

INTERNET SOUNDS DEATH KNEEL FOR USE TAXES: STATES CONTINUE TO SCREAM OVER LOST REVENUES

The number of commercial web sites¹ and Internet² use continues to grow at an alarming rate.³ With growth comes benefits and burdens.

¹ See Susan A. Dunn, *Negotiating Web Site Agreements*, 444 PRAC. L. INST. 467, 469 (1996) (defining web site as "a collection of files stored on a file server that is accessible to users of the World Wide Web, a network of servers and information available on the Internet.").

² See GEORGE S. MACHOVEC, TELECOMMUNICATIONS, NETWORKING AND INTERNET GLOSSARY 56 (1993) (defining Internet as "[t]he collection of networks that connect government, university, and commercial agencies . . . any set of interconnected, logically independent networks"); see also *Compuserve, Inc. v. Patterson*, 89 F.3d 1257, 1260 n.2 (6th Cir. 1996) (defining Internet by first explaining that: "[c]omputer networks are systems of interconnected computers that allow the exchange of information between computers. The Internet is the world's largest computer network, often described as a 'network of networks.'" (citations omitted); *Inset Sys., Inc. v. Instruction Set, Inc.*, 937 F. Supp. 161, 163 (D. Conn. 1996) (defining "[t]he Internet [as] a global communications network linked principally by modems which transmit electronic data over telephone lines"). Additionally, in *Panavision International, L.P. v. Toeppen* the court defined:

The Internet [as] an international computer 'super-network' . . . used by . . . individuals, corporations, organizations, and educational institutions worldwide In recent years, businesses have begun to use the Internet to provide information and products to consumers and other businesses. Every Internet user has a unique address consisting of one or more address components. This address is commonly referred to as the 'domain' or 'domain name.' On the Internet, domain names serve as the primary identifier of the Internet user. Businesses on the Internet commonly use their business names (e.g., IBM) with the designation '.com' (e.g., IBM.com) as their domain names. The designation '.com' identifies the name holder as a commercial entity.

938 F. Supp. 616, 618 (C.D. Cal. 1996) (citation omitted).

Further, the *Inset Systems* court explained that:

[d]omain addresses are similar to street addresses, in that it is through this domain address that Internet users find one another. A domain address consists of three parts: the first part identifies the part of the Internet desired such as world wide web (www), the second part is usually the name of the company or other identifying words, and the third part identifies the type of institution such as government (.gov) or commercial (.com), etc.

937 F. Supp. at 163; see also Richard P. Klau, *Welcome to the Wide, Wide World of Domain Names, Trademarks and the Courts*, STUDENT LAW., Jan. 1997, at 14, 14 (explaining that domains are divided into two main categories: (1) "top-level" and (2) "second-level" domains). As noted by Klau:

Internet 'top'-level domains are subdivided into several categories. The 'top'-level domains designate the type of organization involved. The most

One such burden includes the possible decline of state use⁴ taxes because of the increased Internet usage for out-of-state purchases.⁵

popular 'top'-level domains in the United States are ".com" (commercial), ".edu" (four-year educational institution), ".gov" (U.S. federal government), ".net" (Internet provider) and ".org" (a catch all, typically used for non-profit organizations).

Id.

³ See *Inset Sys.*, 937 F. Supp. at 163 (noting that the peak of Internet operators reaches roughly 30 million); *Panavision*, 938 F. Supp. at 618 (same); Vinton G. Cerf, *Research Pays Off (Federal Research Budget Is Essential)*, 271 SCI. 1343, 1343 (1996) (noting enormous Internet expansion); *Division on the World Wide Web*, 25 N.J. ST. TAX NEWS 3, 4-5 (1996) (noting that within roughly a half-year's time, the tax web site of New Jersey had been viewed beyond 13,000 times and represents future expansion avenues for interchange); Dunn, *supra* note 1, at 469 (explaining that within recent years commercial web sites have increased greatly); Joseph M. Fisher, *Internet Seen as Means of Providing Legal Notice*, NAT'L L. J., July 1, 1996, at C3 (providing that Internet use rate should grow by at least 50% in coming years, with operators approaching 40 million); Klau, *supra* note 2, at 14 (pointing out the explosive growth of domain sites, resulting in various litigation issues); John Newberry, *Out-of-Office Experiences*, A.B.A.J., Sept. 1996, at 54, 57 (explaining that web sites represent the wave of the future: "[i]f you don't have it, it's going to be odd."); Richard Raysman & Peter Brown, *Revolving Jurisdiction and Venue on the Internet*, N.Y. L.J., Sept. 10, 1996, at 3 (noting that recent Internet growth correlates to a similar increase in Internet litigation); M. Mitchell Waldrop, *Culture Shock On The Networks*, 265 SCI. 879, 879 (1994) (same); Richard S. Zembek, Comment, *Jurisdiction and the Internet: Fundamental Fairness in the Networked World of Cyberspace*, 6 ALB. L.J. SCI. & TECH. 339, 344 (1996) (providing rough estimate of on-line operators near a maximum of one hundred million).

⁴ See *infra* notes 6-8 and accompanying text (discussing definition of use tax and its purposes).

⁵ See *Internet Symposium: Legal Potholes Along the Information Superhighway*, 16 LOY. L.A. ENT. L.J. 541, 572 (1996) (explaining the possibility of an eroding tax base because of Internet sales). Speaker R. Scot Grierson explained that use and sales taxes generate significant revenues. See *id.* at 573. Specifically, Grierson noted these types of taxes account for \$200 billion in annual revenues, approximately 35% of state and local government tax dollars. See *id.*

Additionally, the State of Texas provides a definite example of the potential hazards a use tax presents within the Internet context. See John Sharp, *Virtual Taxation: Electronic Commerce Poses Problems for State Tax Collections*, GOV'T FIN. REV., Aug., 1996, at 36, 36 (explaining that Texas' use tax accounts for greater than half the total tax dollars). In 1994, Texas lost \$235 million in use taxes within the mail-order context. See *id.* at 37.

This problem continues as a result of out-of-state Internet purchases. See *id.* at 36, 37 (noting that the explosive Internet growth effectively will render mail-order catalogs obsolete, as the Internet is more cost effective and attractive to customers who buy spontaneously). Further, recently a multitude of companies now advertise their products via the Internet. See *id.* at 36. Tax experts estimate that by the turn of the century, Internet sales may reach \$7 billion. See *id.* Similarly by the year 2000, approximately one million companies are expected to be marketing products via the Internet. See *id.* Sharp explains this skyrocketing growth represents a possible intangible revenue source; this "virtual mall" represents a pseudo "storefront" enabling "users to browse through catalogs." See *id.* at 37; see also Kaye K. Caldwell, *Solving State and Local Use Tax Collection Problems*, 11 STATE TAX NOTES 185, 185 (1996) (discussing that the crux of the use tax problem lies in out-of-state purchases); *Comments on the Effect of Tax Reform*

"Use taxes are imposed on the privilege of ownership of possession, storage, use or consumption of goods in the state . . . [and are] collected on items bought in *another* state but *used* in the taxing state."⁶ The use tax compliments a particular state's sales tax by attempting to ensure taxation of a particular transaction.⁷ The main purpose of this tax is to avoid decreasing tax revenues.⁸ The majority of states impose use taxes in addition to their sales taxes.⁹ The crux of the problem, however, lies with use tax collection, resulting in lost revenues.¹⁰

on *State and Local Governments*, 11 STATE TAX NOTES 253, 254 (1996) (noting that during 1994, use and sales taxes accounted for 33% of "the 50 states combined"); *Commerce on the Net Poses Knotty Tax Issues*, N.Y. L.J., Sept. 5, 1996, at 5 (noting that states want to assure their Internet revenue streams, which may reach a billion dollars in annual revenues).

⁶ ALL STATES TAX GUIDE ¶ 5003, at 5011 (1994) (emphasis added); see also JEROME R. HELLERSTEIN & WALTER HELLERSTEIN, II STATE TAXATION, ¶ 22.06[2][b], at 22-41 to -42 (1992) (defining use tax as "'any tax levied on, with respect to, or measured by, sales, receipts from sales, purchases, storage or use of tangible personal property'") (quoting 4 U.S.C. § 110(b) (1985)); R. Scot Grierson, *Constitutional Limitations on State Taxation: Sales and Use Tax Nexus on the Information Highway*, 10 STATE TAX NOTES 589, 589 (1996) (noting that a use tax supplements a sales tax that otherwise would lack constitutional authority for its imposition); "Tax-Free" Shopping, 25 N.J. ST. TAX NEWS 3, 15 (1996) (examining use tax question regarding whether purchases made in Delaware and brought back to New Jersey were truly "tax free"). Specifically, the article explained:

[W]hile purchases made in Delaware are not subject to any sales tax in Delaware, they are not 'tax free' for New Jersey residents. When goods that are not tax-exempt in New Jersey are brought into this State for use here, the user must pay a 'compensating use tax' to New Jersey. The requirement of paying use tax has been part of the Sales and Use Tax Act since 1966. See N.J. [STAT. ANN. § 54:32B-6 (West 1986 & Supp. 1996)]. The purpose of this requirement is to ensure that out-of-state purchases of goods used mainly in the State are subject to the same tax liability as purchases of the identical items within the State. Residents cannot avoid sales tax simply by crossing State lines. *Coppa v. Taxation Div. Dir.*, 8 N.J. Tax 236, 252 ([N.J.] Tax Ct. 1986).

Id. (emphases added). Additionally, the article pointed out two ways to comply with use tax obligations owed. See *id.* First, a taxpayer can voluntarily pay within a certain number of days upon returning and filing to his or her domiciled state Form ST-18. See *id.* Alternatively, payment may be delayed until the taxpayer files his or her annual state return. See *id.*; see also Appendices A-C (providing New Jersey State tax return, detailing line 40 for "use" tax computation (Appendix A); directions for computation (Appendix B); and form ST-18 (Appendix C)).

⁷ See ALL STATES TAX GUIDE, *supra* note 6, at 5011.

⁸ See *id.* There are four main purposes of a use tax: first, the obvious purpose involves an additional revenue source; second, to eliminate avoidance of sales tax by simply making purchases in a different state; third, to achieve a fair balance between state and federal taxes; and fourth, to alleviate discrimination. See *id.*; see also Grierson, *supra* note 6, at 589 (explaining that an equal playing field is achieved with use taxes, which should discourage out-of-state purchases that attempt to save tax dollars).

⁹ See NATIONAL SURVEY OF STATE LAWS at 398-406 (Richard A. Leiter ed., 1993) (providing that Alaska, Montana, New Hampshire, and Oregon represent the minority of

State and local governments should not burden their respective citizens to ensure collection of use taxes that relate to purchases of tangible personal property through commercial web sites. This would only further complicate state tax returns. Individual taxpayers should not be required to ascertain whether they must pay and calculate a use tax on their out-of-state Internet purchases. Instead, collection at the time of sale better ensures states their much-needed revenues.¹¹ Congressional legislation should determine the specific companies that must comply.¹²

To better illustrate a transaction implicating a use tax, a hypothetical factual scenario¹³ within the Internet must first be assumed. Elite Computers, Inc. manufactures and directly sells computers. It became incorporated in Oregon and opened for business early in January 1996. Elite's manufacturing operations and principal place of business are also located in Oregon, which does not have a use tax. No operations, sales force, or distributions of catalogs are outside of this state. Realizing the cost effectiveness and potential huge market outside of Oregon, Elite established a web site to market and place credit-card orders for its computers. Elite only charged for the cost of the computer, as its policy was not to collect and remit use taxes to applicable states.

At the close of the 1996 fiscal year, Elite's sales exceeded \$2 billion. Two-thirds of this amount, approximately \$1.3 billion, originated from sales from states other than Oregon. Further, New Jersey, which does have a use tax,¹⁴ alone accounted for \$5 million.

Customer X, a New Jersey resident, is an avid computer aficionado. Needing a new laptop, yet desperately wanting to avoid a New Jersey sales tax and not realizing the use tax self-assessment requirements,

states that do not impose a use tax). Further, of the majority of states that do impose use taxes, the tax percentages range between two and seven. *See id.*

¹⁰ See ALL STATES TAX GUIDE, *supra* note 6, at 5011 (noting that questions often arise over collection of use taxes); Caldwell, *supra* note 5, at 185; Betsy Dotson, *Mail-Order Sales: GFOA and Coalition Petition the Federal Trade Commission*, GOV'T FIN. REV., Aug. 1, 1996, at 46, 47 (explaining that most customers are unaware of use tax obligations, e.g., a recent Florida survey demonstrated that upwards of 40% of customers fail to realize tax implications of mail-order sales); *Commerce on the 'Net Poses Knotty Tax Issues*, *supra* note 5, at 5 (explaining the real problem lies in collection of the use tax); Grierson, *supra* note 6, at 589 (illustrating that collection becomes an issue as states must rely on willing taxpayer assent, or require nonresident companies to accumulate and submit the use taxes).

¹¹ See *supra* note 5 and accompanying text (discussing use tax amounts as percentages of total revenues and example of losses that currently have resulted due to use taxes).

¹² See *Commerce on the 'Net Poses Knotty Tax Issues*, *supra* note 5, at 7.

¹³ This assumed factual scenario [hereinafter Hypothetical] is referred to throughout this Comment.

¹⁴ See N.J. STAT. ANN. § 54:32B-6 (West 1986 & Supp. 1996).

Customer X surfs the Internet. Customer X is thrilled at Elite's seemingly rock-bottom price and impulsively gives his credit card number. Within a week the computer is delivered. Customer X is extremely excited and pleased with the tax saving. Unfortunately, two weeks later, Customer X's computer crashes. After Elite refused to fix the computer, Customer X is in tears and consults a lawyer. Customer X files suit in the United States District Court for the District of New Jersey. Moreover, New Jersey's additional efforts to require Elite to collect and remit use taxes to its state failed.¹⁵ As a result, the State of New Jersey has intervened as plaintiffs.

This Comment focuses on the collection of use taxes that relate to the purchase of tangible personal property through commercial web sites over the Internet.¹⁶ Part I presents the constitutional obstacles to be overcome before states may subject nonresident companies to use taxes. Part II discusses administrative feasibility of imposing use taxes and possible federal legislation to alleviate an otherwise Commerce Clause violation. Finally, Part III concludes that congressional action is necessary to limit future litigation. Absent congressional guidelines, states will continually try to expand the concept of physical presence attempting to avoid a Commerce Clause violation and require nonresident companies to collect and remit use taxes.

I. CONSTITUTIONAL OBSTACLES

The United States Supreme Court recently addressed a similar use tax collection problem within the mail-order context in *Quill Corp. v. North Dakota*.¹⁷ The facts of *Quill* involved North Dakota's attempt to require Quill Corp., a nonresident mail-order company that has no offices or personnel in North Dakota, to collect and remit use tax revenues on products acquired for utilization within North Dakota.¹⁸ Although the Court ultimately found a violation of the Commerce Clause,¹⁹ no Due Process Clause²⁰ violation occurred.²¹ *Quill's* constitutional analyses and

¹⁵ The State of New Jersey's attempts were in addition to voluntary taxpayer compliance.

¹⁶ See Hypothetical, *supra* note 13 and accompanying text.

¹⁷ 504 U.S. 298, 301 (1992).

¹⁸ See *id.* (emphasis added); see also *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753, 753-54 (1967) (involving similar facts); *infra* notes 19-32 and accompanying text (discussing the *Quill* Court's reasoning and outcome).

¹⁹ See *infra* notes 45-71 and accompanying text for Commerce Clause analysis.

²⁰ See *infra* notes 25-44 and accompanying text for due process analysis.

²¹ See *Quill*, 504 U.S. at 308, 317-18. Writing for the majority, Justice Stevens first analyzed due process concerns prior to addressing interstate commerce issues. See *id.* at

reasoning similarly applies to use tax collection within the Internet arena. Specifically, the following three issues must be examined: (1) whether an out-of-state company's web site comports with due process;²² (2) does the Commerce Clause still present an insurmountable obstacle to requiring out-of-state companies to collect and remit use taxes;²³ and (3) if an interstate violation is found, may and should Congress waive this violation.²⁴

A. Does a Single Web Site Comport with Due Process?²⁵

The issue of due process²⁶ often arises within the personal jurisdiction context, as it relates to states' attempts to require nonresident companies to collect and remit applicable use taxes.²⁷ The *Quill* Court realized that since 1967 there has been considerable change concerning due process law.²⁸ Resolution of this issue depends on whether a nonresident defendant "[has] certain minimum contacts with [the forum state] such that the maintenance of the suit does not offend 'traditional notions of fair

306, 309. The Justice noted, however, that the Due Process and Commerce Clauses have different purposes. *See id.* at 305. Specifically, Justice Stevens explained that:

The two constitutional requirements differ fundamentally, in several ways . . . [W]hile Congress has plenary power to regulate commerce among the States and thus may authorize state actions that burden interstate commerce, see *International Shoe Co. v. Washington*, 326 U.S. 310, 315 (1945), it does not similarly have the power to authorize violations of the Due Process Clause.

Id.

²² For due process violation analysis see *infra* notes 25-44.

²³ For Commerce Clause analysis see *infra* notes 45-71.

²⁴ For waiver of Commerce Clause violation see *infra* notes 57-71.

²⁵ See Hypothetical, *supra* note 13 and accompanying text.

²⁶ See JOSEPH W. GLANNON, CIVIL PROCEDURE EXAMPLES AND EXPLANATIONS 3-5 (2d ed. 1992). Specifically, Glannon explained:

A state would violate [due process protection] if its courts entered judgments against defendants without following a fair judicial procedure, and fair procedure includes not only such traditional elements as the right to counsel or to cross-examine witnesses, but also *appropriate limits* on the places *where* a defendant can be required to defend a lawsuit.

Id. at 3 (emphases added).

Additionally, Glannon continued his due process explanation by examining the "minimum contacts" analysis. *See id.* at 4 (explaining a court examines the character of the state connections to answer whether jurisdiction is proper).

²⁷ See, e.g., *Compuserve, Inc. v. Patterson*, 89 F.3d 1257, 1262 (6th Cir. 1996). To ascertain whether a defendant has been properly subjected to judicial jurisdiction, a court must find that the following two requirements are satisfied: (1) the particular state's long-arm statute and (2) the constitutional requirement of due process. *See id.* For purposes of this Comment, however, only the due process issue will be explored.

²⁸ See *Quill Corp. v. North Dakota*, 504 U.S. 298, 307 (1992).

play and substantial justice.’”²⁹ Building on the historical standard of *International Shoe*, the *Quill* majority acknowledged that the minimum contacts standard must be evaluated against the backdrop of “reasonableness.”³⁰ Physical presence is no longer a necessity; rather, the inquiry centers around whether a nonresident company deliberately seized financial rewards from the litigation state.³¹ Accordingly, the

²⁹ *International Shoe Co. v. Washington*, 326 U.S. 310, 316 (quoting *Milliken v. Meyer*, 311 U.S. 457, 463 (1940)).

³⁰ See *Quill*, 504 U.S. at 307. Specifically, Justice Stevens wrote:

In [the] spirit [of *International Shoe*], we have abandoned more formalistic tests that have focused on a defendant’s ‘presence’ within a State in favor of a more flexible inquiry into whether a defendant’s contacts with the forum made it *reasonable*, in the context of our federal government, to require it to defend the suit in that State.

Id. (emphasis added); see also *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 299 (1980) (Brennan, J., dissenting) (concluding that the majority read *International Shoe* conservatively); Zembek, *supra* note 3, at 351 (explaining that the *International Shoe* standard permits jurisdictional capacity of the states to be enlarged).

Additionally, Justice Brennan, writing for the Court in *Burger King Corp. v. Rudzewicz*, enumerated factors to determine reasonableness:

‘[T]he burden on the defendant,’ ‘the forum State’s interest in adjudicating the dispute,’ ‘the plaintiff’s interest in obtaining convenient and effective relief,’ ‘the interstate judicial system’s interest in obtaining the most efficient resolution of controversies,’ and the ‘shared interest of the several States in furthering fundamental substantive social policies.’

471 U.S. 462, 476-77 (1985) (quoting *World-Wide Volkswagen*, 444 U.S. at 292).

³¹ See *Quill*, 504 U.S. at 307. Specifically, the Court posited:

Jurisdiction in these circumstances may not be avoided merely because the defendant did not physically enter the forum State. Although territorial presence frequently will enhance a potential defendant’s affiliation with a State and reinforce the reasonable foreseeability of suit there, it is an incapable fact of *modern commercial life* that a substantial amount of business is transacted solely by mail and *wire communications across state lines*, thus obviating the need for physical presence within a State in which business is conducted. So long as a commercial actor’s efforts are ‘purposefully directed’ toward residents of another State, we have consistently rejected the notion that an absence of physical contacts can defeat personal jurisdiction there.

Id. at 307-08 (quoting *Burger King*, 471 U.S. at 476) (emphases added); see also *World-Wide Volkswagen*, 444 U.S. at 297-98 (explaining that due process is not offended in circumstances where the facts demonstrate a company transports goods within an established trading market with anticipation that those very same goods will be bought by patrons of the state in which litigation pursues); Zembek, *supra* note 3, at 352-53 (laying-out a three-part test to ascertain the constitutionality of specific jurisdiction). Compare *Gray v. American Radiator & Standard Sanitary Corp.*, 176 N.E.2d 761, 762, 766 (Ill. 1961) (holding an Ohio valve manufacturer liable for suit in Illinois based on stream of commerce theory) with *Asahi Metal Indus. Co. v. Superior Ct.*, 480 U.S. 102, 106, 112-13 (1987) (O’Connor, J.) (plurality) (reasoning that simply positioning company goods within an established trading market fails to constitute deliberate actions geared at the state in which suit proceeds; accordingly, the facts indicated that a Japanese producer should not be required to defend a suit in California because of the unfairness).

Quill Court reasoned that Quill Corporation definitely focused its marketing efforts at North Dakota citizenry.³²

Courts have recently revisited the issue of due process, deciding the cases upon independent factual inquiries.³³ For example, *Compuserve, Inc. v. Patterson* represents a matter of first impression to the Sixth Circuit.³⁴ In *Compuserve*, defendant Patterson, a resident of Texas, entered into a software agreement with Compuserve, Inc., which is headquartered in Ohio.³⁵ Defendant's sole contacts with Ohio were over the Internet.³⁶ The Sixth Circuit recognized the ability of the Internet to greatly expand a company's potential market far beyond a single state's border.³⁷ Ac-

³² See *Quill*, 504 U.S. at 308. Specifically, the Court recognized the significance of Quill's yearly solicitation for its goods by mailing advertising into North Dakota. See *id.* at 304; see also *supra* note 18 and accompanying text for the factual situation of Quill's mail-order business.

Justice Stevens analysis continued by explaining that Quill Corporation had adequate notice that its business procedures may expose it to suit in a different state. See *Quill*, 504 U.S. at 308 (quoting *Shaffer v. Heitner*, 433 U.S. 186, 218 (1977) (Stevens, J., concurring)). The Court enunciated the North Dakota Supreme Court's reasoning for not requiring physical presence. See *id.* at 301. As highlighted by the Justice Stevens, the North Dakota Supreme Court stated that the enormous legal modernization within the prior twenty-five years has caused the requirement of physical presence to become outmoded. See *id.* In agreement, the Supreme Court concluded its due process analysis by stating that today due process elements are satisfied despite a company's absence in the state taxing forum. See *id.* at 308.

³³ See *Compuserve*, 89 F.3d at 1259-60 (involving the Internet); *Panavision Int'l v. Toeppen*, 938 F. Supp. 616, 618 (C.D. Cal. 1996) (same); *Inset Sys., Inc. v. Instruction Set, Inc.*, 937 F. Supp. 161, 162-63 (D. Conn. 1996) (same); *Bensusan Restaurant Corp. v. King*, 937 F. Supp. 295, 297 (S.D.N.Y. 1996) (same); *Playboy Enter., Inc. v. Chuckleberry Publ'g, Inc.*, 939 F. Supp. 1032, 1033 (S.D.N.Y. 1996) (same); *Highway Auto Sales, Inc. v. Auto-Konig of Scottsdale, Inc.*, 943 F. Supp. 825, 825 (N.D. Ohio 1996) (involving advertisement in national publication); *Pres-Kap, Inc. v. System One, Direct Access, Inc.*, 636 So. 2d 1351, 1351-52 (Fla. Dist. Ct. App. 1994) (involving computer terminals used by travel agent).

³⁴ See *Compuserve*, 89 F.3d at 1262. Writing for the majority, Judge Brown explained:

This case presents a novel question of first impression: Did Compuserve make a *prima facie* showing that contacts with Ohio, which have been *almost entirely electronic in nature*, are sufficient, under the Due Process Clause, to support the district court's exercise of personal jurisdiction over [the defendant]?

Id. (emphases added).

³⁵ See *id.* at 1260.

³⁶ See *id.* Specifically, Compuserve enters into agreements with customers to afford them Internet opportunities. See *id.* Additionally, Compuserve serves as an Internet medium that enables its customers to purchase computer merchandise. See *id.* This suit originated from the contract entered into with Compuserve, where defendant Patterson marketed his software via the Internet. See *id.*

³⁷ See *id.* at 1262. Specifically, the *Compuserve* court stated that:

The Internet represents perhaps the latest and greatest manifestation of these historical, *globe-shrinking* trends. It enables anyone with the right

cordingly, the court decided that the parties' Internet interactions were substantial enough to withstand a due process challenge.³⁸

Similarly, *Inset Systems* involved the Internet, where the United States District Court for the District of Connecticut found that the defendant's actions were enough that due process was not offended by requiring the defendant, a Massachusetts corporation, to litigate in Connecticut's foreign jurisdiction.³⁹ The *Inset Systems* court's conclusion relied upon the defendant's purposeful establishment of a web site to advertise over the Internet, effectively reaching beyond Massachusetts into the Connecticut market.⁴⁰

equipment and knowledge—that is, people like [defendant] Patterson—to operate an *international business cheaply*, and *from a desktop*. That business operator, however, remains entitled to the protection of the Due Process Clause, which mandates that potential defendants be able 'to structure their primary conduct with some minimum assurance as to where the conduct will and will not render them liable to suit.' *World-Wide Volkswagen*, 444 U.S. at 297 []. Thus, this case presents a situation where we must *reconsider the scope* of our jurisdictional reach.

Id. (emphases added). See also Zembek, *supra* note 3, at 343, explaining that the vital asset of the Internet is its capacity to shrink the globe, effectively drawing Internet customers closer together.

Additionally, the Sixth Circuit explained the decreased need for federal due process protection (relating to annoying suits), given the advances in technology and transportation. *Compuserve*, 89 F.3d at 1262. Further, the court emphasized the parties continuous contact. See *id.* at 1265. Judge Brown explained that purposeful availment is determined by contact nature. See *id.* Lastly, the court determined the fairness of subjecting the defendant to the court's jurisdiction. See *id.* at 1267-68 (finding this requirement satisfied because of the material bond between the parties).

³⁸ See *Compuserve*, 89 F.3d at 1263 (concluding that the Due Process Clause failed to be offended; finding defendant Patterson deliberately reached beyond Texas advertising his software by utilizing Compuserve as the major hub).

³⁹ See *Inset Sys., Inc. v. Instruction Set, Inc.*, 937 F. Supp. 161, 162, 165 (D. Conn. 1996). The dispute herein centered around an alleged trademark infringement. See *id.* at 162-63. The plaintiff, Inset, conducted operations primarily within Connecticut; whereas, defendant (ISI) operated the same within Massachusetts. See *id.* Further, ISI supplied computer services worldwide, however, it had no operations or employees within Connecticut. See *id.* ISI seized "INSET.COM" as its Internet domain address, which it utilized for product marketing. See *id.*; see also *supra* note 2 (defining domain and giving examples).

In addressing the due process issue, Judge Covello correctly stated that the answer depends on all the present facts before the court. See *Inset Sys.*, 937 F. Supp. at 165. Specifically, the judge explained that the "due process inquiry rests upon the *totality of the circumstances* rather than any mechanical criteria. . . ." *Id.* (quoting *Combustion Eng'g, Inc. v. NEI Int'l Combustion, Ltd.*, 798 F. Supp. 100, 105 (D. Conn. 1992) (emphasis added)).

⁴⁰ See *Inset Sys.*, 937 F. Supp. at 165. The *Inset Systems* court determined that the reasonableness requirement was satisfied. See *id.* (finding that proficient settlement results by allowing litigation to proceed in Connecticut). Further, the court reasoned:

[ISI] has directed its advertising activities via the Internet . . . toward not only the [S]tate of Connecticut, but to *all* states. The Internet . . . [is] de-

The hypothetical scenario posed earlier,⁴¹ is analogous to *Compuserve*, *Inset Systems*, and *Quill*. At a minimum, a company that establishes a web site in addition to the *Quill* facts cannot win a due process challenge in a foreign state.⁴²

The real issue, however, is whether Elite's single web site and lack of operations and sales force outside of Oregon can subject it to suit in a New Jersey federal court. The *Compuserve* and *Inset Systems* courts' conclusions suggest that given the correct factual situation, a web site may indeed withstand due process scrutiny.⁴³ Despite the fact that Elite's operations are solely within Oregon, the company's marketing efforts were of a nationwide scope. Utilizing a sole web site to market its computers, Elite effectively generated sales that were primarily outside of its resident state of Oregon.

signed to communicate with people and their businesses in every state. Advertisement on the Internet can reach as many as 10,000 Internet users within Connecticut alone. Further, once posted on the Internet, unlike television and radio advertising, the advertisement is available *continuously* to any Internet user. ISI has therefore, purposefully availed itself of the privilege of doing business within Connecticut.

Id. (emphases added). Cf. *Panavision Int'l, L.P. v. Toeppen*, 938 F. Supp. 616, 618, 621-22 (C.D. Cal. 1996) (denying defendant's motion to quash, explaining that within this tort context, a defendant that deliberately directs activity toward the forum state is liable, because the sole purpose for establishing the web site was to hinder people from Internet transactions unless states received prior remuneration); *Highway Auto Sales, Inc. v. Auto-Konig of Scottsdale, Inc.*, 943 F. Supp. 825, 825, 830 (N.D. Ohio 1996) (granting defendant's motion to transfer for a contract dispute, reasoning that absent greater contact than a sole defendant's advertisement within a national magazine, due process is not satisfied); *Playboy Enter., Inc. v. Chuckleberry Publ'g, Inc.*, 939 F. Supp. 1032, 1033-34, 1036 (S.D.N.Y. 1996) (granting plaintiff's motion for contempt, finding that a prior, permanent injunction to not market defendant's magazine within the United States was violated by later marketing the product over the Internet). But see *Bensusan Restaurant Corp. v. King*, 937 F. Supp. 295, 297, 301 (S.D.N.Y. 1996) (dismissing plaintiff's complaint, reasoning that the record was void of allegations that the defendant attempted to solicit customers outside the state in which they were located); *Pres-Kap, Inc. v. System One, Direct Access, Inc.*, 636 So. 2d 1351, 1351, 1353 (Fla. Dist. Ct. App. 1994) (reversing the district court's decision, finding that the facts failed to demonstrate the reasonableness of requiring the defendant to litigate a lease dispute in Florida, when establishment and service was solely within New York).

⁴¹ See Hypothetical, *supra* note 13 and accompanying text.

⁴² See *supra* notes 17-32 and accompanying text discussing *Quill*. Specifically, the *Quill* Court ruled that a company conducting a mail-order business, purposely mailing numerous catalogs into a nonresident state, comports with due process. See *Quill Corp. v. North Dakota*, 504 U.S. 298, 306-08 (1992). Accordingly, a company having both a mail-order business similar to *Quill Corporation's* and a web site will sustain a due process challenge.

⁴³ See *Compuserve, Inc. v. Patterson*, 89 F.3d 1257, 1260, 1268-69 (6th Cir. 1996) (reversing a district court's dismissal for lack of personal jurisdiction because Internet contacts were sufficient to withstand a due process challenge); *Inset Sys.*, 937 F. Supp. at 165 (finding due process satisfied because defendant's Internet actions were purposefully focused toward another nonresident state).

Specifically, greater than two-thirds of its first-year sales, approximately \$1.3 billion, came from residents beyond Oregon's borders. New Jersey alone accounted for \$5 million. Realizing the Internet's cost efficiency and global reach, Elite purposely established its web site to reach beyond Oregon and it reaped the resulting financial benefits. It was Elite's initial decision that enabled the transaction to occur in the first place because it offered the goods.⁴⁴ The significant quality and continuous nature of the above contacts, in light of today's technologically advanced society, lead to the conclusion that subjecting Elite to jurisdiction in New Jersey is reasonable. Accordingly, the outer-limits of our Constitution's Due Process Clause are flexible enough to encircle Elite's actions, allowing suit to proceed within New Jersey.

*B. Does the Commerce Clause Present an Insurmountable Obstacle to Requiring Out-of-State Companies to Collect and Remit Use Taxes?*⁴⁵

In analyzing the Commerce Clause,⁴⁶ the *Quill* majority relied on the importance of maintaining an unambiguous use tax law and stare decisis.⁴⁷ Writing for the Court, Justice Stevens began the Commerce Clause analysis by quoting the Constitution for the origin of its powers.⁴⁸

⁴⁴ But see Richard K. Herrmann, *Crossing the Virtual Line on the Internet*, Spring 1996, at 8 (finding that the recipient initiates the link of Internet connections). The significant fact remains, however, that without the web site to present the offer, there would be no opportunity for a recipient to accept. See *id.*

⁴⁵ See Hypothetical, *supra* note 13 and accompanying text.

⁴⁶ See generally STEVEN L. EMANUEL, *EMANUEL LAW OUTLINES: CONSTITUTIONAL LAW* 27-28 (13th ed. 1995) (explaining the United States Constitution's Commerce Clause and how it involves regulations between the various states).

⁴⁷ See *Quill*, 504 U.S. at 317; see also BLACK'S LAW DICTIONARY 1406 (6th ed. 1990) (defining stare decisis as the "[p]olicy of courts to stand by precedent and not disturb settled point"). But despite the fact that *Quill*'s majority decided to use stare decisis as an additional reason for its decision, subsequent cases and commentators indicate the point is anything but settled.

⁴⁸ See *Quill*, 504 U.S. at 309. Specifically, the Court began by stating: Article I, § 8, cl. 3, of the Constitution expressly authorizes Congress to 'regulate Commerce with foreign Nations, and among the several States.' [The Constitution] says nothing about the protection of interstate commerce in the absence of any action by Congress. Nevertheless, as Justice Johnson suggested in his concurring opinion in *Gibbons v. Ogden*, 9 Wheat. 1, 231-[]32, [](1824), the Commerce Clause is more than an affirmative grant of power; it has a *negative sweep* as well. The Clause, in Justice Stone's phrasing, 'by its own force' prohibits certain state actions [e.g., attempting to require out-of-state companies to collect and remit applicable use taxes] that interfere with interstate commerce.

Id. (citation omitted) (emphasis added). See also *Western & Southern Life Ins. Co. v. State Bd.*, 451 U.S. 648, 652 (1981), explaining that despite the lack of federal legislation, challenged state actions may still violate the Commerce Clause. Additionally, the

To determine the constitutionality of state taxing schemes, Justice Stevens reaffirmed the four-part test of *Complete Auto Transit, Inc. v. Brady*.⁴⁹

The Court then reiterated the vital distinction between the purposes of the Commerce and Due Process Clauses⁵⁰ and concluded by finding a "corporation may have 'minimum contacts' with a taxing State as required by the Due Process Clause, and yet lack the 'substantial nexus' with that State as required by the Commerce Clause."⁵² The Court then conceded that despite more adaptable guidelines regarding the Commerce Clause, there had been no suggestion to not adhere to indisputable rules.⁵³ The majority concluded that a substantial nexus was absent be-

Quill Court acknowledged fewer restrictions on state taxing powers due to substantial development of the dormant Commerce Clause. See *Quill*, 504 U.S. at 309 (citing P. HARTMAN, FEDERAL LIMITATIONS ON STATE AND LOCAL TAXATION §§ 2:9-2:17 (1981)). See generally EMANUEL, *supra* note 46, at 69, 93-95 (explaining dormant Commerce Clause issues and related state tax questions); GEOFFREY R. STONE ET AL., CONSTITUTIONAL LAW 312-15 (2d ed. 1991) (discussing taxation issues relating to interstate commerce).

⁴⁹ See *Quill*, 504 U.S. at 310-11 (citing *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977)). A state tax meets constitutional muster provided the tax:

'[1] is applied to an activity with *substantial nexus* with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State.'

Id. (citation omitted) (emphasis added); see also BLACK'S LAW DICTIONARY 1044 (6th ed. 1990) (defining nexus as "[a] multistate corporation's taxable income can be apportioned to a specific state *only if* the entity has established a sufficient *presence*, or *nexus*, with that state") (emphases added).

Further, the majority noted that concern centered on the first part of *Complete Auto*'s test, which dealt with substantial nexus. See *Quill*, 504 U.S. at 311. Accordingly, *Quill*'s Commerce Clause analysis also focused on the substantial nexus prong. See *id.* at 313. Because this threshold element was not satisfied, the Court's Commerce Clause analysis ended there. See *id.*; see also Grierson, *supra* note 6, at 597 (concluding that "[n]exus is always the *first* line of inquiry") (emphasis added).

⁵⁰ See *Quill*, 504 U.S. at 312. The Due Process Clause protects the individual more against a particular state, whereas the Commerce Clause focuses on financial effects on the United States as a whole, resulting from various state taxation laws. See *id.* But see *id.* at 327 (White, J., concurring in part and dissenting in part) (finding that the four-part test of *Complete Auto* remains rooted with due process reasoning; accordingly, a distinct concept of nexus lacks justification).

⁵¹ See *supra* note 49 (defining nexus).

⁵² *Quill*, 504 U.S. at 313. The Court further explained that despite the Court's prior comments [] suggest[ing] that every tax that passes contemporary Commerce Clause analysis is also valid under the Due Process Clause, it does *not* follow that the converse is as well true: A tax may be consistent with [d]ue [p]rocess and yet unduly burden interstate commerce. See, e.g., *Tyler Pipe [Indus.], Inc. v. Washington State [Dep't] of Revenue*, 483 U.S. 232 (1987).

Id. at 313-14 n.7 (emphasis added).

⁵³ See *id.* at 314. Justice Stevens explained that any such burdens are outweighed by an unambiguous law and the doctrine of *stare decisis* should be followed. See *id.* at 315-17. Further, the Justice noted that a clear rule enables states to realize the outer limits

cause of Quill Corporation's lack of "physical presence" in North Dakota. This, the Court asserted, prohibited the State of North Dakota from imposing a duty on Quill to collect and remit taxes.⁵⁴

Applying the majority's "bright-line" rule to the hypothetical facts presented⁵⁵ also leads to a Commerce Clause violation because a "nexus"⁵⁶ is lacking. New Jersey's attempt to require Elite to collect and remit applicable use taxes to its state, without a "physical presence" within New Jersey's borders, remains fatal. The only possible presence Elite has in New Jersey is its reach of its web site via the Internet. But this fact, given the language of *Quill*'s majority, fails to rise to a level of "physical presence" therein. Accordingly, New Jersey's collection attempts fail to withstand Commerce Clause scrutiny.

that dictate the extent a particular state may reach to tax. See *id.* at 315-16; see also William D. Townsend & Cheridah Renuart, 'Experimental' Was the Word for Tax Picture in 1995--and Is in 1996, 10 STATE TAX NOTES 148, 148-49 (1996) (noting that in Florida, a mail-order company's attendance during daily meetings held over various years failed to establish a substantial nexus). But see *Quill*, 504 U.S. at 329, 331 (White, J., concurring in part and dissenting in part) (proclaiming disagreement with the majority's continued adherence to a bright-line rule because unfairness outweighed the convenience; further, the instability in this area suggests stare decisis is inapplicable); *Orvis Co. v. Tax Appeals Tribunal*, 654 N.E.2d 954, 955, 958 (N.Y. 1995) (holding that the presence of a mail-order vendor was enough to require a collection/remittance duty; specifying physical nexus only required something greater than least presence); Grierson, *supra* note 6, at 597 (concluding that resolution of the constitutionality of a state's ability to mandate non-resident sellers to collect and remit use taxes begins with examining nexus; the nexus controversy, however, remains anything but over); Harriet Hanlon, *COST Sales Tax Conferees Discuss 'Nexus Aplenty'*, 11 STATE TAX NOTES 559, 561 (1996) (explaining that despite *Quill*'s requirement of a minimum "physical presence" to meet nexus requirements, there will be states that continually attempt to locate an attributional nexus); Harriet Hanlon, *MTC Examines Making (Tax) Money On the Internet*, 9 STATE TAX NOTES 408, 409 (1995) (explaining that the Internet makes prevailing nexus guidelines outdated) [hereinafter *MTC Examines*]; but see BLACK'S LAW DICTIONARY 130 (6th ed. 1990). *Black's Law Dictionary* defines attribution as follows:

Under certain circumstances, the tax law applies attribution rules to assign to one taxpayer the ownership interest of another taxpayer. If, for example, the stock of X Corporation is held 60% by M and 40% by S, M may be deemed to own 100% of X Corporation if M and S are mother and son. In such a case, the stock owned by S is attributed to M. Stated differently, M has a 60% 'direct' and a 40% 'indirect' interest in X Corporation. It can also be said that M is the 'constructive' owner of S's interest.

Id.

⁵⁴ See *Quill*, 504 U.S. at 317-18.

⁵⁵ See Hypothetical, *supra* note 13 and accompanying text.

⁵⁶ See *supra* note 49 and accompanying text (defining nexus).

C. *May and Should Congress Waive this Commerce Clause Violation?*⁵⁷

"Congress has plenary power . . . [to] *authorize* state actions that *burden* interstate commerce."⁵⁸ This rule grants Congress the power to decide whether it serves sufficient national interests to require that particular companies collect and remit use taxes to the applicable states.⁵⁹ The more significant and debatable issue is whether Congress should indeed waive a Commerce Clause violation in the context of the hypothetical facts proposed.⁶⁰

Despite the various opinions advanced in *Quill*, the Justices agree that the ultimate resolution may be determined by congressional legislation.⁶¹ In dictum,⁶² the *Quill* majority explained that their Commerce Clause conclusion was less difficult due to the underlying fact that Congress may disagree and alter the outcome of the case.⁶³ The *Quill* major-

⁵⁷ See Hypothetical, *supra* note 13 and accompanying text.

⁵⁸ *Quill*, 504 U.S. at 305 (quoting *International Shoe Co. v. Washington*, 326 U.S. 310, 315 (1945)) (pronouncing it is no longer questionable that Congress may permit state actions that would otherwise violate the Commerce Clause) (emphasis added); see *Western & S. Life Ins. Co. v. State Bd.*, 451 U.S. 648, 652-53 (1980) (noting that congressional authority exists to authorize what would otherwise constitute state violations of interstate commerce, which insulates particular state actions from potential Commerce Clause attack); *Heart of Atlanta Motel, Inc. v. United States*, 379 U.S. 241, 258 (1964) (explaining that congressional authority exists to govern local occurrences adversely affecting interstate commerce).

⁵⁹ See Hypothetical, *supra* note 13 and accompanying text. Accordingly, Congress may decide that Elite Computers (and others similarly situated) is required to collect and remit use taxes to the State of New Jersey.

⁶⁰ See Hypothetical, *supra* note 13 and accompanying text; see also *infra* notes 61-71 and accompanying text (discussing violation of Commerce Clause given hypothetical facts).

⁶¹ See *Quill*, 504 U.S. at 318-19; *id.* at 320 (Scalia, J., concurring) (resting Justice Scalia's decision on stare decisis grounds, yet realizing that the ultimate Commerce Clause decision remains in Congress's hands); see *id.* at 331 (White, J., concurring in part and dissenting in part) (acknowledging that Congress may indeed overturn the majority's decision).

⁶² See BLACK'S LAW DICTIONARY 454 (6th ed. 1990). *Black's Law Dictionary* defines dictum as the following:

A statement, remark, or observation . . . an observation or remark made by a judge in pronouncing an opinion upon a cause, concerning some rule, principle, or application of law, or the solution of a question suggested by the case at bar, but not necessarily involved in the case or essential to its determination.

Id.

⁶³ See *Quill*, 504 U.S. at 318 (dictum). Realizing that Congress has the final say, Justice Stevens admitted that the legislative branch is likely more capable of settling this issue. See *id.* Because of the numerous states that assess use taxes, the Justice explained that a different opinion than that reached today "might raise thorny questions concerning the retroactive application of [use] taxes and might trigger substantial unanticipated liabil-

ity explained that the most intelligent decision may involve legislative rather than judicial action.⁶⁴

Therefore, our hypothetical⁶⁵ Commerce Clause violation⁶⁶ may be overridden by congressional legislation. Additionally, the *Quill* Court's dictum⁶⁷ rings louder in Congress's ears given the wide ranging use and issues presented by the Internet⁶⁸ and web sites.⁶⁹ Accordingly, congressional action limits unneeded future litigation⁷⁰ and provides states their much-needed use tax revenues.⁷¹

II. FEDERAL LEGISLATION⁷²

A. Administrative Feasibility

Having established that Congress may authorize a state Commerce Clause violation, potential administrative obstacles in assessing use taxes

ity;" *id.* n.10, again conceding that the legislative branch may be the wiser avenue to pursue in determining this debate. *See id.* Additionally, the majority pointed out that its due process decision no longer presented an obstacle to federal legislation. *See id.* at 318.

⁶⁴ *See id.* at 318-19 (quoting *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 638 (1981)) (White, J., concurring); *see also Commerce on the 'Net Poses Knotty Tax Issues*, *supra* note 5, at 7 (concluding that the most logical solution entails some type of congressional action); Hanlon, *MTC Examines*, *supra* note 53, at 409 (explaining that today's computer age has made nexus concepts outdated).

⁶⁵ *See Hypothetical*, *supra* note 13 and accompanying text.

⁶⁶ For Commerce Clause analysis and conclusion, *see supra* notes 45-65, *infra* notes 67-71, and accompanying text.

⁶⁷ *See Quill*, 504 U.S. at 318-19.

⁶⁸ For a definition of Internet, *see supra* note 2.

⁶⁹ *See supra* notes 3-5 and accompanying text (discussing increased Internet use and related issues); *see also supra* note 1 (defining web site).

⁷⁰ *See Grierson*, *supra* note 6, at 589-90. Grierson stressed:

Information service providers should be forewarned that *states* will aggressively pursue alternative arguments in order to acquire nexus over out-of-state sellers, despite the apparent 'safe harbor' provided under the physical presence standard. States will argue that, given changes in technology and the imminent social and economic changes produced by the information highway, it simply is unrealistic to apply the physical presence rule to information highway transactions.

Id. at 590 (emphases added); *see also Caldwell*, *supra* note 5, at 185 (explaining that states plan to introduce modern, experimental nexus theories in an attempt to establish a nexus for nonresident companies).

Further, Grierson explained that a mail-order business (similar to what *Quill Corp.* was engaged in) and today's computer-supported businesses differ dramatically. *See Grierson*, *supra* note 6, at 593 (noting that unlike a mail-order company's limited connections with the litigation state, computer companies have uninterrupted state occupancy by utilization of the Internet's network communications base).

⁷¹ *See supra* note 5 and accompanying text (explaining and illustrating the significance of use tax revenues to the states that impose them).

⁷² *See Hypothetical*, *supra* note 13 and accompanying text.

must be considered prior to requiring companies to collect and remit out-of-state use taxes due. The Supreme Court in *Quill* clearly expressed that in the future Congress should reassess⁷³ possible legislation to aid the courts in this complicated and ever-changing area.⁷⁴ Although the *Quill* Court's holding did not rest on administrative feasibility of requiring out-of-state mail-order vendors to remit use taxes, the Court briefly touched on this issue when explaining the procedural history.⁷⁵ Had no Commerce Clause violation been found, given the language used and context, the Court probably would agree that the administrative burden is not too great.⁷⁶

Any alleged administrative burden, however, at the time the Supreme Court rendered *Quill*, is lessened today and will further decrease as technology advances.⁷⁷ Newly developed software will greatly ease

⁷³ See *Quill*, 504 U.S. at 318. Writing for the majority, Justice Stevens noted that Congress considered past legislation to aid the mail-order dilemma. See *id.* n.11 (citing H.R. 2230, 101st Cong. § 2 (1989); S. 480, 101st Cong. § 2 (1989); S. 2368, 100th Cong. § 3 (1988); H.R. 3521, 100th Cong. § 2 (1987); S. 1099, 100th Cong. § 2 (1987); H.R. 3549, 99th Cong. (1985)). Additionally, the Justice explained that past congressional hesitance in enacting legislation likely was the result of deference to the judiciary branch because of prior due process rulings. See *id.* at 318. But the *Quill* Court's due process result openly invites and suggests congressional action. See *id.* at 318-19.

⁷⁴ See *id.*

⁷⁵ See *id.* at 303. Specifically, the North Dakota Supreme Court explained that technological advances with computers have decreased administrative burdens. See *id.* Compare Brief for Respondent at *12, *Quill Corp. v. North Dakota*, 1991 WL 538776 (U.S. 1992) (explaining that computer technology would enable *Quill Corp.* to easily comply with remittance of applicable use taxes) with Brief for Petitioner at *8-9, *Quill Corp. v. North Dakota*, 1991 WL 538773 (U.S. 1992) (noting the unlikelihood of state and local governments to coordinate efforts to rid potential burdens, and arguing that state use taxes would create disorder if nationally adopted).

⁷⁶ See *Quill*, 504 U.S. at 301 (noting that the North Dakota Supreme Court's reasons were guided by "the tremendous social, economic, commercial, and legal innovations") (citation omitted).

⁷⁷ See Grierson, *supra* note 6, at 597 (pointing out that companies currently can trace Internet transactions by utilizing modern software); see also Amy Hamilton, *Online Demonstration of Netscape's Tax Tracking Software Coming Soon*, 9 STATE TAX NOTES 1613, 1613 (1995) (explaining that Netscape Communications Corp. and AVP Systems plan to market use tax software in Internet based companies in the near future); Adrienne Redd, *State Expands Use of Electronic Tax Filing Again*, 7 E. PA. BUS. J., Sept. 16, 1996, available in 1996 WL 8862642, at *1 (explaining that the Pennsylvania Department of Revenue created the use tax software, which will be sent to companies at no cost). But see Caldwell, *supra* note 5, at 186. Caldwell listed five potential hazards that currently are confronting states that wish to impose a collection duty on nonresident sellers:

1. Businesses will not collect taxes, unless forced to do so, if the burden of collection is too great.
2. Buyers won't pay use taxes if they are not asked to.
3. Businesses won't collect use taxes if they believe it makes their businesses less competitive.

the alleged burdens of complying with the multitude of differing state and local use tax rates.⁷⁸ Accordingly, the current administrative feasibility fails to pose an insurmountable obstacle to future congressional action.

4. Congress has no intention of requiring businesses without nexus to collect use taxes. The last time this issue came to vote in the Senate (in 1995) it was voted down by a 2-1 margin.

5. The Supreme Court is unlikely to reverse the Commerce Clause ruling in *Quill*.

Id.

Given the enormous growth and potential reach of the Internet, Congress should reconsider the fourth problem noted above. See also *supra* note 73 and accompanying text (discussing examples of prior congressional proposals within the mail-order context).

As noted above, the *Quill* majority agrees that Congress is free and wise to reconsider this issue. See *supra* notes 63-64 and accompanying text. Caldwell's proposed solution does not try to create new nexus arguments, judiciary or congressional aid. See Caldwell, *supra* note 5, at 186. Rather, Caldwell suggests that state revenue departments should collect from the individual purchasers. See *id.*

Caldwell's proposal has two required parts:

1. State collection of use tax from buyers.
2. Cooperative agreements among the states to implement voluntary vendor use tax collection programs. New York, New Jersey, and Connecticut already have similar programs in place.

Id.

Further, Caldwell explained the effects of such a proposal as follows:

1. Due to education on use tax payment responsibilities and implementation of easy methods of payment, buyers will no longer believe that purchasing from a vendor who is not required to collect use tax is a good bargain. Therefore lack of taxes will no longer serve as a selling point in mail or Internet/on-line purchases of tangible personal property. When the purchasers realize that they have to pay the tax anyway they will no longer seek out 'tax-free' vendors.
2. More vendors will collect use taxes due to the ease of collecting and remitting the tax, as a customer service, and because of lessened possible liability for taxes due to participation in the voluntary collection program.

Id.

⁷⁸ See Hamilton, *supra* note 77, at 1613 and accompanying text (discussing that newly developed use tax computer programs allow Internet sellers to account for use taxes throughout the nation); see also Sharp, *supra* note 5, at 38 (suggesting that a unified, sole statewide use tax rate might be possible congressional legislation).

Specifically, Hamilton's discussions with the chief executive officer of AVP Systems, Daniel L. Sullivan, revealed:

[T]he [tax] software database [is] 'mind-boggling in its complexity,' can track sales and use tax rates in more than 65,000 combinations of tax jurisdictions and determine whether a product is in fact taxable in each of them. The tax master file includes all sales, use, and transit tax rates carried out to five decimal places for every jurisdiction in the United States and for Canada's goods and services tax and provincial sales taxes. The company's tax lawyers and researchers constantly monitor and update the 65,000 tax jurisdiction combinations; information on changes in tax laws comes directly from the taxing authorities themselves. The system is able to track and calculate the taxes largely through ZIP Code information re-

B. Legislative Proposals

Having determined the minimal administrative burden with imposing use taxes on nonresident companies, possible legislative proposals should be addressed. Despite some disagreement that congressional legislation represents the best answer to lost use taxes within the Internet scheme, commentators agree that Congress represents a possible solution to this ongoing dilemma.⁷⁹ As noted by the *Quill* Court, Congress previously considered legislation within the mail-order context.⁸⁰

The various bills proposed by the Senate and House of Representatives suggested three vital jurisdictional elements: that (1) the sale occur within the taxing state; (2) such sales be purposeful and continuous; and (3) a threshold annual sales amount within a particular state or in relation to the country as a whole is met.⁸¹ Although these proposals have not been enacted, they represent future potential within the Internet context. Senate Proposal 480, one example⁸² of suggested legislation within the mail-order context, sought to legalize state taxation relating to purchases of tangible goods by out-of-state dwellers.⁸³ Additionally, Congress might utilize a "carrot-stick" approach.⁸⁴ With or without congressional

quired of a customer before an electronic commerce transaction can take place.

Hamilton, *supra* note 77, at 1613 (emphases added). Further, Sullivan anticipated that most companies that sell via the Internet will implement such software to counter customers who solely make Internet purchases in the hopes of avoiding any use taxes. *See id.*

⁷⁹ *See* Caldwell, *supra* note 5, at 186-87 (conceding that congressional action is certainly one answer).

⁸⁰ *See Quill Corp. v. North Dakota*, 504 U.S. 298, 318 n.11 (1992) (citing H.R. 2230, 101st Cong. § 2 (1989); S. 480, 101st Cong. § 2 (1989); S. 2368, 100th Cong. § 3 (1988); H.R. 3521, 100th Cong. § 2 (1987); S. 1099, 100th Cong. § 2 (1987); H.R. 3549, 99th Cong. (1985)); *see also Interstate Sales Tax Collection Act of 1987 and the Equity in Interstate Competition Act of 1987, Hearings on H.R. 1242, 1891, and 3521 Before the Subcomm. on Monopolies and Commercial Law, 100th Cong. 25-26 (1988)* [hereinafter *Interstate Sales*] (statement of Hon. George Sinner, Governor, North Dakota) (testifying that the proposed legislation would bring local and foreign businesses on an equal playing field and maintain a credible and fair tax policy). *But see Interstate Sales, supra*, at 67 (statement of George W. Park, President, Seed Co., Inc.) (explaining that his mail-order business would adversely suffer because he needed a multitude of sales to earn a reasonable return, indicating that further costs will hurt profits).

⁸¹ *See* S. 480; H.R. 2230; S. 2368.

⁸² *See supra* note 81 and accompanying text (explaining the similarity of past Senate and House of Representatives proposals).

⁸³ *See* S. 480.

⁸⁴ *See, e.g., Equal Employment Opportunity Comm'n v. Commercial Office Prod. Co.*, 486 U.S. 107, 118 (1988) (noting that a pure carrot approach gives states an incentive to act but does not discipline them for inaction). *See generally* EMANUEL, *supra* note 46, at 62 (explaining that Congress may indirectly achieve certain objectives by conditioning federal funds, which effectively acts as a "dangling carrot"); STONE, *supra* note 48,

action, state collection proposals might entail pure, voluntary compliance,⁸⁵ third-party collection officers,⁸⁶ or mandatory disclosure.⁸⁷

Specifically, tailoring of Senate Proposal 480 represents a very viable proposal for Internet transactions, as it seeks to ensure that necessary jurisdictional elements are satisfied to comport with due process.⁸⁸ Accordingly, future proposed legislation might take a slightly similar, yet modified form.⁸⁹ If Congress were to pass similar legislation, Elite Computers⁹⁰ would be subject to jurisdiction within New Jersey.

at 510-11 (implying carrot stick approach within Civil Rights Act context, explaining that an incentive to desegregate federal funds would be eliminated).

In our hypothetical example, the "carrot" might be the federal government's promise of additional state funds, provided that they require companies doing business within state borders to collect and remit use taxes to the applicable states.

⁸⁵ See Dotson, *supra* note 10, at 47 (concluding that voluntary cooperation by companies in forwarding applicable use taxes better guarantees much-needed state revenues).

⁸⁶ See Internet Symposium, *supra* note 5, at 576. Speaker R. Scot Grierson explained that another use tax collection scheme is referred to as "electronic cash or DigiCash." See *id.* The design of this proposal is to enable the purchaser's address and/or credit card number to remain confidential. See *id.* Only the third party beneficiary would know billing data. See *id.* Implementation would entail states contracting with private third parties who would be responsible for forwarding collected use taxes. See *id.*

⁸⁷ See Dotson, *supra* note 10, at 46 (noting the filing of a Federal Trade Commission petition to require that mail-order businesses completely disclose use tax consequences applicable to the sale). This represents a possible solution within the Internet context. See *id.* It would simply require some type of on-line, web site disclosure prior to consummation of the purchase. See *id.* Although potential options, these state proposals likely fail to be the best solution to ensure that states collect use tax revenues.

⁸⁸ See S. 480. The proposal there suggested that jurisdictions meet the following requirements:

A State shall have power to require a person to collect a State sales [and/or use] tax imposed with respect to the sale of tangible personal property if-

(1) the destination of sale is in such State, and

(2) such person [or corporation]-

(A) engages in regular or systematic soliciting of sales in such State, and

(B) during the 1-year period ending September 30 of the calendar year preceding the calendar year in which the sale occurs, has gross receipts from the sale of such tangible personal property-

(i) in the United States exceeding \$12,500,000, or

(ii) in such State exceeding \$500,000.

Id. (emphases added).

⁸⁹ See *supra* note 88 and accompanying text (discussing original Senate proposal S. 480). For purposes of this Comment, the following proposed legislation utilizes the format and certain contents from Senate Proposal Number 480. See *id.* Additionally, please note that changes from Senate Proposal Number 480 are indicated within brackets. A possible proposal might entail the following:

A State [imposing use taxes] shall have power to require a person [and/or corporation/partnership] to collect [and remit to] a State [use] tax[es] imposed with respect to the sale of tangible personal property [commenced by utilizing a web site and Internet to advertise and market their respective

Straightforward analysis supports this conclusion. First, Elite Computers purposely chose a web site⁹¹ and the Internet⁹² to market products outside Oregon, its principal place of business⁹³ and state of incorporation. Second, the facts unquestionably demonstrate that Elite's operations were ongoing, systematic, deliberate, and purposefully directed toward reaching a national market beyond Oregon's borders. These directed efforts were more than rewarded as sales from New Jersey alone accounted for almost \$5 million, which satisfies the suggested threshold level of \$1 million within a particular state. Accordingly, under this assumed federal statute, jurisdiction would be proper. Therefore, New Jersey could impose a use tax collection duty on Elite Computers.

III. CONCLUSION: CONGRESSIONAL LEGISLATION IS NECESSARY TO LIMIT FUTURE LITIGATION

Congress should legislate in the area of state attempts to require nonresident companies to collect and remit use taxes. Due to the potential negative effect of Internet sales on vital use tax revenues,⁹⁴ state ar-

products in states other than that where they are domiciled and/or incorporated] if-

- (1) [For purposes of determining subsection 2(A) herein, a court should make its own factual inquiry]
- (2) such person, [corporation, and/or partnership]-
 - (A) engages in regular, systematic, [or ongoing, purposeful, deliberate, etc.] sales in such State [utilizing a web site via the Internet], and
 - (B) [a one-year accounting reveals] that gross revenues [sales] from the sale of such tangible personal property [within the State referred to in sub-section (A) above]-
 - (i) in the United States exceeding [\$1 billion], or
 - (ii) in such State exceeding [\$1 million].

⁹⁰ See Hypothetical, *supra* note 13 and accompanying text.

⁹¹ See *supra* note 1 for a definition of web site.

⁹² See *supra* note 2 for a definition of Internet.

⁹³ See BLACK'S LAW DICTIONARY 1149 (6th ed. 1990) (defining place of business as "[t]he location at which one carries on his business . . . service of process may be made [here]"); see also *id.* at 485 (defining corporate domicile as "[p]lace considered by law as [nerve] center of corporate affairs and place where its functions are discharged"). Additionally, principal place of business can be understood by reference to commercial domicile:

A concept employed to permit taxation of property or activity of nonresident corporation by state in which managerial activities occurred in quantity and character sufficient to avoid contention of nonresident corporation that taxation of its activities and property located outside bounds of taxing state amounted to deprivation of property without due process.

Id. (quoting *North Baton Rouge Dev. Co. v. Collector*, 304 So. 2d 293, 297 (La. 1974)).

⁹⁴ See *supra* note 5 and accompanying text (discussing potential negative effects of the Internet on state use tax revenues).

guments to expand the meaning of "physical presence" will continue in the hopes of sustaining a Commerce Clause challenge.⁹⁵ No longer is due process an insurmountable hurdle; rather, it meets constitutional scrutiny.⁹⁶ In fact, in *Quill's* dicta,⁹⁷ the United States Supreme Court emphasized that future resolution of this Commerce Clause issue may better be handled by Congress.⁹⁸ The Court's call for legislative guidance is magnified today by ever-increasing⁹⁹ Internet usage.¹⁰⁰ It remains unnecessary to clog court dockets with additional litigation. Certainty of use tax collection does not lie with voluntary citizen compliance.¹⁰¹ Rather, the wise choice is for congressional legislation, perhaps a modified version of Senate Proposal 480,¹⁰² which avoids a possible Commerce Clause¹⁰³ violation and ensures states their much needed revenues.¹⁰⁴

Gregory A. Ichel, C.P.A.

⁹⁵ See *supra* note 70 and accompanying text (explaining that states' efforts to expand the meaning of "nexus" will not subside, but continue in the attempt to redefine this context within the new Internet context).

⁹⁶ See *supra* notes 25-44 and accompanying text (analyzing Due Process Clause issue presented by a company's single web site via the Internet).

⁹⁷ See *supra* note 62 (defining dictum).

⁹⁸ See *Quill Corp. v. North Dakota*, 504 U.S. 298, 318-19 (1992).

⁹⁹ See *supra* note 3 and accompanying text (explaining the potential increases in Internet usage).

¹⁰⁰ See *Quill*, 504 U.S. at 318-19.

¹⁰¹ See *supra* note 10 and accompanying text (noting that most consumers are unaware of the requirement to pay use taxes).

¹⁰² See *supra* note 89 (outlining possible future congressional legislation).

¹⁰³ See *supra* notes 57-71 and accompanying text (analyzing dormant Commerce Clause issues and conclusions).

¹⁰⁴ See *supra* note 5 and accompanying text (noting the importance of use taxes to states' total revenues).

[illegible]

APPENDIX B

1996 Form NJ-1040 Line by Line Instructions

21

Line 39 - Balance of Tax

Subtract Line 38 from Line 37 and enter the result on Line 39.

Line 40 - Use Tax Due on Out-of-State Purchases

If you were a New Jersey resident and you purchased items or services that were subject to New Jersey sales tax, you are liable for the use tax at the rate of 6% of the purchase price if:

1. Sales tax has not been paid;
or
2. Sales tax has been collected out-of-State at a rate less than 6%.

In determining the net amount of use tax due, sales tax paid to certain other states may be taken as credit. Use tax is due 20 days after the items enter New Jersey. Use Form ST-18 to remit the use tax on a more timely basis.

✓ Form ST-18 is provided in this booklet for your convenience (in the center of the booklet with other tax forms). You may photocopy the Form ST-18 provided and use it to remit use tax throughout the year. You should know that New Jersey does have access to records maintained by out-of-State businesses and does bill customers directly for use tax including penalty and interest.

If you owe use tax and are remitting it with Form NJ-1040, enter the amount on Line 40. If you owe no use tax, enter "0.00."

Line 41 - Total Tax

Total Lines 39 and 40 and enter on Line 41.

Line 42 - Total New Jersey Income Tax Withheld

Enter on Line 42 the total New Jersey income tax withheld, as shown on your W-2, W-2G and/or 1099-R statement(s). The W-2 must indicate the amount of New Jersey tax withheld and the "State" box must indicate that the tax withheld was New Jersey income tax. Enclose the state copy of each withholding statement (W-2, W-2G, 1099-R). Enclose Form 1099-R with the return only if New Jersey income tax was withheld.

Do not include on Line 42 amounts withheld as New Jersey workforce development partnership fund/unemployment insurance/health care subsidy fund contributions (shown on the W-2 as WD/UI/HC, if combined, or WD, UI and HC, if stated separately) or New Jersey disability insurance (may be shown as DI). These are not New Jersey income tax withholdings and may not be used as credits on Line 42. See instructions for Lines 45 and 46 for more information on excess workforce development partnership fund/unemployment insurance/health care subsidy fund contributions and/or disability insurance contributions.

All W-2 statements must reflect your correct social security number for the withholdings to be credited. If the social security number is missing or incorrect, you must obtain a corrected W-2 from your employer. Only your employer/payer can issue or correct this form. If you have not received a W-2 form by February 15, 1997, or if the form you received is incorrect, contact your employer/payer immediately.

Line 43 - Property Tax Credit

✓ If you satisfied the eligibility requirements (see page 18) and you did not claim a property tax deduction on Line 35, you are entitled to a property tax credit. Do not complete Line 43 if you claimed a property tax deduction on Line 35. If your gross income on Line 29, Form NJ-1040, is \$7,500 or less, make no entry on Line 43.

Line 44 - New Jersey Estimated Payments/Credit from 1995 Tax Return

Enter on Line 44 the total of:

- Estimated tax payments made for 1996
- Credit applied from your 1995 tax return
- Amount, if any, paid to qualify for an extension of time to file

✓ If you changed your name because of marriage, divorce, etc., and you made estimated tax payments using your former name, enclose a statement with your return explaining all the payments you and/or your spouse made for 1996 and the name(s) and social security number(s) under which you made payments.

✓ If your spouse died during the year and any estimated payment(s) were made under the deceased spouse's social security number and other payments were made under your social security number, you must enclose a statement with your return listing the social security numbers and the amounts submitted under each social security number.

Credit for Excess Contributions to: Workforce Development Partnership Fund, Unemployment Insurance, Health Care Subsidy Fund and/or Disability Insurance (Lines 45 and 46)

You may take credit for excess workforce development partnership fund/unemployment insurance/health care subsidy fund contributions and/or disability insurance contributions withheld by two or more employers. For 1996, the maximum employee workforce development partnership fund/unemployment insurance/health care subsidy fund contribution was \$112.50, and the maximum employee disability insurance contribution was \$90.00. If you had two or more employers and you contributed more than the maximum amount(s), you must enclose a completed Form NJ-2450 with your return to claim the credit.

continued

APPENDIX C

New Jersey Use Tax

What is Use Tax?

Use tax occurs when goods and services (of tangible personal property) are purchased for use in New Jersey but sales tax was not collected or sales tax was collected at a rate less than the New Jersey sales tax rate (currently 6%). The purchaser is liable for the payment of use tax at the New Jersey sales tax rate.

Some Examples of Use Tax are:

1. An item (e.g., furniture) is purchased out-of-State for use in New Jersey and no sales tax was collected. (Purchase was made in a state that does not impose a sales tax); 6% use tax is due to New Jersey.
2. An item (e.g., jewelry) is purchased out-of-State for use in New Jersey on which the state sales tax collected was at a lower rate than New Jersey's. Generally use tax is due only on the difference. If you paid 5% state sales

tax in another state, you should submit 1% use tax to New Jersey.

3. Some mail order companies are not registered to collect New Jersey sales tax. When you purchase goods and services through the mail and those items are normally subject to New Jersey sales tax, use tax is due on the amount of the sale if New Jersey sales tax was not paid.

How to Remit Use Tax

Complete the Use Tax Return (Form ST-18, below) and file it within twenty days after property is brought into New Jersey or report the use tax on Line 40 of Form NJ-1040. Enter zero on Line 40, if you have no use tax to report. Businesses registered with the Division for sales tax purposes report use tax on New Jersey Sales and Use Tax Returns (Forms ST-50 and ST-51).

Here is the New Jersey Use Tax
Photocopy Form ST-18 and use it as

Return, Form ST-18, for your use.
needed throughout the year.

USE TAX REMITTANCE Form ST-18 (3-94)		STATE OF NEW JERSEY DIVISION OF TAXATION		FOR OFFICIAL USE ONLY	
		PLEASE READ INSTRUCTIONS ON REVERSE SIDE			
PURCHASER'S NAME AND ADDRESS (PRINT) _____ _____ _____		SELLER'S NAME AND ADDRESS (PRINT) _____ _____ _____		1 AMOUNT OF PURCHASES \$ _____	
Social Security or Federal Identification Number _____		Attach Rider if Necessary _____		2 USE TAX (Line 1 x .06) _____	
IDENTIFY TAXABLE ITEM(S) PURCHASED		PRICE PAID		3 CREDIT, IF ANY, FOR TAX PAID IN JURISDICTION OF PURCHASE (See Instruction for Line 3) _____	
a) _____ \$ _____		_____		4 AMOUNT DUE (Line 2 Less Line 3 Plus Line 4) \$ _____	
b) _____ \$ _____		_____			
c) _____ \$ _____		_____			
(If more taxable items were purchased, attach rider)		(Carry Total to Line 1)			
I CERTIFY THAT ALL THE INFORMATION GIVEN IS CORRECT _____					
Signature _____ Date _____					

If you purchased any taxable items or services on which Sales Tax was not collected or was collected at a rate less than 6%, then you are liable for Use Tax at a rate of 6% of the purchase price. Credit for any Sales Tax paid to other states or jurisdictions may be taken. (See Instructions for Line 3)

INSTRUCTIONS FOR COMPLETING USE TAX RETURN (Form ST-18)

LINE 1 - Enter the Total Amount of all purchases subject to the Use Tax.

LINE 2 - Multiply Line 1 by 6% (.06) and enter the amount of Use Tax.

LINE 3 - Enter credit for sales tax previously paid ONLY on purchases where items or services were received outside of New Jersey.

A. TAX PAID TO ANOTHER STATE AT 8% OR HIGHER - If you paid Sales Tax on the purchase at the current New Jersey rate of 6% or a higher rate to another state or jurisdiction and did not take delivery in New Jersey, NO Use Tax is due New Jersey. No credit will be given for such payments on items or services delivered into New Jersey or for taxes paid in foreign countries.

B. TAX PAID TO ANOTHER STATE AT LESS THAN 6% - If you paid sales tax on the purchase at less than the current New Jersey rate of 6% and did not take delivery in New Jersey, Use Tax is due New Jersey in the amount of any difference.

LINE 4 - Subtract line 3 from line 2 and enter result on line 4.

Mail this form upon completion with your payment to: State of New Jersey, Use Tax, CN-261, Trenton, N.J. 08646

KEEP A COPY FOR YOUR RECORDS.

For information regarding the ST-18 and its completion contact: Division of Taxation, Taxpayer Service Branch, Office of Communication, CN-281, Trenton, N.J. 08646-0281 or call (609) 588-2200.

PRIVACY ACT NOTIFICATION

The Tax Reform Act of 1976, P.L. 94-455, modified at 42USC 405(c)(2)(C)(i), authorizes the use of social security numbers in the administration of a tax law. The Division will use the number for tax account identification and tax administration and collection purposes.