under the Commerce Clause in enacting IFTA. Congress would not be “regulating commerce” in such a scenario but would instead be attempting to regulate non-discriminatory state taxing authority itself, a field of operation the framers of the Constitution chose to leave off the enumerated powers of the federal government. See *National Federation of Independent Businesses v. Sebelius*, 567 U.S. \_\_\_, 132 S.Ct. 2566, 2577-8 (2012)(the enumerated powers granted to the federal government did not include

plenary power to force citizens to engage in commerce or live healthier lifestyles—such powers are left to the states.).

## V. CONCLUSION

The Illinois statute is constitutional. The U.S. Supreme Court has long recognized that the in-state activities of third parties acting on behalf of out of state vendors is sufficient to give the state jurisdiction to impose a sales and use tax collection responsibility. Public Act 96-1544 relies on that constitutional precept in specifying that in-state solicitation carried out via commission-based Internet sales linkages creates nexus for the remote vendor.

The Illinois statute does not violate the Internet Tax Freedom Act. Nothing in the ITFA prohibits the states from passing laws concerning, clarifying or “directed to” the subject of Internet sales; the law only prohibits discriminatory taxes on transactions conducted over the Internet. Under Illinois law, any substantial in-state solicitation by a seller’s representatives will subject that seller to sales and use tax collection obligations. In addition, to the extent the the form of “performance marketing” at issue in this case is unique, it cannot supply the basis for a claim that it has been treated less favorably than dissimilar activity. Finally, the court should presume that Congress knows how to write a preemption statute, and if the Congress wished to preempt state laws establishing nexus standards for Internet solicitation activities, it would have done so. The judgment of the circuit court should be reversed.