

ORIGINAL

In The  
Supreme Court of Ohio

NEWEGG, INC., :  
Appellant, : Case No. 2015-0483  
v. : Appeal from the Ohio Board of  
JOSEPH W. TESTA, : Tax Appeals, BTA Case No. 2012-234  
TAX COMMISSIONER OF OHIO, :  
Appellee. :

NOTICE OF CROSS APPEAL

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## NOTICE OF CROSS-APPEAL

Joseph W. Testa, Tax Commissioner of Ohio (“Commissioner”), hereby gives notice of his cross appeal to the Supreme Court of Ohio from a Decision and Order of the Ohio Board of Tax Appeals (the “BTA”) journalized in Case No. 2012-234 on February 26, 2015 (hereafter “*BTA Decision and Order*”). A true copy of the *BTA Decision and Order* being appealed is attached hereto as Exhibit A and incorporated herein by reference.

This cross appeal is taken as a matter of right pursuant to Ohio Revised Code (“R.C.”) 5717.04, which provides, in part, that “[i]f a timely notice of appeal is filed by a party, any other party may file a notice of appeal within ten days of the date the first notice of appeal was filed or within the time otherwise prescribed in this section, whichever is later.”

### Procedural Posture

In this appeal, on March 25, 2015, Newegg, Inc. (hereafter “Newegg”), filed a notice of appeal to this Court from the *BTA Decision and Order*. Accordingly, pursuant to the above-quoted language of R.C. 5717.04, the Commissioner hereby timely files this protective cross-appeal.

The appeal by Newegg and this cross-appeal filed by the Commissioner herein involve the Tax Commissioner’s assessment of Commercial Activity Tax (CAT) assessment for unpaid tax for the period from 2005 to 2011 pursuant to R.C. 5751.01(H)(3). Because Newegg’s sales of goods to Ohio consumers produced taxable gross receipts exceeding \$500,000 each year during the 2005-2012 taxable periods at issue, the Tax Commissioner applied the plain language of the bright-line statutory standard to determine that Newegg had “substantial nexus with this state” as the General Assembly has defined that phrase for CAT purposes in R.C. 5751.01(H)(3) and R.C. 5751.01(I)(3) and was therefore subject to the CAT.

In its Notices of Appeal to the BTA, rather than challenging the constitutionality of the Tax Commissioner's actions or the relevant statutes, Newegg pinned its argument to the statutory exclusion from gross receipts set forth in former R.C. 5751.01(F)(2)(aa) of "any receipts for which the tax imposed by this chapter is prohibited by the Constitution or laws of the United States or the Constitution of Ohio."

Newegg argued that the U.S. Supreme Court's dormant Commerce Clause jurisprudence was incorporated through this exclusion statute as "tax . . . prohibited by the Constitution . . . of the United States." In Newegg's view, R.C. 5751.01(F)(2)(aa) places a duty on the Tax Commissioner to determine whether the person who earned receipts constitutionally may be taxed. Under R.C. 5751.01(F)(2)(aa), Newegg argued to the BTA that the Tax Commissioner must apply his understanding of the U.S. Supreme Court's dormant Commerce Clause jurisprudence to determine the taxability of each taxpayer, without regard to the clear-cut Ohio CAT statutes that define substantial nexus.

But the statute is an exclusion from gross receipts, not an incorporation of federal common law. And the Tax Commissioner demonstrated to the BTA that Newegg's arguments didn't hold water. Contrary to Newegg's reading, this division of the statute has nothing to do with the issue of whether Newegg, as a business entity engaged in commercial activities, has constitutional nexus with Ohio. R.C. 5751.01(F)(2)(aa) delineates the taxability of certain receipts, as opposed to persons subject to the CAT.

The import of R.C. 5751.01(F)(2)(aa) is to exclude certain receipts that, by their very nature, may not be taxed. For example, Ohio could not collect a tax on receipts for which the federal government had already, and lawfully, excluded from state taxability under the inter-governmental tax immunity doctrine. Still, this division has nothing to do with the taxability of

the business itself—indeed, Ohio could find that some, but not all, of a person’s receipts are excluded from the definition of “gross receipts” under R.C. 5751.01(F)(2)(aa).

Further, the statute cannot be construed as Newegg suggests, because it would be at odds with R.C. 5751.02, which instructs that the CAT tax applies to persons *whether or not* they have substantial nexus with the state. R.C. 5751.02 (“Persons on which the commercial activity tax is levied include, *but are not limited to*, persons with substantial nexus with this state.” Likewise, Newegg’s misinterpretation would render meaningless express language of R.C. 5751.01(H)(3) and (I) of the CAT defining “substantial nexus,” and “bright-line presence,” respectively, and would completely eviscerate the meaning of R.C. 5751.01(I)(3).

Thus, Newegg’s proposed interpretation of a statute that provides an exclusion from gross receipts puts that statute squarely at odds with the *very statute that levies the CAT*. In reality, any valid challenge raised by a taxpayer based on a claimed lack of substantial nexus with Ohio would necessarily depend on challenging the constitutionality of R.C. 5751.02, which Newegg has not done in this case. As such, Newegg’s statutory arguments were easily dispelled by the BTA.

Further, the Tax Commissioner explained to the BTA that Newegg chose not to challenge the constitutionality of the CAT nexus provisions head-on, but adopted this statutory construction argument as a litigation strategy to skirt the rocks and shoals that accompany a true constitutional challenge.

The BTA’s order held that Newegg did not raise an as-applied constitutional challenge, but merely tried to incorporate the federal Commerce Clause jurisprudence as a matter of statutory construction. Indeed, the BTA recognized that “The parties hereto agree that Newegg has not challenged the constitutionality of the relevant statutes, but has instead, challenged the

commissioner's conclusion that Newegg is liable for the commercial activity tax, which Newegg argues is prohibited by the U.S. Constitution.” *BTA Decision and Order* at unnumbered page 3. Accordingly, the BTA considered Newegg’s arguments only in the context of statutory interpretation as receipts “excluded” from the definition of “gross receipts” under R.C. 5751.01(F)(2)(aa): “Specifically, Newegg claims its gross receipts are *excluded* from the CAT, pursuant to the U.S. Constitution, Commerce Clause, and the ‘substantial nexus’ and corresponding ‘in-state presence analysis encountered thereunder. See R.C. 5751.01(F)(2)(*aa*).” (Emphasis added). *BTA Decision and Order* at unnumbered page 3.

The BTA had no difficulty concluding that Newegg’s attempt to incorporate the federal Commerce Clause jurisprudence as a matter of statutory construction to override the General Assembly’s interpretation was foreclosed by the plain operation of the CAT statutes that apply *regardless* of whether the taxpayer has “substantial nexus” under the U.S. Supreme Court’s Commerce Clause jurisprudence. As the BTA held, “[e]ven without considering any constitutional claims, however, we conclude, *under the plain language set forth therein*, the pertinent CAT statutes do not impose such an in-state presence requirement (emphasis added).” *BTA Decision and Order* at unnumbered page 4. And “[W]e are constrained to follow the mandate of the General Assembly in concluding that appellant, an out-of-state seller, has substantial nexus within this state by virtue of its gross receipts for the reporting periods in question.” *Id.* (quoting from *L.L. Bean, Inc. v. Levin* (Mar. 6, 2014), BTA No. 2010-2859).

The BTA did recognize a limit to its own jurisdiction, stating that “[a]ny constitutional implications of the relevant statutory authority must be considered by a tribunal that has jurisdiction over such questions of constitutional interpretation.” *Id.* at unnumbered page 3. However, in light of the BTA’s holding that Newegg did not advance a constitutional claim, and

that the statutory interpretation advanced by Newegg was fatally defective, this statement was mere dicta.

Moreover, the BTA did not, in any part of its decision, hold that Newegg had properly raised an as-applied constitutional challenge in its Notices of Appeal. Indeed, Newegg recognized that the BTA held that Newegg failed to raise an as-applied constitutional challenge, to which Newegg assigns error in its appeal to this Court, or alternately argues that this language applied only to a “facial challenge.” See Newegg’s Notice of Appeal at 10, ¶ 5. In support, Newegg cites the BTA’s Decision on page 3, wherein the BTA quotes Newegg’s Assigned Errors to the BTA. *Id.* But this is disingenuous. The BTA does not at all state that Newegg raised an as-applied challenge. Instead, the decision merely reproduces, verbatim, all of Newegg’s assignments of error, none of which contain an as-applied challenge to the constitutionality of Ohio’s CAT statutes.

This lack of an as-applied challenge in Newegg’s Notices of Appeal to the BTA means that this Court has no jurisdiction over such challenges. This Court has held that one who challenges the constitutionality of the Tax Commissioner’s application of a tax statute to particular facts is required to raise that challenge at the first available opportunity during proceedings before the Tax Commissioner. See, *Cleveland Gear Co. v. Limbach*, 35 Ohio St. 3d 229, 229, (1988), syllabus at 2 (“The question of whether a tax statute is unconstitutional when applied to a particular state of facts must be raised in the notice of appeal to the Board of Tax Appeals, and the Board of Tax Appeals must receive evidence concerning this question if presented, even though the Board of Tax Appeals may not declare the statute unconstitutional.”); see also, *Bd. of Educ. of S.-W. City Sch. v. Kinney*, 24 Ohio St. 3d 184, 185-187 (1986), citing *Sun Finance & Loan Co. v. Kosydar* (1976), 45 Ohio St.2d 283, 284, fn. 1. Otherwise, it would

be “impossible to develop the factual record necessary for the resolution of the case.” *Bd. of Educ. of S.-W. City Sch.*, 24 Ohio St. 3d at 186, citing *Petrocon v. Kosydar*, 38 Ohio St.2d 264 (1974). Therefore, a failure to properly raise such a constitutional challenge constitutes a waiver of that issue. *Bd. of Educ. of S.-W. City Sch.*, 24 Ohio St. 3d at 186. Moreover, when the Tax Commissioner’s Final Determination does not resolve a particular error (because it was not raised by the taxpayer), then there is no basis for appeal regarding that error. *CNG Dev. Co. v. Limbach*, 63 Ohio St.3d 28, 32 (1992).

To be sure, Newegg may raise a facial challenge to the constitutionality of these statutes for the first time before this Court. See, *Cleveland Gear Co. v. Limbach*, 35 Ohio St. 3d 229, 229, (1988), syllabus at 1. But the as-applied challenge is jurisdictionally foreclosed.

Therefore no as-applied challenge to the CAT is properly before this Court. By failing to raise it at the BTA, Newegg cannot raise it now.

Still, in an abundance of caution, the Tax Commissioner files this Cross-Appeal protectively and conditionally, in the event that this Court were to find that the BTA stated or held that Newegg did raise an as-applied challenge to the constitutionality of the CAT statutes in its Notices of Appeal to the BTA. Hereby, the Tax Commissioner preserves his right to make challenges thereto.

**Errors in the Decision of the BTA:**

As cross-appellant, the Tax Commissioner complains of the following errors in the Decision and Order of the Board:

1. The BTA erred, as a matter of fact and law, to the extent that it stated or held in its BTA Decision and Order that Newegg had raised an as-applied challenge to the constitutionality of any statutes in its Notices of Appeals to the BTA.

2. To the extent that the BTA stated or held in its BTA Decision and Order that Newegg had raised an as-applied challenge to the constitutionality of any statutes in its Notices of Appeal to the BTA, the BTA erred, as a matter of fact and law, because, by their express terms, Newegg's Notices of Appeal to the BTA contained no as-applied challenges to the constitutionality of any CAT statutes. R.C. 5717.02; *Cleveland Gear Co. v. Limbach*, 35 Ohio St. 3d 229, 229, (1988); *Bd. of Educ. of S.-W. City Sch. v. Kinney*, 24 Ohio St. 3d 184, 185-187 (1986).
3. To the extent that the BTA stated or held in its BTA Decision and Order that Newegg had raised an as-applied challenge to the constitutionality of any statutes in its Notices of Appeal to the BTA, the BTA erred, as a matter of fact and law, in failing to hold that even if Newegg had attempted to raise an as-applied challenge to the constitutionality in its Notices of Appeal, such attempt lacked the specificity required to state a challenge to the constitutionality of any CAT statute. R.C. 5717.02; R.C. 5717.04; *Norandex, Inc. v. Limbach*, 69 Ohio St. 3d 26, 31,(1994) fn.1; *Richter Transfer Co. v. Bowers*, 174 Ohio St. 113, 114 (1962); *see, also, Queen City Valves v. Peck*, 161 Ohio St. 579, 583 (1954).
4. Because Newegg failed to specify an as-applied challenge to the constitutionality any CAT statutes in its Notices of Appeal to the BTA, this Court lacks jurisdiction over those challenges now, and must dismiss them. R.C. 5717.02; R.C. 5717.04; *Cleveland Gear Co. v. Limbach*, 35 Ohio St. 3d

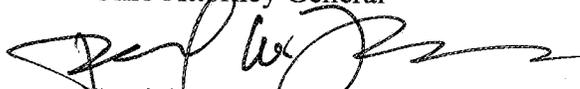
229, 229, (1988); *Bd. of Educ. of S.-W. City Sch. v. Kinney*, 24 Ohio St. 3d 184, 185-187 (1986).

WHEREFORE,

For the above reasons, this Court should dismiss and refuse to consider Newegg's Assignments of Error 1, 2, and 3 on subject matter jurisdictional grounds because Newegg failed to raise those errors to the BTA. To the extent that the BTA in its Decision and Order stated or held that Newegg had validly raised any as-applied challenge(s) to the constitutionality of any CAT statutes, the BTA erred as a matter of fact and law in so stating or holding.

Respectfully submitted,

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**CERTIFICATE OF SERVICE**

I hereby certify that the foregoing Notice of Cross-Appeal was filed by hand-delivery with the Ohio Supreme Court, 65 South Front St., Columbus, Ohio 43215, and the Ohio Board of Tax Appeals, 30 E. Broad St., 24<sup>th</sup> Floor, Columbus, Ohio 43215, and was served by certified mail return receipt requested this 6 day of April, 2015, upon the following:

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Daniel Fausey

OHIO BOARD OF TAX APPEALS

NEWEGG, INC., (et. al.),

CASE NO(S). 2012-234

Appellant(s),

( COMMERCIAL ACTIVITY TAX )

vs.

DECISION AND ORDER

JOSEPH W. TESTA, TAX COMMISSIONER OF  
OHIO, (et. al.),

Appellee(s).

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Entered Thursday, February 26, 2015

Mr. Williamson and Mr. Harbarger concur.

This matter is considered by the Board of Tax Appeals upon a notice of appeal filed on behalf of appellant Newegg, Inc. ("Newegg"). Newegg appeals from a final determination of the Tax Commissioner in which the commissioner affirmed six commercial activity tax assessments against Newegg. The subject assessments relate to periods from July 1, 2005 through December 31, 2009, the first through fourth quarters of 2010, and the first quarter of 2011. This matter is considered by the Board of Tax Appeals upon the notice of appeal, the statutory transcript ("S.T.") certified to this board by the Tax Commissioner, the record of this board's hearing ("H.R."), and any written argument filed by the parties. We note that Appellee's exhibits 4-11, 22-24, 30, 36, and 39-43, as jointly redacted by the parties, are received into evidence.

In its brief, Newegg, which is headquartered in Industry, California, describes itself as selling

"computer-related products, including gaming products, to consumers across the United States, including consumers residing in the State of Ohio. \*\*\* Newegg is a pure online retailer, meaning that it sells its products *only* online. \*\*\* It does so via an Internet website \*\*\* located on the Company's servers in California and New Jersey. \*\*\* Separate legal entities operate a Newegg website in China \*\*\*. Customers located anywhere in the world other than China and Canada access the same website to purchase Newegg products \*\*\*. \*\*\* The Company has warehouses and other physical locations only in Tennessee, California, and New Jersey. \*\*\*" (Emphasis sic.). Newegg Brief at 8. Before this board, Newegg presented extensive testimony and evidence relating to the operations of its website, its email promotions and online advertising, and its participation in comparison websites and an internet affiliate program, as well as its non-internet based marketing efforts. Newegg Brief at 10-23.

In its notice of appeal to this board, Newegg specified the following:

"1. Because Newegg engages in no commercial activity within the State of Ohio and, likewise, neither owns nor leases property in the state, either directly or indirectly, the Company is not 'doing business in the state' under R.C. 5751.02. The Commercial Activity Tax, therefore, does not apply.

"2. Newegg lacked a 'substantial nexus with this state' under R.C. 5751.01(H) inasmuch as it (a) neither owned nor used 'part or all of its capital in this state' [R.C. 5751.01(H)(1)]; (b) lacks a 'certificate of compliance with the laws of this state authorizing [it] to do business in this state' [R.C. 5751.01(H)(2)]; and (c) does not 'otherwise [have] nexus in this state...under the constitution [sic] of the United States.' [R.C. 5751.01(H)(4)].

"3. Newegg lacked a "'bright-line presence" in this state' under R.C. 5751.01(H)(3) & (I) inasmuch as it did not have: (a) 'at any time during the calendar year property in this state with an aggregate value of at least fifty thousand dollars' [R.C. 5751.01(I)(1)]; (b) 'during the calendar year payroll in this state of at least fifty thousand dollars' [R.C. 5751.01(I)(2)]; (c) during the calendar year 'taxable gross receipts of at least five hundred thousand dollars,' inasmuch as (i) none of its gross receipts are subject to taxation in Ohio; and (ii) it had no taxable sales within the State of Ohio [R.C. 5751.01(I)(3)]; or (d) 'during the calendar year within this state at least twenty-five per cent of the person's total property, total payroll, or total receipts.' [R.C. 5751.01(I)(4)]. In addition, Newegg was not 'domiciled in this state as an individual or for corporate, commercial, or other business purposes.' [R.C. 5751.01(I)(5)].

"4. Newegg's receipts are not subject to taxation because, under R.C. 5751.01(F)(2)(ff), such tax is 'prohibited by the Constitution or laws of the United States....'

"5. Ohio statutes should be interpreted to avoid the imposition of the CAT on Newegg, inasmuch as imposing the tax on Newegg would violate the

Company's rights under the Commerce Clause of the United States Constitution. \*\*\*

"6. Application of the CAT to Newegg would violate the Company's rights under the Commerce Clause of the United States Constitution since Newegg does not possess the requisite 'bright-line' physical presence in Ohio. \*\*\* Since the bright-line physical presence test applies to taxes like the CAT, the assessments are void in their entirety, and the Determination should be vacated.

"7. The penalty should be abated. The Commissioner erred in arbitrarily and capriciously assessing penalties for each of the aforesaid reasons, and in light of Newegg's good faith reliance upon existing federal constitutional law in regard to the application of the 'substantial nexus' test to cases involving gross receipts taxes, as well as sales and use taxes and other state taxes." Notice of Appeal at 5-7.

Initially, we note that the findings of the Tax Commissioner are presumptively valid. *Alcan Aluminum Corp. v. Limbach* (1989), 42 Ohio St.3d 121. It is incumbent upon a taxpayer challenging a finding of the Tax Commissioner to rebut the presumption and establish a right to the relief requested. *Belgrade Gardens, Inc. v. Kosydar* (1974), 38 Ohio St.2d 135; *Ohio Fast Freight v. Porterfield* (1972), 29 Ohio St.2d 69; *National Tube v. Glander* (1952), 157 Ohio St. 407. The taxpayer is assigned the burden of showing in what manner and to what extent the Tax Commissioner's determination is in error. *Federated Department Stores v. Lindley* (1983), 5 Ohio St.3d 213.

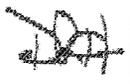
The parties hereto agree that Newegg has not challenged the constitutionality of the relevant statutes, but has instead, challenged the commissioner's conclusion that Newegg is liable for the commercial activity tax, which Newegg argues is prohibited by the U.S. Constitution. Specifically, Newegg claims its gross receipts are excluded from the CAT, pursuant to the U.S. Constitution, Commerce Clause, and the "substantial nexus" and corresponding "in-state presence" analysis thereunder. See R.C. 5751.01(F)(2)(z) (as such section was numbered in July 2005).

Upon review of the arguments raised, we find this board's pronouncement in *L.L. Bean, Inc. v. Levin* (Mar. 6, 2014), BTA No. 2010-2853, unreported, settled on appeal (Nov. 20, 2014), 11/20/2014 Case Announcements, 2014-Ohio-5119, to be controlling, to the extent Newegg raises constitutional claims. As we held in *L.L. Bean*, "this board makes no findings with regard to the constitutional questions presented. The parties, through the presentation of evidence and testimony and the submission of briefs to this board, have set forth their respective positions regarding the constitutional validity of the commissioner's application of the statutory provisions in question \*\*\* and we find such arguments may only be addressed on appeal by a court which has the authority to resolve constitutional challenges." *Id.* at 6-7. See, also, *MCI Telecommunications Corp. v. Limbach* (1994), 68 Ohio St.3d 195; *S. S. Kresge Co. v. Bowers* (1960), 170 Ohio St. 405, paragraph one of the syllabus; *Herrick v. Kosydar* (1975), 44 Ohio St. 2d 128, 130; *Roosevelt Properties Co. v. Kinney* (1984), 12 Ohio St. 3d 7, 8; *Cleveland Gear Co. v. Limbach* (1988), 35 Ohio St. 3d 229, paragraph one of the syllabus. Any constitutional implications of the relevant statutory provisions must be considered by a tribunal that has jurisdiction over such questions of constitutional interpretation.

Herein, based upon the applicable commercial activity tax statutory provisions, Newegg was assessed commercial activity tax for the periods in question. R.C. 5751.02(A). The commissioner determined that Newegg had substantial nexus with this state, i.e., a "bright-line presence" in the state, because it had at least \$500,000 in taxable gross receipts for the periods assessed. R.C. 5751.01(H)(3); R.C. 5751.01(I)(3); R.C. 5751.033(E) (as such sections were numbered in July 2005). Newegg, as L.L. Bean before it, contends that its gross receipts cannot be taxed under the commercial activity statutes under consideration herein because it lacks an "in-state presence," as required by the Commerce Clause, necessary to establish "substantial nexus." See *Quill Corp. v. North Dakota* (1992), 504 U.S. 298 (1992), *Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue*, 483 U.S. 232 (1987). Newegg Brief at 24, et seq. Even without considering any constitutional claims, however, we conclude, under the plain language set forth therein, the pertinent CAT statutes do not impose such an in-state presence requirement. See *L.L. Bean*, supra.

As we stated in *L.L. Bean*, supra, "[a] plain reading of the statutes under consideration provides that an entity has substantial nexus with this state if it has a bright-line presence in this state, which is defined as having taxable gross receipts of at least five hundred thousand dollars \*\*\*. While we recognize that an out-of-state seller must have "substantial nexus" with a taxing state, *Quill*, supra, we are also cognizant of the explicit statutory language of R.C. 5751.01(H), where, by definition, substantial nexus exists if any of the elements set forth in R.C. 5751.01(H)(1)-(4) are met. \*\*\* [W]e are constrained to follow the mandate of the General Assembly in concluding that appellant, an out-of-state seller, has substantial nexus within this state by virtue of its gross receipts for the reporting periods in question." Id. at 9-10.

Thus, following this board's precedent established in *L.L. Bean*, supra, it is the decision of the Board of Tax Appeals that the final order of the Tax Commissioner must be, and hereby is, affirmed.

BOARD OF TAX APPEALS		
RESULT OF VOTE	YES	NO
Mr. Williamson		
Mr. Harbarger		

I hereby certify the foregoing to be a true and complete copy of the action taken by the Board of Tax Appeals of the State of Ohio and entered upon its journal this day, with respect to the captioned matter.



Kathleen M. Crowley, Board Secretary