American University Law Review

Volume 65 | Issue 5

2016

Beyond *Quill* and Congress: The Necessity of Sales Tax Enforcement and the Invention of a New Approach

Lila Disque
*Multistate Tax Commission*

Helen Hecht
*Multistate Tax Commission*

Follow this and additional works at: https://digitalcommons.wcl.american.edu/aulr

Part of the Tax Law Commons

**Recommended Citation**
Available at: https://digitalcommons.wcl.american.edu/aulr/vol65/iss5/2

This Article is brought to you for free and open access by the Washington College of Law Journals & Law Reviews at Digital Commons @ American University Washington College of Law. It has been accepted for inclusion in American University Law Review by an authorized editor of Digital Commons @ American University Washington College of Law. For more information, please contact kclay@wcl.american.edu.
Beyond *Quill* and Congress: The Necessity of Sales Tax Enforcement and the Invention of a New Approach
BEYOND *QUILL* AND CONGRESS:  
THE NECESSITY OF SALES TAX ENFORCEMENT AND THE INVENTION OF A NEW APPROACH:

LILA DISQUE** & HELEN HECHT***

TABLE OF CONTENTS

Introduction ........................................................................................................... 1164

I. The U.S. Sales Tax System and Related Enforcement Issues ................................. 1167

II. The EU VAT System and Related Enforcement Issues .................................... 1174

III. The Seeds of Invention .................................................................................. 1179

IV. Potential Legal or Other Impediments ......................................................... 1185
   A. The Constitutional Challenge to Colorado’s Information Reporting Requirements ........................................... 1186
   B. Potential First Amendment Challenge ............................................................. 1190
   C. The “Non-Discrimination” Provision of the Internet Tax Freedom Act ......................................................... 1192

Conclusion .......................................................................................................... 1194

* This Article does not represent the views of the Multistate Tax Commission, its Executive Director, or its member states.

** Counsel, Multistate Tax Commission. Ms. Disque has been with the Commission since 2012. She received her J.D. from the U.C. Davis School of Law and her LL.M. from Georgetown.

*** General Counsel, Multistate Tax Commission. The Commission is an intergovernmental agency whose members, the heads of state revenue agencies, work together on common issues in the area of multistate taxation. Ms. Hecht is an attorney and a certified public accountant and has spent over thirty years in state and local tax work, fifteen of those years in private practice working in the KPMG, LLP state and local tax practice and for a law firm in Albuquerque, New Mexico. Prior to the Commission, Ms. Hecht was tax counsel for the Federation of Tax Administrators. She began her career at the New Mexico Taxation and Revenue Department.
INTRODUCTION

The U.S. consumption tax—the sales and use tax—has been plagued by a seemingly intractable problem: it is built on an enforcement system that depends on seller-collection. But under U.S. Supreme Court precedent, states cannot require “remote” sellers (those without some kind of physical presence in the state) to collect and remit the tax. Consequently, states instead attempt to collect the tax from resident purchasers through self-reporting—a method that has proven to be much less effective. Congress has the power to grant states enforcement authority over remote sellers, but has long denied that assistance to the states. But what if the states had an alternative approach to enforcing the tax on remote purchases? And what if this approach could be implemented without the need for action by Congress or the Supreme Court? The “seeds” of that approach have already been planted.

It is no surprise that state and local governments rely on sellers to help enforce the sales and use tax imposed on purchases by consumers. Sellers have the means to withhold and pay over the tax received as part of the purchase price. Just as importantly, sellers create information and maintain records in the regular course of their business, which are necessary for determining and confirming the proper amount of tax. Despite the limits imposed by the Supreme Court, this enforcement system worked well historically because commercial success required physical proximity to markets. But e-commerce has undermined this system. As a result, states now face a situation in which the parameters of the sales and use tax are increasingly dictated not by the principles of good tax policy or legislative choice, but by the limits of an outdated approach to enforcement. This reality is especially evident in the extent to which

2. See infra notes 95–100 (explaining why self-reporting has been less effective).
3. See Quill Corp., 504 U.S. at 311, 317 (holding that under the Commerce Clause, a state cannot require a remote seller to collect sales tax unless it has a physical presence in the state).
4. See Donald Bruce et al., E-Tailer Sales Tax Nexus and State Tax Policies, 68 NAT'L TAX J. 735, 735–36 (2015), http://icepp.gsu.edu/files/2015/09/E-Tailer.pdf (“E-tailers can locate their revenue generating websites anywhere without affecting their customers’ shopping experience and can often exploit nationwide markets with physical locations in only one or a few states. These characteristics provide e-tailers with more locational flexibility than their bricks and mortar counterparts, and this flexibility in turn may heighten the potential influence of state tax policies on decisions about where to locate key operational assets.”).
state use taxes are generally collected on consumer purchases of
digital goods and services—which is seldom.\(^5\)

The conventional wisdom is that for the states to solve the sales tax
enforcement problem, and thus remove this barrier to taxing the
“new economy,” one of two things must occur. Either Congress must
act to expand state jurisdiction to require remote-seller collection of
tax, or the Supreme Court must eliminate the bar created by its
precedent.\(^6\) State and local governments have devoted substantial
time and resources to making progress down one or both of these
two paths, but with little success.\(^7\) For nearly sixteen years, the

5. See Michael Mazerov, States Should Embrace 21st Century Economy by Extending
Sales Tax to Digital Goods and Services, CTR. ON BUDGET & POL’Y PRIORITIES I (Dec. 13, 2012),
that some states have included certain digital goods in their tax bases and that the
revenue loss from states failing to do so is significant, but also cautions that

[t]he major limitation on collecting the tax due arises from the U.S.
Supreme Court’s 1992 Quill decision. The Court held in Quill that a state
cannot require an out-of-state seller to collect sales tax on sales to the state’s
residents if the seller does not have a “physical presence”—facilities or
employees—within the state. By their very nature, most sales of digital goods
and services can be delivered over the Internet without the seller’s physical
presence in the purchasers’ states. While tax on the purchase is still legally
due directly from the purchaser, there is no effective way to enforce payment
by household purchasers.

Id. at 24–25 (footnote omitted); see Hayes R. Holderness, Revenue Department’s Cloudy Minds Lead to Wrong Answers, in STATE AND LOCAL TAXATION 8-53 to 8-84 (8th ed. 2015).

6. See, e.g., H. Beau Baez III, Taxing Internet Sales: Trying to Make a Two-Thousand-
Year-Old Jurisdiction Test Work in the Dot-Com Economy, 64 TAX LAW. 807, 849 (2011)
(“The states should look not only to Congress but also to the Supreme Court to help
solve this problem.”); Alexandria Rose Finch, Slow Connections for E-Tailer Nexus:
Bringing Sales and Use Taxes up to Speed in an E-Commerce Economy, 42 STETSON L. REV. 293, 320 (2012) (“First, it is clear from Quill, the [Internet Tax Freedom Act], the
individual state attempts to tax Internet sales, and the [Streamlined Sales and Use
Tax Agreement] that any solution to the problem must come from the federal
level.”); David H. Gershel, Comment, The Day of Reckoning: The Inevitable Application
of State Sales Tax to Electronic Commerce, 14 TUL. J. TECH. & INTELL. PROP. 335, 362
(2011) (“Whether Congress or the Supreme Court creates the standard for the
legality of click-through nexus laws, the building momentum behind this tax-on-
technology movement means the issue cannot be ignored for much longer.”); Geoffrey E. Weyl, Comment, Quibbling with Quill: Are States Powerless in Enforcing Sales
and Use Tax-Related Obligations on Out-of-State Retailers?, 117 PA. ST. L. REV. 253, 276
come from Congress.”).

7. See Marketplace Fairness—Big 7, NGA Letters, NAT’L GOVERNORS ASS’N (Nov. 8,
2014), http://www.nga.org/cms/home/federal-relations/nga-letters/economic-
development-commerce-c/col2-content/main-content-list/marketplace-fairness—
big-7.html (expressing, in a letter from the “Big 7” to the House and Senate
Streamlined Sales and Use Tax Agreement has attempted to simplify the sales tax system so that Congress would be persuaded to grant tax collection authority. But, this effort, like others, has failed to reach this goal. Recently, the National Conference of State Legislatures advised state lawmakers that “[w]e cannot depend on Congress to heed the calls of their state legislative partners” to solve the problem, urging states instead to act legislatively to expand tax collection duties, challenging Supreme Court precedent, if necessary. But for the states to attempt to bring a direct challenge seeking to overturn Supreme Court precedent only raises a number of other difficult issues.

This either-Congress-or-the-Supreme-Court formulation of the necessary solution to the sales tax enforcement problem has a number of flaws. First, neither Congress nor the Supreme Court is obligated to address the issue, and neither seems in a hurry to do so. Second, although it would be a simple matter for Congress or the Court to expand the legal jurisdiction of the states (assuming they wished to do so), legal jurisdiction alone does not solve the practical problems of enforcing collection from remote actors. But perhaps most importantly, this formulation imposes a false dichotomy—that the solution must come from either Congress or the Supreme Court—which assumes that there are no other options. But there are, and perhaps it is time to consider them.

This Article posits that it is time for states to consider alternative enforcement tools and to take advantage of the information technology that makes electronic commerce possible. This Article will not try to tackle the necessary technology requirements, although...
it certainly appears that they are well within the reach of the states. Instead it considers whether this alternative is viable from a legal perspective. According to the U.S. Court of Appeals for the Tenth Circuit, this alternative is legally viable. However, this question is still dependent on whether there are other constraints imposed by the Constitution or federal statute.\(^{13}\)

This Article acknowledges that this alternative approach also depends on the willingness of policy makers to take on potential political opposition. Instead, of course, they might simply allow the tail to continue to wag the dog—permitting the current enforcement system to dictate the scope of the tax. But that will not necessarily be an easy abdication. The economic inefficiencies created by a narrowing of the consumption base, the competitive disadvantages imposed on local businesses, the actions of other countries in enforcing their own consumption taxes on U.S. businesses, and the limitations on revenue sources will create growing pressures to which at least some states may respond. Assuming that even a few intrepid lawmakers manage to create a viable enforcement alternative, so as to allow the natural broadening of the tax base and leveling of the competitive playing field, it will likely not take long before there are many imitators.

This Article first looks briefly at the U.S. sales tax system and the legal limits on the states’ authority to use out-of-state sellers to collect the tax. Next, this Article considers the decision of the European Union (EU) to amend the value added tax (VAT) imposed by EU countries so as to require all remote sellers of digital goods to collect and remit sales taxes on a market-sourcing basis. Additionally, this Article considers the EU’s general approach to enforcement, the inherent limitations of that approach, and other solutions being discussed. Finally, this Article suggests how the holding by the Tenth Circuit in *Direct Marketing Ass’n v. Brohl*\(^{14}\) has opened up a new enforcement approach and considers the legal questions that might accompany this approach.

I. THE U.S. SALES TAX SYSTEM AND RELATED ENFORCEMENT ISSUES

Consumption taxes are vitally important as a revenue source, accounting for thirty-one percent of total revenues in certain


\(^{14}\) 814 F.3d 1129 (10th Cir. 2016).
developed countries in 2012.\textsuperscript{15} Virtually every country today imposes some form of sales tax or VAT.\textsuperscript{16} Consumption taxes traditionally rely on seller or other third-party collection and reporting.\textsuperscript{17} Cross-border sales can, therefore, pose a particular enforcement problem.\textsuperscript{18} If purchasers can buy from sellers operating outside the government’s jurisdiction so that the sellers have no obligation to collect the tax or report information, consumption tax enforcement will be much more difficult. Conspicuous systematic tax avoidance can also undermine a voluntary tax system as a whole.

Of course, the enforcement role of third parties in state and federal tax systems goes beyond the use of sellers to collect sales taxes. For example, employers are routinely subjected to withholding and reporting obligations for the personal income taxes or other payroll taxes owed on wage income paid to individual employees under federal and state tax laws.\textsuperscript{19} Furthermore, the role of third parties in maintaining and reporting information is not simply incidental to tax collection.\textsuperscript{20} While information reporting may or may not be accompanied by a tax-collection or withholding obligation, no collection or withholding obligation is ever imposed without a corresponding information reporting requirement.\textsuperscript{21} To the extent that the tax system depends upon complex rules applied to specific facts, the ability of the third party to capture, process, and report information is critical. So, for example, employers not only withhold and pay over tax for employees, but they capture wage, benefit, and expense reimbursement information and use that data to file an IRS Form 940 return and to provide employees a Form W-2.\textsuperscript{22} The information maintained by employers is the basis for confirming that the proper tax—ultimately owed by the employee—has been withheld and paid.

\begin{itemize}
\item \textsuperscript{16} Id. at 14.
\item \textsuperscript{17} Sarah W. Salter, E-Commerce and International Taxation, 8 New Eng. J. of Int’l & Comp. Law 5, 6 (2002).
\item \textsuperscript{18} Id.
\item \textsuperscript{19} See, e.g., 26 U.S.C. §§ 3401 (a)–3406 (2012).
\item \textsuperscript{21} Employer’s Tax Guide, supra note 20, at 41.
\item \textsuperscript{22} Id. at 5–6.
\end{itemize}
This information maintenance and reporting is no less essential to sales and use tax enforcement. By their nature, such taxes are imposed on the day-to-day purchases by individuals, virtually none of whom should be expected to maintain detailed records of those purchases, and a number of whom (e.g., minors, those with disabilities, transients, etc.) could hardly be required to do so.23 But unlike consumers, sellers do maintain detailed sales records for a multitude of reasons, including customer relations, marketing, obtaining credit, financial accounting, and federal income tax compliance.24 It is unremarkable, therefore, that the state sales and use tax enforcement system also takes advantage of this detailed sales information, requiring that sellers use it to report the tax. The seller will not only file a report with the state tax agency but will also provide to the customer some type of a bill of sale or invoice showing tax charged and collected as part of the sale.25 Not only would this provide the customer with documentation that the customer's use tax obligation has been discharged, it would also allow states to perform other actions with respect to enforcement, such as audits.

States may also reasonably conclude that requiring sellers to report certain information, with or without collection of the tax, will increase compliance. This has been demonstrated where, for example, the Internal Revenue Service (IRS) imposes certain information reporting requirements without the requirement to withhold or collect.26 In those situations, the information-reporting obligation, by itself, will increase tax compliance by the party required to pay the tax.27 And, in situations in which the taxpayer

23. The authors are aware of no states that impose a general requirement upon such individuals to maintain records for the purpose of verifying the proper amount of taxes paid.

24. See for example the general requirements for record keeping imposed by Treas. Reg. § 1.6001-1(a)(1990); see also Ridgeley A. Scott, Reimbursed Employee Expenses: New Tales from the Grimm Brothers, 28 WILLAMETTE L. REV. 1 (1991) which recounts efforts by the federal government to craft requirements for business record keeping that would obviate the need for record keeping by employees, something that has not worked well, in the area of non-taxable expense reimbursement.


26. See Tax Gap for Tax Year 2006: Overview, INTERNAL REVENUE SERV. (Jan. 6, 2012) ("[C]ompliance is far higher when reported amounts are subject to information reporting and, more so, when subject to withholding.").

27. Id. (estimating the net misreporting percentage, "defined as the net misreported amount as a ratio of the true amount," at eight percent for amounts subject to substantial information reporting alone, and fifty-six percent for amounts subject to no withholding or information reporting); IRS Releases New Tax Gap Estimates; Compliance Rates Remain Statistically Unchanged from Previous Study, INTERNAL.
must rely on the third-party information to be able to voluntarily comply (that is, to self-assess), this information-reporting obligation is not merely helpful, but is essential.

But the states’ ability to impose a tax collection obligation on sellers has been limited by the Supreme Court. Under the Court’s Commerce Clause jurisprudence, a state cannot require a remote seller to collect sales tax unless that seller has some sort of physical presence within that state. In National Bellas Hess, Inc. v. Department of Revenue of Illinois and Quill Corp. v. North Dakota, the Court held that requiring out-of-state mail-order sellers to collect the sales tax imposed an undue burden on those sellers including, in particular, “[t]he many variations in rates of tax, in allowable exemptions, and in administrative and record-keeping requirements.”

In Quill, for the first time, the Court delineated two distinct standards for state taxing jurisdiction, or nexus, under the Due Process Clause and Commerce Clause. Under the Due Process Clause, a seller establishes a nexus for sales and use tax purposes if it purposefully directs its activities to residents of the state. This is a relatively low threshold, often referred to as “minimum contacts.” The Commerce Clause, however, requires a “substantial nexus,” and for sales tax collection purposes, physical presence is the required bright-line rule. The Court’s decision in Quill in 1992 not to


28. Quill Corp. v. North Dakota, 504 U.S. 298, 311, 317 (1992). The North Dakota Commissioner of Taxation, Heidi Heitkamp, at the time of the case, is now the U.S. Senator from North Dakota. She delivered the opening address at American University Law Review’s 2016 Symposium discussing how it was that Quill came to be litigated in the manner that it was and also provided fascinating insight on the history of that litigation.

29. 386 U.S. 753 (1967).


32. Bellas Hess, 386 U.S. at 759 (footnotes omitted) (noting that there thousands of tax rates throughout the country and that exemptions and administrative rules differed between states).

33. Quill, 504 U.S. at 305.

34. Id. at 306, 312 (stating that notice or fair warning is sufficient to satisfy the Due Process Clause nexus requirement).

35. Id. at 307.

36. Id. at 311.
overrule its 1967 decision in *Bellas Hess* relied heavily on stare decisis.\textsuperscript{37} The Court also expressed that this decision was “made easier” by the fact that Congress could overrule *Bellas Hess*, if it chose to.\textsuperscript{38}

It is important to also note that under two other Supreme Court cases, *Scripto, Inc. v. Carson*\textsuperscript{39} and *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*,\textsuperscript{40} third parties acting on behalf of a seller within a state are deemed to create a nexus for the seller under both the Due Process Clause and the Commerce Clause.\textsuperscript{41} This type of nexus is sometimes referred to as representational nexus, and has been relied upon in a number of cases.\textsuperscript{42} The *Scholastic Book Clubs* cases, in particular, are notable. The third parties who created nexus for the out-of-state sellers in those cases were not typical salespeople and were not affiliated with the seller; instead, they were school teachers who helped students place orders and also helped deliver the books sold by the seller.\textsuperscript{43} The Connecticut Supreme Court found that the teachers acted as Scholastic’s representatives, even though there was no agreement compelling them to serve as its agents or salespeople and they received no direct compensation from Scholastic.\textsuperscript{44} The Court of Appeals of Tennessee noted that Scholastic utilized Tennessee schools and teachers to facilitate sales to school children in Tennessee, and the teachers created “a de facto

\textsuperscript{37} *Id.* at 317.

\textsuperscript{38} *Id.* at 318–19.

\textsuperscript{39} 362 U.S. 207 (1960).

\textsuperscript{40} 483 U.S. 232 (1987), superseded by statute, WASH. REV. CODE. § 82.04.440 (1987).

\textsuperscript{41} *Tyler Pipe*, 483 U.S. at 250; *Scripto*, 362 U.S. at 208–11.

\textsuperscript{42} See, e.g., Scholastic Book Clubs, Inc. v. State Bd. of Equalization, 255 Cal. Rptr. 77, 79–81 (Cal. Ct. App. 1989); New Mexico Taxation & Revenue Dep’t v. Barnesandnoble.com LLC, 2013-NMSC-023, 303 P.3d 824, 826–27, 829 (N.M. 2013); Orvis Co. v. Tax Appeals Tribunal, 654 N.E.2d 954, 956–57, 961 (N.Y. 1995). See generally Standard Pressed Steel Co. v. Dep’t of Revenue of Wash., 419 U.S. 560 (1975). The taxpayer-appellee in *Standard Pressed Steel Co. v. Department of Revenue of Washington* challenged Washington’s business and occupation tax on Due Process Clause and Commerce Clause grounds. 419 U.S. 560, 562 (1975). Standard’s only in-state presence was one employee, who worked from his home. *Id.* at 561. His primary duty was to consult with Boeing, Standard’s primary customer, regarding its anticipated needs for aerospace fasteners and to follow up on any post-delivery difficulties. *Id.* The Court upheld the constitutionality of the imposition of the tax because the appellant’s full-time job allowed Standard to keep Boeing as its primary customer. *Id.* at 562, 564.


\textsuperscript{44} *Scholastic Book Clubs*, 38 A.3d at 1199–200.
marketing and distribution mechanism." Both courts therefore held that Scholastic's connections with the state's schools and teachers established a "substantial nexus" sufficient to justify the imposition of sales and use tax under the Commerce Clause.\[46\]

Although the majority in Quill referred to the physical presence rule, or substantial nexus rule, as a "bright line rule," it is debatable whether this turned out to be true. The majority’s apparent hope that a bright-line rule would simplify determining when sellers are required to collect the tax, was doubted even in 1992, by Justice White who stated in a separate opinion: "[I]t is a sure bet that the vagaries of 'physical presence' will be tested to their fullest in our courts."\[47\] Justice White was correct; in an economy that is moving from tangible goods to intangibles and services, states are finding that the physical presence standard is badly matched to how business is now being done.\[48\]

One way that states have brought the physical presence standard into better alignment with e-commerce is through the enactment of so-called "click-through nexus" statutes (also known as "Amazon" statutes).\[49\] These statutes impose a collection and reporting duty on some remote retailers who market using in-state representatives compensated on a commission-like basis, including in-state organizations that put on their own websites a link to the seller's website (i.e., online referrals via weblink).\[50\] New York was the first state to enact click-through nexus legislation, in 2008.\[51\] The law was

45. Scholastic, 373 S.W.3d at 565.
46. Scholastic Book Clubs, 38 A.3d at 1200; Scholastic, 373 S.W.3d at 565. But see Scholastic Book Clubs, Inc. v. State Dep't of Treasury, Revenue Div., 567 N.W.2d 692, 695 (Mich. Ct. App. 1997) (holding that imposition of the sales and use tax did violate the Commerce Clause because "the use of teachers, without more, [did] not establish a substantial nexus").
48. See generally Laura Mahoney et al., States See Little Revenue from Online Sales Tax Laws, Keep Pressure on Congress, BNA DAILY TAX REPORT (Jan. 8, 2014), http://www.bna.com/states-little-revenue-n17179881226. Even in cases not involving digital goods or services, state courts were imposing a quantitative or qualitative test on whether physical presence existed. See Richard D. Pomp, STATE AND LOCAL TAXATION 9-157 (8th ed. 2015).
50. Mahoney et al., supra note 48.
51. Act of April 23, 2008, Ch. 57, pt. OO-1, 2008 N.Y. Laws 2844 (codified at N.Y. TAX LAW §§ 1101 et seq.) (adding a subparagraph (vi) to N.Y. TAX LAW § 1101(b)(8) that reads: "For purposes of subclause (I) of clause (C) of subparagraph (i) of this
immediately challenged by Amazon.com and Overstock.com.\textsuperscript{52} New York’s click-through nexus law was upheld by the state’s highest court against facial challenges on Due Process and Commerce Clause grounds,\textsuperscript{55} and the U.S. Supreme Court denied certiorari.\textsuperscript{54} Nevertheless, e-commerce in particular has proven to be a challenge for state enforcement systems constrained by a physical presence requirement.\textsuperscript{55} A number of states that have passed click-through nexus statutes have seen remote sellers simply terminate their agreements with in-state representatives.\textsuperscript{56}

Since \textit{Quill}, there have been repeated efforts to expand state taxation of remote sales via congressional action.\textsuperscript{57} Of all of the paragraph, a person making sales of tangible personal property or services taxable under this article ("seller") shall be presumed to be soliciting business through an independent contractor or other representative if the seller enters into an agreement with a resident of this state under which the resident, for a commission or other consideration, directly or indirectly refers potential customers, whether by a link on an internet website or otherwise, to the seller, if the cumulative gross receipts from sales by the seller to customers in the state who are referred to the seller by all residents with this type of an agreement with the seller is in excess of ten thousand dollars during the preceding four quarterly periods ending on the last day of February, May, August, and November. This presumption may be rebutted by proof that the resident with whom the seller has an agreement did not engage in any solicitation in the state on behalf of the seller that would satisfy the nexus requirement of the United States constitution during the four quarterly periods in question. Nothing in this subparagraph shall be construed to narrow the scope of the terms independent contractor or other representative for purposes of subclause (I) of clause (C) of subparagraph (i) of this paragraph").

\textsuperscript{52} Overstock.com, Inc. v. State Dep’t of Taxation & Fin., 987 N.E.2d 621, 622 (N.Y. 2013) (noting that both Amazon.com, LLC and Overstock.com were plaintiffs).

\textsuperscript{53} \textit{Id.} at 622.


\textsuperscript{55} \textit{See generally} Laura Mahoney et al., \textit{ supra} note 48.

\textsuperscript{56} \textit{See, e.g.}, \textit{Id.} ("Amazon has terminated and will not accept new affiliates in Arkansas, Colorado, Maine, Minnesota, Missouri, North Carolina or Rhode Island. Overstock.com Inc. will not accept affiliates in New York, North Carolina, Rhode Island, Illinois, Arkansas or any state in which the law deems Overstock to have nexus for sales and use tax purposes because of affiliate agreements, according to its website.").

proposed bills introduced, the Marketplace Fairness Act\(^5\) (MFA) of 2013 has had the most success. The MFA would permit states that are members to the Streamlined Sales and Use Tax Agreement, or that meet specifications under the MFA, to require sellers to collect and remit sales and use taxes on remote sales.\(^6\) On May 6, 2013, the U.S. Senate passed the MFA by a majority vote of sixty-nine to twenty-seven.\(^7\) However, the bill languished in the House and eventually died.\(^8\) The MFA of 2015\(^9\) was reintroduced in the Senate in March, 2015 and referred to the Senate Committee on Finance, where it remains.\(^10\)

So, for over two decades, the problem has grown. The Supreme Court has not seen fit to overturn \textit{Quill}, and Congress has not accepted the Court’s invitation to address the problem through federal legislation. Meanwhile, the EU has expanded the general scope of the VAT imposed by countries within the Union to include the electronic sale of digital goods and, more recently, to require that remote sellers collect the rate of tax imposed in the country where the consumer purchases those goods.\(^11\)

\section*{II. THE EU VAT SYSTEM AND RELATED ENFORCEMENT ISSUES}

In 2015, the EU updated the general VAT rules applicable to digital companies.\(^12\) The VAT is a broad, general consumption tax assessed on the value added to goods and services at each stage of production.\(^13\) The tax is calculated on each sale as a percentage of the sale price minus the tax paid at previous stages.\(^14\) The 2015

\begin{itemize}
\item \textit{Quill} v. \textit{Vermont}, 454 U.S. 1 (1981);
\item \textit{Quill} v. \textit{North Dakota}, 534 U.S. 283 (2002);
\item \textit{Quill} v. \textit{Mississippi}, 534 U.S. 283 (2002).
\end{itemize}
update built on the EU’s 2003 measure requiring companies located outside the EU to collect the VAT on the sale of goods and services digitally delivered to individual consumers in EU member states.\footnote{68} Under the previous iteration of the rule, businesses selling digital goods into Europe who are “non-established operators” (lacking a fixed establishments in the EU) could charge consumer customers the VAT of a single “member state of identification” with which they have certain connections.\footnote{69} Large digital companies like Amazon and Google neatly minimized the applicable VAT by establishing their member state of identification in countries with favorable VAT rates (generally Luxembourg) and registering all their European sales there.\footnote{70} But, as of January 1, 2015, all digital companies—whether located within or outside the EU—that sell telecommunications, broadcasting, and electronic services to customers in EU countries must collect and report the VAT based on the rate in the country where the customer resides.\footnote{71} The EU has also established a Mini One Stop Shop\footnote{72} (MOSS), which allows payments and returns to be made electronically from a single Member State of Identification.\footnote{73} The applicable tax is broad: there is no minimum sales threshold, and virtually all goods and services that can be purchased and downloaded by retail consumers on the web fall within the scope of the VAT rules.\footnote{74}

In 2003, the EU’s imposition of tax reporting duties on remote sellers of digital goods without a permanent establishment in the EU, even at the single state’s rate, was not without controversy. Although

\begin{itemize}
  \item \footnote{72} The Mini One Stop Shop (MOSS), REVENUE IRISH TAX & CUSTOMS, http://www.revenue.ie/en/tax/vat/leaflets/mini-one-stop-shop.html (last visited May 17, 2016) (“The Mini One Stop Shop is an optional scheme which allows businesses that supply telecommunications, broadcasting or e-services to consumers in Member States in which they do not have an establishment to account for the VAT due on those supplies via a web-portal in one Member State.”).
no complaint was ever formally brought to the World Trade Organization (WTO), Karen Myers, Chairman of the U.S. Council for International Business's Subcommittee on e-Commerce, testified before Congress that the disparity in VAT rates for EU and non-EU firms might violate WTO rules. Like interstate taxation, international taxation is a delicate balance, and there was some discussion of retaliatory taxation from countries outside the EU, including the United States. However, because the consumption taxes in this country are imposed at the state level, rather than at the federal level, it is unclear how any retaliatory taxation would be instigated.

EU countries that impose a VAT have come to rely on a slightly different enforcement approach than that taken by the United States. Because of the nature of the VAT, rather than the ultimate seller having the sole duty to collect, report, and pay over the tax, all sellers in the chain of commerce must report information and collect tax on their sales. Information reported by "up-stream" businesses can therefore be compared with information reported by "down-stream" businesses. Requiring businesses to maintain this information fosters voluntary compliance, even where the information is not automatically provided to the particular tax authority—even especially from businesses that can be expected to regularly maintain detailed information in electronic format.

Even though the VAT enforcement system allows countries to use information reported by businesses in the chain of commerce, when a business is located in a non-VAT country, or a VAT country that does not cooperatively share information, that mechanism can break down. So, for example, while U.S. businesses have been required to


78. Id.

collect the VAT since 2003, there appears to be either a general lack of awareness or a lack of willingness to cooperate.\textsuperscript{80} Regardless of their authority and unquestioned jurisdiction to impose tax, the EU countries can face the same kind of practical difficulties that any enforcement action over a remote actor is bound to face.\textsuperscript{81} Some believe the tax may be unenforceable without the cooperation of the U.S. government:

Enforcement will be difficult without Washington’s help, but Europe’s tax collectors are determined to try. U.S. businesses with a branch office in Europe, for example, could probably be forced to comply. Another option being considered is “blackening out” the Web sites [of] companies that refuse to register for VAT collection. But consider that despite having highly centralized systems of Internet service provision, authoritarian governments (such as China) have been unable to control access to dissident Web sites. The Internet is simply too massive and decentralized to police effectively.

That enforcement problem is why Europe is calling for increased “international collaboration” on tax collection, meaning that the IRS would monitor U.S. companies’ compliance with EU tax law.\textsuperscript{82}

Other efforts have been attempted to augment VAT enforcement. In 2006, the United Kingdom implemented a “Web Robot,” an application designed to spot high-volume traders that fail to register for the VAT.\textsuperscript{83} It is unclear how successful that effort has been, but the Web Robot’s expansion to small businesses and personal ventures in 2011 indicates at least some success.\textsuperscript{84}

In May 2015, the European Commission announced that an estimated €168 billion in VAT revenues had been lost due to noncompliance or non-collection in 2013—amounting to 15.2% of all VAT revenue.\textsuperscript{85} This may be attributable to a lack of awareness of the collection duty, but there is also a possibility that smaller

\begin{itemize}
  \item \textsuperscript{81} See id.
  \item \textsuperscript{83} COMPTROLLER AND AUDITOR GENERAL, UK NATIONAL AUDIT OFFICE, VAT ON E-COMMERCE 6 (2006), https://www.nao.org.uk/report/vat-on-e-commerce.
  \item \textsuperscript{84} See Julia Kollewe, The Dangers of Moonlighting from Work, AOL (June 18, 2011, updated Sept. 30, 2011, 12:22 PM), http://money.aol.co.uk/2011/06/18/the-dangers-of-moonlighting-from-work.
\end{itemize}
companies are ceasing to sell into the EU due to the new rules. There have also been reports that the VAT credit and refund mechanisms, and the administration of those mechanisms, have been the targets of outright fraud. In 2015, the Organisation for Economic Co-operation and Development (OECD) released a report titled *Addressing the Tax Challenges of the Digital Economy*. In the report, the OECD notes that direct-consumption-based taxes on digital commerce raise questions regarding nexus; how to value data generation for tax purposes; and the characterization of transactions generally.

The OECD's report also contains some suggested changes to the enforcement system, including a "significant economic presence" nexus standard. Such a standard might use a sales threshold, or might also consider other "digital factors" when imposing regulatory duties such as whether the seller has obtained a local domain name, uses a local platform, or takes local payment options. It could also look to whether the seller has ongoing customer relationships, and especially whether the seller collects substantial data from those customers. Interestingly, the OECD's report also discusses a withholding mechanism for collecting tax on digital transactions, imposed not on sellers in the chain of commerce, but on payment


88. Id. at 99.

89. Id. at 107 (suggesting this new nexus concept to reflect situations where businesses have a sustained economic presence in a country through digital technology rather than by having a physical presence).

90. Id. at 107–09.

91. Id. at 101; 110–11.
processors, stating: “One possible solution would be to require intermediaries processing the payment [for purchases] to withhold on the payment in a B2C context. As a practical matter, however, this presents several technical issues.” This proposed withholding mechanism, however, would need to be further developed.

To summarize, the EU appears to be committed to imposing tax on sales of digital goods and to taking the necessary steps to enforce that tax even where sellers are outside the EU. Assuming EU countries are successful, the enforcement mechanisms they use may inspire imitation. Their success in enforcing the VAT on sales made by U.S. companies might also create some pressure for the United States to collect sales taxes due on digital goods sold electronically to consumers in this country to level the global playing field.

III. THE SEEDS OF INVENTION

What alternative approach might individual American states take to improve the enforcement system used for sales and use taxes? The “seeds” of such an approach have already been planted.

The first seed of the alternative approach has been around for some years. After Quill, states began experimenting with ways to allow consumers to self-report the tax on their purchases from remote vendors. States also have made an effort to simplify use tax reporting as much as possible for in-state consumers, particularly because many are unaware of the reporting requirement and have failed to keep records of their purchases. For example, California eases the burden on taxpayers by allowing them to report use tax based either on their actual purchases or by using a percentage of their income, using a “look-up table.” This approach, also taken by a number of other states, is further simplified by providing

92. Id. at 114.
96. See Use Tax Collection on Income Tax Returns Reporting and Collections, JUX LAW FIRM, http://jtix.law/use-tax-collection-on-income-tax-returns-reporting-and-collections (last visited May 17, 2016). Professor Richard Pomp states that L.L. Bean was instrumental in getting Maine to adopt a box on its income tax return estimating how much use tax was owed by various income groups in an unsuccessful attempt to
reporting information and instructions. Some data shows that states with look-up tables for reporting use tax have a higher “participation” rate (that is, a higher percentage of taxpayers reporting some amount of tax) but a slightly lower per return amount. In any case, compliance rates are uneven.

These consumer-reporting mechanisms have not been subjected to legal challenges, but they do have two significant downsides. First, if a resident reports no use tax, it may be because she has determined that she does not owe any tax, or it may be that she is simply disregarding her reporting obligation. To determine which is the case, the state would have to perform an audit on that resident. Auditing any significant percentage of resident consumers, however, would be impossible. But the second, and perhaps more important downside, is that it is not clear how the state could possibly verify that additional tax is due, even with an audit, given that most individuals do not regularly keep records of all purchases so that the tax owed can be verified.

The second seed of the alternative enforcement approach for remote sales tax has been suggested in this Article, but has not been applied in the way that it could be. It involves using employers to withhold and pay the use tax owed by resident wage-earners. Those employers already withhold federal and possibly state income taxes and also report unemployment impositions to the states. Perhaps one reason states have not attempted this employer-withholding approach is because it would require the state to assert the amount of tax due for each employee and would also require it to show some reasonable basis for that amount. Also, if taxpayers can simply apply for refunds of the amounts withheld, the state would still need to have some means to verify those refunds.

Colorado has provided the third seed of the alternative approach. Under Colorado law, sellers who are “retailers” and are “doing

---

99. See MAC TAYLOR, CALIFORNIA LEGISLATIVE ANALYST'S OFFICE, UNDERSTANDING CALIFORNIA'S SALES TAX 22 (2015), http://www.lao.ca.gov/reports/2015/finance/sales-tax/understanding-sales-tax-050615.aspx (“Due to data limitations, it is difficult to estimate the 'tax gap'—the difference between taxes owed and taxes paid. Recent estimates indicate that California's use tax gap could be $1 billion or more.”).
business" in the state have a statutory tax collection and reporting duty. But because Quill prevents Colorado from imposing a tax-collection duty on out-of-state sellers that lack physical presence, those retailers that do not collect the tax are instead required to comply with the information-reporting requirements under a statute passed in 2010. This statute requires the seller to provide each purchaser with a notice that tax has not been collected and will have to be paid by the purchaser. The seller must also mail annual notices to Colorado customers who purchased more than $500 in goods from them in the preceding calendar year, informing the customer of purchase dates, items bought, and the amount of each purchase made. Finally, the seller must annually report information on Colorado purchasers to the state revenue department, including purchasers' names, billing addresses, shipping addresses, and total purchase amounts for the previous calendar year. While Colorado has taken the lead in implementing this information reporting approach, other states may well decide to follow that lead. For several years, states in the Multistate Tax Commission's Executive and Uniformity Committees have been working on a model statute using this approach.

Information supplied by sellers under this type of information-reporting system could address both the issue of how a state might verify that resident self-reported tax is accurate, and how states might determine amounts to be withheld under an employer-withholding system. But, the Colorado law was quickly challenged by sellers who dispute its constitutionality. The Tenth Circuit ultimately rejected that challenge, and its ruling is discussed further in the next section.

102. COLO. REV. STAT. § 39-21-112(3.5) (2010).
103. COLO. CODE REGS. § 201-1:39-21-112.3.5(2) (2010).
104. COLO. CODE REGS. § 201-1:39-21-112.3.5(3)(a)(ii).
105. COLO. REV. STAT. § 39-21-112(3.5)(d)(II)(A).
Building on Colorado law, the approach suggested here would require states to do the following: (1) collect data from remote sellers on sales made to in-state residents, broken down by general taxable category; (2) use that data to determine the tax amounts owed by in-state residents (consumers) on remote purchases; and (3) inform residents of the tax due and provide their employers with the information allowing them to withhold the tax from wages paid. So, for example, based on information reported by remote sellers, the state might determine that a resident made $1000 of remote taxable purchases in the prior year. Assuming an eight percent tax rate, the resident would owe eighty dollars. Rather than requiring the resident to pay this tax directly to the state all at once, the state could allow the resident’s employer to withhold the tax and pay it over to the state. Assuming the employee is paid monthly in this case, the employer would withhold $6.14 each pay period. States might determine that it is necessary to impose other requirements as well. For example, the withholding mechanism might apply only up to a maximum amount. So, if the resident owed more than $200 in total tax, for instance, the excess would have to be paid immediately or interest might also be assessed. States might impose a requirement for paying estimated taxes, based on similar criteria used for income taxes.\textsuperscript{108} Residents who are not currently employed would also have to pay the tax directly, or perhaps through estimated quarterly payments.\textsuperscript{109}

Whether such an approach could be adopted depends on whether we expect the Tenth Circuit’s ruling to be the final word and perhaps whether certain other legal questions can be answered, as discussed further in the next section. But it also ultimately depends on the technical feasibility of this approach—and in particular, whether remote sellers would be able to provide the information necessary. So, a little perspective on the issue of feasibility is in order before its legal analysis.

In 1992, when Quill upheld the bright-line physical presence rule\textsuperscript{110} of Bellas Hess,\textsuperscript{111} no one had yet made an online retail purchase.\textsuperscript{112} The first World Wide Web server and browser, created by Tim Berners-Lee in 1990, opened for commercial use in 1991, the year

\begin{itemize}
\item \textsuperscript{108} See 26 U.S.C. \textsection 6654(d)(1)(B) (2012).
\item \textsuperscript{109} See 26 U.S.C. \textsection 6654(c).
\item \textsuperscript{111} Nat’l Bellas Hess, Inc. v. Dep’t of Revenue, 386 U.S. 753, 758-59 (1967).
\item \textsuperscript{112} See Dave Roos, \textit{The History of E-commerce, HOWSTUFFWORKS.COM} (Apr. 15, 2008), http://money.howstuffworks.com/history-e-commerce.htm (stating that the first processors of online credit card sales emerged in 1994 and 1995).
\end{itemize}
litigation began in *Quill*. That year, the National Science Foundation eliminated a ban on commercial businesses operating over the Internet, which allowed for the possibility of Web-based e-commerce. The first secured online purchase did not take place until 1994. From there, Internet sales skyrocketed, largely due to the development of security protocols and high speed Internet connections such as Digital Subscriber Line (DSL), making faster connection speeds and faster online transaction capability possible.

In 2010, the Boston Consulting Group determined that the Internet accounted for 4.7% of all U.S. economic activity in that year, exceeding the contributions of the federal government (4.3%). If the Internet was considered its own industry, it would be larger than the United States’ education, constructions, or agricultural industries. According to a 2014 online retail sales forecast from Forrester Research Inc., U.S. e-retail sales (that is, consumer sales) are expected to grow from $263 billion in 2013 to $414 billion in 2018, amounting to a total annual growth rate of 9.5%. The study predicts that e-retail’s share of total retail sales will continue to increase, from eight percent in 2013 to eleven percent in 2018. This forecasted growth from $263 billion in 2013 to $414 billion in 2018 is a 57.4% increase in the dollar amount of consumer sales. Contrast these online sales with $180 billion in remote (mail-order) sales in 1992.

The technology that enables Internet retailers to be so competitive with each other also gives them distinct competitive advantages over brick-and-mortar stores. Internet retailers require minimal downtime, and can remain open twenty-four hours a day, year-round.

114. Roos, *supra* note 112.
118. Id.
120. Id.
121. Id.
Retail websites are a natural extension of the social networking community because large online retailers generally offer customers the opportunity to post comments on, and see reviews of, every aspect of a product. Online shopping also offers easy price comparison—an ability that has overlapped into the real world: Amazon now offers a price-checking app that allows shoppers to scan a product at the mall and purchase it online.

When it comes to their ability to collect information, online sellers clearly have advantages. In the world of online sales, information is currency; online sellers habitually track purchasers' activities in order to target their marketing. Internet retailers collect and purchase an incredible range of information:

[Stores collect] demographic information like your age, whether you are married and have kids, which part of town you live in, how long it takes you to drive to the store, your estimated salary, whether [you have] moved recently, what credit cards you carry in your wallet and what Web sites you visit. [Stores] can buy data about your ethnicity, job history, the magazines you read, if [you have] ever declared bankruptcy or got divorced, the year you bought (or lost) your house, where you went to college, what kinds of topics you talk about online, whether you prefer certain brands of coffee, paper towels, cereal or applesauce, your political leanings, reading habits, charitable giving and the number of cars you own.

---


126. Id.; see also Andrew McAfee & Erik Brynjolfsson, Big Data: The Management Revolution, HARV. BUS. REV. (Oct. 2012), https://hbr.org/2012/10/big-data-the-management-revolution/ar (“It is estimated that Walmart collects more than 2.5 petabytes of data every hour from its customer transactions. A petabyte is one quadrillion bytes, or the equivalent of about 20 million filing cabinets’ worth of text.”).
Online sellers use this data with great success to prompt online purchases. For example, via its data collection, Target may infer that a woman is pregnant—and start targeting her with relevant advertisements—before anyone else knows. Amazon, meanwhile, has patented what it calls “anticipatory shipping,” a method through which it can begin delivering packages even before a customer clicks “buy.”

Hulu publicizes the fact that it can provide targeted local advertisements based on Nielsen DMA, state, or zip code. It knows when an advertisement has been viewed to completion, and bases its fees on that metric. In April 2015, Hulu announced its plan to pair with advertisers to make co-branded advertisements. In answer to the question of “why a brand would want to pay extra money to create a co-branded ad specifically to run on Hulu,” Hulu responds that its user data helps make more targeted ads. “We’re using our insights to how our users search the site, come back, content they’re watching, what platforms they’re watching [on],” says said Hulu’s senior VP-advertising sales Peter Naylor.

Given the technology Internet sellers have developed to enable them to successfully grow and compete, it is not unreasonable to expect that these sellers could also report amounts of sales made to customers by state and according to certain general categories. This information would enable states to then determine the use taxes likely owed by residents and to, if necessary, respond to any refund claims or contested assessments.

IV. POTENTIAL LEGAL OR OTHER IMPEDIMENTS

It does not appear that there are any serious legal constraints on the states that would prevent them from using information to determine and assess tax directly to resident purchasers. Nor does it appear that there is any impediment to requiring an employer to

127. See McAfee & Brynjolfsson, supra note 126.
128. Duhigg, supra note 125.
131. Id.
133. Id.
134. Id.
withhold the tax from resident-employee wages. Of course, even private parties are sometimes entitled to collect debts from employees through garnishments, facilitated by employer withholding. But there are potential obstacles to imposing a requirement on sellers to provide the necessary information: possible ongoing constitutional challenges to information reporting requirements including a potential First Amendment challenge, and a possible challenge under the "discriminatory tax" provision of the Internet Tax Freedom Act.135

A. The Constitutional Challenge to Colorado's Information Reporting Requirements

After Colorado enacted its information reporting requirements, remote sellers immediately objected, acting through the Direct Marketing Association (DMA)—a trade association of retailers, many of which sell to Colorado residents but do not collect sales and use taxes.136 DMA filed suit claiming the notice and reporting requirements violated the dormant Commerce Clause by discriminating against and unduly burdening interstate commerce.137

The case rose to the Supreme Court, but not on the merits of the constitutional claims; instead, the issue concerned the Tenth Circuit's finding that the Tax Injunction Act (TIA) deprived the district court of jurisdiction over the suit.138 The TIA prohibits federal courts from hearing suits involving the "assessment, levy or collection" of a state tax. The Supreme Court reversed the Tenth Circuit's ruling, concluding that for purposes of the TIA, the Colorado notice and reporting requirement was not an "assessment, levy, or collection" of a tax.139

This conclusion proved important in the ultimate determination of the constitutional challenge on remand, as well.140

In general, the DMA faced a high bar. Lawmakers have great latitude in adopting policies that differentiate between groups of taxpayers. In the absence of any constitutional protection, the default standard for evaluating any differences in state tax treatment

137. Id. at 1128.
138. Id. at 1129.
139. Id.
140. This argument, that the Tax Injunction Act (TIA) issue and the determination of the merits are connected, was made before the Supreme Court. See, e.g., Brief of Interested Law Professors as Amici Curiae at 15–17, Direct Mktg. Ass’n v. Brohl, 814 F.3d 1129 (10th Cir. 2016) (No. 12-1175), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2608807.
is rational basis. Under the Commerce Clause, however, state laws may not discriminate against interstate commerce. In general, the Supreme Court's modern dormant Commerce Clause doctrine focuses on preventing economic protectionism. Such protectionism may be represented by barriers to entry imposed on out-of-state businesses. Or it may emanate from state laws that burden out-of-state business interests and benefit instate interests.

The issue for the Tenth Circuit in DMA was unusual in that it could have fallen between two recognized lines of Supreme Court precedent. One line involves state tax laws as applied to out-of-state businesses and to interstate commerce generally. The other line of cases involves state regulatory rules that may impact interstate commerce or apply to out-of-state businesses. How the Tenth Circuit evaluated the discrimination depended on which line of cases applied. But regardless, the claim before it had to include two fundamental elements: (1) differential treatment that actually disfavors the challengers vis-à-vis another group, and (2) some basis for asserting that the Commerce Clause entitles the challengers, as a class, to a more exacting review of this differential treatment. Otherwise, as discussed above, the treatment would have fallen within the legislature's broad discretion.

144. See Sporhase v. Nebraska, 458 U.S. 941, 944, 960 (1982) (striking down Nebraska’s statutory scheme of issuing permits allowing the withdrawal of ground water in Nebraska for transport and use in a different state only if such state grants reciprocal rights for groundwater to be withdrawn and transported to Nebraska).
145. Oregon Waste Sys., Inc., 511 U.S. at 99 (explaining that if a state statute discriminates against interstate commerce by effecting “differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter,” it is per se invalid).
146. See Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 276 (1977) (involving a tax assessed by Mississippi against a Michigan motor carrier that transported automobiles into Jackson, Mississippi via railroad from out-of-state locations and then delivered the automobiles to in-state car dealers via trucks).
147. See Pike v. Bruce Church, Inc., 397 U.S. 137, 138 (1970) (involving an agricultural company with operations in Arizona and California burdened by Arizona law requiring cantaloupes to be packaged in a certain manner before being transported across state lines).
149. See supra notes 141–42 and accompanying text.
Upon remand of the case from the Supreme Court, the Tenth Circuit, on February 22, 2016, ruled in favor of Colorado on the merits.\textsuperscript{150} It appears to have based its decision in significant part on the Supreme Court's treatment of the TIA issue. In addition to having determined that Colorado's information reporting requirements were not tax "collection" under the TIA, the Supreme Court had also explicitly characterized \textit{Quill}'s rule as applying to "tax collection."\textsuperscript{151} As far as the Tenth Circuit was concerned, this greatly weakened the DMA's claims of discrimination and undue burden.\textsuperscript{152}

More specifically, the circuit court of appeals rejected the DMA's claim that information reporting requirements facially discriminated against out-of-state retailers because, as a group, out-of-state companies with some physical presence in the state were regularly subject to tax collection obligations rather than information reporting.\textsuperscript{153} Therefore, it was not a company's geographic location that determined whether it was subject to the information reporting requirements, but rather whether it could be required, under \textit{Quill}, to collect tax.\textsuperscript{154}

The Tenth Circuit also concluded that the information requirements were not discriminatory in their effect.\textsuperscript{155} It rejected the DMA's claim that "any differential treatment" between in-state and out-of-state entities can establish unconstitutional discrimination.\textsuperscript{156} And, since Colorado consumers legally owed tax regardless of whether the seller collected it or only reported information to the state, the DMA could not argue that the information reporting requirements put remote retailers at some competitive disadvantage.\textsuperscript{157} Moreover, the DMA had not shown that the remote sellers it represented were similarly situated with any comparison class of retailers for discrimination purposes.\textsuperscript{158} And finally, the DMA had also not shown the requirements imposed a discriminatory economic burden on remote vendors when compared with the burden imposed on collecting sellers.\textsuperscript{159} As far as the undue

\begin{itemize}
\item\textsuperscript{150} Direct Mktg. Ass'n v. Brohl, 814 F.3d 1129 (10th Cir. 2016).
\item\textsuperscript{151} \textit{Id.} at 1137 (emphasizing the Supreme Court's characterization of \textit{Quill} as establishing a principle concerning the requirement to collect taxes).
\item\textsuperscript{152} \textit{Id.} at 1139.
\item\textsuperscript{153} \textit{Id.} at 1141.
\item\textsuperscript{154} \textit{Id.}
\item\textsuperscript{155} \textit{Id.} at 1141-42.
\item\textsuperscript{156} \textit{Id.} at 1142.
\item\textsuperscript{157} \textit{Id.} at 1143.
\item\textsuperscript{158} \textit{Id.}
\item\textsuperscript{159} \textit{Id.} at 1142-44.
\end{itemize}
burden claim, the circuit court of appeals relied almost entirely on the Supreme Court's holding that the information reporting requirements were not the equivalent of tax collection under the TIA and thus Quill was not controlling.¹⁶⁰

A concurrence filed by Tenth Circuit Judge Gorsuch provides support for those who are considering whether an alternative approach to use tax enforcement is feasible—at least from a legal standpoint.¹⁶¹ Prompted by the DMA's arguments, Judge Gorsuch pondered the possibility that "many (all?) states can be expected to follow Colorado’s lead" and concluded that the Supreme Court, by reinforcing a rule the Justices themselves admitted was "formalistic" and "artificial," had virtually "invited states to impose comparable duties" in response.¹⁶² He went on to explain:

In this way, Quill might be said to have attached a sort of expiration date for mail order and [I]nternet vendors' reliance interests . . . by perpetuating its rule for the time being while also encouraging states over time to find ways of achieving comparable results through different means. In this way too Quill is perhaps unusual but hardly unprecedented, for while some precedential islands manage to survive indefinitely even when surrounded by a sea of contrary law, a good many others disappear when reliance interests never form around them or erode over time. And Quill’s very reasoning—its ratio decidendi—seems deliberately designed to ensure that Bellas Hess’s precedential island would never expand but would, if anything, wash away with the tides of time.¹⁶³

The challenge to Colorado-style information reporting requirements may not be over. The DMA could petition the Supreme Court to review the Tenth Circuit’s ruling and challenges could also be raised if other states pass similar statutes. The Supreme Court could easily reach the same conclusion as the Tenth Circuit—that the information-reporting requirements imposed on remote sellers are essentially a derivative set of the requirements imposed on all sellers.¹⁶⁴ It might also be difficult for the DMA to convince the

¹⁶⁰. Id. at 1145–46.
¹⁶¹. Id. at 1147–48 (Gorsuch, J., concurring).
¹⁶². Id. at 1151.
¹⁶³. Id.
¹⁶⁴. See Alabama Dep’t of Revenue v. CSX Transp., Inc., 135 S. Ct. 1136, 1143–44 (2015) (rejecting arguments by a rail carrier that, under a provision of the federal “4-R Act” generally prohibiting taxes “that discriminate,” the railroad need only show that the state imposed one tax on its fuel purchases because a separate, but possibly equivalent, tax was imposed on purchases by competitors); Associated Indus. of Mo. v. Lohman, 511 U.S. 641, 649–50, 656 (1994) (rejecting out-of-state businesses'
Court that its remote-seller members, as a class, are entitled to a heightened standard of review. Normally, if differential treatment does not depend on whether the affected businesses operate primarily outside the state, then the Commerce Clause will not prevent that differential treatment.\textsuperscript{165}

It should be noted that, outside of the sales tax arena, states have sometimes imposed differential reporting requirements related to tax enforcement on parties outside the state. For example, states may require out-of-state businesses to provide information to establish that they are not doing business in the state so as to be subject to a particular tax. States may require partnerships with activities in the state to withhold and report income tax for nonresident partners.\textsuperscript{166}

It seems unlikely that the Supreme Court would now apply \textit{Quill} so as to create some sort of special sub-class of out-of-state businesses entitled to more favorable treatment generally than other out-of-state businesses. No case has ever held that \textit{Quill} applies to create such a sub-class for any purpose other than protecting out-of-state sellers without physical presence from tax collection duties. Justice Kennedy, writing separately in \textit{DMA}, characterized \textit{Quill}'s holding as “tenuous” and placed the blame on stare decisis.\textsuperscript{167} Justice Kennedy also cited \textit{Pearson v. Callahan}\textsuperscript{168} for the proposition that stare decisis is weakened where “experience has pointed up the precedent’s shortcomings.”\textsuperscript{169}

\textbf{B. Potential First Amendment Challenge}

In addition to claiming that the Colorado information-reporting requirements violated the Commerce Clause, the DMA also claimed that

\begin{itemize}
\item \textsuperscript{165} See \textit{Gen. Motors Corp. v. Tracy}, 519 U.S. 278, 298–99 (1997) (explaining that differential tax treatment of out-of-state businesses is not discriminatory where the treatment is due to differences in the products those businesses provide); \textit{see also} \textit{Exxon Corp. v. Governor of Md.}, 437 U.S. 117, 126 (1978) (holding that “[t]he fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination against interstate commerce”).
\item \textsuperscript{167} \textit{Direct Mktg. Ass’n v. Brohl}, 135 S. Ct. 1124, 1134 (2015) (Kennedy, J., concurring) (noting that that the Court relied on the doctrine “to reaffirm the physical presence requirement . . . despite the fact that under the more recent and refined test elaborated in \textit{Complete Auto Transit, Inc. v. Brady}, ‘contemporary Commerce Clause jurisprudence might not dictate the same result’ as the Court had reached in \textit{Bellas Hess.”} (internal citations omitted)).
\item \textsuperscript{168} \textit{555 U.S. 223} (2009).
\item \textsuperscript{169} \textit{DMA}, 135 S. Ct. at 1135 (Kennedy, J., concurring) (citing \textit{Pearson}, 555 U.S. at 233).
\end{itemize}
they violated customers’ free speech rights under the First Amendment.\textsuperscript{170} The DMA did not include those claims in its Motion for Preliminary Injunction and Incorporated Memorandum of Law, but noted:

The DMA in its Complaint contends that the Act and Regulations chill the exercise of free speech of both consumers and retailers, trample the right to privacy of consumers, and deprive retailers of proprietary, trade secret information without due process or fair compensation.\ldots These claims present important issues of constitutional law, some of which are matters of first impression, regarding the extent to which customer purchase information is protected by the Constitution and whether the government may compel disclosure of such information from businesses without any procedures that allow either the customer or the retailer to raise objections before the disclosure is made or penalties attach.\textsuperscript{171}

It is difficult to know exactly what DMA expects to allege if this claim should ever be litigated, but there is one other federal district court that has addressed the issue: the U.S. District Court for the Western District of Washington in \textit{Amazon.com LLC v. Lay.}\textsuperscript{172} In 2009, the North Carolina Department of Revenue (DOR) audited Amazon and sent a request to the Internet retailer seeking “all information for all sales to customers with a North Carolina shipping address by month in an electronic format.”\textsuperscript{173} In response, Amazon provided the DOR with “detailed information about millions of purchases made by North Carolina customers” along with “the Amazon Specific Identification Number ("ASIN") for every purchase,\ldots which permits access to the specific and detailed description of the product,” but without customer-identifying information.\textsuperscript{174} When asked for this information, Amazon refused and filed suit in federal district court alleging that the state’s request for this information would violate its customers’ free speech rights.\textsuperscript{175}

While it appears that North Carolina did not seek and did not intend for Amazon to provide purchase information for in-state customers that identified specific products, the state refused to return the initial information Amazon provided while it was negotiating with


\textsuperscript{172} 758 F. Supp. 2d 1154 (W.D. Wash. 2010).

\textsuperscript{173} \textit{Id.} at 1159.

\textsuperscript{174} \textit{Id.}

\textsuperscript{175} \textit{Id.} at 1159–60.
the company to provide the other information needed.\textsuperscript{176} The federal district court ultimately concluded that Amazon was entitled to summary judgment on its First Amendment claim, stating that "[t]he First Amendment protects a buyer from having the expressive content of her purchase of books, music, and audiovisual materials disclosed to the government."\textsuperscript{177} The court reasoned that the fear of government tracking would chill a customer's choice of what to read or watch or listen to.\textsuperscript{178} North Carolina could not show a compelling reason to keep the purchase information because it admitted that it had no need or use for the details of its residents' purchases.\textsuperscript{179}

It seems that in most cases, First Amendment issues can be avoided by ensuring that information required does not contain the details of certain types of products purchased. Because sales and use tax exemptions generally follow broad categories, observing this limitation would not unduly hamper the proper calculation of tax.\textsuperscript{180}

\textbf{C. The "Non-Discrimination" Provision of the Internet Tax Freedom Act}

The Internet Tax Freedom Act (ITFA) prohibits "multiple or discriminatory taxes on electronic commerce."\textsuperscript{181} The term "electronic commerce" generally includes all manner of commercial transactions conducted over the Internet.\textsuperscript{182} The term "discriminatory tax" is broadly defined. It includes a tax imposed on Internet transactions unless the tax is also imposed (at rate that is the same or higher) on transactions involving similar goods or services.
accomplished through other means. A “discriminatory tax” also includes a collection obligation that is imposed on “a different person or entity than in the case of transactions involving similar . . . goods . . . accomplished through other means.” And it includes any tax imposed where “the sole ability to access a site on a remote seller’s out-of-[s]tate computer server is considered a factor in determining a remote seller’s tax collection obligation.” It further includes a tax collection obligation that is imposed because “a provider of Internet access service or online services is deemed to be the agent of a remote seller . . . as a result of the display of a remote seller’s information or content on the [provider’s] out-of-[s]tate computer server.” Finally, it includes a tax collection obligation imposed because the provider is deemed to be the agent of the remote seller “solely as the result of . . . the processing of orders through the out-of-[s]tate computer server of a provider.”

Because of ITFA, care must be taken in how tax or tax collection duties are imposed on all sales across the Internet, including sales of digital goods. It appears that ITFA’s provisions are concerned with imposing tax-collection obligations on e-commerce. There is no prohibition under ITFA that would prohibit states from imposing information-reporting requirements related to sales made into a state for the purpose of use tax enforcement. Therefore, to the extent third parties, including Internet providers or other intermediaries, have information that can be useful to states for determining resident use tax liabilities, imposing an information-reporting requirement would be permissible, even though imposing a tax-collection obligation would not.

Whether ITFA imposes any restraint on the ability of states to impose on employers an obligation to withhold an amount for payment of an employee’s use tax is less clear. It is at least arguable that this might be covered by ITFA’s definition of “discriminatory tax” as including a collection obligation imposed on “a different person or entity than in the case of transactions involving similar . . .
goods . . . accomplished through other means." ¹⁸⁹ There have been few challenges to a state tax under ITFA's "discriminatory tax" provision. ¹⁹⁰ But in one, the Illinois Supreme Court ruled that, under ITFA, "performance marketing" (the use of certain marketing approaches, which sellers pay for based on sales made) cannot be the basis for asserting nexus over sellers that use the Internet unless the state also asserts nexus on the basis of performance marketing done through broadcast media or otherwise in Illinois. ¹⁹¹ Similarly, therefore, assuming the definition of "discriminatory tax" might cover employer withholding of use tax, it would only apply if the tax to be withheld was limited to tax on goods sold over the Internet. Employer withholding certainly need not be limited to tax on goods sold over the Internet. Rather, states could impose the withholder-collection requirement on any tax determined to be due on purchases by residents where the seller does not include the tax, regardless of how the sale is made.

CONCLUSION

This Article proposes that, depending on the ultimate outcome of the DMA case and possibly similar litigation, states may have the opportunity to bypass both Congress and the Supreme Court in finding an alternative that will allow them to better enforce the sales and use tax on remote sales. Of course, this begs the question whether the DMA case itself might not someday end up back at the Supreme Court. With respect to that prospect, the authors make no prediction. But assuming Colorado-style information-reporting requirements withstand challenges by remote sellers the states may want to contemplate how information reporting could, at least, supplement the existing enforcement system and give them the means to ensure that residents are paying the tax owed with as little additional burden as possible. This further assumes—the authors think, safely—that there has been and will continue to be a revolution in information technology that will permit this adaptation. It is, after all, this same technology that has, in large part, created the problem with the existing enforcement system.

¹⁸⁹. ITFA § 1104(2)(A)(iii).