Interstate Commerce (Completed)

Constitutional Construction

Under our federal form of government, each level of government has its own constitutionally designated powers and responsibilities. The states, through adoption of the Federal Constitution, surrendered certain rights and responsibilities to the federation government. However, each state remains a sovereign unit of government. Governmental powers and responsibilities not constitutionally designated to the Federal Government remain with the states. Others are designated to the states by specific Federal Constitutional provision. The states and federal government share others. The power to tax is one such power shared by all.

Out of necessity for the common good, authors of the Federal Constitution, and the original state governments, provided many limitations on the state's practices in governing its citizens and territories. Among these are certain provisions providing limitations on the state's authority to implement and collect taxes. As students of American history might well expect, the common theme of these protections was the prevention of "taxation without representation." Each state has been generally allowed to tax its own subjects as it wishes without interference from the Federal Government under the theory that they have power to influence such laws through the election process. Four clauses of the Federal Constitution have been frequently credited with attributing protections for those not possessing the ballot's influence. Protections, known as the Privileges and Immunities Clause, the Due Process Clause, the Commerce Clause and the equal protection clause, have not always been applied consistently. However, their application has generally been restricted to cases with interstate implications.

With each state possessing the freedom to tax its subjects within its boundaries at its own discretion, numerous taxes have been implemented by the various states. Currently, the most popular taxes among the states are property taxes, sales or use taxes and privilege taxes based on net worth, net income or some variation of gross receipts. By nature, property taxes are assessed on property within the state and with the exception of mobile property used in interstate commerce, are largely unaffected by federal limitations. These limitations do affect the imposition of net income taxes, sales or use taxes and gross receipts taxes when interstate transactions are involved. A "sales tax" may be a tax on the purchaser with collection responsibility placed on the seller or a tax on the seller with the right to pass the tax expense on to the purchaser. In either case, a vendor who fails to satisfy the collection requirements of a state and remit the tax collections to the state is subject to the liability himself. While "sales taxes" are also limited to intrastate transactions, all states imposing sales taxes also impose

companion use taxes. As a collection method, vendors making taxable sales into the state use are required to collect and remit this seller's use tax within Constitutional limitations.

Interpretation of the constitutional protections has evolved over the years through interpretation by the U. S. Supreme Court and the various state courts. As the case law evolves, an evolution is taking place, currently shifting to lower levels of contact required for imposition of taxation. At the present time, the constitutional protections against "taxation without representation" have all but given way to a standard of protection that might better be termed as protection against "taxation without warning."

Along with the freedom to exercise its own discretion in implementing methods of taxation at its own choosing, is the power to interpret its own laws and grant exemptions from taxation within constitutional limitations. Consequently, uniformity between taxes from state to state is limited even when the tax is defined the same. This presents a significant challenge to the business community in attempting to comply with the various differing state requirements.

Constitutional Issues In Multi State Taxation

As an inherent attribute of sovereignty, each state possesses the power to tax any subject within its jurisdiction without action of the people. Since the power to tax flows from the power to make laws, the law making body of each state possess the powers of taxation in that state. The only limitations on this taxing power, except limitations arising from the nature of the tax itself, are those contained in the federal and state constitutions.

The U.S. Constitution prohibits state taxation of imports and exports (U.S. Constitution, Article I, Sec. 10, Clause 2) and provides a legal framework around which taxation of interstate activities must fit. The Fourteenth Amendment provides: "No state shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any state deprive any person of life, liberty or property without due process of law: nor deny any person within its jurisdiction the equal protections of the law." The Constitution also grants Congress the power to regulate commerce among the states (U.S. Constitution, Article I, Sec. 8, Clause 3). Since the power to tax is a power to regulate, any taxation must fall within the authorization provided by Congress.

To date, Congress has passed few laws authorizing taxation of interstate commerce. One such law, the McCarran-Ferguson Act explicitly delegates the regulation and taxation of insurance companies to the States, removing entirely any Commerce Clause restriction upon the States' power to tax the insurance business. However, absent such enabling legislation in other industries, under the principles of the "negative commerce clause," any taxation that imposes a substantial burden on interstate

commerce constitutes an attempted regulation thereof by the state and consequently is invalid.

In recent years most of the challenges to the states' rights to tax foreign corporations have branded a tax as either a violation of the due process clause or a burden on interstate commerce.

Taxation under the Commerce Clause

"Franchise taxes" are those taxes imposed on the privilege or license of a corporation to engage in corporate activity, usually the "privilege to do business" in the taxing state. The measure of such a tax may be one of a number of things, such as net income, the capital stock of the corporation, the portion of its capital employed in the state, net worth or its net or gross receipts. It is the thing that is taxed (the franchise), rather than the thing by which the tax is measured, that determines its constitutionality. The tax remains a tax on the privilege of commercial enterprise in the state, regardless of the thing by which it is measured. The United States Supreme Court has ruled that a state tax on interstate sales designated as a tax on the privilege of doing business does not violate the Commerce Clause of the U.S. Constitution per se. The Court said that a state tax on interstate commerce is not unconstitutional if the tax is applied to an activity with a substantial connection (nexus) with the taxing state, is fairly apportioned, does not discriminate against interstate commerce and is fairly related to the services provided by the taxing state.

Considering a gross receipts tax, the Supreme Court has said: "* * * under the commerce clause, in the absence of Congressional action, state taxation, whatever its form, is precluded if it discriminates against interstate commerce or undertakes to lay a privilege tax measured by gross receipts derived from activities in such commerce which extend beyond the territorial limits of the taxing state. Such a tax, at least when not apportioned to the activities carried on within the state burdens the commerce in the same manner and to the same extent as if the exaction were for the privilege of engaging in interstate commerce, and would, if sustained, expose it to multiple tax burdens, each measured by the entire amount of the commerce, to which local commerce is not subject."

On February 24, 1959, the U.S. Supreme Court ruled a state could tax the income of a foreign corporation earned within its borders solely in interstate commerce. The Court's decision has been summarized as follows: "Net income from the interstate operations of a foreign corporation may be subjected to state taxation provided the levy is not discriminatory and is properly apportioned to local activities within the taxing state forming sufficient nexus to support the same." The U.S. Supreme Court also upheld a Mississippi tax on the privilege of doing business applied to the gross proceeds of an interstate carrier where vehicles that were manufactured outside Mississippi were shipped into the state by rail and then loaded onto the taxpayer's trucks for delivery to Mississippi dealers. The Court held that a tax on the privilege of doing business does not

violate the Commerce Clause of the federal Constitution if it is applied to an interstate activity having 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.

The court has further stated "To justify the exaction by a state of a money payment burdening interstate commerce, it must affirmatively appear that it is demanded as reimbursement for the expense of providing facilities, or of enforcing regulations of the commerce which are within its constitutional power." Such a tax must also be reasonable in amount. A tax of 2% of the market value of every motor vehicle, imposed as a condition precedent to the issuance of a certificate of title and the operation of motor vehicles over the highways of the state, was held to be valid where it was not shown that the amount of the tax was in excess of the fair compensation for the use of the highways.

As previously stated, in the years since the U.S. Supreme Court decision in National Bellas Hess in 1967 and prior to Quill in 1992, challenges of the constitutional standard of nexus referred to the Due Process and Commerce Clause Standard together. In National Bellas Hess, the Court stated, "These two claims are closely related. For the test whether a particular state exaction is such as to invade the exclusive authority of Congress to regulate trade between the States, and the test for a State's compliance with the requirements of due process in this area are similar." Specifically to interstate commerce, the court said, "State taxation falling on interstate commerce . . . can only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys." The court continued "And in determining whether a state tax falls within the confines of the Due Process Clause, the Court has said that the 'simple but controlling question is whether the state has given anything for which it can ask return".

In Quill, the court affirmed the "bright line" physical presence test of National Bellas Hess is still required under the Commerce Clause but found such physical presence is not required to satisfy Due Process safeguards. In so ruling, the Court distinguished the minimum contact requirement of the Due Process Clause from the substantial nexus requirement of the Commerce Clause, confirming that the two requirements are not identical. In its decision in Quill, the court stated, "The Complete Auto analysis reflects these concerns about the national economy. The second and third parts of that analysis, which require fair apportionment and non-discrimination, prohibit taxes that pass an unfair share of the tax burden onto interstate commerce. The first and fourth prongs, which require a substantial nexus and a relationship between the tax and State-provided services, limit the reach of State taxing authority so as to ensure that State taxation does not unduly burden interstate commerce. Thus, the "substantial-nexus" requirement is not, like due process "minimum-contacts" requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce. Accordingly, contrary to the State's suggestion, a corporation may have the "minimum contacts" with a taxing State as required by the Due Process Clause, and yet lack the "substantial nexus" with that State as required by the Commerce Clause."

With this said, the question remains as to what level of activity is required to meet the "substantial nexus" of Complete Auto. In reaching its decision in Quill, the court placed no constitutional significance to the presence of copies of computer programs belonging to Quill and licensed for use by customers within the state. In this act, the court affirmed that more than a slight physical presence is required. The Supreme Court established in Scripto v. Carson that the presence need not be manifested by property or employees of the company. Rather representation by independent sales representatives resident within the state, regularly soliciting business for the benefit of the company will satisfy this requirement.

Under the U.S. Supreme Court's current interpretation of the Commerce Clause, a state tax that impacts interstate commerce is valid if it meets the following requirements:

1. It is applied to an activity with substantial connection with the state,

2. It is fairly apportioned,

3. It does not discriminate against interstate commerce, and

4. It is fairly related to the services provided by the taxing state.

When international commerce is involved, in addition to the criteria above, a tax may not do either of the following:

1. Create a risk of multiple taxation, or

2. Prevent the federal government from speaking "with one voice when regulating commercial relations with foreign governments."

Interpretation of what level and consistency of activity is required to meet the "substantial nexus" standard continues to vary. In a 1984 technical assistance memo, the State of Florida claimed, "occasional presence of the corporation's representatives in Florida to make repairs and sales are activities that would establish a sufficient nexus with Florida." Washington courts have ruled that the state of Washington was not prohibited by the Commerce Clause of the U.S. Constitution from levying its wholesaling business and occupation tax on sales made in Washington by an out-of-state manufacturer whose only contact with Washington consisted of solicitation of sales by a non-resident independent contractor. However the Texas Court of Appeals recently ruled the Comptroller, despite an administrative rule adopted in 1983, could not impose the franchise tax on an out-of-state retailer that only solicited sales through independent contractors in Texas.

Taxation under the Due Process Clause

In general, the Supreme Court has construed the Due Process Clause of the Fourteenth Amendment to limit the territorial reach of the states' taxing powers. With respect to taxation of interstate business, this general restraint has been applied in essentially two situations. First, the Due Process Clause has been invoked to forbid the exercise of state tax power on the ground that the state lacks a sufficient connection (nexus) with the taxpayer. As the Court declared in a phrase it has frequently repeated: "Due process requires some definite link, some minimum connection between a state and the person, property, or transaction it seeks to tax.

Second, even if a taxpayer has sufficient nexus with the state to subject the taxpayer to the state's taxing jurisdiction, the Due Process Clause requires that the measure of the tax fairly reflect the taxpayer's activities in the state. Thus, the Court has construed the Due Process Clause as requiring that the states, in taxing the property or income of an interstate enterprise, include within the tax base only that portion of the taxpayer's property or income fairly apportioned to the taxpayer's activities in the state.

Unlike the Commerce Clause that grants power to Congress to regulate, the Due Process Clause is a prohibitive in nature. Congress does not have the power to interpret or modify the protections of the Due Process Clause. Changes in application of the Due Process provisions of our Constitution can only come from the U.S. Supreme Court or by Constitutional amendment.

For years, the Commerce Clause and the Due Process Clause were viewed together as the Supreme Court had indicated that the requirements of the Commerce and Due Process Clauses in the nexus and apportionment contexts were substantially the same. Under the current standard for application of the Due Process clause, the essential question is simply whether it is reasonable, in light of a taxpayer's contacts with the state, for the state to assert tax jurisdiction over the taxpayer. In a recently published opinion, the Supreme Court stated "if a foreign corporation purposefully avails itself of the benefits of an economic market in the forum state, it may subject itself to the State's in personam jurisdiction even if it has no physical presence in the State." Consequently, this standard is sometimes referred to as an economic nexus standard.

Taxation under the Privileges and Immunities Clauses

There are two clauses in the U. S. Constitution guaranteeing to the citizens the privileges and immunities provided to the citizens of a state also are applied to citizens of other states. In defining the relationships between the states, the authors of the Constitution provided "The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States." In 1866, Citizenship and the rights thereof were further defined to include "No State shall make or enforce any law which shall abridge the Privileges and Immunities of citizens of the United States; . . ."

Protections of is provision were severely limited by the Supreme Court six years later when the Court refused to extend its protections to prohibiting a state from legislatively granting a monopoly for the operation of slaughter houses in a specified geographic territory. With this decision, the Privileges and Immunities section of the Fourteenth Amendment was separated from the Due Process and Equal Protection clauses, both contained in the same section. Application of the Privileges and Immunities Clauses has additionally been limited to citizens. Since corporations are not citizens, these protections are not applicable to corporations. Consequently, the Privileges and Immunities provisions have had a minor role.

Current construction of the Privileges and Immunities protection limits its protection to forbidding any state from discriminating against citizens of another state in favor of citizens of that state. This construction was applied by the Court in declaring a New York tax unconstitutional where the Court stated "A state may not barter away the right, conferred upon its citizens by the Constitution of the United State, to enjoy the privileges and Immunities of citizens when the go into other states." Like the Commerce Clause, this protection is not provided to citizens of the state, but to citizens of other states traveling or conducting business in that state. A tax that subjects citizens of the state to greater taxation than is imposed on non-residents doing the same business in the state is not prohibited by this construction of the clause. Where the States have had a compelling reason to protect its own interest the courts have allowed discriminatory taxation when it does not blatantly discriminate simply on the basis of residency.

Possibly because much the same protections have been attributed to the Commerce Clause that is not hindered by the decision in the Slaughterhouse cases or limited in application to citizens, the Privileges and Immunities Clause is not frequently cited by the courts. However, unlike the Commerce Clause and similar to the Due Process Clause, the Article IV, Section 2, Clause 1, is prohibitive in nature. Congress has only limited power to interpret or modify the protections of the Privileges and Immunities Clause. Significant changes in the application of this clause can only come from the U.S. Supreme Court or by Constitutional amendment. In years to come, because of the separation of Commerce Clause from Due Process protections in Quill, this clause may gain new importance in that it restricts the power delegated to Congress under the Commerce Clause.

Equal Protection Provisions

Application of restrictions on taxation based on the Equal Protection Clause of the Fourteenth Amendment has been somewhat inconsistent. In the last quarter century, the Court found offense to this clause in a New Mexico property tax exemption granted only to Vietnam veterans who had resided in the State prior to May 8, 1976, discriminating against those relocating into the state after that date but not to California's Proposition 13 provisions allowing higher property assessment for residents relocating to the State after the 1975 reassessment. In general, a discriminatory tax may survive the restrictions of this provision if it can be established that it furthers a legitimate state purpose and its discrimination is not entirely based on residency.

State Constitutional Restrictions on Taxation

While the federal constitution limits the imposition of taxes on interstate commerce, no state is required, under federal law, to adopt any specific scheme of taxation. Each state government is formed under state constitutional authority, granting it specific powers to govern its citizens and commerce within its borders. Significant differences exist between the provisions of the various state constitutions. Among the powers controlled by the various state constitutions is the power to levy taxes. Most, if not all, provide some limitations on taxation of the citizens and commerce in the state. Each state must structure its taxing system within the powers granted to the legislative body by the state constitution. While many provisions are similar from state to state, each has its own unique provisions relating to the powers granted to its legislature to impose taxes.

As would be expected, the objectives of the local political and business community frequently influence the taxation policies of the states. While taxation of interstate activities must not "unfairly" discriminate against interstate commerce, states frequently attempt to structure their tax schemes to "export" as much of the tax burden as possible. A recent trend has been for the states to adopt provisions with an apportionment formula more heavily weighted toward sales. This results in local businesses who export goods to other states paying less while out of state businesses selling their goods in the local market pay more. In states where tourism is a major source of revenue, it is common to find more consumption-based taxation.

Each state also has a judicial system charged with interpreting the laws of its state. This includes taxation on interstate commerce within its boarders. While the U.S. Supreme Court is the ultimate authority on federal limitations, many issues have not and may never be brought before the U.S. Supreme Court. All state taxation issues are decided in a state court prior to the federal Court considering the issue. In doing so, state courts are required to provide an interpretation of particular circumstances before the U.S. Supreme Court issues a proclamation on that matter. Unless the issue is appealed to the federal Court from the first state high court making such a determination the standard established by that court will control application in that state. State courts have frequently interpreted federal limitations more restrictively than the U.S. Supreme Court eventually holds. As it applies within that state, the lower limit remains the law even after the U.S. Supreme Court sets a higher limit for other jurisdictions unless the decision of the state court is later overturned.

Because of the various applications within the states, identical business activities may be subject to tax in one state and exempt for lack of nexus in another state with a similar or identical tax. Activities in each state must be analyzed independently to determine nexus established by those activities in that state.

Case Law Development In Multistate Taxation

As with all other constitutional issues, the U.S. Supreme Court is the ultimate interpretive authority for the restrictions on taxation provided in the U. S. Constitution. Being this Court is under no compulsion to consider any specific appeal and able to reject cases without providing its reasoning to the public, it would be a significant error to totally discount, as irrelevant, what the Supreme Court does not say in its refusal to consider issues. While subject to possible misinterpretation, much weight is often given to the Courts refusal to consider specific cases. It would also be unreasonable to consider issues of taxation in total isolation from other issues of commerce to which the Court passes judgment.

Early Constitutional application provided broad taxing authorities to the states with minimal interference from Congress and the Federal Constitution. In 1868, the states ratified Amendment XIV to the U. S. Constitution, which reads in part "No State shall make or enforce any law which shall bridge the privileges and Immunities of the citizens of the United States." In reaching its decision in the Slaughter House Cases, the court questioned this language facially. In so doing, the Court asked "Was it the purpose of the fourteenth amendment, by the simple declaration that no State should make or enforce any law which shall abridge the privileges and immunities of citizens of the United States, to transfer the security and protection of all the civil rights which we have mentioned, from the States to the Federal government? And where it is declared that Congress shall have the power to enforce that article, was it intended to bring within the power of Congress the entire domain of civil rights heretofore belonging exclusively to the States?" In answering these questions, the Court reasoned that accepting this premise would provide such a shift in power from the states to the federal government that it was unreasonable to accept the states had this as the intent of in ratifying the amendment. The Court observed that the State had a compelling reason and duty to protect its citizens. These protections were reasoned to include controlling where certain industries may be undertaken within its boundaries. By facially accepting the Privileges and Immunities Clause of the Fourteenth Amendment, it was reasoned the states may have a compelling reason to restrict the conduct of its citizens to protect the interest of the State. The Court reasoned that facial application of this clause would prevent the states from exercising such control. With this reasoning, the Court refused to apply the Privileges and Immunities Clause to restrict the control a state exercises over its own citizens.

Scripto v. Carson

The 1960 U. S. Supreme Court decision in Scripto has been the nexus standard followed by most states for more than forty years. Scripto, a Georgia corporation, had an advertising specialty division selling writing instruments to for distribution as advertising and promotional items. They employed 10 independent contractors within the State of Florida for the purpose of soliciting such sales. With the customer's use being subject to a use tax in the State of Florida, Florida demanded Scripto collect and remit their tax on sales shipped into the State. Relying largely on Miller Bothers Co., Scripto refused to do so, claiming lack of sufficient activity in the State to permit the imposition of such a

collection requirement. The Court found the required minimum contact, absent in Miller Brothers, present here by the sales solicitation activities in Florida. The Court further refused to place significance on the fact that the salesmen were independent contractors, stating "The formal shift in the contractual tagging of the salesman as 'independent' neither results in changing his local function of solicitation nor bears upon its effectiveness in securing a substantial flow of goods into Florida... To permit such formal "contractual shifts" to make a constitutional difference would open the gates to a stampede of tax avoidance." Continuing and quoting a prior Florida case, "Moreover, we cannot see, from a constitutional standpoint, 'that it was important that the agent worked for several principals.' The test is simply the nature and extent of the activities of the appellant in Florida."

With the Scripto pronouncement, the Court had established a basis for attritional nexus, where contractual obligations with an independent contractor may be sufficient to provide the minimum connection to satisfy both the Commerce and the Due Process Clauses. In dismissing consideration of activities of the agent representing others as constitutionally insignificant, and focusing on the nature and activities of the in-State business conducted, the Court threw new doors open wide for the states claims of nexus.

The following year, the State of Illinois joined ten other states and enacted legislation aimed at forcing out of state mail order retailers to collect use taxes on their behalf. The Illinois act expanded the definition of activities of a retailer maintaining a place of business in the State to include solicitation of orders sent to an out of state location for acceptance and fulfillment by means of catalogues or other advertising materials in the state.

National Bellas Hess

National Bellas Hess, Inc. was a Delaware Corporation, with offices and distribution facilities in Missouri. They had no place of business in Illinois. They had no employee or independent agents soliciting orders in Illinois. Their activities in Illinois were limited to solicitation through catalogs and advertising flyers, sent by U.S. mail, to Illinois residents who were on national mailing lists. Orders were sent to Missouri for acceptance and fulfillment, with goods delivered by common carrier or U.S. mail. Believing the requirement to be a violation of the Due Process and Commerce Clauses, National Bellas Hess refused to collect and remit Illinois use tax as prescribed under Illinois law.

The Attorney General of Illinois bought suit against National Bellas Hess for taxes not collected and remitted, announcing that he hoped to protect Illinois retailers from this unfair competition. The Illinois Supreme Court, placing no significance to the difference of solicitation by brokers in Scripto and the catalogue and flyer solicitation in this case, upheld the collection requirements of the law.

Having agreed to hear National's appeal, the Federal Court noted that the claims of Commerce and Fourteenth Amendment's Due Process Clause were closely related. Unlike the Illinois Court, the Federal Court found significance in the differences between this case and Scripto. In its discussion, the Court noted that Scripto had ten agents conducting continuous and regular solicitation in the State. In differentiating this case, the Court observed, "the Court has never held that a State may impose the duty of use tax collection and payment upon a seller whose only connection with customers in the State is by common carrier or the United States mail."

Likewise, the Court found significant differences between this and other mail order houses where the seller had been required to collect the tax and similarities to instances where they were not. Going on to say, "In order to uphold the power of Illinois to impose use tax burdens on National in this case, we would have to repudiate totally the sharp distinction which these and other decisions have drawn between mail order sellers with retail outlets, do no more than communicate with customers in the State by mail or common carrier as part of a general interstate business. But this basic distinction, which until now has been generally recognized by the state taxing authorities, is a valid one, and we decline to obliterate it."

The marriage of the Commerce Clause and the Fourteenth Amendment's Due Process Clause in National would survive for twenty-five years. Under this interpretation, it was outside the authority of congress to regulate the requirements for collection of use taxes since the protections of the Due Process Clause are absolute.

Complete Auto Transit

Complete Auto Transit, Inc., a Michigan corporation, was licensed by the interstate Commerce Commission as an interstate contract carrier throughout the United States. Complete Auto was engaged in the business of delivering automobiles to General Motor's dealerships throughout the country. In some locations, autos were shipped by rail to distribution points operated by Complete Auto where they were loaded on Complete Auto's trucks for the final leg of delivery to the dealers. Complete Auto operated such a distribution point in the Jackson, Mississippi. This facility included a yard where autos were sometimes stored for brief periods awaiting available trucks, an office and facilities for servicing their trucks.

Mississippi imposed a tax for the purpose of engaging in business in the State. The operation of a transportation service within the State was included in as a taxable business to the extent that the service was performed between two points in the State. Complete Auto delivered, from its Mississippi distribution yard, to points within and without the State. Mississippi assessed its business privilege tax on Complete solicitors, or property within a State, and those who auto's delivery from their Mississippi yard to Mississippi dealers but not to out of State dealers. Complete Auto paid the tax and

sued for refund of the tax paid arguing the activity to be protected by the Interstate Commerce Clause. State courts upheld the tax, finding the tax on these activities not to be offensive to the Commerce Clause since all activity taxed took place within the State. Basing their case entirely on Spector Motor Services, Complete Auto appealed to the U.S. Supreme Court, where the Court found sufficient federal question to hear the case. Unlike the state courts, the federal court chose to accept the contention that the service performed was interstate commerce. In presenting its arguments to the high Court, the State stressed the absence of relationship to economic reality in the taxing limits of Spector. The argument was not lost on the Court who expressed frustration with prior courts in perpetuating the significance given to draftsmanship in Spector.

In a unanimous decision, the Court took the opportunity to overturn its earlier decision of Spector Motor Service. Instead, the Court ruled that a tax on the privilege of doing business in the state will not be held to violate the Commerce Clause when it is applied to an interstate activity:

1. With a substantial nexus with the taxing state,
2. Is fairly apportioned,
3. Does not discriminate against interstate commerce, and
4. Is fairly related to the services provided by the State.

As previously presented in this text, this remains the standard under which Interstate Commerce Clause offense is judged.

National Geographic Society

Later the same year, Supreme Court once again widened the opening of doors in its ruling in National Geographic Society, imposing a liability for collection of California's use tax on mail order sales into the state. National Geographic Society was engaged in the business of publishing a periodical, for distribution to members of the Society and limited subscription. The Society also sold maps, atlases, globes and books, primarily by mail order, from its offices in Maryland and Washington DC. During the period at issue, the Society had gross receipts of over $85,000 from such mail order sales to California customers. A third source of revenue for the Society was the sale of advertising space in the periodical. The Society maintained two offices in the State of California for the purpose of soliciting advertising. Only minor quantities of maps, globes, etc were sold "over the counter" at the California offices, with such sales given no significance by the courts.

While the membership, subscription and advertising sales were not subject to sales or use tax, the sale of maps, atlases, etc were subject to California tax. California courts found the Due Process and Commerce Clause requirements satisfied when an out of state seller conducts a substantial mail order business with residents in the State if the seller has the slightest presence within the State. The Society argued that National Bellas Hess required nexus creating relationships not only between the out of State business and the State but also between the activities of the seller in the State and the transaction subject to the tax. While seemingly rejecting the California court's "slightest presence" standard, the Federal Court found the offices of the Society in California need not be related to the taxable transactions to form the required nexus.

Tyler Pipe Industries, Inc.

The State of Washington imposes a business and occupation tax (B&O), which is a gross income tax applied to activities in the State. The tax applied to activities of extracting raw materials, manufacturing, making wholesale sales and making retail sales in the State. A different tax rate is applied to each activity. From 1950 to 1986, an exemption, known as a Multiple Activities Exemption, was available from the manufacturing tax, for goods sold at wholesale in the State. No exemption was allowed for taxes paid on manufacturing activities to other states.

Tyler Pipe Industries, Inc., was a Delaware corporation, commercially domiciled in Texas. They marketed nationwide including within the State of Washington. Tyler had no manufacturing in Washington. The State of Washington levied an assessment against Tyler for unpaid B&O taxes on its wholesale sales. Tyler challenged the imposition of the tax claiming, among other arguments, it violated the Commerce Clause of the U.S. Constitution. Washington courts upheld the tax and Tyler appealed to the U.S. Supreme Court. The Federal Court found the Multiple Activities Exemption discriminated on its face, favoring in-State manufactured goods in offense to the Commerce Clause.

Quill Corporation

The Supreme Court dissolved the marriage of the Due Process Clause and the Commerce Clause in presenting its 1992 Quill decision. In so doing, it affirmed the "bright line" rule of Bellas Hess under the Commerce Clause permitting out-of-state mail order vendors without a physical presence in the state to avoid collection of the state's use tax. As to the Due Process requirements, the Court found compelling precedent in non-tax case law to remove the "bright line" physical presence requirement. Instead, the Court determined that Due Process requirements are satisfied when business activities are "purposefully directed" toward residents of the state.

Quill, an out-of-state mail order retailer, had no more than an insignificant amount of tangible property and no sales representatives in North Dakota. All North Dakota sales

were solicited by advertisements in national periodicals, catalogs, flyers and telephone calls. They did have a minor amount of computer software that they retained title to licensed for use in the State. This software enabled the customer to query Quill's inventory files to ascertain whether desired items were in inventory stock and place an order directly if desired. North Dakota regulations required a business sending three or more advertisements into the State in a 12-month period to collect use tax from customers in the State. Quill contended that the State did not have the constitutional authority to compel it to collect such taxes and refused to do so. The State Tax Commissioner filed action in its courts to collect from Quill the taxes with penalty and interest it had refused to collect. The trial court found in the favor of Quill based on Bellas Hess and the Commissioner appealed to the State Supreme Court.

The State High Court concluded that Bellas Hess was no longer applicable due to changes in the national economy and growth of the mail order business and reversed the lower court.

In final analysis, the U.S. Supreme Court agreed with the State High Court in respect to the Due Process protections but not to the Commerce Clause protections. Reviewing non-tax findings of the Court since Bellas Hess, the Court found physical presence was no longer required to satisfy the Due Process requirements of the Fourteenth Amendment. Quoting prior findings, the Court repeated, "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." Concluding its review of modern case law surrounding Due Process stating "In 'modern commercial life' it matters little that such solicitation is accomplished by a deluge of catalogs rather than a phalanx of drummers: the requirements of due process are met irrespective of a corporation's lack of physical presence in the taxing State. Thus, to the extent that our decisions have indicated that the Due Process Clause requires physical presence in a State for the imposition of duty to collect a use tax, we overrule those holdings as superseded by developments in the law of due process." Thus, a new Due Process standard of "purposeful direction" of business activity became the standard of taxation nexus under the Due Process Clause.

Likewise, the Court found an evaluation in the cases involving the Commerce Clause since Bellas Hess. This Court disagreed with the State Court's conclusion that this evolution had made the findings of Bellas Hess obsolete under the Commerce Clause. The Court also rejected North Dakota's claims that Quill had physical presence within the State by virtue of "sales on approval" and software licensed for use by residents of the State. In final analysis, the Court extolled the benefits of a "bright line" test finding comfort in the power of Congress to legislatively provide further restrictions at its desire. With this the Court reaffirmed the Commerce Clause holding under Bellas Hess, respecting the authority of Congress to loosen or tighten the states' taxing authority at will.

Michigan Use Tax Nexus Standard

On May 12, 1999 the Michigan Department of Treasury issued Revenue administrative Bulletin 1999-1 Use Tax Nexus Standards. The bulletin describes the jurisdictional standard to determine whether a seller is subject to the collection requirements of Michigan's Use Tax.

The bulletin applies jurisdictional standards established by the U.S. Supreme Court from 1939 to the present. Judicial law is the controlling interpretation of federal law and must be given full retroactive effect in all cases still open on direct review and as to all events. Accordingly, the standards described within the RAB shall be enforced by the Department and given full jurisdictional effect to all open years and for cases still open and on direct review.

Once nexus is established by a seller for use tax collection purposes, nexus shall exist for that seller from the date of contact forward for the remainder of that month and for the following 11 months. Either the seller or the Department may submit proof that a longer or shorter period more reasonably reflects the sales that were proximately caused by the seller's in-state contacts under the facts and circumstances.

An out-of-state seller is subject to Michigan's use tax collection responsibility when it engages in any of the following activities:

1. It has one or more employees resident or temporarily present in Michigan engaging in any activity other than those described in paragraph 7 below. An employee temporarily present in Michigan for two days will create nexus.

2. It owns, rents, leases, maintains, or has the right to use and uses tangible personal or real property that is permanently or temporarily physically located in Michigan.

3. Its employees own, rent, lease, use, or maintain an office or other place of business in Michigan.

4. It has goods delivered to Michigan in vehicles the out-of-state seller owns, rents, leases, uses, or maintains or has goods delivered by a related party acting as a representative of the out-of-state seller.

Examples:

A company that uses its own trucks to deliver goods to purchasers in Michigan will have nexus with Michigan.

A company, that has its wholly owned subsidiary acting as its representative, delivers goods to purchasers in Michigan will have nexus with Michigan.

A company that has all of its goods delivered to purchasers in Michigan by an unrelated common carrier will not have nexus with Michigan.

5. Its agents, representatives, independent contractors, brokers or others, acting on its behalf, own, rent, lease, use, or maintain an office or other place of business in Michigan, and this property is used in the representation of the out-of-state seller in Michigan.

6. Its agents, representatives, independent contractors, brokers or others acting on behalf of the out-of-state seller, are regularly and systematically present in Michigan conducting activities to establish or maintain the market for the out-of-state seller whether or not these individuals or organizations reside in Michigan.

7. Activities that establish or maintain the market for the out-of-state seller include, but are not limited to, the following:

    a. Soliciting sales;

    b. Making repairs or providing maintenance or service to property sold or to be sold;

    c. Collecting current or delinquent accounts, through assignment or otherwise, related to sales of tangible personal property or services;

    d. Delivering property sold to customers;

    e. Installing or supervising installation at or after shipment or delivery;

    f. Conducting training for employees, agents, representatives, independent contractors, brokers or others acting on the out-of-state seller's behalf, or for customers or potential customers;

    g. Providing customers any kind of technical assistance or service including, but not limited to, engineering assistance, design service, quality control, product inspections, or similar services;

    h. Investigating, handling, or otherwise assisting in resolving customer complaints;

    i. Providing consulting services; or

    j. Soliciting, negotiating, or entering into franchising, licensing, or similar agreements.

8. Regular and systematic presence exists if at least 2 days of presence occurs in Michigan on an annual ("annual" meaning a 12 month period) basis.

9. Lawyers, accountants, investment bankers, and other similar professionals in Michigan who perform services for an out-of-state seller in their professional

capacity shall not be considered to be establishing or maintaining the market on behalf of the out-of-state seller.

10. If none of an out-of-state seller's contacts in Michigan fall under paragraph 6)(a) and its only contacts with Michigan are limited to any of the contacts listed below, such contacts will be presumed not to create nexus.

    a. Meeting with in-state suppliers of goods or services;

    b. In-state meetings with government representatives in their official capacity;

    c. Attending occasional meetings (e.g., board meetings, retreats, seminars and conferences sponsored by others, schools or other training sponsored by others, etc.);

    d. Holding recruiting or hiring events;

    e. Advertising in the state through various media;

    f. Renting to or from an in-state entity customer lists;

    g. Attending a trade show at which no orders for goods are taken and no sales are made.

Once nexus is established by a seller for use tax collection purposes, nexus shall exist for that seller from the date of contact forward for the remainder of that month and for the following 11 months.

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