IN THE ALABAMA TAX TRIBUNAL

NEWEGG, INC.	§	
	§	
Taxpayer,	§	Docket No. S. 16-613
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

ANSWER

COMES NOW, the State of Alabama Department of Revenue, by and through its counsel and answers Newegg, Inc.'s, notice of appeal.

Background

On October 22, 2015, the Alabama Department of Revenue (the "Department") promulgated Rule 810-6-2-.90.03, Ala. R. Admin. P. (the "Rule"), which requires certain out-of-state sellers to collect and remit use tax to the state, pursuant to Section 40-23-67, Ala. Code 1975. The Rule requires out-of-state sellers to collect and remit use tax if the sellers lack a physical presence in Alabama but have a substantial economic presence in the state. Under the Rule, an out-of-state seller has a substantial economic presence in the state if the seller sold more than $250,000 of tangible personal property into the state during the previous calendar year. In order for the Rule to apply to an out-of-state seller, the seller must also conduct one or more of the activities listed in Section 40-23-68, Ala. Code 1975.

The Rule applies to all transactions on or after January 1, 2016. Thereafter, the Department determined that Newegg met the triggering requirements of the Rule and, thus, had to collect and

remit use tax to the Department for sales of tangible personal property made into the state. The Department entered its final assessment on May 12, 2016, leading to this appeal.

Argument

Newegg presents two principle arguments in its appeal. First, Newegg argues that the Rule is unconstitutional under Quill Corp. v. North Dakota, 504 U.S. 298 (1992). Second, Newegg argues that it does not conduct any of the activities in the state that are listed in Section 40-23-68. Newegg has not presented any argument challenging the amount of the final assessment.

Constitutional argument

In order for a state to tax a person or business in interstate commerce, the state must meet the requirements of the Due Process Clause, U.S. Const. amend. XIV, § 1, and the Commerce Clause, U.S. Const. art. I, § 8, cl. 3, of the United States Constitution.

Due Process Clause

Newegg has not presented any arguments related to the ability of the state to subject Newegg to taxation under the Due Process Clause of the United States Constitution. Therefore, the Department will not address the Due Process Clause at this time. If Newegg later introduces a Due Process Clause argument, the Department will address the issue at the appropriate time.

Commerce Clause

It is well understood that "[i]nterstate commerce may be required to pay its fair share of state taxes." D.H. Holmes Co. v. McNamara, 486 U.S. 24, 31 (1988). In Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977), and its progeny, the United States Supreme Court established a four-part test to determine whether a state tax meets the requirements of the Commerce Clause. The four prongs of the Compete Auto test are: (1) whether the tax is applied to an activity with substantial nexus with the taxing State, (2) whether the tax is fairly apportioned, (3) whether the

tax discriminates against interstate commerce, and (4) whether the tax is fairly related to the services provided by the State. See Quill Corp. v. North Dakota, 504 U.S. 298, 311 (1992).

In Quill, the United States Supreme Court held that states could not require sellers to collect and remit sales and use taxes for purchases made to residents of the state unless the seller had a physical presence in the state. Thus, the Court established what it referred to as a bright-line rule regarding the first prong of the Compete Auto test. Under Quill, if the seller does not have a physical presence in the taxing state, then the seller does not have substantial nexus with the taxing state; a lack of physical presence ends the analysis at the first prong of the Compete Auto test and prevents the taxing state from applying the tax to the seller. Quill, 504 U.S. at 311.

The Department acknowledges that the Rule is at odds with the decision in Quill. However, the Department argues that developments in the national economy have diminished the applicability of the reasoning in Quill and have made the physical presence rule established by Quill unworkable. "[T]he fact that a decision has proved 'unworkable' is a traditional ground for overruling it." Montejo v. Louisiana, 556 U.S. 778, 792 (2009) (citing Payne v. Tennessee, 501 U.S. 808, 827 (1991)). As the United States Supreme Court has also stated:

> "Beyond workability, the relevant factors in deciding whether to adhere to the principle of stare decisis include the antiquity of the precedent, the reliance interests at stake, and of course whether the decision was well reasoned." Montejo v. Louisiana, 556 U.S. 778, ——, 129 S.Ct. 2079, 2088–2089, 173 L.Ed.2d 955 (2009) (overruling Michigan v. Jackson, 475 U.S. 625, 106 S.Ct. 1404, 89 L.Ed.2d 631 (1986)). We have also examined whether "experience has pointed up the precedent's shortcomings." Pearson v. Callahan, 555 U.S. 223, ——, 129 S.Ct. 808, 816, 172 L.Ed.2d 565 (2009) (overruling Saucier v. Katz, 533 U.S. 194, 121 S.Ct. 2151, 150 L.Ed.2d 272 (2001)).

Citizens United v. FEC, 558 U.S. 310, 362-63 (2010). "Stare decisis is not an inexorable command; rather, it 'is a principle of policy and not a mechanical formula of adherence to the latest

decision.'" Payne v. Tennessee, 501 U.S. 808, 828 (1991) (quoting Helvering v. Hallock, 309 U.S. 106, 119 (1940)).

The Quill physical presence rule is no longer workable in today's national economy and has significant shortcomings in practice. The state suffers a significant negative impact though the loss of tax revenue as a result of the Quill rule. The Quill rule also places in-state "main street" retailers, who must collect and remit sales tax, at a disadvantage to certain out-of-state retailers, who do not. Furthermore, Newegg and other sellers who lack a physical presence in the state will experience only a small burden when collecting the use tax under the Rule. Finally, if a bright-line rule is still needed, then an economic presence rule is a better, more sensible bright-line test of substantial nexus than the Quill physical presence rule.

After the removal of the infirmity caused by the Court's decision in Quill, the Rule meets all four prongs of the Complete Auto test. As to the first prong, Newegg has substantial nexus in the state of Alabama because it makes a significant amount of sales into the state and has other contacts with the state. As to the second prong, the Rule requires the collection of use tax only on sales made into the state; therefore, it is fair to apportion all of the sale to the state. As to the third prong, although the Rule applies only to sellers who lack a physical presence in the state, sellers with a physical presence in the state are already required to collect and remit sales tax, an equivalent tax. Therefore, no extra burden is placed on out-of-state sellers. As to the fourth prong, sales and use taxes are used to fund education, the court system, law enforcement, and other vital services provided by the state; services that are relied on by Newegg and other out-of-state sellers.

Regulation argument

Newegg has also argued that its activities in Alabama do not fall within any of the conditions imposed by the Rule. The Rule provides:

(1) Notwithstanding the provisions of Rule 810-6-2-.90.01, entitled Seller's Responsibility to Collect and Pay State Sales Tax and Seller's Use Tax, out-of-state sellers who lack an Alabama physical presence but who are making retail sales of tangible personal property into the state have a substantial economic presence in Alabama for sales and use tax purposes and are required to register for a license with the Department and to collect and remit tax pursuant to Section 40-23-67, Code of Ala. 1975, when,

(a) Seller's retail sales of tangible personal property sold into the state exceed $250,000 per year based on the previous calendar year's sales; and

(b) Seller conducts one or more of the activities described in Section 40-23-68, Code of Ala. 1975;

(2) Sellers may satisfy the requirements described in (1) above by one of the following methods:

(a) Using the collecting, reporting and remitting provisions of Article 2, Chapter 23 of Title 40, Code of Ala. 1975, or

(b) Using the collecting, reporting and remitting provisions created by the Simplified Sellers Use Tax Remittance Act codified at 40-23-191 through 40-23-199, Code of Ala. 1975.

(3) This rule shall apply to all transactions occurring on or after January 1, 2016.

Rule 810-6-2-.90.03, Ala. R. Admin. P.

In particular, Newegg argues that it does not conduct any of the activities described in section 40-23-68, which contains a list of activities that, if conducted in the state, will require an out-of-state seller to collect and remit use tax on sales of tangible personal property made into the state. The Department argues that Newegg conducts two of the activities listed in section 40-23-68. The Department argues that Newegg "maintains any other contact with this state that would allow this state to require the seller to collect and remit the tax due under the provisions of the

Constitution and laws of the United States"[1], § 40-23-68(b)(9), and that it "distributes catalogs or other advertising matter and by reason thereof receives and accepts orders from residents, within the State of Alabama." § 40-23-68(b)(10).

Absent the restrictions imposed by Quill, the state has authority under the United States Constitution to require Newegg to collect and remit use tax on purchases of tangible personal property that are made into the state. Additionally, based on its information and belief, the Department asserts that Newegg distributes advertising and promotional materials into the state and receives orders as a result of those advertisements and promotional materials. Because Newegg conducts one or more of the activities listed in section 40-23-68, Newegg is required to collect and remit use tax to the State.

Informal Discovery Requests

Pursuant to § 40-2B-2(j)(1) and § 40-2B-2(j)(3), Ala. Code 1975, and Rule 877-X-1-.14, Ala. R. Admin. P., of the Tribunal's regulations, the Department has included with its answer "written questions in the nature of interrogatories" and a "request for production of documents." The information sought by the Department is calculated to result in the production of admissible evidence related to the following relevant areas:

1. The nature and extent of Newegg's contacts with the state and its residents,
2. The sophistication of Newegg's ability to track customers, orders, and goods,
3. The current ability of Newegg to collect and remit state sales taxes, and
4. The costs incurred by Newegg in collecting state sales taxes.

[1] The authority of the state under the United States Constitution to require Newegg to collect and remit use tax on sales of tangible personal property into the state is admittedly dependent on the overturning of Quill.

All of the above-listed areas of inquiry are relevant to whether the state's regulation meets the four-part Complete Auto test and also are relevant to whether the Quill decision remains workable and relevant in the current economy.

Scheduling Order

The Department proposes that the parties, working together, develop and submit a scheduling order to the Tribunal. The scheduling order would cover such issues as discovery deadlines, expert witnesses, briefing schedules, and other related items.

RESPECTFULLY SUBMITTED on this the 26th day of August, 2016.

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CERTIFICATE OF SERVICE

I hereby certify that I have this date served a true and correct copy of the above document on:

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by placing a copy of same in the United States Mail, first-class postage prepaid and addressed to their regular mailing address, on this the 26th day of August, 2016.

OF COUNSEL