A SOLUTION TO USE TAX AVOIDANCE: TRANSACTION REPORTING REQUIREMENTS FOR REMOTE SELLERS

Comment

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I. INTRODUCTION: A USELESS USE TAX

Jessica is a first-year law student at Texas Tech University School of Law. A week before classes start, she goes to the campus bookstore and purchases a book for her torts course. The book is $119.99 before sales tax is applied. Her classmate, Richard, buys the same book from a small, out-of-state bookstore over the Internet. The book is $119.99, and no sales tax is collected. Score!

Many people, like Richard, avoid paying sales tax by purchasing items from remote sellers over the Internet. These small personal purchases are rarely reported despite Texas having use tax statutes that make the purchaser liable for a tax equal to the total sales tax, which would otherwise be imposed on the purchase.[1] The reasons Texans and citizens of other states with use tax statutes do not report their tax-free Internet purchases range from ignorance of their state's use tax statute to the realization that without transaction reporting requirements for remote sellers, the probability of getting caught is negligible.[2] In either case, use tax avoidance places in-state retailers at a disadvantage and erodes the state's tax base.[3] Passive use tax avoidance particularly affects Texas because sales and use taxes comprise a substantial portion of the state's tax revenue, representing 56% of the total state tax revenue in 2010.[4]

Sales and use taxes are currently imposed by forty-five of the fifty states and the District of Columbia.[5] In Texas, if a retailer located in the state sells a taxable item to a purchaser located in the state, the retailer must collect a state sales tax of 6.25% and local sales tax of up to 2%.[6] But if a retailer that lacks a "substantial nexus" with the state sells a taxable item to a purchaser located in the state, a tax equal to the total sales tax is imposed on the purchaser; this is assuming the item is being purchased for storage, use, or

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1. TEX. TAX CODE ANN. §§ 151.101, 321.104, 323.104 (West 2016).
2. WALTER HELLERSTEIN ET AL., STATE AND LOCAL TAXATION: CASES AND MATERIALS 44 (10th ed. 2014).
3. *See* DONALD BRUCE ET AL., STATE AND LOCAL GOVERNMENT SALES TAX REVENUE LOSSES FROM ELECTRONIC COMMERCE 11 (2009), http://cber.utk.edu/ecomm/ecom0409.pdf.
4. H.R. 82-3, at 1 (Tex. 2011), http://www.hro.house.state.tx.us/pdf/focus/ Revenue82.pdf.
5. Irwin Indus. Tool Co. v. Ill. Dep't of Revenue, 938 N.E.2d 459, 469 (Ill. 2010).
6. TEX. TAX § 151.051(a)–(b); *Sales and Use Tax*, TEX. COMPTROLLER'S OFF., http://comptroller.texas.gov/taxes/sales/ (last visited Dec. 9, 2016) ("Local taxing jurisdictions . . . can also impose up to 2 percent sales and use tax for a maximum combined rate of 8.25 percent.").

other consumption in the state and an exemption does not apply.[7] For purchasers who are inclined to self-report and pay the use tax on their online purchases, the Texas Comptroller's website provides Tax Form 01-156.[8] There is no way to measure the exact amount of tax revenue the State of Texas is failing to collect due to Internet purchases, but it is safe to assume that the majority of citizens have never seen Tax Form 01-156.[9] Fortunately, the solution to the problem of use tax avoidance does not lie in attempting to force each individual purchaser to report every use-tax-eligible purchase; rather, the solution lies in imposing transaction reporting requirements on remote sellers that lack a substantial nexus to the taxing state.[10]

States currently employ an assortment of methods by which they collect use taxes on sales made by remote sellers that do not satisfy the substantial nexus requirement as defined by the United States Supreme Court in *Quill Corp. v. North Dakota*.[11] Some states rely on the purchaser to self-report the use tax.[12] Utah, for instance, politely requests that purchasers who "do not have a Utah sales tax license/account [to] report the use tax on [their] income tax return[s]."[13] Texas, which does not have an income tax, posts a use tax reporting form on the Internet, but it does not appear to be very effective; this is unfortunate because Texas is currently losing tax revenue due to low oil prices.[14] Other states have passed legislation colloquially referred to as "Amazon tax" laws.[15] In New York, for example, remote sellers are "presumed to be soliciting business through an independent contractor" if New York residents agree to refer potential customers to the seller in return

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7. TEX. TAX §§ 151.101, 321.104, 323.104; *see* Sw. Bell Yellow Pages v. Combs, No. 03–07–00638–CV, 2009 WL 211633, at *3 (Tex. App.—Austin Jan. 30, 2009, pet. denied) ("[P]rinted material that serves as a component of some other finished product is excluded from the use tax . . . .").

8. *Texas Use Tax Return*, TEX. COMPTROLLER'S OFF., https://www.comptroller.texas.gov/tax info/forms/01-156.pdf (last visited Nov. 2, 2016).

9. *See, e.g.*, Martin Swant, *State of Alabama Sending Tax Notices to Some Consumers for Online, Out-of-State Purchases*, AL.COM: BLOG (Sept. 5, 2010, 10:00 AM), http://blog.al.com/businessnews /2010/09/state_of_alabama_sending_tax_n.html (underscoring the fact that only 0.38% of Alabama income tax returns reported use-tax-eligible purchases).

10. *See* discussion *infra* Section II.E (discussing Colorado's attempt to extract use taxes from out-of-state sellers by requiring these sellers to collect the tax from in-state buyers).

11. Quill Corp. v. North Dakota, 504 U.S. 298, 314 (1992) (requiring that retailers have "a physical presence in the taxing State" before use tax obligations may be imposed).

12. *See, e.g.*, *Utah Use Tax for Internet and Catalog Purchases*, UTAH ST. TAX COMM'N, http://www.incometax.utah.gov/topics/use-tax (last updated Nov. 24, 2015).

13. *Id.*

14. *Texas Use Tax Return*, *supra* note 8; *cf.* BRUCE ET AL., *supra* note 3, at 11 (forecasting Texas sales and use tax revenue losses from e-commerce sales at $870 million for the 2012 calendar year). Texas is currently suffering tax revenue losses due to low oil prices, so it is imperative to recoup these losses—reporting requirements aimed at collecting unreported use taxes are a viable means by which to do so. *See, e.g.*, John Krohn & Robert McManmon, *Oil Price Decline Leads to Lower Tax Revenues in Top Oil-Producing States*, U.S. ENERGY INFO. ADMIN. (Mar. 12, 2015), http://www.eia.gov/todayinenergy/ detail.cfm?id=20332.

15. Joel Griffiths, Comment, *Use It or Lose It: State Approaches to Increasing Use-Tax Revenue*, 60 U. KAN. L. REV. 649, 659 (2012).

for consideration of some sort.[16] This rebuttable presumption, which is difficult and costly to rebut, allows New York to require remote sellers to collect and remit state use taxes.[17]

In 2010, Colorado implemented yet another method by which to limit use tax avoidance: transaction reporting requirements.[18] Under the 2010 law, if a retailer did not collect Colorado sales tax, it was required to furnish information related to sales made to Colorado residents to the Colorado Department of Revenue.[19] Refusal could lead to a Colorado district court holding the retailer in contempt.[20] The law primarily affected remote sellers lacking a substantial nexus to Colorado because every other retailer is required to collect Colorado sales or use tax.[21]

The law was immediately challenged by an association of remote sellers who market products directly to consumers by means of varied media.[22] In 2012, the United States District Court for the District of Colorado issued an injunction prohibiting the enforcement of the reporting requirements against retailers who lack a physical presence in Colorado.[23] The district court held that the reporting requirements were unconstitutional because they violated both prongs of the Dormant Commerce Clause.[24] First, the district court concluded that the requirements discriminated against remote sellers and, more generally, interstate commerce.[25] Second, the district court concluded that the requirements imposed "an undue burden on interstate commerce under the standard established in *Quill*."[26] After a brief sojourn in the Supreme Court of the United States to address a technical matter, the case returned to the United States Court of Appeals for the Tenth Circuit for consideration on the merits.[27] The Tenth Circuit concluded that the reporting requirement did not discriminate against or unduly burden interstate commerce.[28] In light of the Tenth Circuit's decision, this Author argues that states, such as Texas, should enact similar statutes.

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16. N.Y. TAX LAW § 1101(b)(8)(vi) (McKinney Supp. 2016).
17. *Id.*
18. COLO. REV. STAT. ANN. § 39-21-112(3.5)(a) (West 2013).
19. *Id.*
20. *Id.*
21. *See id.* § 39-26-105(1)(a)(I)(A) (holding every retailer that makes a sale in the state liable for payment of the sales tax); *see also id.* § 39-26-204(2) (requiring retailers doing business in Colorado to collect and remit the state use tax).
22. Direct Mktg. Ass'n v. Huber (*Direct Mktg. Ass'n I*), No. 10–cv–01546–REB–CBS, 2012 WL 1079175, at *2 (D. Colo. Mar. 30, 2012), *rev'd*, 814 F.3d 1129 (10th Cir. 2016).
23. *Id.* at *11.
24. *Id.* at *10.
25. *Id.*
26. *Id.*
27. Direct Mktg. Ass'n v. Brohl (*Direct Mktg. Ass'n III*), 135 S. Ct. 1124, 1134 (2015). The Supreme Court's review was limited to deciding whether the Tax Injunction Act (TIA) applied to the district court's decision. *Id.* at 1127.
28. Direct Mktg. Ass'n v. Brohl (*Direct Mktg. Ass'n IV*), 814 F.3d 1129, 1132 (10th Cir. 2016).

This Comment addresses the different collection methods states have when trying to collect use taxes, with a special emphasis on transaction reporting requirements. Part II explores the different use tax collection methods states currently employ or for which they have advocated. Part II also adumbrates the history of the Dormant Commerce Clause, specifically in relation to state taxation. Part III provides an analysis of the constitutional issues encountered when a state attempts to require a remote seller to provide transaction records despite the seller not having a physical presence in that state. Part IV presents arguments in favor of the adoption of reporting requirements by Texas and other states; it also provides recommendations for how to draft reporting requirements in a manner that avoids Dormant Commerce Clause challenges. Part V concludes with a summary of the constitutional issues surrounding reporting requirements and methods to circumvent those issues.

II. A HISTORY OF USE TAX COLLECTION METHODS

A. And God Said, "Let There Be Use Taxes"

After certain states enacted the first sales taxes in the 1930s, they realized that residents were crossing the border into neighboring states that had not implemented a sales tax so that they could purchase goods tax-free.[29] To prevent a loss in tax revenue, states imposing a sales tax enacted use tax laws to complement their sales tax laws.[30] In a 1937 decision upholding Washington's imposition of a use tax on contractors using machinery to construct a dam on the Columbia River,[31] Justice Benjamin Cardozo listed the primary reasons that states have use tax statutes:

> One of its effects must be that retail sellers in Washington will be helped to compete upon terms of equality with retail dealers in other states who are exempt from a sales tax or any corresponding burden. Another effect, or at least another tendency, must be to avoid the likelihood of a drain upon the revenues of the state, buyers being no longer tempted to place their orders in other states in the effort to escape payment of the tax on local sales.[32]

29. *See* Andrew J. Haile, *Affiliate Nexus in E-Commerce*, 33 CARDOZO L. REV. 1803, 1806 (2012); Liz Emanuel, *When Did Your State Adopt Its Sales Tax?*, TAX FOUND. (July 11, 2014), http://taxfoundation.org/blog/when-did-your-state-adopt-its-sales-tax (providing a map illustrating the year each state implemented its sales tax statute and noting that the "trend began with Mississippi in 1930").

30. *See* Haile, *supra* note 29, at 1806. Use taxes apply to the in-state consumption of items purchased out of state because sales tax collection duties do not extend to remote sellers. Nat'l Geographic Soc'y v. Cal. Bd. of Equalization, 430 U.S. 551, 555 (1977).

31. Henneford v. Silas Mason Co., 300 U.S. 577, 579 (1937).

32. *Id.* at 581.

Justice Cardozo's observations are just as true today, if not more so, due to the invention of the Internet.[33] The Internet, however, has also made the imposition of use tax collection requirements on remote sellers more difficult due to two primary constitutional obstacles.[34]

When trying to force a remote seller to collect and remit state use taxes, the first obstacle a state has to overcome is the Due Process Clause of the Fourteenth Amendment.[35] This obstacle is not as difficult to overcome as it once was and can be satisfied merely by showing that a remote seller "has purposefully directed its activities" at a state.[36] One reason why the Due Process Clause is no longer a substantial obstacle is that there is no longer a "physical presence" requirement.[37] The reason for this shift in due process legal theory is best illustrated in *Burger King Corp. v. Rudzewicz*, in which Justice Brennan explained that because a defendant "manifestly has availed himself of the privilege of conducting business [in a specific state], and because his activities are shielded by 'the benefits and protections' of the forum's laws[,] it is presumptively not unreasonable to require him to submit to the burdens of litigation in that forum as well."[38] As of now, "purposeful availment" is the test for determining whether a remote seller can be required to collect and remit state use taxes.[39]

When trying to force a remote seller to collect and remit state use taxes, the second obstacle a state must overcome is the Dormant Commerce Clause.[40] In 1941, the Supreme Court held that the Dormant Commerce Clause did not prohibit a state from requiring a retailer with stores in the state to collect and remit use taxes on mail order purchases processed outside of the state.[41] The Court reasoned that interstate commerce was not burdened

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33. *Id.*

34. *See* discussion *infra* Section II.A (noting the use tax collection issues posed by the Due Process and Dormant Commerce Clauses).

35. U.S. CONST. amend. XIV, § 1 ("[N]or shall any State deprive any person of life, liberty, or property, without due process of law . . . ."); *see also* Miller Bros. Co. v. Maryland, 347 U.S. 340, 344–45 (1954) ("[D]ue process requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.").

36. Quill Corp. v. North Dakota, 504 U.S. 298, 308 (1992) (underscoring the fact that Quill relied on North Dakota's legal infrastructure to protect the market and on North Dakota's physical infrastructure to allow for the distribution of twenty-four tons of Quill catalogs and flyers that were mailed into the state each year).

37. *Id.*

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

39. *Quill*, 504 U.S. at 307; *see* Michiana Easy Livin' Country, Inc. v. Holten, 168 S.W.3d 777, 784–85 (Tex. 2005) (listing the three elements required to show purposeful availment).

40. U.S. CONST. art. I, § 8, cl. 3 ("The Congress shall have Power . . . [t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes . . . ."); *see also* Okla. Tax Comm'n v. Jefferson Lines, Inc., 514 U.S. 175, 180 (1995) (stating that the Dormant Commerce Clause prohibits a state from placing "burdens on the flow of commerce across its borders that commerce wholly within those borders would not bear").

41. Nelson v. Sears, Roebuck & Co., 312 U.S. 359, 362 (1941).

because unlike true out-of-state sellers, the retailer in that case was receiving benefits from the state by having stores located within its borders.[42]

The test for whether a retailer can be required to collect use taxes was eventually laid out in *Complete Auto Transit, Inc. v. Brady*, which did not actually involve a use tax statute but upheld Mississippi's "privilege of doing business" tax.[43] The test focuses on four factors.[44] First, the entity must have a "sufficient nexus"—also referred to as a substantial nexus—with the taxing state.[45] Second, the tax must not discriminate against interstate commerce.[46] Third, the tax must be fairly apportioned.[47] Fourth, the tax must be related to services provided by the taxing state.[48] Many states that try to impose use tax collection obligations on remote online sellers encounter problems regarding the substantial nexus requirement.[49] States can indubitably force retailers with stores located in the state to collect and remit state sales taxes because "[t]here is 'nexus' aplenty" if a retailer has a store located in the state.[50] But what if a retailer does not have a store or make sales in a state?

The Supreme Court answered this question in *Quill Corp. v. North Dakota* when it reaffirmed that a state cannot impose tax collection duties on remote sellers who lack a substantial nexus with the state.[51] In defining substantial nexus, the Court relied on a bright-line test established in *National Bellas Hess, Inc. v. Department of Revenue of Illinois*.[52] The test focuses on whether a retailer has a physical presence in the taxing state.[53] The Court deemed *Bellas Hess* to be consistent with *Complete Auto*.[54] Because the *Complete Auto* test now has a physical presence requirement, retailers whose actions satisfy the "minimum contacts" test required under the Due Process Clause may still avoid the imposition of tax collection duties if they do not

42. *Id.* at 365.

43. Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 278, 289 (1977).

44. *Id.* at 278.

45. *Id.*

46. *Id.*

47. *Id.*

48. *Id.*

49. St. Tammany Par. Tax Collector v. Barnesandnoble.com, 481 F. Supp. 2d 575, 580 (E.D. La. 2007).

50. D.H. Holmes Co. v. McNamara, 486 U.S. 24, 33 (1988).

51. Quill Corp. v. North Dakota, 504 U.S. 298, 312 (1992).

52. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 758 (1967) ("But 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."), *overruled in part by Quill*, 504 U.S. 298.

53. *Quill*, 504 U.S. at 315 ("Whether or not a State may compel a vendor to collect a sales or use tax may turn on the presence in the taxing State of a small sales force, plant, or office.").

54. *Id.* at 311.

have a physical presence in the taxing state.[55] The Dormant Commerce Clause is thus a particularly stalwart shield for remote sellers.[56]

B. Pay to All What Is Owed: Self-Report Taxes to Whom Taxes Are Owed

One solution to use tax avoidance is to encourage self-reporting. In states such as California, the state income tax return contains a section in which a citizen can report purchases qualifying for use tax liability.[57] This is a convenient way to provide notice to citizens of their duty to pay a use tax on their untaxed purchases from remote sellers. States, such as Washington and Texas, that do not have an income tax do not have as easy of a forum by which to notify citizens of their use tax obligations.[58] Both states provide a downloadable paper reporting form, and Washington allows online reporting and payment; however, these states do not notify taxpayers about use taxes on an annual basis, so it is unlikely that Washington and Texas will collect much tax revenue from private individuals.[59]

The stark reality is that most individuals will not pay use taxes on qualifying purchases because they do not know about use taxes or are willing to gamble on not getting caught.[60] Self-reporting is, therefore, not a viable option for use tax collection.[61] According to a 2012 estimate by the National Conference of State Legislatures, states lost $23 billion due to their inability to collect use taxes directly from remote sellers.[62] At the state level, the Alabama Department of Revenue estimated that their state alone lost an estimated $100 million in unreported use tax revenue in 2010.[63]

It is obvious that reliance on self-reporting is not a practical solution to the problem of use tax avoidance. Private individuals purchase items ranging from tennis shoes to five-pound gummy bears from online retailers and avoid paying any taxes because enforcing self-reporting is just not feasible.[64]

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55. *Id.* at 312.

56. ERIKA K. LUNDER, TAXATION OF INTERNET SALES AND ACCESS: LEGAL ISSUES 4 (2014), https://www.fas.org/sgp/crs/misc/R43800.pdf ("The Supreme Court has not revisited the issue of when a state may impose use tax obligations on a seller since *Quill*.").

57. *For Personal Use*, CAL. ST. BOARD EQUALIZATION, http://www.boe.ca.gov/sutax/usetax.htm#Personal (last visited Nov. 19, 2016).

58. *Income Tax*, WASH. ST. DEP'T REVENUE, http://dor.wa.gov/content/FindTaxesAndRates/IncomeTax/ (last visited Nov. 19, 2016); *Texas*, TAX FOUND., http://taxfoundation.org/state-tax-climate/texas (last visited Nov. 19, 2016).

59. *Use Tax*, WASH. ST. DEP'T REVENUE, http://dor.wa.gov/content/FindTaxesAndRates/UseTax/ (last visited Nov. 19, 2015).

60. *See, e.g.*, Swant, *supra* note 9.

61. *Id.*

62. Scott T. Allen, Comment, *Adapting to the Internet: Why Legislation Is Needed to Address the Preference for Online Sales That Deprives States of Tax Revenue*, 66 TAX LAW. 939, 942 (2013).

63. J. Sims Rhyne, III, Comment, *A Useless Use Tax: Why Alabama Is the Poster Child for the Streamlined Sales and Use Tax Agreement*, 42 CUMB. L. REV. 337, 337–38 (2011).

64. *See, e.g.*, Swant, *supra* note 9 (underscoring the fact that only 0.38% of Alabama income tax returns reported use-tax-eligible purchases).

Retailers with a physical presence in a state are losing business because of the unfair advantage that remote sellers have over them.[65] States are also losing out on tax revenue.[66] This is why states and local retailers have pushed for laws allowing for the imposition of use tax liability on remote sellers.[67]

C. There Was a Woman Called Susan Combs; She Was a Chief Tax Collector, and She Favored Affiliate Taxes

States' enactment of "Amazon laws" or Amazon taxes, named after the online retail giant, constitutes another response to use tax avoidance.[68] Also referred to as "affiliate taxes," these laws target remote sellers who engage in performance marketing by using the contractual relationship between the remote seller and the in-state advertising affiliate to establish a substantial nexus to the state.[69] This type of nexus is sometimes referred to as an "attributional nexus" because the activities of the in-state affiliate are attributed to the remote seller.[70] In *Quill*, the Court noted that this type of nexus was used to uphold the imposition of a use tax collection duty in a case from 1960 in which the remote seller used independent contractors for its in-state solicitation.[71]

On March 10, 2011, Illinois's own Amazon law, a "click-through" nexus statute, took effect; it was designed to prevent in-state purchasers from skirting state sales and use taxes.[72] This law redefined retailers "maintaining a place of business in this state" to include retailers "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 of the person's Internet website."[73] The "by a link" language in the definition targets pay-per-click advertising while excluding pay-per-view advertising from the attributional nexus the definition creates.[74]

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65. *See* Michael Mazerov, *Amazon's Arguments Against Collecting Sales Taxes Do Not Withstand Scrutiny*, CTR. ON BUDGET & POL'Y PRIORITIES, http://www.cbpp.org/research/amazons-arguments-against-collecting-sales-taxes-do-not-withstand-scrutiny (last updated Nov. 29, 2010).

66. *Id.*

67. *Id.*

68. Corey Bass, Comment, *Taxation of Internet Transactions: Developing a Clear Rule to End State Law Inconsistencies in the Aftermath of* Amazon.com v. N.Y. Department of Taxation and Finance, 44 CUMB. L. REV. 119, 132 (2013).

69. Performance Mktg. Ass'n v. Hamer (*Performance Mktg. Ass'n II*), 998 N.E.2d 54, 56 (Ill. 2013).

70. Haile, *supra* note 29, at 1812.

71. Quill Corp. v. North Dakota, 504 U.S. 298, 306 (1992) (citing Scripto, Inc. v. Carson, 362 U.S. 207 (1960)).

72. *Performance Mktg. Ass'n II*, 998 N.E.2d at 55.

73. *Id.* at 56 (citing 35 ILL. COMP. STAT. ANN. 105/2(1.1) (West 2010)).

74. *See* Joseph Henchman, *Illinois Supreme Court Strikes Down "Amazon Tax"*, TAX FOUND.: TAX POL'Y BLOG (Oct. 18, 2013), http://taxfoundation.org/blog/illinois-supreme-court-strikes-down-amazon-tax-0.

The Performance Marketing Association immediately challenged Illinois's click-through nexus law.[75] The trial court held that the law ran afoul of the Commerce Clause by failing to satisfy the substantial nexus requirement.[76] The trial court also held that the law was preempted by the Internet Tax Freedom Act (ITFA),[77] which prohibits states from imposing discriminatory taxes on e-commerce.[78] Accordingly, the trial court granted summary judgment in favor of the plaintiff.[79]

The case, styled *Performance Marketing Association v. Hamer*, was directly appealed to the Illinois Supreme Court, where it was affirmed.[80] The court held that the click-through provision violated the ITFA because remote sellers were not taxed if they entered into performance marketing contracts with affiliates that operated via non-Internet forms of media (i.e., print publishers).[81] The court declined to address the plaintiff's Commerce Clause argument.[82] The court did note, however, that the law did not require the sales for which the affiliate was responsible to be made by Illinois residents.[83] *Performance Marketing* is instructive as to the type of language to avoid when drafting affiliate tax laws: Internet-specific language.[84]

New York amended its tax code to establish an attributional nexus through in-state marketing affiliates three years before Illinois enacted its affiliate tax law.[85] New York Governor David Paterson signed the affiliate tax provision—referred to as the "Commission-Agreement Provision"—into law on April 23, 2008.[86] Amazon challenged the law on Commerce Clause and due process grounds two days later; Overstock followed suit the following month.[87] Unlike Illinois's affiliate tax law, New York's affiliate tax law was upheld as constitutional.[88]

The language of New York's Commission-Agreement Provision is quite different from the language found in Illinois's affiliate tax law, though the

75. *See* Performance Mktg. Ass'n v. Hamer (*Performance Mktg. Ass'n I*), No. 2011 CH 26333, 2012 WL 2090791 (Ill. Cir. Ct. May 7, 2012).

76. *Id.*

77. Internet Tax Freedom Act, Pub. L. No. 105-277, 112 Stat. 2681-719 (1998) (codified at 47 U.S.C. § 151 note (2000)).

78. *Performance Mktg. Ass'n I*, 2012 WL 2090791, at *2.

79. *Id.*

80. Steven M. Hogan, *Internet Taxes on Trial: New Strategies for Litigating Remote-Seller Sales and Use Tax Cases*, 88 FLA. B.J., Feb. 2014, at 31, 32.

81. *Performance Mktg. Ass'n II*, 998 N.E.2d 54, 56–60 (Ill. 2013) ("Such contractual arrangements are not limited to the Internet. They are also used in print and broadcast media, where promotional codes are used to generate and track sales.").

82. *Id.* at 59–60.

83. *Id.* at 56.

84. *See id.* at 56–58.

85. N.Y. TAX LAW § 1101(b)(8)(vi) (McKinney Supp. 2016).

86. Amazon.com LLC v. N.Y. State Dep't of Taxation & Fin., 877 N.Y.S.2d 842, 846 (N.Y. Sup. Ct. 2009), *aff'd as modified by* 913 N.Y.S.2d 129 (N.Y. App. Div. 2010).

87. Overstock.com, Inc. v. N.Y. State Dep't of Taxation & Fin., 987 N.E.2d 621, 624 (N.Y. 2013).

88. *Id.* at 627.

basic concept is the same.[89] One difference is that the Commission-Agreement Provision includes the language "refers potential customers, whether by a link on an Internet website *or otherwise*," which avoids an ITFA challenge.[90] Furthermore, the Commission-Agreement Provision requires $10,000 of sales to New York residents before a retailer is brought within the purview of the law.[91] The Commission-Agreement Provision also creates a rebuttable presumption that the retailer is soliciting business through an independent contractor when it enters into a performance marketing contract with a New York resident.[92] After *Performance Marketing* was decided, Illinois revised its affiliate tax law to reach non-Internet affiliates and include an in-state sales requirement; it now closely mirrors New York's Commission-Agreement Provision.[93]

When Amazon and Overstock appealed their cases to the New York Court of Appeals, the issue before the court was whether the Commission-Agreement Provision violated the Dormant Commerce Clause and the Due Process Clause.[94] The court first addressed the Commerce Clause challenge, explaining that *Quill*'s physical presence requirement is "satisfied if economic activities are performed in New York by the seller's employees or on its behalf."[95] The court then rejected the plaintiffs' due process argument concerning the rebuttable presumption, noting that the New York State Department of Taxation and Finance provided an annual certification option to make it easier to rebut.[96] The court also made an insightful observation:

> The world has changed dramatically in the last two decades, and it may be that the physical presence test is outdated. An entity may now have a profound impact upon a foreign jurisdiction solely through its virtual projection via the Internet. That question, however, would be for the United States Supreme Court to consider.[97]

Whether the current Supreme Court would overrule *Quill*'s physical presence requirement is hard to predict, but Justice White's dissent in *Quill* may provide some clues.[98]

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89. *Compare* N.Y. TAX § 1101(b)(8)(vi) (creating an attributional nexus regardless of whether the affiliate advertised via the Internet), *with* 35 ILL. COMP. STAT. ANN. 105/2(1.1) (West 2012) (creating an attributional nexus only through Internet advertising).

90. N.Y. TAX § 1101(b)(8)(vi) (emphasis added).

91. *Id.*

92. *Id.*

93. 35 ILL. COMP. STAT. ANN. 105/2(1.1).

94. Overstock.com, Inc. v. N.Y. State Dep't of Taxation & Fin., 987 N.E.2d 621, 624 (N.Y. 2013).

95. *Id.* at 625.

96. *Id.* at 627.

97. *Id.* at 625.

98. Quill Corp. v. North Dakota, 504 U.S. 298, 328–29 (1992) (White, J., concurring in part and dissenting in part).

Judge Smith, the lone dissenter in *Overstock.com*, expressed his hesitation at circumventing Supreme Court precedent concerning the physical presence requirement and adopting Justice White's dissent from *Quill* as law.[99] However, as Justice Frankfurter once said, "Wisdom too often never comes, and so one ought not to reject it merely because it comes late."[100] In *Quill*, Justice White's partial dissent focused on "[t]he illogic of retaining the physical-presence requirement . . . not because of any logical relation to fairness or any economic rationale related to principles underlying the Commerce Clause, but simply out of the supposed convenience of having a bright-line rule."[101] In the age of e-commerce, the iniquity of retaining *Quill*'s physical presence requirement is greater than Justice White could have imagined when he wrote his opinion.[102] The next time the Supreme Court has an opportunity to cast aside *Quill*'s bright-line physical presence rule, the Justices will have to decide whether to adhere to the doctrine of stare decisis or adapt to changing technology.[103] Despite there being a number of progressive Justices on the Court, any state advocating for a new nexus rule will have to overcome the always present obstacle of stare decisis as well as the obstacle of technological illiteracy.[104]

Though the focus of this Section has been on affiliate tax statutes thus far, attributional nexuses are also grounded in common law. In Texas, the question of what constitutes "doing business" for franchise tax purposes led to the creation of a common law attributional nexus between foreign holding companies and their subsidiaries operating in Texas.[105] Attributional nexuses may arise between companies and their distribution centers as well.[106] This is the position that former Texas Comptroller Susan Combs took when she presented Amazon with a $269 million tax bill.[107] Texas dropped its $269 million demand after Amazon threatened to close its distribution facility in Irving, Texas—which would have eliminated 119 jobs—and to not build any more facilities in the state.[108] In return for Texas forgiving the company's

99. *Overstock.com, Inc.*, 987 N.E.2d at 627 (Smith, J., dissenting).

100. Henslee v. Union Planters Nat'l Bank & Tr. Co., 335 U.S. 595, 600 (1949) (Frankfurter, J., dissenting).

101. *Quill*, 504 U.S. at 328–29 (White, J., concurring in part and dissenting in part).

102. *See, e.g.*, Mazerov, *supra* note 65.

103. *See, e.g.*, *id.*

104. *See generally* Mark Grabowski, *Are Technical Difficulties at the Supreme Court Causing a "Disregard of Duty"?*, 3 CASE W. RES. J.L. TECH. & INTERNET 93 (2012) (providing a list of blunders by the current Justices that indicate a profound lack of understanding regarding how basic technologies operate).

105. Lawrence Indus., Inc. v. Sharp, 890 S.W.2d 886, 888, 892 (Tex. App.—Austin 1994, writ denied).

106. Ross Ramsey, *Let's Make a Deal, Amazon Tells Texas*, N.Y. TIMES (June 23, 2011), http://www.nytimes.com/2011/06/24/us/24ttramsey.html.

107. *Id.*

108. Assoc. Press, *Texas-Amazon Sales Tax Deal Benefited Both Sides, Data Shows*, WASH. TIMES (Aug. 9, 2015), http://www.washingtontimes.com/news/2015/aug/9/texas-amazon-sales-tax-deal-benefited-both-sides-d/?page=all.

$269 million in back taxes, Amazon agreed to begin collecting state sales taxes starting July 1, 2012.[109] The company also agreed to open more Texas facilities, investing $300 million in capital into the state and creating over 6,000 jobs.[110] This Amazon–Texas dispute underscores how affiliate nexuses do not work because companies can merely sever ties with their marketing affiliates and distribution centers to destroy the nexus.

The seven states with affiliate tax statutes (assuming more states do not adopt affiliate tax laws) face the problem of remote sellers removing their in-state sales affiliates, just like Amazon threatened to do in Texas with respect to its distribution centers.[111] Amazon actually followed through with its threats to cut all of its ties with its North Carolina and Rhode Island affiliates after those states adopted affiliate tax statutes.[112] Even if the Supreme Court were to lessen substantial nexus requirements to the point that affiliate tax laws were not needed, states may also face a more practical issue: boycotts by some remote sellers.[113] For affiliate tax laws to work, states must cooperate and adopt uniform affiliate tax laws.[114] Cooperation of this sort between all fifty states is rare due to a number of factors, including the interests of lobbyists.[115] For instance, the Streamlined Sales and Use Tax Agreement (SSUTA), designed to simplify state sales and use tax collection by remote sellers, still has only twenty-four member states despite being formed in 2000.[116] Fortunately, states have other avenues they can pursue when attempting to prevent use tax avoidance.[117]

D. And Behold a Pale Horse: And His Name That Sat on Him Was Congress

Federal legislation is one way to avoid state coordination problems. In *Quill*, the Court signaled that if Congress so desired, it was "free to decide whether, when, and to what extent the States may burden interstate mail-order concerns with a duty to collect use taxes."[118] In hopeful

109. *Id.*

110. Ramsey, *supra* note 106.

111. Michael J. Bouey, Note, *Avoiding Delegation Doctrine Challenges to Internet Sales Tax Legislation: Lessons Learned from the Main Street Fairness Act*, 10 PITT. TAX REV. 203, 209 (2013); Griffiths, *supra* note 15, at 660.

112. Griffiths, *supra* note 15, at 660.

113. *See, e.g.*, Colorado Governor's Message, Governor Bill Ritter, Jr., Statement on Amazon.com (Mar. 8, 2010) (available on Westlaw) (login and search required).

114. Ricky Hutchens, Note, *Desperate Times Call for Desperate Measures: States Lead Misguided Offensive to Enforce Sales Tax Against Online Retailers*, 68 VAND. L. REV. 575, 598–600 (2015).

115. Jonathan Weisman, *Push to Require Online Sales Tax Divides the G.O.P.*, N.Y. TIMES (Apr. 28, 2013), http://www.nytimes.com/2013/04/29/us/politics/bill-on-sales-tax-for-internet-purchases-divides-republicans.html.

116. Allen, *supra* note 62, at 943.

117. *See infra* Sections II.D–E (illustrating how Congress and the courts have attempted to remedy the problems presented by use tax ordinances).

118. Quill Corp. v. North Dakota, 504 U.S. 298, 318 (1992).

preparation, states such as Colorado passed legislation preparing for federal authorization to collect use taxes from remote sellers.[119] To date, Congress has yet to pass any legislation granting states the power to collect use taxes from remote sellers lacking a substantial nexus to the state; this is not for a lack of trying, though.

On July 29, 2011, the Main Street Fairness Act was introduced to the United States Senate and read twice before it was referred to the Committee on Finance, where it died.[120] The Main Street Fairness Act required states to become a party to the SSUTA[121] and granted the SSUTA Governing Board the authority to define the "small seller exception" and other important terms.[122] If the Main Street Fairness Act had been passed, Congress's broad grant of authority to the SSUTA Governing Board could have led to a "delegation doctrine" challenge.[123]

On April 16, 2013, the Marketplace Fairness Act of 2013 was introduced to the Senate.[124] On May 6, 2013, the Senate passed an amended version of the bill.[125] The roll call shows the bill passed with sixty-nine yeas, twenty-seven nays, and four not voting.[126] After being referred to the House Subcommittee on Regulatory Reform, Commercial, and Antitrust Law on June 14, 2013, the bill languished in legislative purgatory and was never passed in the United States House of Representatives.[127]

The Marketplace Fairness Act of 2013 was drafted carefully to preempt any delegation doctrine challenges.[128] First, it characterized "small seller" as a "remote seller [that] has gross annual receipts in total remote sales in the United States in the preceding calendar year exceeding $1,000,000."[129] Second, it provided minimum requirements that could be followed by states not parties to the SSUTA.[130]

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119. COLO. REV. STAT. ANN. § 39-26-104(2) (West 2013) ("Upon the effective date of an act of congress that authorizes states to require certain retailers to pay, collect, or remit state or local sales taxes . . . .").

120. *Summary: S.1452 — 112th Congress (2011-2012)*, CONGRESS.GOV, https://www.congress.gov/bill/112th-congress/senate-bill/1452 (last visited Nov. 2, 2016) [hereinafter *Summary: S.1452*].

121. Bouey, *supra* note 111, at 218.

122. *Id.* at 219.

123. *Id.*

124. *Summary: S.743 — 113th Congress (2013-2014)*, CONGRESS.GOV, https://www.congress.gov/bill/113th-congress/senate-bill/743 (last visited Nov. 19, 2016) [hereinafter *Summary: S.743*].

125. *Id.*

126. *U.S. Senate Roll Call Votes 113th Congress - 1st Session*, U.S. SENATE, http://www.senate.gov/legislative/LIS/roll_call_lists/roll_call_vote_cfm.cfm?congress=113&session=1&vote=00113#position (last visited Nov. 2, 2016).

127. *Summary: S.743*, *supra* note 124.

128. *See* Bouey, *supra* note 111, at 205.

129. Marketplace Fairness Act of 2013, S.B. 743, 113th Cong. § 2(c) (as referred to the H. Comm. on the Judiciary, May 20, 2013).

130. *Id.* § 2(b).

In another attempt to enact a federal law, the Marketplace Fairness Act of 2015 was introduced in the Senate on March 10, 2015.[131] The fact that the bill is currently in the Senate Committee on Finance does not bode well for its chances of passing because the Senate Committee on Finance's Chairman is Senator Orrin Hatch (R-Utah); Senator Hatch was one of the twenty-seven "nay" votes in 2013.[132] Even if the bill passes the Senate, it would still have to pass the House.[133] The House is a tough obstacle because it is controlled by Republicans, whose constituents largely oppose taxes on Internet sales.[134] Remote sellers will undoubtedly fight it on the lobbying front as well. There has also been criticism at the state level because the bill requires states to provide tax-calculating software and certification procedures to remote sellers free of charge.[135] Between the lack of support from voters, opposition from remote sellers, and concerns about compliance costs, the Marketplace Fairness Act of 2015 does not appear to be a viable solution to use tax avoidance.

E. And the District Court Said, "Collect No More than You Are Authorized to Do"

One state has decided to eschew waiting for a federal law or enacting its own Amazon law, which may not survive a lawsuit. To supplement tax revenues, Colorado instead decided to require all retailers conducting business in the state to collect a use tax if they sold an item for storage, use, or consumption in the state that was not subject to any sales taxes at the time of purchase.[136] In 2010, the state estimated that the revenue lost due to use tax noncompliance would increase by upwards of $20 million each year, with most of this loss attributable to Internet sales by remote sellers.[137] Later that year, Colorado legislators introduced House Bill 10-1193 in an attempt to require remote sellers to collect use taxes; the bill included an affiliate tax provision.[138] That provision did not survive.[139]

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131. *Summary: S.698 — 114th Congress (2015-2016)*, CONGRESS.GOV, https://www.congress.gov/bill/114th-congress/senate-bill/698 (last visited Nov. 19, 2016).

132. *See Membership*, U.S. SENATE COMMITTEE ON FIN., http://www.finance.senate.gov/about/membership/ (last visited Nov. 18, 2016) ("Orrin Hatch is fighting to lower taxes, strengthen Medicare, Medicaid and Social Security, and open markets to American products."); *U.S. Senate Roll Call Votes 113th Congress - 1st Session*, *supra* note 126.

133. *See* Alyssa Brown, *Americans, Especially the Young, Oppose Internet Sales Tax*, GALLUP (June 20, 2013), http://www.gallup.com/poll/163184/americans-especially-young-oppose-internet-sales-tax.aspx.

134. *See id.*

135. James Bull Sterling, *Remote Seller Sales and Use Tax Law: How Proposed Law Will Impact South Carolina*, 65 S.C. L. REV. 827, 849 (2014).

136. COLO. REV. STAT. ANN. § 39-26-204(2) (West 2013).

137. *Direct Mktg. Ass'n III*, 135 S. Ct. 1124, 1128 (2015).

138. Tyler Murray & Eric J. Zinn, *Colorado and the "Amazon Tax"—Recent History*, 41 COLO. LAW. 43, 47 (2012).

139. *Id.*

After protests and threats from large online retailers, the bill was changed to remove the affiliate tax provision and add new notice and reporting requirements.[140] The first notice requirement provided that remote sellers not collecting Colorado sales taxes must send notice to Colorado purchasers that they have a duty to pay use taxes on their purchases; each failure was subject to a $5 penalty.[141] The second notice requirement provided that remote sellers not collecting sales tax must send, via first-class mail, annual notice to Colorado purchasers informing them of all of their purchases and their duty to pay use taxes;[142] each failure was subject to a $10 penalty.[143] The reporting requirement provided that remote sellers not collecting Colorado sales tax must file an annual statement listing the names of each purchaser and their total purchase amount to the Colorado Department of Revenue;[144] each failure was subject to a $10 penalty multiplied by the number of purchasers that should have been reported.[145]

Even with these changes, Amazon, one of the large online retailers that protested the original bill, still ended its relationship with all of its affiliates in Colorado.[146] The Direct Marketing Association, which also opposed the notice and reporting requirements, filed for an injunction in the United States District Court for the District of Colorado, alleging violations of the Commerce Clause and Due Process Clause.[147] The Direct Marketing Association argued that the notice requirements caused out-of-state retailers to incur extra time and expense.[148] The Direct Marketing Association further explained that the reporting requirements would cause out-of-state retailers to lose revenue: consumers would choose to use in-state retailers to avoid the Colorado Department of Revenue knowing what products they were purchasing.[149] The district court granted a limited injunction, proscribing the application of the notice and reporting requirements to retailers who did not pass the physical presence test provided by *Quill*.[150]

III. THE CONSTITUTIONALITY OF REPORTING REQUIREMENTS

In *Direct Marketing Association v. Huber*, the district court held Colorado's notice and reporting requirements unconstitutional under the

140. *Id.* at 48.
141. COLO. REV. STAT. ANN.§ 39-21-112(3.5)(c)(I)–(II).
142. *Id.* § 39-21-112(3.5)(d)(I)(A)–(B).
143. *Id.* § 39-21-112(3.5)(d)(III)(A).
144. *Id.*
145. *Id.* § 39-21-112(3.5)(d)(III)(B).
146. Colorado Governor's Message, *supra* note 113.
147. *Direct Mktg. Ass'n I*, No. 10–cv–01546–REB–CBS, 2012 WL 1079175, at *2 (D. Colo. Mar. 30, 2012), *rev'd*, 814 F.3d 1129 (10th Cir. 2016).
148. First Amended Complaint at 12, *Direct Mktg. Ass'n I* (D. Colo. Mar. 30, 2012) (No. 10–cv–01546–REB–CBS), 2010 WL 6646489.
149. *Id.* at 18.
150. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *11.

Dormant Commerce Clause.[151] The first part of the court's analysis centered on the law's discriminatory effect on interstate commerce.[152] The second part of the court's analysis examined the law's undue burden on interstate commerce.[153] The following analysis is not exactly what the Tenth Circuit adopted in its decision on the merits, but the Author believes it is a good alternative in jurisdictions that refuse to accept the reasoning of the Tenth Circuit.

A. Discrimination Against Interstate Commerce

Discrimination claims are subjected to a two-tier analysis.[154] First, courts must decide "whether the challenged statute regulates evenhandedly with only 'incidental' effects on interstate commerce, or discriminates against interstate commerce either on its face or in practical effect."[155] If a court deems the statute facially or practically discriminatory, the state is allowed an opportunity to justify the statute by showing that it furthers legitimate state interests.[156] The court examines the state's justification under a lens of strict scrutiny.[157] The state must also show that no alternative, non-discriminatory methods were available to achieve its interests.[158]

1. Are Colorado's Reporting Requirements Discriminatory?

In *Huber*, the defendant argued that differential treatment did not necessarily constitute discrimination.[159] The court correctly indicated, however, that this reasoning only applies to cases in which the statute is not facially or practically discriminatory.[160] The court then determined that the statute's notice and reporting language made it invalid.[161] The court reasoned that because under Colorado law all in-state businesses were required to collect and remit state sales tax, the statute only applied to in-state businesses that were violating the law and out-of-state retailers that were exempt from

151. *Id.* at *10.

152. *Id.* at *3.

153. *Id.* at *7.

154. *Id.* at *3.

155. Hughes v. Oklahoma, 441 U.S. 322, 336 (1979).

156. New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 278 (1988) ("Our cases leave open the possibility that a State may validate a statute that discriminates against interstate commerce by showing that it advances a legitimate local purpose . . . .").

157. *Hughes*, 441 U.S. at 336 ("At a minimum such facial discrimination invokes the strictest scrutiny of any purported legitimate local purpose and of the absence of nondiscriminatory alternatives.").

158. *Id.*

159. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *5; *see also* Kleinsmith v. Shurtleff, 571 F.3d 1033, 1041 (10th Cir. 2009) ("Not every benefit or burden will suffice-only one that 'alters the competitive balance between in-state and out-of-state firms.'") (quoting Cherry Hill Vineyard, LLC v. Balddcci, 505 F.3d 28, 36 (1st Cir. 2007)).

160. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *5.

161. *Id.* at *7.

having to collect and remit state sales tax.[162] The court was unwilling to allow Colorado to hide behind its careful wording and held the statute was discriminatory in practice.[163]

2. Are Colorado's Reporting Requirements Justified?

Once a party has demonstrated discrimination, "the burden falls on the State to justify it both in terms of the local benefits flowing from the statute and the unavailability of nondiscriminatory alternatives adequate to preserve the local interests at stake."[164]

In *Huber*, the defendant presented the court with three legitimate interests.[165] The Colorado Department of Revenue argued that the notice and reporting requirements encouraged compliance with tax laws, enhanced its ability to collect use tax revenues, and promoted "the fair distribution of the cost of government."[166] The last of these interests—making remote retailers pay their fair share of the cost of government—has been recognized by many courts as a legitimate interest in Dormant Commerce Clause cases.[167] The court recognized all three interests as legitimate.[168]

The justification analysis does not stop at proof of legitimate interests, though.[169] Reasonable alternatives must be considered.[170] The court focused on three reasonable alternatives proffered by the Direct Marketing Association when deciding whether the notice and reporting requirements were justified.[171] The Direct Marketing Association argued that Colorado could include a use tax line on its state income tax return, increase audits of business consumers, and use government funds to notify residents of their use tax obligations.[172] The court agreed, finding that the Colorado Department of Revenue could advance its interests via nondiscriminatory

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162. *Id.* at *4.

163. *Id.* at *6.

164. Hunt v. Wash. State Apple Advert. Comm'n, 432 U.S. 333, 357 (1977) (citing Dean Milk Co. v. Madison, 340 U.S. 349, 354 (1951)).

165. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *6.

166. *Id.*

167. *See* Interstate Transit, Inc. v. Lindsey, 283 U.S. 183, 185 (1931) (citing Kane v. New Jersey, 242 U.S. 160, 168–69 (1916)) ("[A state] may impose even upon motor vehicles engaged exclusively in interstate commerce a charge, as compensation for the use of the public highways, which is a fair contribution to the cost of constructing and maintaining them and of regulating the traffic thereon."); *see also* Or. Waste Sys., Inc. v. Dep't of Envtl. Quality of Or., 511 U.S. 93, 102–03 (1994) (Souter, J., dissenting) (citing Maryland v. Louisiana, 451 U.S. 725, 758–59 (1981)) ("Under [the compensatory tax] doctrine, a facially discriminatory tax that imposes on interstate commerce the rough equivalent of an identifiable and 'substantially similar' tax on intrastate commerce does not offend the negative Commerce Clause.").

168. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *6.

169. *See id.*

170. *Id.*

171. *Id.*

172. *Id.*

alternatives and therefore could not prove that its discriminatory reporting requirements were justified.[173]

In light of the district court's decision, it is clear that any state considering reporting requirements as a solution to use tax avoidance must be ready to show that there are no reasonable alternatives.[174] Courts require states to make this showing by providing solid evidence, not mere speculation or conjecture.[175] Citing to studies showing that use tax lines on state income tax returns and public awareness campaigns have been ineffective in other states may be sufficient evidence, but courts can be quite strict in Dormant Commerce Clause cases.[176] Instead, states trying to enact discriminatory reporting requirements would likely have to exhaust alternatives and provide statistics proving their ineffectiveness.[177]

B. Undue Burden on Interstate Commerce

Quill was concerned with whether a state could "compel a vendor to collect a sales or use tax" despite the vendor not having a physical presence in the state.[178] Despite the fact that Colorado's notice and reporting requirements do not constitute the collection of taxes, the district court in *Huber* concluded that these requirements were the type of burdens on interstate commerce that *Quill* sought to address and that *Quill* provided a "safe-harbor" to retailers lacking a physical presence in Colorado.[179] The district court's expansion of *Quill*'s safe-harbor to reporting requirements was unwarranted and unwise. This is because the Supreme Court has never indicated that *Quill* was intended to apply to anything other than taxes, and by expanding the scope of *Quill*, the district court eliminated yet another means by which states could remedy use tax avoidance.

The Supreme Court's decision in *Direct Marketing Association v. Brohl*, despite not addressing the undue burden claim decided at the trial level in *Huber*, provided a great explanation of the distinction between a tax collection obligation and a reporting requirement.[180] The case went to the Supreme Court after the Tenth Circuit reversed the district court's decision on the grounds that the TIA prohibited the district court from enjoining the

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173. *See id.*

174. *See id.*

175. Granholm v. Heald, 544 U.S. 460, 492–93 (2005) ("The Court has upheld state regulations that discriminate against interstate commerce only after finding, based on concrete record evidence, that a State's nondiscriminatory alternatives will prove unworkable.").

176. C & A Carbone, Inc. v. Town of Clarkstown, N.Y., 511 U.S. 383, 421–22 (1994) (explaining that discriminatory regulations face "virtually fatal scrutiny" in some cases).

177. *See Direct Mktg. Ass'n I*, 2012 WL 1079175, at *6.

178. Quill Corp. v. North Dakota, 504 U.S. 298, 315 (1992).

179. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *8 ("I conclude that the burdens imposed by the Act and the Regulations are inextricably related in kind and purpose to the burdens condemned in *Quill*.").

180. *See Direct Mktg. Ass'n III*, 135 S. Ct. 1124, 1128–32 (2015).

notice and reporting requirements.[181] The TIA states that "district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law."[182] The Court held that enjoining the reporting requirements would not prevent the levy or collection of Colorado taxes.[183]

The Court relied on the federal tax code in coming to the conclusion that enjoining reporting requirements did not constitute enjoining the collection or levy of taxes, explaining that information gathering is "a phase of tax administration procedure that occurs before assessment, levy, or collection."[184] The Court continued by opining that not every provision of the tax code that assists with the collection of taxes is subject to the TIA.[185] Thus, Colorado's reporting requirements are not themselves an obligation to collect sales or use tax, even though they may assist with the collection of taxes.[186]

The Court's decision logically suggests that *Quill* should not apply to Colorado's reporting requirements. *Quill* provides a safe-harbor from sales and use tax collection duties to remote sellers lacking a substantial nexus to the taxing state.[187] The TIA prohibits district courts from preventing the levy or collection of state taxes.[188] Thus, because Colorado's reporting requirements do not run afoul of the TIA, *Quill* should not apply.

The district court in *Huber* decided to expand the scope of *Quill* to cover information gathering provisions of state tax codes, despite the fact that other courts have chosen to take a narrower approach to interpreting *Quill*.[189] Fortunately, the Tenth Circuit reversed the district court's decision.[190]

C. *Justice Thomas: A Friend of Tax Collectors and the Comity Clause*

In *Brohl*, the Supreme Court hinted that the Tenth Circuit should reverse the district court's decision and dismiss the case pursuant to the "comity doctrine."[191] The comity doctrine cautions federal courts from disrupting state fiscal operations if the claim has not first been adjudicated in state

181. *Id.* at 1129.
182. Tax Injunction Act, 28 U.S.C. § 1341 (2016).
183. *Direct Mktg. Ass'n III*, 135 S. Ct. at 1129.
184. *Id.*
185. *Id.* at 1131.
186. *See id.* at 1129–31.
187. Quill Corp. v. North Dakota, 504 U.S. 298, 312–15 (1992).
188. Tax Injunction Act, 28 U.S.C. § 1341 (2016).
189. *See, e.g.*, Tax Comm'r of W. Va. v. MBNA Am. Bank, N.A., 640 S.E.2d 226, 232 (W. Va. 2006) ("*Quill's* physical-presence requirement for showing a substantial Commerce Clause nexus applies only to use and sales taxes and not to business franchise and corporation net income taxes.").
190. *Direct Mktg. Ass'n IV*, 814 F.3d 1129, 1132 (10th Cir. 2016).
191. *Direct Mktg. Ass'n III*, 135 S. Ct. at 1134 n.7 ("[W]e leave it to the Tenth Circuit to decide on remand whether the comity argument remains available to Colorado.").

court.[192] The comity doctrine can also be applied even if the TIA cannot be applied because the doctrine has a greater scope.[193]

The Court recently wrote, "Comity's constraint has particular force when lower federal courts are asked to pass on the constitutionality of state taxation of commercial activity."[194] Though Colorado's reporting requirements do not impose a duty to collect taxes, they do assist in the collection of tax revenue; accordingly, they are a good candidate for the application of the comity doctrine.[195]

The Tenth Circuit could have thus spared Colorado's reporting requirements a swift death at the hands of the district court and forced the Direct Marketing Association to take its complaints to a state court. However, it chose to reverse the district court's decision and issue a ruling on the merits.[196]

D. The Tenth Circuit's Reasoning

The Tenth Circuit's reasoning in reversing the district court followed a slightly different path than this Author's analysis in Part III.[197] The primary difference is that the Tenth Circuit did not address whether Colorado's reporting requirements were justified and whether alternative methods existed. This is because the Tenth Circuit held that the reporting requirements were not discriminatory—while this Author agreed with the district court's finding that they were discriminatory—merely justified.[198] However, the Tenth Circuit did hold that *Quill* did not apply to Colorado's reporting requirements because *Quill* only applies to the collection of sales and use taxes.[199] So, the part of the Tenth Circuit's analysis discussing *Quill* is the same as this Author's analysis.[200]

The primary difference in the analysis is interesting, though; some may even say it is counterintuitive. The Tenth Circuit disagreed with the district court's reasoning that because in-state retailers had to collect Colorado sales tax, meaning that the reporting requirements only applied to out-of-state retailers, the law was therefore discriminating against interstate commerce.[201]

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192. Levin v. Commerce Energy, Inc., 560 U.S. 413, 417 (2010).

193. *See id.* (noting that "[m]ore embracive than the TIA [is the] the comity doctrine"); *see also* Fair Assessment in Real Estate Ass'n v. McNary, 454 U.S. 100, 110 (1981) ("Thus, the principle of comity which predated the Act was not restricted by its passage.").

194. *Levin*, 560 U.S. at 421.

195. *Direct Mktg. Ass'n III*, 135 S. Ct. at 1131.

196. *Id.* at 1129.

197. *See supra* Part III (noting that a state must exhaust other available options before enacting reporting requirement statutes).

198. *Direct Mktg. Ass'n IV*, 814 F.3d 1129, 1140–44 (10th Cir. 2016).

199. *Id.* at 1138, 1144 (relying on Am. Target Advert., Inc. v. Giani, 199 F.3d 1241, 1255 (10th Cir. 2000)).

200. *See generally id.*

201. *Id.* at 1139–40.

The Tenth Circuit first explained that although the title of the reporting requirements statute is "An Act Concerning the Collection of Sales and Use Taxes on Sales Made by Out–of–State Retailers, . . . the Supreme Court has cautioned that '[t]he title of a statute cannot limit the plain meaning of the text.'"[202] Accordingly, it looked to the text of the statute, which never mentioned "out-of-state retailers," and concluded the law was not facially discriminatory.[203] But then, the Tenth Circuit held that the law was not practically discriminatory either.[204] This is because the "differential treatment must adversely affect interstate commerce to the benefit of intrastate commerce to trigger dormant Commerce Clause concerns."[205] In this case, the Direct Marketing Association failed to show how Colorado's reporting requirements were going to place out-of-state retailers at a *disadvantage* to in-state retailers, who were already forced to collect and remit sales tax, arguably a more onerous task than reporting purchasers' information to the government.[206]

Basically, because the reporting requirements would not apply to in-state retailers who actually followed Colorado sales tax collection laws, they practically discriminate, technically speaking, but because they merely ensure that all businesses are on equal footing and do not provide a benefit to intrastate commerce, they do not discriminate, legally speaking.[207] States within the Tenth Circuit can now enact similar statutes without worrying as much about a Dormant Commerce Clause challenge.[208] However, states in other circuits may need to draft their statutes in a different manner than Colorado did so as to avoid Dormant Commerce Clause challenges.

IV. HOW TO CURB USE TAX AVOIDANCE IN TEXAS

A. Reporting Requirements: The Preferable Solution to Use Tax Avoidance

Texas requires retailers "engaged in business in [the] state" to collect use taxes, even if the sale is made via the Internet.[209] Oftentimes, retailers will just include the use tax as part of the sales price.[210] Texas defines "retailers engaged in business" as retailers that have a physical location, franchisee, substantial ownership interest in a distribution center, items

202. *Id.* at 1141 (quoting Pa. Dep't of Corr. v. Yeskey, 524 U.S. 206, 212 (1998)).
203. *Id*.
204. *Id.* at 1142.
205. *Id.*
206. *See generally id.* at 1129.
207. *See generally id.*
208. *See id.* (holding that a Colorado sales and use tax statute did not violate the Dormant Commerce Clause).
209. TEX. TAX CODE ANN. § 151.103 (West 2016).
210. *Id.*

stored for retail, or representatives located in the state.[211] Texas also includes in this description retailers that engage "in regular or systematic solicitation of sales of taxable items in this state" by advertising via print, radio, television, telephone, or the Internet.[212] However, this "solicitation of sales" subsection appears to run afoul of *Quill*'s physical presence test.[213] Instead of risking litigation over this possibly unconstitutional subsection, Texas should adopt transaction record reporting requirements for remote retailers who lack a physical presence in the state by adding language similar to the language used in Colorado's reporting requirement statute.[214]

Reporting requirements are better than affiliate tax laws for two reasons. First, because affiliate tax laws, like New York's Commission-Agreement Provision, seek to impose use tax obligations on remote sellers lacking a physical presence in the state, the Supreme Court is more likely to hold that they fail *Quill*'s physical presence test.[215] On the other hand, reporting requirements arguably do not even fall within *Quill*'s scope.[216] Second, affiliate nexuses can be destroyed by the remote seller if the remote seller fires all of its in-state affiliates.[217] This means affiliate tax laws only work if every state, or almost every state, chooses to adopt them.[218] There is no way to circumvent reporting requirement provisions, with the exception of limiting sales.[219]

Reporting requirements are also a more realistic option than waiting for the House to pass the Marketplace Fairness Act or similar legislation.[220] The anti-tax sentiment in the United States makes it difficult for federal legislators to pass laws preventing use tax avoidance; that is, it is not difficult to discern that constituents enjoy "tax-free" Internet purchases.[221] Thus, states should show initiative and pass reporting requirements if they want to stop use tax avoidance.

Reporting requirements also avoid one of the most practical concerns with the imposition of sales tax collection duties on remote sellers: the cost

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211. *Id.* § 151.107(a).

212. *Id.* § 151.107(a)(4).

213. *Compare id.* (allowing for a tax to be imposed without a physical presence), *with* Quill Corp. v. North Dakota, 504 U.S. 298, 315 (1992) (holding that retailers must have a physical presence in the state before a tax can be imposed).

214. *See* COLO. REV. STAT. ANN. § 39-21-112(3.5)(a) (West 2013).

215. *See* N.Y. TAX LAW § 1101(b)(8)(vi) (McKinney Supp. 2016).

216. *See Quill*, 504 U.S. at 317. *Quill* merely reaffirmed the Court's use of "a bright-line rule *in the area of sales and use taxes*." *Id.* at 316 (emphasis added). *Quill*'s bright-line rule is limited to sales and use taxes; yet, the district court in *Huber* applied it to reporting requirements. *See Direct Mktg. Ass'n I*, No. 10–cv–01546–REB–CBS, 2012 WL 1079175, at *4 (D. Colo. Mar. 30, 2012).

217. *See* Griffiths, *supra* note 15, at 660.

218. *See id.*

219. COLO. CODE REGS. § 201-1:39-21-112.3.5(1)(A)(iii) (2010) (providing that a retailer is exempt from the reporting requirements if it made less than $100,000 in total gross sales to Colorado purchasers in the prior calendar year and expects the same for the current calendar year).

220. *See supra* Section II.D.

221. *See, e.g.*, Brown, *supra* note 133.

of compliance with the different collection and filing procedures that each state has for its respective sales and use taxes, which vary in rate.[222] The list of tax exempt items also varies between states.[223] These variations in tax rates, administrative procedures, and exemptions were of great concern to the Court when it decided *Bellas Hess*.[224] Reporting requirements place the burden of sorting out what is taxable on the taxing state and the purchaser, instead of the remote retailer.[225] The remote retailer's only duty is to send in a list of every purchase.[226] No sorting is required because the retailer is not actually collecting the taxes.[227]

By imposing reporting requirements on remote sellers that do not currently collect state use taxes, states would be able to avoid a menagerie of issues.[228] Unlike affiliate tax laws, remote retailers cannot shed their reporting requirement duties merely by severing ties with their in-state affiliates.[229] Moreover, courts may be less likely to extend *Quill*'s scope to include reporting requirements because reporting requirements do not impose tax collection duties on remote retailers.[230] States also do not need to wait for Congress's approval before implementing reporting requirements.[231] Finally, reporting requirements shift the burden of deciding which purchases are use tax eligible from the retailer to the taxing state and purchaser.[232]

B. How to Avoid Commerce Clause Challenges

Despite being the preferable solution to use tax avoidance, future reporting requirements need to be drafted in a manner that preempts the legal challenges Colorado's reporting requirements have faced. One way to avoid a claim of discrimination against interstate commerce would be to include a provision in the tax code that requires the state to compensate remote retailers for the cost of compliance with the reporting requirements.[233] A slightly simpler solution may be to implement the alternative methods listed by the

222. Bass, *supra* note 68, at 120.

223. *Id.*

224. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 759 (1967), *overruled in part by* Quill Corp. v. North Dakota, 504 U.S. 298 (1992).

225. *See* COLO. REV. STAT. ANN. § 39-21-112(3.5)(d)(I)–(II) (West 2013) (focusing on the "if known by the retailer" language).

226. *Id.*

227. *Direct Mktg. Ass'n III*, 135 S. Ct. 1124, 1129 (2015).

228. *See supra* Part II.

229. *See supra* Section II.B.

230. *Direct Mktg. Ass'n III*, 135 S. Ct. at 1129.

231. *See supra* Section II.D.

232. *See* COLO. REV. STAT. ANN. § 39-21-112(3.5)(d)(I)–(II) (West 2013) (focusing on the "if known by the retailer" language).

233. *See infra* Section IV.B.1 (discussing the idea that Texas could offer reimbursement to businesses for the costs of complying with use tax statutes).

district court in *Huber*.[234] A final piece of advice to states would be to name the act containing the reporting requirements anything other than "An Act Concerning the Collection of Sales and Use Taxes on Sales Made by Out–of–State Retailers," which is what Colorado did.[235]

1. States Could Offer to Compensate Retailers for the Cost of Compliance

To avoid unduly burdening remote sellers, states could offer to reimburse them for any costs associated with new reporting requirements. In *Barclays Bank PLC v. Franchise Tax Board of California*, the Supreme Court held that reporting requirements that only applied to foreign, multinational businesses did not violate the Dormant Commerce Clause because the requirements had a special "reasonable approximation" option.[236] The Court reasoned that because there was an exception that allowed reasonable approximations if the cost of compliance were too great for a business, the regulations were not unduly burdensome.[237] The Court had previously recognized that "not every exercise of state authority imposing some burden on the free flow of commerce is invalid."[238]

States that choose to implement use tax reporting requirements could preempt Commerce Clause challenges by offering to compensate remote sellers so that the cost of compliance is not prohibitively burdensome.[239] A majority of states already compensate retailers for some of the costs of complying with sales and use tax collection laws.[240] These states reimburse vendors for computer hardware, software, and other expenses.[241] Colorado's reporting requirements also only apply to retailers with more than $100,000 in sales to Colorado purchasers, so small sellers will not be impacted.[242] As for larger retailers, they will likely be more equipped to deal with reporting requirements.[243]

Compensating vendors for compliance costs with reporting requirements is not a novel idea, but it has not been discussed in much

234. *Direct Mktg. Ass'n I*, No. 10–cv–01546–REB–CBS, 2012 WL 1079175, at *6 (D. Colo. Mar. 30, 2012). The nondiscriminatory alternatives enumerated in *Huber* were to include a use tax reporting line on state income tax returns, increase audits of business consumers, and notify consumers of their duty to pay use tax. *Id.*

235. *Direct Mktg. Ass'n IV*, 814 F.3d 1129, 1141 (10th Cir. 2016).

236. Barclays Bank PLC v. Franchise Tax Bd. of Cali., 512 U.S. 298, 314 (1994).

237. *Id.*

238. Hunt v. Wash. State Apple Advert. Comm'n, 432 U.S. 333, 349 (1977).

239. *See* David Gamage & Devin J. Heckman, *A Better Way Forward for State Taxation of E-Commerce*, 92 B.U. L. REV. 483, 509 (2012).

240. *Id.* ("Twenty-eight states compensate vendors to some degree for the costs of complying . . . .").

241. *Id.*

242. COLO. CODE REGS. § 201-1:39-21-112.3.5(1)(A)(iii) (2010).

243. *See* JOEL SLEMROD & VARSHA VENKATESH, THE INCOME TAX COMPLIANCE COST OF LARGE AND MID-SIZE BUSINESSES (2002), http://www.bus.Umich.edu/otpr/ WP2004-4.pdf (using statistics to show that larger businesses are less burdened than small businesses by tax compliance costs, such as record keeping and return preparation.

detail.[244] With states losing billions in use tax revenue, the cost of reimbursing remote retailers would likely be minimal in comparison.[245] It would also help avoid costly litigation of the sort Colorado is currently embroiled in.[246] This is but one option states could choose; there are other options, but each has its own sets of costs and benefits to weigh.[247]

2. Exhaust All Alternatives: Desperate Times Call for Reporting Requirements

In *Huber*, the lack of concrete evidence showing that the plaintiff's proposed alternatives were unreasonable proved fatal to the Department of Revenue's attempt to justify its discriminatory reporting requirements.[248] Therefore, before enacting reporting requirements, states may want to exhaust the alternatives listed in *Huber*.[249] After the alternatives fail, states will have evidence to present if they are taken to court.[250]

States that do not already include a use tax line on their resident income tax forms can include a line.[251] When the inclusion of a line for use tax reporting does not solve the state's revenue loss issues, the state can present its lost revenue estimates as evidence.[252] If a state does not have an income tax, they can mail notices to all of its residents.[253] The cost of mailing the notices may exceed the additional use tax revenue collected.[254] That would surely be sufficient evidence to justify a discriminatory statute.[255] States should also cite to *Quill* and the trial court's decision in *Hamer* if asked why they did not enact an affiliate tax.[256] Moreover, states could explain that

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244. Gamage & Heckman, *supra* note 239, at 527 ("[W]e conclude that all Commerce Clause concerns would be completely alleviated were a state to impose information-reporting requirements while adequately compensating remote vendors for all of the compliance costs they thereby incur.").

245. *See, e.g.*, BRUCE ET AL., *supra* note 3.

246. *See generally Direct Mktg. Ass'n I*, No. 10–cv–01546–REB–CBS, 2012 WL 1079175, at *6 (D. Colo. Mar. 30, 2012).

247. *See supra* Part II.

248. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *6 ("The record contains essentially no evidence to show that the legitimate interests advanced by the defendant cannot be served adequately by reasonable nondiscriminatory alternatives.").

249. *Id.*

250. *Id.*

251. *Id.*

252. *See, e.g.*, Scott W. Gaylord & Andrew J. Haile, *Constitutional Threats in the E-Commerce Jungle: First Amendment and Dormant Commerce Clause Limits on Amazon Laws and Use Tax Reporting Statutes*, 89 N.C. L. REV. 2011, 2025 (2011) (reporting that the inclusion of a use tax line on the North Carolina state income tax form only resulted in an additional $5.1 million in use tax revenue being collected, leaving an estimated $145 million in unpaid use taxes on Internet purchases).

253. *See Direct Mktg. Ass'n I*, 2012 WL 1079175, at *7.

254. *See id.*

255. *See id.* at *6.

256. *See* Quill Corp. v. North Dakota, 504 U.S. 298 (1992); Performance Mktg. Ass'n v. Hamer, No. 2011 CH 26333, 2012 WL 2090791 (Ill. Cir. Ct. May 7, 2012).

affiliate tax laws can be circumvented by remote sellers firing all in-state affiliates.[257]

This option may be the easiest and possibly the most cost efficient method of justifying reporting requirements.[258] States can at least attempt this option before turning to reimbursement.[259] This avenue is better for states such as Texas that do not have an income tax on which it can include a line for use tax reporting.[260]

3. *Add Wording to Preempt Challengers Under* Quill

Even if states preempt a discrimination claim, they may still be subject to an undue burden claim under *Quill*.[261] States have the option of taking the chance that the Supreme Court will decline to extend *Quill* to reporting requirements, like the district court did in *Huber*.[262] States could make the argument that reporting requirements are not tax collection obligations, strictly speaking.[263] This would be consistent with the Court's decision in *Brohl*, which held that the TIA did not apply to reporting requirements.[264] States could also underscore the fact that reporting requirements are not as burdensome as tax collection obligations.[265] As the Tenth Circuit noted in its decision on the merits, the district court in *Huber* should not have extended *Quill* to Colorado's reporting requirements, but until the Supreme Court says otherwise, states should worry about other courts following in the district court's footsteps.[266]

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257. *See* Griffiths, *supra* note 15, at 660.

258. *Compare Stamps*, USPS.COM, https://store.usps.com/store/browse/category.jsp?CategoryId=buy-stamps (noting that the current price of a stamp is $0.47), *with* Joshua D. McCaherty, *The Cost of Tax Compliance*, TAX FOUND.: TAX POL'Y BLOG (Sept. 11, 2014), http://taxfoundation.org/ blog/cost-tax-compliance (estimating the cost of tax compliance for businesses to be $4.4 billion in 2012). *Cf. supra* Section IV.B.I (proposing compensating retailers for the cost of compliance as a method to avoid challenges under *Quill*). The cost of purchasing ink, paper, envelopes, and stamps for a one-time mailing to a few million people (depending on the state) would be in the millions of dollars, not the billions (which is what it would cost to reimburse businesses for annual tax compliance costs).

259. *See supra* Section IV.B.I (discussing the burdens associated with offering to reimburse businesses for the cost of complying with use tax statutes).

260. *Texas*, *supra* note 58.

261. *See supra* Section III.B (discussing use tax reporting requirements' undue burden on interstate commerce).

262. *See Direct Mktg. Ass'n I*, No. 10–cv–01546–REB–CBS, 2012 WL 1079175 (D. Colo. Mar. 30, 2012).

263. *See id.* at *8.

264. *See Direct Mktg. Ass'n III*, 135 S. Ct. 1124, 1129–32 (2015).

265. *See* Nat'l Bellas Hess, Inc. v. Dep't of Revenue, 386 U.S. 753, 759 (1967) (displaying concern over the possibility that retailers will be exposed to the "many variations in rates of tax" between states if states are allowed to tax remote sellers), *overruled in part by* Quill Corp. v. North Dakota, 504 U.S. 298 (1992); *see also supra* Section III.B (discussing the use tax's potential undue burden on interstate commerce).

266. *Direct Mktg. Ass'n I*, 2012 WL 1079175, at *8.

To avoid having their reporting requirements declared unconstitutional, states should include wording in their statutes that indicates a purpose other than the collection of use taxes. In *Huber*, the district court concluded that *Quill* applied because "the sole purpose of the burdens imposed by the [reporting requirements] is the ultimate collection of use taxes."[267] States could phrase their reporting requirements so as to indicate a secondary purpose, which would distance the reporting requirements from *Quill*'s purview.[268] For instance, the Colorado Office of Economic Development and International Trade could use the reported information for big-data studies.[269] *Quill* does not apply to data collection, especially if used for purposes other than just tax collection.[270] Thus, big-data studies may be a means by which states can avoid undue burden challenges.

4. An Example Reporting Requirement Provision for the Texas Tax Code

Researchers have consistently indicated that Texas is one of the states losing the most revenue due to use tax avoidance in the age of e-commerce.[271] Texas is also one of only seven states without a personal income tax, meaning that it cannot include a use tax line on its income tax return.[272] Further, Texas is one of the states that has attempted to enact an affiliate tax law, only to have the whole ordeal end poorly.[273] The bill passed the Texas Senate, but Governor Rick Perry vetoed it.[274] Amazon had already cut ties with all of its in-state affiliates.[275] Thus, Texas is the perfect candidate for reporting requirements because it has very few alternatives to exhaust and could share the data with the Economic Development and Tourism Division of the Governor's Office to avoid challenges under *Quill*.[276] The state could also offer to reimburse retailers that can show a hardship.[277]

An example of a Texas house bill to enact reporting requirements, drafted by this Author, is as follows:

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267. *Id.*

268. *See supra* Part III.

269. *About Us*, COLO. OFF. ECON. DEVELOP. & INT'L TRADE, http://choosecolorado.com/about-us/ (last visited Dec. 29, 2016) (listing economic research as one function of the agency).

270. *See supra* Section III.B.

271. *See, e.g.*, BRUCE ET AL., *supra* note 3 (forecasting Texas sales and use tax revenue losses from e-commerce sales at $870 million for the 2012 calendar year).

272. Stephanie Leonard Yarbrough, *Why South Carolina Should Eliminate the Personal Income Tax*, 66 S.C. L. REV. 667, 670 (2015).

273. *Actions: HB 2403*, TEX. LEGIS. ONLINE, http://www.legis.state.tx.us/BillLookup/Actions.aspx?LegSess=82R&Bill=HB2403 (last visited Nov. 19, 2016).

274. *Id.*

275. Sherry Tehrani, *Welcome to the Amazon: Leading Online Retail from Local Tax Avoidance into Your Backyard*, 67 TAX LAW. 875, 891 (2014).

276. *See supra* Section IV.B.3 (noting that additional wording in a statute can avoid a Commerce Clause challenge).

277. *See supra* Section IV.B.1 (discussing how states could compensate retailors for the cost of their compliance with the use tax reporting requirements).

Texas Tax Code § 111.004 – Power to Examine Records and Persons

(a) For the purpose of carrying out the terms of this title the comptroller may examine at the principal or any other office in the United States of any person, firm, agent, or corporation permitted to do business in this state *or that makes sales to purchasers in this state*, all books, records and papers and also any of their officers or employees under oath.[278]

. . . .

(e) The comptroller, or his or her agent, employee, or representative, has the authority to request the sales records, receipts, and papers of any retailer that does not collect Texas sales tax on sales made to purchasers in Texas.[279]

(f)(1) If a retailer that does not collect Texas sales tax refuses to provide any of the information or materials listed in (e) of this section when requested by the comptroller, or his or her agent, employee, or representative, the comptroller, by subpoena, may require the retailer's presence and production by him or her of any of the information or materials listed in (e).

(2) If the retailer does not respond to the subpoena, the comptroller may ask any judge of any district court of the State of Texas to enforce the subpoena by any means appropriate, including an attachment against the retailer for contempt.[280]

(g)(1) Retailers that do not collect Texas sales tax must file an annual statement for each purchaser making Texas purchases with the Office of the Texas Comptroller on the approved forms found on the office's website. This annual statement should also be provided to the Economic Development and Tourism Division of the Governor's Office. The annual statement shall indicate the total amount paid by each purchaser for Texas purchases during the preceding calendar year. The annual statement must be filed on or before the twentieth day of February of each year.

(2) Failure to file the annual statement will subject the retailer to a penalty of fifteen dollars for each purchaser that should have been included in such annual statement, unless the retailer shows reasonable cause for such failure.[281]

278. TEX. TAX CODE ANN. § 111.004 (West 2016). The italicized portion of the text is the only addition to the current text of Subsection (a).

279. *See* COLO. REV. STAT. ANN. § 39-21-112(1) (West 2013). The Author relied heavily on the Colorado reporting requirement statute when drafting these proposed subsections.

280. *See id.* § 39-21-112(3.5)(a).

281. *See id.* § 39-21-112(3.5)(d)(II)(A), (III)(A).

C. An Interstate Transaction Reporting Database

If the Supreme Court rules that *Quill* extends to reporting requirements, states would have one final option—they could cooperate. The SSUTA has only been able to recruit twenty-four states over the past fifteen years, but this is because tax schemes are more complex and varied than reporting requirements.[282] States could require businesses incorporated or headquartered in the state to provide transaction records for all sales to out-of-state purchasers; this way there would be no nexus issue.[283] The states could then exchange the data and use computer programs to find the purchases subject to each state's use tax. By requiring transaction record reporting as opposed to actual tax collection, states would also allay the fears of the Supreme Court with regards to subjecting retailers to the Sisyphean task of keeping current with every state's tax schemes.[284]

V. CONCLUSION

States are losing hundreds of millions of dollars in tax revenue due to use tax avoidance.[285] Some states that collect income tax have begun including a line for use tax on the income tax form, but that has proven ineffective.[286] Other states have enacted affiliate tax laws, but if challenged in federal court, these laws would likely be held unconstitutional under *Quill*.[287] There is also the practical issue of remote retailers cutting ties with all in-state affiliates.[288] States have also been waiting for Congress to act and authorize the collection of state use taxes from remote retailers.[289] Colorado is the only state to pursue an alternative route, enacting notice and reporting requirements that retailers who do not collect sales and use taxes must follow.[290]

The constitutionality of Colorado's reporting requirements is questionable even with the Tenth Circuit's stamp of approval, but with a few changes, similar reporting requirements could be implemented successfully

282. Allen, *supra* note 62, at 943.

283. *See, e.g.*, D.H. Holmes Co., Ltd. v. McNamara, 486 U.S. 24, 33 (1988).

284. Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill., 386 U.S. 753, 759 (1967) (displaying concern over the possibility that retailers will be exposed to the "many variations in rates of tax" between states if states are allowed to tax remote sellers), *overruled in part by* Quill Corp. v. North Dakota, 504 U.S. 298 (1992).

285. *See, e.g.*, BRUCE ET AL., *supra* note 3, at 8.

286. *See supra* Section II.B (discussing self-reporting solutions to use tax avoidance).

287. *See supra* Section II.C (discussing affiliate tax statutes in other states and their constitutionality).

288. *See* Griffiths, *supra* note 15, at 660.

289. *See supra* Section II.D (explaining how federal legislation can help states collect use tax).

290. *See supra* Section II.E (explaining potential issues that notice and reporting requirements can pose online retailors under the Dormant Commerce Clause).

in states outside of the Tenth Circuit, such as Texas.[291] Texas cannot include a use tax line on its income tax form because it has no income tax, so the only alternative it has is mailing notices to each and every resident.[292] Once this fails to generate an adequate amount of owed use tax revenue, Texas will be able to show that it has no reasonable alternative to the reporting requirements.[293] Texas could also include language to try to avoid a challenge under *Quill*, or it could argue for a very narrow reading of *Quill* and hope its argument prevails in court.[294] At a time when Texas is currently losing revenue, primarily due to oil prices, the Legislature should consider reporting requirements as a means by which to recoup some of the lost revenue.[295]

Use tax reporting requirements appear to be the most constitutional and practicable solution to use tax avoidance. Accordingly, states should enact statutes similar to Colorado's statute but with alterations that preempt Dormant Commerce Clause challenges.

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291. *See supra* Section IV.B (discussing potential Commerce Clause challenges to use tax statutes and how to avoid them).

292. *See supra* Section IV.B.2 (discussing two alternatives to reporting requirements).

293. *See supra* Section IV.B.2 (noting that states must exhaust all reasonable alternatives before enacting a statute that burdens interstate commerce).

294. *See supra* Section IV.B.3 (discussing the additional language that can help a use tax statute survive a Commerce Clause challenge).

295. *See, e.g.*, Krohn & McManmon, *supra* note 14.