Supreme Court of Ohio Clerk of Court - Filed August 31, 2015 - Case No. 2015-0483

In the Supreme Court of Ohio

Newegg, Inc.,	:	
	:	Case No. 2015-0483
	:	
Appellant,	:	
	:	Appeal from the Ohio
v.	:	Board of Tax Appeals
	:	
Joseph W. Testa,	:	
Tax Commissioner of Ohio,	:	
	:	BTA Case No. 2012-234
Appellee.	:	

MERIT BRIEF OF APPELLANT NEWEGG, INC.

Martin I. Eisenstein (PHV 1095-2015)
(Counsel of Record)
Matthew P. Schaefer (PHV 2399-2015)
BRANN & ISAACSON
184 Main Street
P.O. Box 3070
Lewiston, ME 04243-3070
Tel. (207) 786-3566
Fax (207) 783-9325
Email: meisenstein@brannlaw.com
mschaefer@brannlaw.com

AND

Edward J. Bernert (0025808)
BAKER HOSTETLER
Capitol Square, Suite 2100
65 East State Street
Columbus, OH 43215-4260
Tel: (614) 462-2687
Fax: (614) 462-2616
Email: ebernert@bakerlaw.com

Counsel for Appellant,
Newegg, Inc.

Mike DeWine (0009181)
Attorney General of Ohio
Christine T. Mesirow (0015590)
Daniel W. Fausey (0079928)
Assistant Attorneys General
Office of the Attorney General
Taxation Section, 25th Floor
Rhodes Tower
30 East Broad Street
Columbus, OH 43215
Tel. (614) 466-5967
Fax (614) 466-8226
christine.mesirow@ohioattorney general.gov
daniel.fausey@ohioattorneygeneral.gov

Counsel for Appellee,
Joseph W. Testa, Tax Commissioner of Ohio

TABLE OF CONTENTS

Page

I. INTRODUCTION 1

II. STATEMENT OF THE CASE.....3

III. STATEMENT OF FACTS 7

A. Newegg Has No Physical Presence In Ohio 7

B. Newegg's Marketing Was Conducted Entirely Outside Of Ohio.....8

1. Newegg's Website Was Not Maintained In Ohio.....8

2. All Of Newegg's Other Marketing Efforts Were Conducted Outside Of Ohio 9

C. The Commissioner's Internet Nexus Theory 11

IV. LAW AND ARGUMENT 16

Proposition of Law 1: R.C. 5751.01(I)(3) is unconstitutional on its face. According to its plain terms, the gross receipts "bright-line-presence" provision of R.C. 5751.01(I)(3) requires that the CAT be imposed on a company solely because the company meets a statutory threshold of $500,000 in annual gross receipts from interstate sales to Ohio consumers, irrespective of whether the company has the in-state presence required under the "substantial nexus" standard for state taxes established by the Supreme Court under the Commerce Clause. *E.g., Tyler Pipe*, 483 U.S. at 250-51; *Commonwealth Edison*, 453 U.S. at 626; *Standard Pressed Steel,* 419 U.S. at 562; *General Motors*, 377 U.S. at 447-48.. 17

A. The CAT Statute, On Its Face, Imposes CAT Liability On Retailers With No Physical Presence In The State Who Make Sales To Ohio Customers In Excess Of The Statutory Gross Receipts Threshold.....17

B. Newegg Received More Than $500,000 In Gross Receipts From Sales Delivered To Ohio Customers And Therefore Has Standing To Challenge The CAT 18

C. Newegg Satisfies The Standards For A Facial Constitutional Challenge.....19

1. Newegg's Facial Challenge To The CAT Statute Depends Upon No Extrinsic Facts 19

TABLE OF CONTENTS (cont'd)

Page

2. The "Presumption Of Constitutionality" Cannot Preserve A Statutory Provision That Is Plainly Unconstitutional On Its Face 19

3. Newegg's Facial Challenge Under The Commerce Clause Is Not Defeated By The "No Set Of Circumstances" *Salerno* Test 21

D. The Commerce Clause Bars Ohio From Imposing The CAT On Companies Based Solely On The Amount Of Sales Made To Customers In The State 24

E. The In-State Presence Requirement Of Substantial Nexus Is Supported By The Supreme Court's Decisions Concerning Sales And Use Taxes.....31

F. State Court Decisions Declining To Apply The Physical Presence Standard To State Income Taxes Are Inapposite.....34

G. No Ohio Decision Has Ever Approved Imposing A State Tax On A Person That Lacked A Physical Presence In The State 37

H. A Finding That Gross Receipts Alone Are Sufficient To Support Ohio's Authority To Tax Would Result In Nationwide Nexus For Any Internet Seller And Is Inconsistent With The Separate Nexus Standards Under The Commerce Clause And The Due Process Clause.....38

I. Fundamental Principles Regarding The Regulation Of Interstate Commerce Require Rejection Of The CAT Statute's Novel Gross Receipts Standard Of Nexus 40

1. The In-State Presence Standard Of Substantial Nexus Is Grounded In The Core Principles Of The Commerce Clause 40

2. Changes In Standards For Requiring Tax Reporting By Remote Sellers Are Properly The Purview Of Congress, Not State Legislatures.....42

3. The Doctrine Of *Stare Decisis* Supports The Conclusion That The Gross Receipts Nexus Provision Of R.C. 5751.01(I)(3) Is Unconstitutional.....43

TABLE OF CONTENTS (cont'd)

Page

Proposition of Law 2: The CAT statute is unconstitutional as-applied to Newegg by the Commissioner. Imposition of the CAT against Newegg, a company with no in-state presence in Ohio, violates the "substantial nexus" standard of the Commerce Clause as established under numerous decisions of the United States Supreme Court. *E.g., Tyler Pipe*, 483 U.S. at 250-51; *Commonwealth Edison*, 453 U.S. at 626; *Standard Pressed Steel,* 419 U.S. at 562; *General Motors*, 377 U.S. at 447-48. Merely obtaining gross receipts in excess of $500,000 annually does not establish constitutional "substantial nexus" under long-standing Supreme Court authority, so applying the CAT based solely on Newegg's gross receipts from sales of goods delivered to Ohio customers violates the Constitution. In addition, because Newegg engaged in no business activities within the State of Ohio sufficient to satisfy the constitutional "substantial nexus" standard, application of the CAT to Newegg on any other basis, whether separate from or together with its gross receipts, is also unconstitutional. 44

A. Newegg Satisfies The Clear and Convincing Standard For An As-Applied Challenge 44

Proposition of Law 3: The assessments against Newegg are invalid under the CAT statute, when its terms are properly construed to avoid constitutional infirmities. Multiple provisions of the CAT statute may be reasonably construed so as to prevent the application of the CAT to Newegg, an out-of-state retailer with no physical presence in Ohio, including R.C. 5751.02(A), R.C. 5751.01(H)(3) and (I)(3) and R.C. 5751.01(F)(2)(jj).. 46

A. Newegg Is Not "Doing Business In This State" Within The Meaning Of R.C. 5751.02(A) And 5751.01(H) 46

B. The CAT Statute Itself Excludes Gross Receipts That Cannot Be Taxed Consistent With The Constitutional Limitations On The State's Authority 47

Proposition of Law 4: No other provision of the CAT statute applies to Newegg. The evidence presented before the Board clearly established that Newegg lacked statutory "substantial nexus with this state" under the other provisions of R.C. 5751.01(H) and lacked "bright-line presence" in Ohio under the other provisions of R.C. 5751.01(I)... 48

A. No Other Provisions Of The CAT Statute Required Newegg To Pay The CAT 48

TABLE OF CONTENTS (cont'd)

Page

B. Any Claim By The Commissioner That Newegg Is Subject To The CAT Under The Constitutional Catch-All Provision Of R.C. 5751.01(H)(4) Is Clearly Refuted By The Evidence 49

V. CONCLUSION 49

VI. CERTIFICATE OF SERVICE 51

TABLE OF CONTENTS (cont'd)

Page

VII. APPENDIX

a. Notice of Appeal, Supreme Court Case No. 15-0483 (filed Mar. 25, 2015) ..... Appx. 1

b. Decision and Order, BTA No. 2012-234 (entered Feb. 26, 2015) ..... Appx. 15

c. Notice of Appeal, Board of Tax Appeals No. 2012-234 (filed Jan. 19, 2012) ..... Appx. 19

d. Final Determination, Assessment Nos. 17201034126112, 17201034427316, 17201034427317, 17201034427318, 17201106110042, and 17201114476189 (filed Nov. 22, 2011) ..... Appx. 28

e. U.S. Constitution, Article I, Section 8, cl. 3 and U.S. Constitution, Amendment XIV, Section 1 ..... Appx. 32

f. R.C. 5751.01 ..... Appx. 33

g. R.C. 5751.02 ..... Appx. 45

h. R.C. 5751.033 ..... Appx. 46

i. R.C. 5751.31 ..... Appx. 48

TABLE OF AUTHORITIES

Cases **Page(s)**

Arbino v. Johnson & Johnson,
116 Ohio St.3d 468, 2007-Ohio-6948, 880 N.E.2d 420 .....20, 21

Arizona Dept. of Revenue v. O'Connor, Cavanaugh, Anderson, Killingsworth & Beshears, P.A.,
192 Ariz. 200, 963 P.2d 279 (Ct.App. 1997).....30, 37

Beaver Excavating Co. v. Testa,
134 Ohio St.3d 565, 2012-Ohio-5776, 983 N.E.2d 1317 .....19, 20

Buchman v. Wayne Trace Local School Dist. Bd. of Edn.,
73 Ohio St.3d 260, 652 N.E.2d 952 (1995) 20, 48

Camps Newfound/Owatonna, Inc. v. Town of Harrison,
520 U.S. 564, 117 S.Ct. 1590, 137 L.Ed.2d 852 (1997).....22

Capital Bank One v. Commr. of Revenue,
453 Mass.1, 899 N.E.2d 76 (2009) 34, 35

Caterpillar, Inc. v. New Hampshire Dept. of Revenue Administration,
144 N.H. 253, 741 A.2d 56 (1999) 23

Caterpillar, Inc. v. Commr. of Revenue,
568 N.W.2d 695 (Minn. 1997).....23

Cent. Greyhound Lines, Inc. v. Mealy,
334 U.S. 653, 68 S.Ct. 1260, 92 L.Ed. 1633 (1948).....31, 32

City of Chicago v. Morales,
527 U.S. 41, 119 S.Ct. 1849, 144 L.Ed.2d 67 (1999).....22

City of Los Angeles v. Patel,
___ U.S. ___135 S.Ct. 2443 (2015).....24

Cleveland Gear Co. v. Limbach,
35 Ohio St.3d 229, 520 N.E.2d 188 (1988) 19

Columbia Gas Transm. Corp. v. Levin,
117 Ohio St.3d 122, 2008-Ohio-511, 882 N.E.2d 400 .....21, 22

TABLE OF AUTHORITIES (cont'd)

Cases (cont'd) **Page(s)**

Commonwealth Edison Co. v. Montana,
453 U.S. 609, 101 S.Ct. 2946, 69 L.Ed.2d 884 (1981) ..... *passim*

Complete Auto Transit, Inc. v. Brady,
430 U.S. 274, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977) ..... *passim*

Comptroller of the Treasury of Maryland v. Wynne,
___ U.S. ___, 135 S.Ct. 1787, 1801, 191 L.Ed.2d 813 (2015) ..... *passim*

Conoco, Inc. v. Taxation & Revenue Dept.,
122 N.M. 736, 931 P.2d 730 (1996) 23

Couchot v. State Lottery Comm.,
74 Ohio St.3d 417, 659 N.E.2d 1225 (1996) 38

Dept. of Revenue v. Assn. of Washington Stevedoring Cos.,
435 U.S. 734, 98 S.Ct. 1388, 55 L.Ed.2d 682 (1978) 28

D.H. Holmes Co. v. McNamara,
486 U.S. 24, 108 S.Ct. 1619, 100 L.Ed.2d 21 (1988) 25

Direct Marketing Assn. v. Brohl,
___ U.S. ___, 135 S.Ct 1124, 191 L.Ed.2d 97 (2015) 34

Doe v. City of Albuquerque,
667 F.3d 1111 (10th Cir. 2012) 22

Emerson Elec. Co. v. Tracy,
90 Ohio St.3d 157, 735 N.E.2d 445 (2000) 22, 23

Field Ents., Inc. v. Washington,
47 Wash.2d 852, 289 P.2d 1010 (1955) 1, 2, 27

Geoffrey, Inc. v. South Carolina Tax Comm.,
313 S.C. 15, 437 S.E.2d 13 (1993) 34, 35

Gen. Motors Corp. v. Washington,
377 U.S. 436, 84 S.Ct. 1564, 12 L.Ed.2d 430 (1964) ..... *passim*

TABLE OF AUTHORITIES (cont'd)

Cases (cont'd) **Page(s)**

Global Knowledge Training, L.L.C. v. Levin,
127 Ohio St.3d 34, 2010-Ohio-4411, 936 N.E.2d 463 19

Goldberg v. Sweet,
488 U.S. 252, 109 S.Ct. 582, 102 L.Ed.2d 607 (1989).....32, 33, 36

Gulf Oil Corp. v. Kosydar,
44 Ohio St.2d 208, 339 N.E.2d 820 (1975) 47

Harrold v. Collier,
107 Ohio St.3d 44, 2005-Ohio-5334, 836 N.Ed.2d 1165 45

Hemi Group, LLC v. City of New York,
559 U.S. 1, 130 S.Ct. 983, 175 L.Ed.2d 943 (2010).....34

Hillenmeyer v. Cleveland Bd. of Review,
2015-Ohio-1623 25

Hughes v. Oklahoma,
441 U.S. 322, 99 S.Ct. 1727, 60 L.Ed.2d 250 (1979).....42

J.C. Penney Natl. Bank v. Johnson,
19 S.W.3d 831 (Tenn.App.Ct. 1999) 2, 30, 37

J.C. Penney v. Wisconsin Tax Comm.,
233 Wis. 286, 289 N.W. 677 (1940).....26

KFC Corp. v. Iowa Dept. of Revenue,
792 N.W.2d 308 (Iowa 2010) 34, 35

Kraft Gen. Foods, Inc. v. Iowa Dept. of Revenue and Fin.,
505 U.S. 71, 112 S.Ct. 2365, 120 L.Ed.2d 59 (1992).....23

Lamtec Corp. v. Dept. of Revenue,
170 Wash.2d 838, 246 P.3d 788 (2011).....2, 30

Marysville Exempted Village School Dist. Bd. of Edn. v. Union Cty. Bd. of Revision,
136 Ohio St.3d 146, 2013-Ohio-3077, 991 N.E.2d 1134 .....30, 31

Memphis Natural Gas Co. v. Stone,
335 U.S. 80, 68 S.Ct. 1475, 92 L.Ed. 1832 (1948).....25, 26

TABLE OF AUTHORITIES (cont'd)

Cases (cont'd) **Page(s)**

Natl. Bellas Hess, Inc. v. Illinois Dept. of Revenue,
386 U.S. 753, 87 S.Ct. 1389, 18 L.Ed.2d 505 (1967) ..... *passim*

Natl. Geographic Soc. v. California Bd. of Equalization,
430 U.S. 551, 97 S.Ct. 1386, 51 L.Ed.2d 631 (1977) 29, 32

New Energy Co. v. Limbach,
486 U.S. 269, 108 S.Ct. 1803, 100 L.Ed.2d 302 (1988) 22

New Mexico Taxation & Revenue Dept. v. Barnesandnoble.com LLC,
2013 NMSC 023, 303 P.3d 824 ..... 2, 30

Northwestern States Portland Cement Co. v. Minnesota,
358 U.S. 450, 79 S.Ct. 357, 3 L.Ed. 421 (1959) 25, 26

Norton Co. v. Dept. of Revenue,
340 U.S. 534, 71 U.S. 377, 95 L.Ed. 517 (1951) 27

Ohio Grocers Assn. v. Levin,
123 Ohio St.3d 303, 2009-Ohio-4872 ..... 2, 20

Oregon Waste Sys., Inc. v. Dept. of Environmental Quality,
511 U.S. 93, 114 S.Ct. 1435, 128 L.Ed.2d 13 (1994) 24

Palazzi v. Estate of Gardner,
32 Ohio St.3d 169, 512 N.E.2d 971 (1987) 18

Peebles v. Clement,
63 Ohio St.2d 314, 408 N.E.2d 689 (1980) 20

Quill Corp. v. North Dakota,
504 U.S. 298, 112 S.Ct. 1904, 119 L.Ed.2d 91 (1992) ..... *passim*

Scholastic Book Clubs, Inc. v. Commr. of Revenue Servs.,
304 Conn. 204, 38 A.3d 1183 (2012) 30

Scripto, Inc. v. Carson,
362 U.S. 207, 80 S.Ct. 619, 4 L.Ed.2d 660 (1960) 29, 31, 32

SFA Folio Collections, Inc. v. Tracy,
73 Ohio St.3d 119, 652 N.E.2d 693 (1995) 20, 37, 38, 48

TABLE OF AUTHORITIES (cont'd)

Cases (cont'd) **Page(s)**

Short Bros., Inc. v. Arlington Cty.,
244 Va. 520, 423 S.E.2d 172 (1992).....37

Std. Pressed Steel Co. v. Washington Dept. of Revenue,
419 U.S. 560, 95 S.Ct. 706, 42 L.Ed.2d 719 (1975)..... *passim*

State v. Lane Bryant, Inc.,
277 Ala. 385, 171 So.2d 91 (1965).....45

State v. Romage,
138 Ohio St.3d 390, 2014-Ohio-783, 7 N.E.3d 1156 21

Travelocity.com LP v. Wyoming Dept. of Revenue,
2014 WY 43, 329 P.3d 131.....30

Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue,
483 U.S. 232, 107 S.Ct. 2810, 97 L.Ed. 199 (1987)..... *passim*

United States v. Salerno,
481 U.S. 739, 107 S.Ct. 2095, 95 L.Ed.2d 697 (1987).....21, 22, 23

Wabash Power Equip., Inc. v. Lindsey,
897 So.2d 621 (La.Ct.App. 2004).....30

Wisconsin v. J.C. Penney,
311 U.S. 435, 61 S.Ct. 246, 85 L.Ed. 267 (1940).....26

Wymslyo v. Bartec, Inc.,
132 Ohio St.3d 167, 2012-Ohio-2187, 970 N.Ed.2d 898 .....44, 45

Constitutional Provisions

U.S. Constitution, Article I, Section 8, cl. 3 ..... *passim*
U.S. Constitution, Amendment XIV, Section 1.....39

State Statutes

Cal. Rev. & Tax. Code § 23101(b)(2) 41
Mich. Comp. Laws § 206.621(1).....41
N.Y. Tax Law § 209(1)(b) 41

TABLE OF AUTHORITIES (cont'd)

State Statutes (cont'd) **Page(s)**

Ohio Revised Code
R.C. 1.47(A) 20, 48
R.C. 5751.01(F) ..... *passim*
R.C. 5751.01(G) 18
R.C. 5751.01(H) ..... *passim*
R.C. 5751.01(I) ..... *passim*
R.C. 5751.02(A) ..... *passim*
R.C. 5751.033(E) 18
R.C. 5751.31 20

Nevada S.B. 483 41
Tenn. Code. Ann. § 67-4-702(27)(A)(iv)(a) 41
Tex. Tax Code § 171.101 41
Washington Subst. S.B. 6138 41

State Regulations

1 Colo. Code Regs. 201-2:39-22-301.1(2)(b)(iii) 41

Municipal Statutes

Los Angeles Municipal Code, § 21.43(e) 41
Philadelphia Business Privilege Tax Regs. § 103(A) 41
San Francisco Business and Tax Regs. Code, § 953 41

Other Authorities

H.R. 2584, Business Activity Tax Simplification Act of 2015,114th Cong. (2015-2016), available at https://www.congress.gov/bill/114th-congress/house-bill/2584/text 43

I. INTRODUCTION

Under the Commerce Clause of the United States Constitution, every state tax must satisfy the "substantial nexus" requirement of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977). For more than 50 years, in a series of cases decided both before and after *Complete Auto*, the Supreme Court has made clear that a state's authority to impose a tax measured by gross receipts depends upon the taxpayer conducting business activities within the state that assist the company to develop and maintain a market there. As the Court explained in *Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue*, 483 U.S. 232, 107 S.Ct. 2810, 97 L.Ed.2d 199 (1987), in response to a challenge to the constitutionality of a state tax on the privilege of doing business in the state that was measured by gross receipts:

> [T]he *crucial factor governing nexus* is whether the activities performed *in this state on behalf of the taxpayer* are significantly associated with the taxpayer's ability to establish and maintain a market in this state for sales.

(Internal citation omitted.) (Emphasis added.) *Tyler Pipe*, 483 U.S. at 250-251; *see also Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 626, 101 S.Ct. 2946, 69 L.Ed.2d 884 (1981) (noting that "the interstate business must have a substantial nexus with the State before *any* tax may be levied upon it"); *Std. Pressed Steel Co. v. Washington Dept. of Revenue*, 419 U.S. 560, 562, 95 S.Ct. 706, 42 L.Ed.2d 719 (1975) (taxpayer had a full-time employee located in the state who "made possible the realization and continuance of valuable contractual relations" for the company); *Gen. Motors Corp. v. Washington*, 377 U.S. 436, 447-448, 84 S.Ct. 1564, 12 L.Ed.2d 430 (1964), *overruled, in part, on other grounds*, *Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue*, 483 U.S. 232, 107 S.Ct. 2810, 97 L.Ed.2d 199 (1987), (taxpayer's in-state activities were "decisive factors in establishing and holding the market"); *Field Ents., Inc. v. Washington*, 47 Wash.2d. 852, 856, 289 P.2d 1010 (1955), *aff'd*, 352 U.S.

806, 77 S.Ct. 55, 1 L.Ed.2d 39 (1956) (tax levy against company upheld based on the presence of a manager, employees and salespeople in the state).

Since its landmark decision in *Tyler Pipe*, the Supreme Court has never held that any different or lesser "substantial nexus" standard applies for determining the validity of a state tax measured by gross receipts. In fact, *Tyler Pipe* continues to be cited by courts throughout the country in support of the in-state activities requirement of substantial nexus. *See, e.g.*, *New Mexico Taxation & Revenue Dept. v. Barnesandnoble.com LLC*, 2013 NMSC 023, ¶¶ 8-10, 303 P.3d 824 (upholding assessment of New Mexico Gross Receipts Tax based on the activities of an affiliated company in the state); *Lamtec Corp. v. Dept. of Revenue*, 170 Wash.2d 838, 849-851 246 P.3d 788 (2011) (*en banc*) (affirming gross receipts tax assessment against company whose sales representatives visited customers in the state); *J.C. Penney Natl. Bank v. Johnson*, 19 S.W.3d 831, 841-842 (Tenn.App.Ct. 1999) (rejecting application of gross receipts tax to company with no in-state presence).

The Ohio Commercial Activity Tax ("CAT") is, like the tax reviewed by the Court in *Tyler Pipe*, a tax on the privilege of doing business measured by gross receipts. *Ohio Grocers Assn. v. Levin*, 123 Ohio St.3d 303, 2009-Ohio-4872, ¶¶ 43-49; R.C. 5751.02(A). As a tax measured by gross receipts, the CAT is properly analyzed for purposes of the Commerce Clause's "substantial nexus" test on the same basis as other state taxes measured by, or levied upon, gross receipts. Yet in the face of *Tyler Pipe* and other Supreme Court and state court decisions reinforcing the in-state presence standard for gross receipts taxes, the Tax Commissioner of Ohio ("Commissioner") contends that the General Assembly elected to disregard the requirement of in-state activities in enacting the CAT, in favor of a test based entirely on whether an out-of-state company makes sales to customers in the state of at least of $500,000 per year. *See* R.C. 5751.01(H)(3), (I)(3). As long as a company has $500,000 or more

in annual sales from Ohio customers, the Commissioner contends, it must pay the CAT. This is true even if a company such as Appellant Newegg, Inc. ("Newegg") does nothing more than communicate with Ohio customers through the instrumentalities of interstate commerce as part of a national business.

On the basis of Newegg's sales volume only, the Commissioner assessed over $1 million against Newegg, a California online retailer with no business activities conducted by, or on its behalf, in Ohio. Newegg disputes the constitutionality of both the Commissioner's interpretation of the CAT statute and his application of the CAT to Newegg's business. Indeed, the Commissioner's interpretation of the statute, if accepted, would render the CAT's gross receipts nexus provision, R.C. 5751.01(I)(3), unconstitutional on its face.

Based on the in-state presence requirement as reaffirmed in *Tyler Pipe* and numerous other decisions (*i.e.,* activities performed in the state on behalf of the taxpayer), this Court should reject the Commissioner's imposition of the CAT on Newegg, reverse the decision of the Board of Tax Appeals ("Board" or "BTA") that affirmed the Commissioner's assessments of CAT against Newegg, and order that the CAT assessments against Newegg be cancelled in full.

II. STATEMENT OF THE CASE

The Ohio Department of Taxation (the "Department") issued six Commercial Activity Tax assessments against Newegg covering, collectively, each of the quarterly periods from July 1, 2005 to March 31, 2011 (the "Tax Period"). *See* Appx. 28-31, Final Determination, Assessment Nos. 17201034126112, 17201034427316, 17201034427317, 17201034427318, 1720106110042, and 17201114476189 (dated Nov. 22, 2011) ("Final Determination"). The total tax resulting from the six assessments is $697,580.00, and the aggregate interest and penalties associated with the assessments are $56,064.57 and $406,050.00, respectively. *Id.* The sole basis for the assessments is that Newegg's annual retail sales to Ohio customers exceeded

$500,000. The Department cited no activities conducted by, or on behalf of, Newegg in Ohio during the Tax Period as support for the assessments. *See id.*

Newegg timely filed petitions for reassessment. (*See, e.g.,* Appellant's Supplement ("Suppl.") 290-299, Petition for Reassessment (dated July 28, 2011)). Newegg asserted in each of its petitions that application of the CAT to Newegg exceeded the State's authority under the Commerce Clause of the United States Constitution because Newegg did not conduct any activities on its own or through representatives in Ohio to establish or maintain an Ohio market. (Suppl. 295-296, 298-299, Petition for Reassessment at 1-2, 4-5).

Newegg also presented statutory arguments in its petitions, including that it was not "doing business in this state" under R.C. 5751.02(A), based on the absence of any in-state activities by Newegg. (Suppl. 296-298, Petition for Reassessment at 2-4). Newegg asserted that a proper interpretation of the CAT statute, especially in light of the principle that statutes should be construed to preserve their constitutionality, required that its "taxable gross receipts" do not include its sales to Ohio customers since, under the Commerce Clause, the company had to engage in business activities in the state to be subject to the CAT. (Suppl. 297-298, Petition for Reassessment at 3-4). Indeed, R.C. 5751.01(F)(2)(ff), as Newegg has argued, expressly states that the term "taxable gross receipts" excludes "any receipts for which the tax imposed by this chapter is prohibited by the constitution or laws of the United States * * *." (Suppl. 298, Petition for Reassessment at 4).

In the Final Determination, the Commissioner rejected all of Newegg's arguments, finding that Newegg's sales of more than $500,000 to Ohio customers, alone, satisfied both the CAT statute and the Commerce Clause substantial nexus requirement. Appx. 28-30, Final Determination at 1-3. Relying on R.C. 5751.01(H)(3), the Commissioner concluded that Newegg had a "substantial nexus with this state," based on the statutorily-defined "bright-line

presence in this state" set forth in R.C. 5751.01(I)(3). Appx. 29-30, Final Determination at 2-3. The Commissioner noted that Subsection (I)(3) requires that the taxpayer during the calendar year has "taxable gross receipts of at least five-hundred thousand dollars." Appx. 30, Final Determination at 3. As to Newegg's constitutional argument, the Commissioner summarily determined as follows:

> The petitioner has more than $500,000 in taxable gross receipts sitused to Ohio for periods assessed and thus, has "bright-line presence." As such, the petitioner has "substantial nexus" with Ohio. Under established Commerce Clause jurisprudence, the imposition of the tax measured by those receipts is not prohibited by the laws or Constitution of either the United States or Ohio.

Id. The Commissioner offered no supporting authority for this conclusion. *Id.*

Newegg timely appealed the Final Determination to the Board, raising the same constitutional and statutory arguments it raised in its petitions for reassessment. Appx. 19-26, Notice of Appeal (dated Jan 19, 2012).

After far-reaching discovery by the Commissioner, including document requests and interrogatories (resulting in the production of virtually every marketing contract of Newegg), a hearing was held before the Board on May 13 and 14, 2014. While the assessments and the Final Determination of the assessments were based solely on the fact that Newegg's sales exceeded the $500,000 annual threshold, the Commissioner in pre-hearing filings advised that he would further argue that Newegg's Internet marketing activities satisfied the Commerce Clause in-state presence test. In response, Newegg presented the live testimony of the key personnel responsible for all of Newegg's marketing and sales activity: James Wu, Newegg's Chief Operating Officer; Maihua (Aaron) Yin, a Marketing Project Manager at the company, and Rong Huo, the Director of eCommerce Development, MIS. Newegg also presented the expert testimony of Eric Goldman, a professor at Santa Clara University Law School and the director of the school's High Tech Law Institute. By agreement of the parties, Professor Goldman was qualified "in the areas

of Internet law, intellectual property, and advertising and marketing law, as well as marketing, including Internet marketing, the use of the Internet to purchase and sell products, and the technology regarding such marketing and sales." (Suppl. 302, Joint Stipulations (dated May 6, 2014) ¶ 4). Professor Goldman's expert report was received in evidence. (Suppl. 303-306, Hearing Exhibit 7 (Expert Report of Eric Goldman dated Mar. 27, 2014)).

The Commissioner presented no fact witnesses, but introduced the testimony from a prior hearing of Frederick Church, a state employee, to present historical background regarding the CAT. (*See* Suppl. 300, Joint Stipulations ¶ 1). With the agreement of Newegg and the authorization of the Board, the Commissioner also presented the deposition testimony of two experts—Joseph Turow, a Professor of Communications at the University of Pennsylvania, and Ashkan Soltani, a private consultant in the area of privacy, security, and behavioral economics—to discuss Newegg's Internet activities. (Suppl. 301, Joint Stipulations ¶ 4). (For ease of reference, Newegg refers to the transcripts of the depositions as "Hearing Transcript, June 17, 2014," with the appropriate page references to the deposition transcripts.)

On February 26, 2015, the Board issued its Decision and Order upholding the Commissioner's Final Determination. Appx. 15-18, Decision and Order (dated Feb. 26, 2015) ("Decision"). The Board declined to address Newegg's as-applied constitutional challenge to the assessments, saying that it lacked the authority to decide "questions of constitutional interpretation." Appx. 17, Decision at 3. It therefore made "no findings with regard to the constitutional questions presented." *Id*. The Board rejected Newegg's argument that the CAT should be construed so as not to run afoul of the well-established in-state activities requirement for gross receipts taxes under the Commerce Clause. Appx. 16-17, Decision at 2-3. Instead, it found that "under the plain language set forth therein, the pertinent CAT statutes do not impose such an in-state presence requirement." Appx. 17, Decision at 3. The Board explained that it

was "constrained to follow the mandate of the General Assembly in concluding that the appellant, an out-of-state seller, has substantial nexus within this state by virtue of its gross receipts * * *." *Id.*

Newegg timely appealed the Board's decision to this Court. Appx. 1-11, Notice of Appeal (dated March 25, 2015). The Commissioner cross-appealed, asserting that Newegg failed to raise as a basis for appeal below the constitutionality of the CAT as applied to Newegg. *See* Notice of Cross-Appeal (dated April 6, 2015) at 3-4. On the same ground as the cross-appeal, the Commissioner then moved to dismiss Newegg's contention that the CAT, as applied to Newegg by the Commissioner, violates the Commerce Clause. *See* Motion to Dismiss (dated June 10, 2015). The Court denied the Commissioner's motion to dismiss on July 22, 2015. *07/22/2015 Case Announcements*, 2015-Ohio-2911 at 4.

III. STATEMENT OF FACTS

A. Newegg Has No Physical Presence In Ohio.

Newegg is headquartered in Industry, California, and sells a variety of computer-related products to consumers across the United States, including consumers residing in Ohio. (Suppl. 5, 63-64, Hearing Transcript, May 13, 2014 at 17, 249-250). Newegg is a pure online retailer, meaning that it sells its products *only* by the Internet. (Suppl. 5, 64, Hearing Transcript, May 13, 2014 at 17, 250). It does so via an Internet website, www.newegg.com (the "Newegg website"), maintained on the company's servers in California and New Jersey. (Suppl. 17, 251, Hearing Transcript, May 13, 2014 at 17, 251). Customers located anywhere in the world, other than China and Canada (where Newegg maintains websites under separate URLs), access the Newegg website to purchase Newegg's products. (Suppl. 24, 64 Hearing Transcript, May 13, 2014 at 93, 251). The Company warehouses its products in California, New Jersey, and Tennessee. (Suppl. 65, Hearing Transcript, May 13, 2014 at 256-257).

During the Tax Period, Newegg conducted no business activities in Ohio, nor did any agents, representatives or employees perform activities in Ohio on its behalf. (Suppl. 6, 66-67, Hearing Transcript, May 13, 2014 at 18-19, 260-263). It had no presence of any kind in Ohio. *Id.* Newegg had no offices, facilities, servers or other tangible assets in the state. (Suppl. 6, 65-67, Hearing Transcript, May 13, 2014 at 18, 256-257, 260-262). It had no employees located in Ohio. (Suppl. 66, Hearing Transcript, May 13, 2014 at 261). It had no bank accounts in Ohio. (Suppl. 67, Hearing Transcript, May 13, 2014 at 262). Indeed, after the Department completed its audit of Newegg, the Commissioner pointed to no in-state presence by, or on behalf of, Newegg as the basis for the CAT assessments issued to the company. Appx. 28, Final Determination at 1.

B. Newegg's Marketing Was Conducted Entirely Outside Of Ohio.

1. Newegg's Website Was Not Maintained In Ohio.

Newegg's primary marketing tool is the Newegg website (Suppl. 5-6, 63, Hearing Transcript, May 13, 2014 at 16-19, 249-250). The Newegg website can be visited by anyone with Internet access. (Suppl. 6, Hearing Transcript, May 13, 2014 at 19-20). Moreover, the Newegg website is the same for every visitor; they each see an identical website not customized in any way, whether for particular users or even geographic areas. (Suppl. 6, 64, Hearing Transcript, May 13, 2014 at 19-20, 251). An Ohio customer shopping with Newegg does so via standard Internet access chosen by the customer using a computer or mobile device to reach and communicate with Newegg's web servers in California and New Jersey. (Suppl. 6, 66 Hearing Transcript, May 13, 2014 at 19, 258). None of Newegg's website assets or activities was located in Ohio, and all communications were carried out between Newegg's servers outside the state and users in Ohio. (Suppl. 6, 66, Hearing Transcript, May 13, 2014 at 18, 260).

2. All Of Newegg's Other Marketing Efforts Were Conducted Outside Of Ohio.

In addition to its website, Newegg used other Internet channels, described below, to market to customers across the United States, including e-mail, paid search, display advertising, and comparison websites. (Suppl. 9, Hearing Transcript, May 13, 2014 at 30-31). Neither Newegg, nor any third parties acting on its behalf, engaged in any activities in Ohio in connection with these additional interstate marketing channels. (Suppl. 6, 10-15, 19, 66-67, Hearing Transcript, May 13, 2014 at 18, 36-38, 41-43, 47-48, 53-54, 70-72, 260-262).

First, Newegg promoted its business using email. (Suppl. 9-10, 66, Hearing Transcript, May 13, 2014 at 30-36, 260). Newegg arranged for third-party service providers to send email promotions to consumers across the globe from locations outside of Ohio. (*Id.*). All of Newegg's email vendors were located in California. (Suppl. 9, Hearing Transcript, May 13, 2014 at 32).

Second, Newegg marketed its business through online advertising. (Suppl. 9-15, Hearing Transcript, May 13, 2014, at 30-31, 36-50). In "paid search," an advertisement is displayed by a search engine. (Suppl. 10, Hearing Transcript, May 13, 2014 at 36-37). Newegg never used a paid search provider located in Ohio, nor was the Company's paid search marketing conducted in Ohio. (Suppl. 9-10, Hearing Transcript, May 13, 2014 at 37-38).

Third, Newegg arranged for advertisements to be displayed (or "published") on third-party websites either by contracting directly with the website's publisher or using an "ad server" to deliver the content of the advertisement to the publisher. (Suppl. 11, Hearing Transcript, May 13, 2014 at 38-39). None of the ad servers or publishers that Newegg used was located in Ohio. (Suppl. 13, Hearing Transcript, May 13, 2014 at 47-48).[1]

[1] Newegg also contracted separately with Google, located in California, to display ads from other companies on the Newegg website. (Suppl. 30, Hearing Transcript, May 13, 2014 at 116-117).

Fourth, Newegg published advertisements through "ad networks" that served as intermediaries for multiple (typically smaller) websites. (Suppl. 11, Hearing Transcript, May 13, 2014 at 40-41). None of these ad networks was located in Ohio. (Suppl. 11-12, Hearing Transcript, May 13, 2014 at 40-43). Newegg specified the general website categories on which ads would be displayed, but it neither knew the identify of, nor could specify, the websites that displayed those ads. (Suppl. 12-13, Hearing Transcript, May 13, 2014 at 43-47).

Some ad networks offered so-called "affiliate" advertising in which a retailer contracts with an ad network to display advertisements on other websites in exchange for compensation based on the sales that result from the advertisements. (Suppl. 15, Hearing Transcript, May 13, 2014 at 54-56). During the relevant time period, Newegg used Commission Junction, a California company, for its affiliate advertising placements. (Suppl. 15, Hearing Transcript, May 13, 2014 at 54). Newegg never requested that Commission Junction identify an affiliate based on where the affiliate was located, and never targeted Ohio affiliates. (Suppl. 15, Hearing Transcript, May 13, 2014 at 55). Indeed, Newegg never targeted Ohio customers through affiliate marketing. (*Id.*). At the conclusion of the audit, the Department found that Newegg's affiliate program did *not* cause Newegg to be subject to the CAT during the Tax Periods. (*See*, Statutory Transcript, Department of Taxation Audit Remarks (updated as of Dec. 9, 2010) at AR-11 – AR-12 of 18.)

Finally, Newegg used comparison shopping websites to promote its products. (Suppl. 14, Hearing Transcript, May 13, 2014 at 52-53). Comparison shopping websites collect data feeds from competing merchants so that shoppers can engage in comparison shopping based on price, shipping costs, or other factors. (*Id.*). None of the comparison shopping websites used by Newegg was located in Ohio. (Suppl. 14, Hearing Transcript, May 13, 2014 at 52-53).

Newegg's only non-Internet marketing effort was a limited campaign to increase awareness of Newegg by college students through print advertisements. (Suppl. 35, Hearing Transcript, May 13, 2014 at 134-135). In this regard, Newegg contracted with CampusLink, a company in California, to do a national mailing of posters and brochures to colleges and universities across the country, including one university in Ohio. (Suppl. 35-36, 56, 117, Hearing Transcript, May 13, 2014 at 135-138, 218-219, May 14, 2014 at 457-458). Identical posters and brochures were sent to all schools. (Suppl. 95, Hearing Transcript, May 14, 2014 at 369-370). CampusLink performed no other services for Newegg. (Suppl. 35, Hearing Transcript, May 13, 2014 at 136). Newegg had no agreements with any of the colleges or universities included in the mailings.

In sum, Newegg promoted its Internet business only through national marketing and advertising programs that were conducted outside of Ohio and did not target the residents of any particular state. (Suppl. 6, 10-15, 19, 66-67, Hearing Transcript, May 13, 2014 at 18-19, 36-38, 41-43, 47-48, 53-54, 70-72, 260-262). The Commissioner offered *no* contradictory evidence showing that Newegg, or any individual or company acting on its behalf, engaged in any activities in Ohio. *Nothing* in the record before the Board, therefore, shows that Newegg performed any in-state activities in Ohio.

C. The Commissioner's Internet Nexus Theory.

Faced with a company that did business through the Internet and engaged in no activities in Ohio, the Commissioner took the position before the Board that interstate online sales created the "functional equivalent" of a physical presence in the Ohio.

As articulated by the Commissioner's experts, the Commissioner claims that when an Ohio consumer interacts with his or her own computer in Ohio, such interaction is a "local interaction" that "take[s] place on the user's computer and/or the user's mobile phone." (Suppl.

174, Hearing Transcript, June 17, 2014, 162-163). This purported "local interaction" supposedly creates an in-state physical presence of Newegg in Ohio. (Suppl. 164, 174, 253-254, Hearing Transcript, June 17, 2014 at 124, 162-163, 238-243). Going further, the Commissioner's expert asserted that the interstate interaction between Newegg and its customers is the "functional equivalent" of the door-to-door salesperson sitting in the consumer's home because in both cases the retailer seeks to make a sale to the consumer. (Suppl. 257, Hearing Transcript, June 17, 2014 at 254-257).[2] The Commissioner's experts conceded that, under this theory, an online retailer would have the "functional equivalent" of a physical presence not only in Ohio, but in every other jurisdiction around the globe when an Internet user located there decides to visit the retailer's website. (Suppl. 254, 257, Hearing Transcript, June 17, 2014 at 242, 254-257).

The reports and testimony of the Commissioner's own experts, however, make clear that a connection between an Ohio Internet user and an out-of-state Internet retailer is purely interstate in nature, not local. The customer initiates this interstate contact with the retailer, by inputting a retailer's Internet address into his or her browser while using the Internet (in the same way that a consumer dials a telephone number or addresses an envelope). (Suppl. 6, 20, 81-82, 168, Hearing Transcript, May 13, 2014 at 19-20, 76, May 14, 2014 at 314-317, 323, June 17, 2014, at 139). The out-of-state server then responds, again via interstate communication

[2] Analogizing an Internet sale to a door-to-door sale is not appropriate, however, because *all* sales communications—whether by mail, telephone, or over the Internet—involve communications with a customer or potential customer. (Suppl. 85-86, Hearing Transcript, May 14, 2014 at 332-333). Some, like the in-home salesperson and a telephone call across state lines, involve the retailer and consumer actually speaking to one another. (Suppl. 86, Hearing Transcript, May 14, 2014 at 333-335). Others, like websites, e-mails, and catalogs, permit the transmittal of written words and images. (Suppl. 87, Hearing Transcript, May 14, 2014 at 336-338). While retailers using mail order, telephone, and Internet communications each pursue sales, that similarity does not transform those means of communication into a physical presence like that of a sales person hawking products from door to door. (Suppl. 92, Hearing Transcript, May 14, 2014 at 357-358).

channels, by transmitting a website over the Internet for the customer to view through his or her browser. (Suppl. 20, 181, Hearing Transcript, May 13, 2014 at 76, May 14, 2014 at 317).

Nor is there any dispute that a web "browser" is software licensed by the Internet user, not the retailer, or that the browser is the "user's agent" which the user, not the retailer, employs to view Internet content or make purchases. (Suppl. 81-82, 100, 139, 164, Hearing Transcript, May 14, 2014 at 314-317, 389-390, Hearing Transcript, June 17, 2014 at 22-23, 124). The consumer selects and controls the browser and the websites the browser visits; can configure the browser to the user's specifications; can freely purge information stored on the browser; and, indeed, can delete the browser entirely from his or her computer. (Suppl. 100, 164, Hearing Transcript, May 14, 2014 at 389, Hearing Transcript, June 17, 2014 at 124).

The Commissioner further argued that Internet retailers have an in-state presence through "digital assets" such as "cached" images and cookies that are downloaded to the computers of Internet users as part of the Internet communication process, but this theory is as ephemeral as the purported "assets" themselves. The "cache" is simply a digital file (or file folder) kept for the benefit of the user. (Suppl. 83, Hearing Transcript, May 14, 2014 at 321). Specifically, when a user visits a website, the web browser may save certain files it needs to display the website. (*Id.*). The next time the user visits that website, the website will load faster because the consumer's browser loads an image from the consumer's hard drive rather than the slower process of downloading another copy of that same image from the retailer's server. (Suppl. 68, 83, Hearing Transcript, May 13, 2014 at 266-268, May 14, 2014 at 321). An Internet seller does not, however, access or control the visitor's cache. (Suppl. 68, 85, Hearing Transcript, May 13, 2014 at 268, Hearing Transcript, May 14, 2014 at 330-331). Rather, an individual user controls his or her own cache and can delete the entire cache—or even particular items within that cache. (Suppl. 83, 156, 167, Hearing Transcript, May 14, 2014 at 322, June 17, 2014 at 90-91, 134).

The Commissioner also claimed that a "functional equivalent" of a physical presence was created based upon so-called digital "cookies" sent to consumers—along with the images and text—over the Internet from the websites they visit. (Suppl. 83-84, 181, 255-257, Hearing Transcript, May 13, 2014 at 323-329, June17, 2014 at 190-191, 249-256). A "cookie" is a short text file containing a string of ones and zeroes. It is not something physical that can be touched or felt. (Suppl. 83-84, 147, 157, Hearing Transcript, May 13, 2014 at 323-326, 328, June 17, 2014 at 56, 97). If a user visits Newegg's website, Newegg's server—like virtually every other website server—transmits these small text file "cookies" to the user's computer in order to allow the server to identify the computer that is visiting the website and so that it can record certain user data to improve consumer experience on the Newegg website. (Suppl. 59, 83-84, 147-148, Hearing Transcript, May 13, 2014 at 232-233, 323-329, June 17, 2014 at 57-58). Cookies only let a retailer like Newegg know when a specific *computer* has returned to access its website; Newegg cannot identify the particular individual using that computer based on the cookie. (Suppl. 162, Hearing Transcript, June 17, 2014 at 114). Indeed, a user must initiate contact with the Newegg servers via his or her browser before cookies will ever be transmitted to the user's computer; the web server never initiates contact with the user's browser to transmit cookies. (Suppl. 60, Hearing Transcript, May 13, 2014 at 235). It is up to the user, via settings on his or her browser, to decide whether or not to accept cookies. (Suppl. 60, 102, 155, 166, Hearing Transcript, May 13, 2014 at 236, May 14, 2014 at 400, and June 17, 2014 at 87, 133).

Many Internet retailers, including Newegg, also permit certain third parties to place cookies on the retailer's website, which may then be stored if a consumer permits his or her browser to do so. These third party cookies may allow a server to record information about the pages visited by the computer (through its browser) as well as the links followed by the computer (again, through its browser), *i.e.*, so-called "clickstream" data. Newegg used certain third-party

vendors, all of which were located outside of Ohio, to collect and analyze such aggregate data on the navigation of its web site by visiting computers. (*See* Suppl. 6-8, 57, 61, Hearing Transcript, May 13, 2014 at 21-26, 222-223). Newegg never sorted the aggregated data by geography, or used it to "profile" or target customers based on their location, and the aggregate data would include information gathered from Internet users across the United States. (Suppl. 6-8, 118-119, 173, Hearing Transcript, May 13, 2014 at 21-26, May 14, 2014 at 464-465, June 17, 2014 at 159-160). Third-party cookies also permit a kind of display advertising through ad networks that is loosely referred to in the industry as "retargeting." (Suppl. 13-14, Hearing Transcript, May 13, 2014 at 47-50). All of the ad networks Newegg used for retargeting services were located outside of Ohio. (Suppl. 13-14, 18-19, Hearing Transcript, May 13, 2014 at 47-50, 69-72, May 14, 2014 at 347).

The Commissioner also suggested before the Board that mobile "apps" downloaded by consumers (including in Ohio) for use on their mobile devices create an in-state presence for a retailer. Newegg did not have a mobile website until 2008, and only made available a mobile app beginning in the fourth quarter of 2009. (Suppl. 15, Hearing Transcript, May 13, 2014 at 56). It is a customer's choice to download the app and the customer may choose to delete the app at any time. (Suppl. 58, Hearing Transcript, May 13, 2014 at 227). Newegg did not use the mobile website or mobile apps to market to customers based on location, nor was it aware that location data was even available. (Suppl. 15, Hearing Transcript, May 13, 2014 at 56-57).

In sum, the factual record regarding Newegg's Internet marketing during the Tax Period demonstrates that Newegg had no physical presence in Ohio, and that neither Newegg, nor any third parties acting on its behalf, engaged in any activities in Ohio during the Tax Period.

IV. LAW AND ARGUMENT

Newegg challenges the CAT assessments against it on multiple, related grounds, each of which derives from the "substantial nexus" requirement for state taxation under the Commerce Clause. *Complete Auto*, 430 U.S. at 279 ("substantial nexus" test). On numerous occasions, the U.S. Supreme Court has applied the substantial nexus test to state taxes measured by gross receipts. *See, e.g., Tyler Pipe*, 483 U.S. at 250 (the "crucial factor governing nexus" is whether in-state activities by or on behalf of the taxpayer assist it to make a market in the state); *Commonwealth Edison*, 453 U.S. at 626 (an "interstate business must have a substantial nexus with the state before *any* tax may be levied upon it") (Emphasis sic.). While Newegg contends that there are reasonable interpretations of the CAT statute that would be consistent with the substantial nexus requirement, thereby rendering the statute inapplicable to an out-of-state company that conducts no activity in Ohio, the Commissioner takes a different view. In the pleadings in this case, the Commissioner insists that the CAT statute, by its plain terms, permits only one interpretation: that the CAT must apply to all companies that meet the $500,000 sales threshold of R.C. 5751.01(I)(3), regardless of whether they satisfy the Commerce Clause's substantial nexus test. He asserts that Newegg's proposed interpretations of the CAT statute to preserve its constitutionality would render Section (I)(3) *meaningless* and that "the CAT tax applies to persons *whether or not* they have substantial nexus with the state."

Newegg thus begins its argument where the Commissioner demands that it must: namely, with the contention that the CAT assessments against Newegg are invalid because the "bright-line presence" provision of R.C. 5751.01(I)(3) on its face violates the "substantial nexus" requirement of the Commerce Clause. Newegg then demonstrates that R.C. 5751.01(I)(3) is unconstitutional as applied to Newegg. Finally, in accordance with the principle that a statute is presumed constitutional, and should therefore be interpreted by the Court so as to avoid a ruling

that the statute, or its application, is unconstitutional, Newegg offers an interpretation of the CAT that bars its application to companies, like Newegg, that have no presence in Ohio and no activities conducted on their behalf in the state.

> **Proposition of Law 1**: R.C. 5751.01(I)(3) is unconstitutional on its face. According to its plain terms, the gross receipts "bright-line presence" provision of R.C. 5751.01(I)(3) requires that the CAT be imposed on a company solely because the company meets a statutory threshold of $500,000 in annual gross receipts from interstate sales to Ohio consumers, irrespective of whether the company has the in-state presence required under the "substantial nexus" standard for state taxes established by the Supreme Court under the Commerce Clause. *E.g.*, *Tyler Pipe*, 483 U.S. at 250-251; *Commonwealth Edison*, 453 U.S. at 626; *Std. Pressed Steel*, 419 U.S. at 562; *Gen. Motors*, 377 U.S. at 447-448.

A. The CAT Statute, On Its Face, Imposes CAT Liability On Retailers With No Physical Presence In The State Who Make Sales To Ohio Customers In Excess Of The Statutory Gross Receipts Threshold.

The CAT is levied on "each person with taxable gross receipts for the privilege of doing business in this state." R.C. 5751.02(A). While the statute extends the reach of the tax to all "persons with substantial nexus with this state"—using the same term the Supreme Court used in *Complete Auto*— it defines the term "substantial nexus" in an unprecedented way, found nowhere in any reported decision by any court. *See* R.C. 5751.01(H)(3). Specifically, the phrase "substantial nexus with this state" includes any company that makes sales of $500,000 or more during a calendar year, irrespective of how it conducts its business and even if it engaged in no activities in Ohio either directly or through a third party. It does so in the following way.

First, R.C. 5751.01(H)(3) states that a person has "substantial nexus with this state" if the person has "bright-line presence" in the state. Second, "bright-line presence" is, in turn, defined to mean, in pertinent part,[3] that a person "has during the calendar year taxable gross receipts of at

[3] The other "bright-line presence" provisions of 5751.01(I), which are irrelevant to Newegg, specify that a company will be subject to the CAT if it is domiciled in the state or has in Ohio (1) at least $50,000 in property, (2) at least $50,000 in payroll, or (3) 25% of its total property, payroll, or gross receipts. *See* R.C. 5751.01(I)(1), (2), (4), (5). Newegg meets none of these

least five hundred thousand dollars." R.C. 5751.01(I)(3). Third, "gross receipts" include amounts derived from the sale of goods to consumers. R.C. 5751.01(F)(1)(a). Fourth, "taxable gross receipts" are gross receipts "sitused to this State under R.C. 5751.033." R.C. 5751.01(G). Finally, gross receipts from the sale of tangible personal property are "sitused" to Ohio (meaning that the CAT statute deems Ohio to be the place at which the gross receipts are realized) if the property is received by the purchaser in Ohio. R.C. 5751.033(E). Newegg's sales via the Internet, which are delivered by common carrier to its customers in Ohio from its warehouses in California, New Jersey, and Tennessee, are thereby "sitused" in Ohio, rendering all of Newegg's interstate sales to Ohio residents "taxable gross receipts" under the CAT.

B. Newegg Received More Than $500,000 In Gross Receipts From Sales Delivered To Ohio Customers And Therefore Has Standing To Challenge The CAT.

There is no dispute that Newegg had more than $500,000 in annual gross receipts from the interstate sales of tangible goods to purchasers in Ohio for all relevant years during the Tax Period. (Suppl. 300-301, Joint Stipulations dated May 13, 2014 ¶¶ 2-3.) In fact, this was the sole basis for the Commissioner's determination to assess the CAT against Newegg, and the sole basis for the Final Determination and the decision of the Board. Appx. 28-30, Final Determination at 1, 3; Appx. 18, Decision and Order at 4. Newegg therefore has standing to challenge the constitutionality of the gross receipts "bright-line presence" provision of the CAT, R.C. 5751.01(I)(3). *See Palazzi v. Estate of Gardner*, 32 Ohio St.3d 169, 175, 512 N.E.2d 971 (1987) (a party within the class to whom the statute applies has standing to challenge its constitutionality).

---

standards, was not assessed based on them, and does not challenge the constitutionality of these provisions.

C. Newegg Satisfies The Standards For A Facial Constitutional Challenge.

1. Newegg's Facial Challenge To The CAT Statute Depends Upon No Extrinsic Facts.

A facial constitutional challenge calls upon the Court to review "only the text of the statute itself" without regard to any "extrinsic facts." *Global Knowledge Training, L.L.C. v. Levin*, 127 Ohio St.3d 34, 2010-Ohio-4411, 936 N.E.2d 463, ¶¶ 17, 18 (citing *Cleveland Gear Co. v. Limbach*, 35 Ohio St.3d 229, 231, 520 N.E.2d 188 (1988)). Newegg contends that the "bright-line presence" provision of R.C. 5751.01(I)(3) is unconstitutional because, by its plain terms, it imposes liability for the CAT on a company based *solely* on the company making sales of at least $500,000 in a calendar year of products that are delivered to Ohio customers, and without regard to any other activities by, or on behalf of, the company. No extrinsic facts are required to evaluate this statutory "bright-line presence" provision against the Commerce Clause substantial nexus standard established by the Supreme Court in a long line of cases.

Indeed, the Commissioner insists, and the Board agreed below, that nothing more than gross receipts by a company in excess of the statutory threshold is required for liability under the CAT statute to attach. *See* Appx. 18, Decision and Order at 4 (finding that under the plain language of R.C. 5751.01(H)(3) and (I)(3), a company with more than $500,000 in sales to Ohio purchasers "has substantial nexus within this state by virtue of its gross receipts").

2. The "Presumption Of Constitutionality" Cannot Preserve A Statutory Provision That Is Plainly Unconstitutional On Its Face.

The Court has explained that statutes enjoy a "strong presumption of constitutionality." *Beaver Excavating Co. v. Testa*, 134 Ohio St.3d 565, 2012-Ohio-5776, 983 N.E.2d 1317, ¶ 27. As a result, "it must appear beyond a reasonable doubt that the legislation and constitutional provisions are clearly incompatible" before a statutory provision may be struck down as

unconstitutional. (Citation omitted.) *Arbino v. Johnson & Johnson*, 116 Ohio St.3d 468, 2007-Ohio-6948, 880 N.E.2d 420, ¶ 25.

These familiar principles, however, do nothing to defeat Newegg's facial challenge, nor its as-applied challenge, as set forth below. Rather, they simply reinforce the basic rule of statutory interpretation that the statute must be construed, if at all possible, to avoid rendering it unconstitutional. R.C. 1.47(A); *see SFA Folio Collections, Inc. v. Tracy*, 73 Ohio St.3d 119, 123, 652 N.E.2d 693 (1995) (reading a state tax statute to "conform with the Commerce Clause" because conformity with the constitution is a "presumed legislative intention"). Thus, while a reviewing court must indulge a presumption in favor of constitutionality, the presumption simply means that "where a statute reasonably allows for more than a single construction or interpretation, it is the duty of the court to choose that construction or interpretation which will avoid rather than raise serious questions as to its constitutionality." *Buchman v. Wayne Trace Local School Dist. Bd. of Edn.*, 73 Ohio St.3d 260, 269, 652 N.E.2d 952 (1995). The "presumption" of constitutionality, however, cannot cure a constitutional violation that is evident on the face of the statute. *See Peebles v. Clement*, 63 Ohio St.2d 314, 321, 408 N.E.2d 689 (1980) (despite the strong presumption of constitutionality, the Court "in interpreting a statute, cannot simply rewrite it to make it constitutional"). Nor does it permit the Commissioner or a reviewing court to ignore established constitutional doctrine.[4]

---

[4] The rationale for the presumption of constitutionality has been questioned. *See Ohio Grocers*, 2009-Ohio-4872, ¶¶ 71-72 (Pfeifer, J., dissenting) (noting that legislators may well rely on the Court to determine the constitutionality of statutory enactments). Here, section 5751.31 of the CAT statute indicates that "the General Assembly explicitly anticipated the constitutional challenge" raised by Newegg. *See Beaver Excavating*, 2010-Ohio-5776, ¶ 12 (citing R.C. 5751.31). In particular, R.C. 5751.31 creates a special procedure for a direct appeal to this Court of certain specific issues, including the constitutionality of the CAT statute's "substantial nexus" provision, R.C. 5751.01(H)(3). Thus, when adopting the statute, the General Assembly invited review of its constitutionality.

Based on these basic principles, Newegg has consistently urged both the Commissioner and the Board below to interpret the CAT statute so as not to apply to Newegg for the very purpose of preserving the statute's constitutionality. *See* Appx. 3-4, 6-8, Notice of Appeal at 3-4, 6-8 (discussing Newegg's arguments and asserted Error of Law regarding erroneous statutory interpretation). The Commissioner, however, has insisted below and in response to Newegg's appeal to this Court that no such interpretation of the CAT statute is possible. *See, e.g.*, Appx. 30, Final Determination at 3. He argues that the General Assembly expressly enacted a mandatory gross receipts "bright-line presence" test that creates CAT liability without regard to any constitutional limitations on the State's taxing powers. Thus, the Commissioner contends there is no saving the CAT statute if the gross receipts test for CAT liability—which permits the imposition of tax on companies with no connection to the state apart from receiving at least $500,000 per year in sales revenue—violates the Commerce Clause.

3. Newegg's Facial Challenge Under The Commerce Clause Is Not Defeated By The "No Set Of Circumstances" *Salerno* Test.

In cases involving facial challenges brought under constitutional provisions other than the Commerce Clause, this Court has applied the so-called *Salerno* test in which a challenger must establish that there "exists no set of circumstances under which the statute would be valid" or, stated differently, that "the law is unconstitutional in all of its applications." *E.g., Arbino*, 2007-Ohio-6948, ¶ 26 (citing *United States v. Salerno*, 481 U.S. 739, 745, 107 S.Ct. 2095, 95 L.Ed.2d 697 (1987) for the "no set of circumstances" test); *State v. Romage*, 138 Ohio St.3d 390, 2014-Ohio-783, 7 N.E.3d 1156, ¶ 7 (the "unconstitutional in all of its applications" test). This Court, however, has *never* applied the *Salerno* test to a facial challenge under the Commerce Clause, even though it has applied this test when reviewing challenges based on other constitutional provisions. In *Columbia Gas Transm. Corp. v. Levin*, 117 Ohio St.3d 122, 2008-Ohio-511, 882

N.E.2d 400, ¶¶ 43, 53-78, this Court analyzed a Due Process claim under the "unconstitutional in all of its applications" standard, but did not apply this test to claims under the Commerce Clause. Similarly, in *Emerson Elec. Co. v. Tracy*, 90 Ohio St.3d 157, 159-60 735 N.E.2d 445 (2000), the Court did not apply the "no set of circumstances" test to a challenge under the dormant aspect of the Foreign Commerce Clause. Indeed, the dissent in *Emerson Electric* expressly noted that the Court had chosen not to apply the *Salerno* "no set of circumstances" formulation in striking down the law challenged in that case. *See* 90 Ohio St.3d at 162-163 (Cook, J., dissenting).

The U.S. Supreme Court has likewise never applied the *Salerno* test to a facial challenge brought against a state statute, let alone a state tax statute, under the Commerce Clause. *See, e.g.*, *Comptroller of the Treasury of Maryland v. Wynne*, ___ U.S. ___, 135 S.Ct. 1787, 1801-1805, 191 L.Ed.2d 813 (2015) (evaluating challenge to state tax under applicable Commerce Clause test); *Camps Newfound/Owatonna, Inc. v. Town of Harrison,* 520 U.S. 564, 575–582 117 S.Ct. 1590, 137 L.Ed.2d 852 (1997) (same); *Quill Corp. v. North Dakota*, 504 U.S. 298, 313-318, 112 S.Ct. 1904, 119 L.Ed.2d 91 (1992) (same); *New Energy Co. v. Limbach*, 486 U.S. 269, 274–280, 108 S.Ct. 1803, 100 L.Ed.2d 302 (1988) (same). Indeed, "[f]ollowing *Salerno*, the [Supreme] Court has repeatedly considered facial challenges simply by applying the relevant constitutional test to the challenged statute without attempting to conjure up whether or not there is a hypothetical situation in which application of the statute might be valid." *Doe v. City of Albuquerque*, 667 F.3d 1111, 1124–1125 (10th Cir. 2012) (brackets added) (collecting cases).[5]

[5] In fact, as commentators and courts have noted, including a plurality of the Supreme Court, the "no set of circumstances" formulation has "never been the decisive factor in any decision of the [Supreme Court], including *Salerno* itself." *Id.* at 1125–1126 (citing *City of Chicago v. Morales*, 527 U.S. 41, 55 n.22, 119 S.Ct. 1849, 144 L.Ed.2d. 67 (1999) and collecting cases). Instead, application of the relevant constitutional standards to the statute's plain terms remains the paramount inquiry and dictates the nature of the Court's review.

Furthermore, the Supreme Court itself declined to apply *Salerno* to a challenge brought to a state income tax statute under the foreign commerce prong of the Commerce Clause. *See Kraft Gen. Foods, Inc. v. Iowa Dept. of Revenue and Fin.*, 505 U.S. 71, 82–83, 112 S.Ct. 2365, 120 L.Ed.2d 59 (1992) (Rehnquist, J. dissenting) (arguing that the Court should have applied *Salerno*); *see also Emerson Elec.*, 90 Ohio St.3d at 162-163 (Cook, J., dissenting) (commenting on Chief Justice Rehnquist's dissent in *Kraft*). The highest courts of at least three other states have since rejected the "no set of circumstances" test in the context of a similar facial challenge to a state tax statute. *See Conoco, Inc. v. Taxation & Revenue Dept.*, 122 N.M. 736, 742–743, 931 P.2d 730 (1996), *cert. denied*, 521 U.S. 1112, 117 S.Ct. 2497, 138 L.Ed.2d 1003 (1997); *Caterpillar, Inc. v. Commr. of Revenue*, 568 N.W.2d 695, 700 n.8 (Minn. 1997), *cert. denied*, 522 U.S. 1112, 118 S.Ct. 1043, 140 L.Ed.2d 108 (1998); *Caterpillar, Inc. v. New Hampshire Dept. of Revenue Administration*, 144 N.H. 253, 258, 741 A.2d 56 (1999).

Even if Newegg were required to show that there is no set of circumstances in which the CAT statute's gross receipts "bright-line presence" provision could be validly applied, Newegg's challenge satisfies that standard. Newegg contends that the gross receipts "bright-line presence" standard is *never* adequate, in and of itself, to satisfy the in-state presence requirement of substantial nexus under governing U.S. Supreme Court precedent. Indeed, the Commissioner's sole basis for the assessment against Newegg was the "bright line presence" test of sales of at least $500,000 under R.C. 5751.01(I)(3). Appx. 28-30, Final Determination at 1, 3. Thus, Newegg's claim in this case is that R.C. 5751.01(I)(3), can never be validly applied—and thus is invalid in all of its possible applications—in light of the Commerce Clause's substantial nexus standard.

Nor can reference to some other part of the CAT statute—such as the other "bright-line presence" provisions, which are based on having property or payroll (*i.e.*, employees) in the

state, or the provision that extends the CAT statute to include any in-state presence that is otherwise sufficient to satisfy the requirements of the Commerce Clause—save the constitutionality of the gross receipts "bright line presence" provision of R.C. 5751.01(I)(3). *See* R.C. 5751.01(H)(4) & (I)(1), (2), (4). As the Supreme Court has recently emphasized, in reviewing a facial challenge to a local law, the "[l]egislation is measured for consistency with the Constitution by its impact on those whose conduct it affects. * * * The proper focus of the constitutional inquiry is the group for whom the law is a restriction, not the group for whom the law is irrelevant." (Internal citation omitted.) *City of Los Angeles v. Patel*, ___ U.S. ___, 135 S.Ct. 2443, 2451 (2015). In fact, the Commissioner recognized in assessing Newegg on the basis of R.C. 5751.01(I)(3) that this section forms a separate and segregable basis, apart from the other sections of the CAT statute, to require a company such as Newegg to pay the CAT. The other provisions of the CAT statute are not relevant to a constitutional challenge to Section (I)(3).

In sum, Newegg is not required to make an additional showing to demonstrate that R.C. 5751.01(I)(3) is unconstitutional on its face, beyond what is required under the applicable standards of the Commerce Clause, to which we now turn.

D. The Commerce Clause Bars Ohio From Imposing The CAT On Companies Based Solely On The Amount Of Sales Made To Customers In The State.

The Commerce Clause delegates to Congress the power "[t]o regulate commerce * * * among the several States." U.S. Constitution, Article I, Section 8, cl. 3. The Commerce Clause has a corresponding "negative" or "dormant" aspect, which expressly restricts the authority of a state to impose undue burdens on interstate commerce. *Oregon Waste Sys., Inc. v. Dept. of Environmental Quality*, 511 U.S. 93, 98, 114 S.Ct. 1435, 128 L.Ed.2d 13 (1994).

Under contemporary dormant Commerce Clause analysis, a state tax on interstate commerce is invalid under the Constitution unless the tax satisfies each of the four prongs of

Complete Auto, 430 U.S. at 279. Under that test, to survive a challenge, a state tax must be (1) applied to an activity with a substantial nexus with the taxing State, (2) fairly apportioned, (3) non-discriminatory with respect to interstate commerce, and (4) fairly related to the services provided by the State. *Id.; Hillenmeyer v. Cleveland Bd. of Review*, 2015-Ohio-1623, ¶ 11. This case concerns the first prong of the *Complete Auto* test—substantial nexus—which is designed to "limit the reach of state taxing authority so as to ensure that state taxation does not unduly burden interstate commerce." *Quill Corp*., 504 U.S. at 313 and n.6. With regard to this prong, the Supreme Court has emphasized in reviewing a tax measured by gross receipts that "[u]nder this threshold test, the interstate business must have a substantial nexus with the State before *any* tax may be levied on it." (Emphasis sic.) *Commonwealth Edison*, 453 U.S. at 626 (citing *Natl. Bellas Hess, Inc. v. Illinois Dept. of Revenue*, 386 U.S. 753, 759, 87 S.Ct. 1389, 18 L.Ed.2d 505 (1967)).

Complete Auto has become the "leading case" regarding the constitutionality of all types of state taxes. *D.H. Holmes Co. v. McNamara*, 486 U.S. 24, 30, 108 S.Ct 1619, 100 L.Ed.2d 21 (1988) (noting application of *Complete Auto* to different types of state taxes). In *Complete Auto*, the Court surveyed its Commerce Clause jurisprudence and formulated this four-pronged test for determining the constitutionality of a state tax in light of principles central to the Commerce Clause. *See* 430 U.S. at 279-286. The Court cited, in particular, four of its decisions that formed the basis for its test. *Id.* at 279 and n. 8. *Complete Auto* itself involved a tax on the privilege of doing business in Mississippi based on the taxpayer's gross receipts, and the four decisions highlighted by the Court involved a variety of state taxes, including a privilege tax measured by gross receipts (*General Motors*), an income tax (*Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 79 S.Ct. 357, 3 L.Ed. 421 (1959)), a franchise tax (*Memphis Natural Gas Co. v. Stone*, 335 U.S. 80, 68 S.Ct. 1475, 92 L.Ed. 1832 (1948)), and a

dividends tax (*Wisconsin v. J.C. Penney*, 311 U.S. 435, 61 S.Ct. 246, 85 L.Ed. 267 (1940)). In each of these cases, the taxpayer engaged in significant in-state activities that satisfied the "substantial nexus" prong of the Court's four-part test. *See Gen. Motors*, 377 U.S. at 442-446 (corporation maintained a branch office and warehouses in the state, and had employees both based in, and who travelled to, the state to call on dealers and staff the warehouse); *Northwestern States*, 358 U.S. at 454-456 (taxpayers had in-state sales and support personnel who regularly solicited orders and communicated with customers in the state); *Memphis Natural Gas*, 335 U.S. at 81 (company had 135 miles of pipeline, two compressing stations, and employees in the state who maintained the pipeline); *Wisconsin v. J.C. Penney*, 311 U.S. at 250-251 (reversing *J.C. Penney Co. v. Wisconsin Tax Comm.*, 233 Wis. 286, 289 N.W. 677, 678, 682 (1940) (state court decision invalidating dividends tax despite presence of nearly 50 retail stores operated by the company)).

The in-state activities requirement embodied in these cases has deep roots. In its gross receipts tax decisions, the Supreme Court has made clear for over 50 years that a state's power to impose such a tax on a non-domiciliary company depends upon whether the out-of-state company engages in activities within the state, either directly or through third-party representatives, that assist the company in making or maintaining a market in the state. An early illustration of the rule was the Court's decision in *General Motors*, which later formed part of the basis for the *Complete Auto* test. In analyzing the constitutionality of the Washington Business & Occupation Tax ("B&O tax") under the Commerce Clause, the Court explained that "[w]here, as in the instant case, the taxing State is not the domiciliary State, *we look to the taxpayer's*

business activities within the State" to determine the constitutionality of a privilege tax measured by gross receipts. (Emphasis added.) 377 U.S. at 441.[6]

The *General Motors* Court reviewed in detail the facts regarding the company's in-state activities. *Id.* at 442-446. Although General Motors was incorporated outside of Washington and had its principal regional offices in Oregon, various divisions of General Motors each had 20 or more employees located in Washington who called-on and supported an in-state network of General Motors dealers. *Id.* at 443-445. The Court found that the in-state employees "performed substantial services in relation to General Motors' functions [in the state], particularly with relation to the establishment and maintenance of sales, upon which the tax was measured." *Id.* at 447. The Court concluded that "we cannot say that the Supreme Court of Washington erred in holding that *these local incidents were sufficient to form the basis* for the levy of a tax that would not run afoul of the Constitution." (Emphasis added.) *Id.* at 447-448.

A decade later, shortly before *Complete Auto* was decided, the Court relied on *General Motors* in again sustaining the Washington B&O tax against a challenge brought by an out-of-state company with an in-state presence. *Std. Pressed Steel*, 419 U.S. at 563. In *Standard Pressed Steel*, the appellant had no offices in Washington, but maintained a full-time employee working in the state whose primary responsibility was consulting with the company's principal in-state customer, Boeing. *Id*. at 561. The Court found that the employee "made possible the realization and continuance of valuable contractual relations between appellant and Boeing." *Id.*

---

[6] In fact, the significance of a company's in-state presence to the validity of a gross receipts tax had been emphasized by the Court even before it decided *General Motors*. *See Field Ents.*, 352 U.S. 806 (per curiam), *aff'ing Field Ents. v. Washington*, 47 Wash.2d at 856 (in-state office, division manager, three district managers, four office employees and 175 salespeople in the state were "decisive factors in establishing and holding the market in this state" for company's products)); *see also Norton Co. v. Dept. of Revenue*, 340 U.S. 534, 537, 71 U.S. 377, 95 L.Ed. 517 (1951) (state lacks authority to impose gross receipts tax on company with no "local incident" in the state).

at 562. The Court thus sustained the tax against a Commerce Clause challenge, concluding that *General Motors* was "almost precisely on point" in that the taxpayer's in-state activities were a substantial factor in establishing and maintaining its market for sales in the state. *Id.* at 563.

After *Complete Auto*, the Court continued to stress the significance of a taxpayer's in-state presence to the validity of a gross receipts tax under the "substantial nexus" standard. In 1978, the Court reiterated *Complete Auto's* four-part test in connection with a challenge to the Washington B&O tax. *Dept. of Revenue v. Assn. of Washington Stevedoring Cos.*, 435 U.S. 734, 750, 98 S.Ct. 1388, 55 L.Ed.2d 682 (1978) (Commerce Clause challenge rejected because of the "obvious nexus between Washington and respondents; indeed, respondents conduct their entire stevedoring operations within the State."). Three years later, in *Commonwealth Edison*, the Court found that a tax on the activity of "severance" of coal removed from a state was properly imposed on transactions in interstate commerce under the *Complete Auto* test. 453 U.S. at 629. The Court noted that *Complete Auto* requires that an "interstate business must have a substantial nexus with the State before *any* tax may be levied on it." (Internal citation omitted.) (Emphasis sic.) *Id*. at 626. The Court further commented that there was no dispute regarding a sufficient in-state presence in that case, since "a substantial, in fact, the only nexus of severance of coal is established in Montana." *Id.* at 617.

Against this back-drop, the Court issued its landmark decision in *Tyler Pipe* regarding taxes measured by gross receipts. The appellant, Tyler Pipe, was a Texas-based company with no office, property or employees in Washington. 483 U.S. at 249. Although Tyler Pipe itself had no direct presence in the taxing state, the company engaged an independent contractor in Washington whose salespeople "acted daily on behalf of Tyler Pipe in calling on its customers and soliciting orders" and thereby "maintain[ed] and improve[d] the name recognition, market

share, goodwill, and individual customer relations of Tyler Pipe." (Internal citation omitted.) (Brackets added.) *Id.*

The Court rejected Tyler Pipe's argument that it lacked the necessary substantial nexus with the state. Relying on two of the Court's sales and use tax precedents, the Court ruled that the in-state presence of the sales representatives was properly attributed to Tyler Pipe despite the fact that that they were independent contractors, rather than employees. *Id.* at 250 (citing *Scripto, Inc. v. Carson*, 362 U.S. 207, 209, 80 S.Ct. 619, 4 L.Ed.2d 660 (1960) (nexus based on ten commissioned sales agents conducting continuous solicitation in the state) and *Natl. Geographic Soc. v. California Bd. of Equalization*, 430 U.S. 551, 556-558, 97 S.Ct. 1386, 51 L.Ed.2d 631 (1977) (in-state sales office unrelated to taxable sales was sufficient for nexus)). Endorsing the decision of the Washington Supreme Court below, the Court stated that "the crucial factor governing nexus is whether *the activities performed in this state on behalf of the taxpayer* are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales." (Emphasis added.) *Id.*

Furthermore, *Tyler Pipe* made clear that mere sales to in-state customers resulting in gross receipts are not sufficient, in and of themselves, to satisfy the substantial nexus requirement of the Commerce Clause. The Court expressly found that the company sold a "large volume of cast iron, pressure and plastic pipe and fittings, and drainage products" in the state. 483 U.S. at 249. Even with evidence of such substantial sales to in-state customers, the Court focused on the company's in-state presence as the basis for the required "substantial nexus" with the state: "We agree that *the activities of Tyler's sales representatives* adequately support the State's jurisdiction to impose its wholesale tax on Tyler." (Emphasis added.) 483 U.S. at 251.

In nearly 30 years since *Tyler Pipe* was decided, the Supreme Court has never held that a different or lesser standard than the in-state presence requirement of *Tyler Pipe* and its forebears

applies to state gross receipts taxes. Meanwhile, numerous state courts have relied on *Tyler Pipe's* in-state presence requirement as the touchstone of "substantial nexus" in a variety of contexts. *E.g.*, *Travelocity.com LP v. Wyoming Dept. of Revenue*, 2014 WY 43, ¶¶ 68-83, 329 P.3d 131 (upholding sales tax assessment against online travel sites based on the activities conducted on their behalf by hotels in the state); *Barnesandnoble.com LLC*, 2013 NMSC 023, ¶¶ 8-10 (upholding assessment of New Mexico Gross Receipts Tax based on the activities of an affiliated company in the state); *Scholastic Book Clubs, Inc. v. Commr. of Revenue Servs.*, 304 Conn. 204, 230, 38 A.3d 1183 (2012) (in-state school teachers who assisted students in ordering books established nexus sufficient for imposition of a use tax collection obligation on out-of-state book seller); *Lamtec Corp.*, 170 Wash.2d at 849-851 (affirming gross receipts tax assessment against company whose sales representatives visited customers in the state) ; *Wabash Power Equip., Inc. v. Lindsey.*, 897 So.2d 621, 627 (La.Ct.App. 2004) (in-state presence of employees establishes nexus for purposes of use tax); *Arizona Dept. of Revenue v. O'Connor, Cavanaugh, Anderson, Killingsworth, & Beshears, P.A.*, 192 Ariz. 200, 206, 963 P.2d 279 (Ct.App. 1997) (because the purchaser had nexus for purposes of a transaction privilege tax based on its activities in the state, the service provider was exempt from obligation to collect the Arizona use tax). In fact, in *J.C. Penney Natl. Bank*, 19 S.W.3d at 841-842, the Tennessee court rejected application of gross receipts tax to company with no in-state presence. In short, there is no decision, by the Supreme Court or any other court, in which a state gross receipts tax assessment has been sustained against a company that, like Newegg, engaged in no activities in a state, either directly or through a third-party.[7] *Tyler Pipe's* in-state presence standard remains the law of the land.

[7] The in-state activities requirement for state taxes measure by gross receipts is so well-established that the Board could have applied it below. *See Marysville Exempted Village School*

E. The In-State Presence Requirement Of Substantial Nexus Is Supported By The Supreme Court's Decisions Concerning Sales And Use Taxes.

The in-state presence requirement applied by the Court in its gross receipts tax precedents is reinforced by the Court's decisions regarding the limitations on state authority to require the collection of state sales and use taxes. Indeed, the in-state (or physical) presence requirement draws support from a series of intertwining Commerce Clause precedents concerning both taxes measured by gross receipts and sales taxes.

In *Bellas Hess, supra*, decided in 1967, the Supreme Court held that the State of Illinois lacked the power to impose a sales/use tax collection obligation on a company located outside the state whose only connection to the taxing state was communicating with customers in the state via the instrumentalities of interstate commerce (*e.g.*, United States mail, common carrier, and, today, the Internet). *See Bellas Hess*, 386 U.S. at 758–760. The company had no facilities, property, employees, or representatives in the state. *Id.* at 754. It did, however, mail catalogs and advertising flyers to recipients in the state, and sold goods via mail order to Illinois residents that were delivered to the purchasers via common carrier and the U.S. mail. *Id.* at 754–755. In striking down the Illinois tax provision, the Supreme Court upheld the "sharp distinction" established in prior cases between sellers with a physical presence in the state, and those without a presence who reached customers only via interstate commerce. *Id.* at 758. While the Court primarily focused on its use tax precedents, including *Scripto* (which was cited with approval in *Tyler Pipe*), as support for its ruling, the Court cited a number of other cases concerning the limitations on state taxing power, including *Cent. Greyhound Lines*, *Inc. v. Mealy*, 334 U.S. 653,

---

Dist. Bd. of Edn. v. Union Cty. Bd. of Revision, 136 Ohio St.3d 146, 2013-Ohio-3077, 991 N.E.2d 1134, ¶ 15 (the limitations on Board's jurisdiction over constitutional questions do not preclude it from giving effect to binding precedent); Appx. 6, Notice of Appeal at 6 (Error 1).

663, 68 S.Ct. 1260, 92 L.Ed. 1633 (1948), in which the Court held that a tax on gross receipts was unconstitutional. *See Bellas Hess*, 386 U.S. at 756-758.

The Supreme Court continued to develop and enforce the in-state presence standard of substantial nexus over the next twenty-five years. As noted above, in *Complete Auto*, the Court cited as support for its four-prong test a series of prior decisions, starting with *General Motors*—a gross receipts tax case. *Complete Auto*, 430 U.S. at 279 n.8. During the same term, the Court likewise relied upon a gross receipts tax decision, this time *Standard Pressed Steel*, along with the use tax precedent of *Bellas Hess*, in finding that a company with an in-state presence could be subjected to an obligation to collect sales/use tax on sales that were unrelated to its in-state activity. *Natl. Geographic*, 430 U.S. at 557-558. Four years later, in *Commonwealth Edison*, the Court again cited *Bellas Hess* for the proposition that an "interstate business must have a substantial nexus with the State before *any* tax may be levied on it." (Emphasis sic.) *Commonwealth Edison*, 453 U.S. at 626.

When the Court next addressed a constitutional challenge to a state gross receipts tax in *Tyler Pipe*, the Court again cited two leading sales tax precedents, *Scripto* and *National Geographic*, in support of its conclusion that that "the crucial factor governing nexus is whether the activities performed in this state on behalf of the taxpayer are associated with the taxpayer's ability to make and maintain a market in this state for the sales." 483 U.S. at 250. The language used by the Court in *Tyler Pipe* to describe the nexus requirement ("activities performed in [the taxing] state"), and the Court's underlying reliance upon sales and use tax decisions requiring a physical presence in the state, conclusively demonstrate that a parallel in-state presence requirement applies to both gross receipts taxes and sales and use taxes. *See also Goldberg v. Sweet*, 488 U.S. 252, 263, 109 S.Ct. 582, 102 L.Ed.2d 607 (1989) (reviewing the constitutionality of an excise tax on the gross receipts from an interstate telephone call, and

noting that "[w]e also doubt that termination of an interstate telephone call, by itself, provides a substantial enough nexus for a State to tax a call. *See Natl. Bellas Hess, Inc. v. Dept. of Revenue of Illinois,* 386 U.S 753 (1967) (receipt of mail provides insufficient nexus.)").

Finally, in 1992, the Supreme Court reaffirmed the physical presence requirement of *Bellas Hess* and again held that, under the Commerce Clause, a retailer with no physical presence in the state cannot be obligated to collect a state's use tax. *Quill,* 504 U.S. at 313–319. Like Bellas Hess, the remote seller in *Quill* had no outlets or salespeople in the taxing state, but delivered catalogs and flyers to customers in the state via mail. In finding the statute violated the Commerce Clause's substantial nexus requirement, the Supreme Court reaffirmed that a vendor "whose only connection with customers in the [taxing] State is by common carrier or United States mail" lacks a physical presence in the state for purposes of the "substantial nexus" requirement of the Commerce Clause. *Id.* at 314–315. Moreover, in upholding the physical presence requirement for sales and use taxes, the Supreme Court in *Quill* cited and relied upon four of its earlier decisions involving state taxes measured by gross receipts: *Goldberg, Tyler Pipe, Standard Pressed Steel*, and *Commonwealth Edison. See Quill,* 504 U.S. at 311 (identifying *Goldberg* and *Commonwealth Edison* as continuing the *National Bellas Hess* line of cases) and 314 (citing *Standard Pressed Steel* and *Tyler Pipe* as cases involving taxpayers who had a physical presence). The Court further noted that any "artificiality" at the edges of the "bright line," physical presence test is more than offset by a rule that "firmly establishes the boundaries of legitimate state authority to impose a duty to collect sales and use taxes" and encourages settled expectations among companies potentially subject to state tax obligations. *Id.* at 315–316.

Quill, like *Tyler Pipe*, has never been called into question by any decision of the Supreme Court. To the contrary, the Court has continued to cite *Quill* favorably with regard to the

limitations on state taxing authority under the Commerce Clause. For example, in *Hemi Group, LLC v. City of New York*, the Court rejected an effort by the City to find a creative way to "end-run its lack of authority" under *Quill*. 559 U.S. 1, 17, 18, 130 S.Ct. 983, 175 L.Ed.2d 943 (2010) (Roberts, J., majority; Ginsburg, J. concurring). In its most recent term, the Court cited *Quill* multiple times in reviewing the constitutionality of Maryland's individual income tax, including for the proposition that the Commerce Clause places limits on the authority of a state to regulate interstate commerce, even where the requirements of the Due Process Clause are satisfied. *Wynne*, 135 S.Ct. at 1798-1799, 1808, 1809.[8] The gross receipts, "bright-line presence" provision of the CAT statute clearly oversteps those fundamental limitations, by imposing CAT liability on an out-of-state company based solely on its gross receipts from the sale of products delivered to Ohio customers via common carrier.

F. State Court Decisions Declining To Apply The Physical Presence Standard To State Income Taxes Are Inapposite.

Several state courts have held that the *Quill* physical presence requirement does not apply to state taxes based on income. *See, e.g., KFC Corp. v. Iowa Dept. of Revenue*, 792 N.W.2d 308, 321-328 (Iowa 2010); *Capital Bank One v. Commissioner of Revenue,* 453 Mass.1, 13, 899 N.E.2d 76 (2009); *Geoffrey, Inc. v. South Carolina Tax Comm.*, 313 S.C. 15, 23, 437 S.E.2d 13 (1993). None of these cases concern gross receipts taxes or purport to show that the in-state activities standard of *Tyler Pipe* has been somehow overruled or abrogated by the Supreme Court

[8] Newegg anticipates that the Commissioner will rely heavily on the concurring opinion filed by Justice Kennedy in *Direct Marketing Assn. v. Brohl*, ___ U.S. ___, 135 S.Ct 1124, 191 L.Ed.2d 97 (2015), in which he suggested that the holding of *Quill* should be reexamined. 135 S.Ct. at 1135. No other member of the Court joined Justice Kennedy's concurrence, and a few weeks later the Court issued its decision in *Wynne*, citing *Quill* favorably. *Id*. at 1798-1799, 1808, 1809. For the reasons discussed in Sections H and I, below, the physical presence standard of *Quill* and the requirement for gross receipts taxes of in-state activities performed on behalf of the taxpayer that assist in the establishment and maintenance of a market in the state each embody the most basic principles of the Commerce Clause and retain their vitality in the Internet era.

sub silentio. Instead, the cases are based on the premise that the Supreme Court's decision in *Quill* demonstrates that it would not "extend" the *Quill* physical presence standard to state income taxes. *E.g.*, *KFC Corp.*, 792 N.W.2d at 325; *Capital Bank One*, 453 Mass. at 13; *Geoffrey*, 313 S.C. at 23 n.4.

While state court cases addressing whether a taxpayer must have a physical presence for purposes of a state tax based on income are not, for a variety of reasons, directly relevant to the question of whether the CAT is unconstitutional under the in-state activities requirement of *Tyler Pipe*, it is noteworthy that the underlying rationale of such decisions simply does not apply in the context of a gross receipts tax. The basis for the refusal by some state courts to "extend" the physical presence test to income taxes is the result of ambiguous language in *Quill* concerning "other types" of state taxes. In one such passage from *Quill*, the Supreme Court stated:

> Although we have not, in our review of *other types of taxes, articulated the same physical presence requirement* that *Bellas Hess* has established for sales and use tax, that silence does not imply repudiation of the *Bellas Hess* rule.

(Emphasis added.) 504 U.S. at 314. A proper understanding of this statement, however, requires consideration of the remainder of the paragraph in which this language appeared.

Earlier in the same paragraph in *Quill*, the Supreme Court referred to "these cases" (by which the Court was referencing *Standard Pressed Steel* and *Tyler Pipe*) as involving "taxpayers who had a physical presence in the taxing State." *Id*. Plainly, the Court in *Quill* did not reject the physical presence test for gross receipts tax in describing the two leading, gross receipts tax nexus cases as reflecting companies with an in-state presence. Indeed, the Court cited with approval *Tyler Pipe* for the proposition that a state tax may pass muster under the Due Process clause, but run afoul of the Commerce Clause. *Id*. at 313 n.7 And by citing gross receipts tax cases with approval elsewhere in its opinion as supporting the "substantial nexus" standard for use taxes articulated in *Bellas Hess*, the Court reaffirmed the parallel in-state presence test in the

gross receipts tax area. *See Quill*, 504 U.S. at 311 (identifying *Goldberg* (which post-dates *Tyler Pipe)* and *Commonwealth Edison* (which post-dates *Standard Pressed Steel*) as continuing the *Bellas Hess* line of cases).

At most, the Supreme Court's statement in *Quill* that "we have not * * * *articulated the same physical presence requirement*" simply means that the formulation of the test under the first-prong of *Complete Auto* has been stated somewhat differently for purposes of gross receipts taxes. Again, in *Tyler Pipe*, the Court focused on an analysis of "*activities performed in this state* on behalf of the taxpayer" that were "significantly associated with the taxpayer's ability to establish and maintain a market" in the state. (Emphasis added.) 483 U.S. at 250.

A second passage in *Quill* referencing "other types of taxes" also does nothing to diminish the applicability of the in-state presence standard to gross receipts taxes. The Court stated that:

> [a]lthough in our cases subsequent to *Bellas Hess* and concerning other types of taxes, we have not adopted a similar *bright-line physical-presence requirement*, our reasoning in those cases does not compel that we now reject the rule that *Bellas Hess* established in the area of sales and use taxes. (Emphasis added.)

504 U.S. at 317. Nothing in this passage supports, or even hints at, abrogation of the *Tyler Pipe* in-state activities requirement, particularly given the citations to *Tyler Pipe* and the Court's other gross receipts tax decisions earlier in the opinion as requiring physical presence. Instead, the passage supports the conclusion that the Court has adopted a different formulation of the in-state presence requirement for gross receipts tax. In *Tyler Pipe*, the Court stated that the necessary in-state activities had to be "significantly associated with the taxpayer's ability to establish and maintain a market in this state for sales." 483 U.S. at 250. Thus, for purposes of gross receipts tax, rather than a "bright line" based on physical presence alone, the activities performed in the state must bear some relation to the taxpayer's ability to exploit the in-state market.

In short, whatever significance state courts have attached to the language of *Quill* with regard to state income taxes, there is no way to read *Quill* as overruling *Tyler Pipe*. Nor has any decision by any court upheld the imposition of a gross receipts tax against a company that lacked an in-state presence. *See J.C. Penney Natl. Bank*, 19 S.W.3d at 841-842 (overturning an assessment of a gross receipts tax and noting that "the Commissioner has pointed to no case in which the Supreme Court of the United States has upheld a state tax where the out-of-state taxpayer had absolutely no physical presence in the taxing state"); *see also O'Connor, Cavanaugh, Anderson, Killingsworth, & Beshears,* 192 Ariz. at 206 (noting the assertion by the state Department of Revenue that "it has found not a single case in which a court has sustained a gross receipts tax on an out-of-state taxpayer" in the absence of a direct physical presence in the state through resident employees or facilities, but finding the necessary in-state presence in that case based on temporary visits to the state by employees to install products sold); *Short Bros., Inc. v. Arlington Cty.*, 244 Va. 520, 525-526, 423 S.E.2d 172 (1992) (*Quill* physical presence requirement is necessary to find nexus for apportionment purposes under the business license tax, which is based on gross receipts of the taxpayer).

G. No Ohio Decision Has Ever Approved Imposing A State Tax On A Person That Lacked A Physical Presence In The State.

Notably, this Court has never issued a decision upholding a state tax against an out-of-state taxpayer that lacked a significant in-state presence. The Court's leading decision regarding the "substantial nexus" requirement of the Commerce Clause for purposes of use tax collection is *SFA Folio.* In that case, the out-of-state retailer, SFA Folio, had an in-state affiliate, Saks-Ohio, that engaged in certain activities in the state on Folio's behalf, including "accepting Folio's returns and distributing Folio's catalogs" in the state. *SFA Folio,* 73 Ohio St.3d at 123, 652 N.E.2d at 697. The Court held that such in-state activities were insufficient to constitute

substantial nexus, because they were a "minimal" part of SFA Folio's business. *Id.* No case decided after *SFA Folio* has called into question the requirement that a taxpayer must engage in sufficient in-state activities to be subject to tax.

This Court's decision in *Couchot v. State Lottery Comm.*, 74 Ohio St.3d 417, 659 N.E.2d 1225 (1996), concerning Ohio *income taxes*, is not to the contrary. The taxpayer in *Couchot*, a resident of Kentucky, travelled to Ohio to purchase an Ohio lottery ticket and, after his numbers were selected in the drawing, returned to the state to claim a cash price of over $20 million. 74 Ohio St.3d at 418. The Court expressly found that the taxpayer's trips into Ohio were sufficient to satisfy the physical presence standard of the Commerce Clause. *Id.* at 425.[9]

H. A Finding That Gross Receipts Alone Are Sufficient To Support Ohio's Authority To Tax Would Result In Nationwide Nexus For Any Internet Seller And Is Inconsistent With The Separate Nexus Standards Under The Commerce Clause And The Due Process Clause.

The substantial nexus requirement is designed to "limit the reach of state taxing authority so as to ensure that state taxation does not unduly burden interstate commerce." *Quill*, 504 U.S. at 313 and n.6. A standard of substantial nexus that depends *solely* on receiving gross receipts from products that are delivered to customers in the State would remove all limitations on state taxing authority over companies doing business in interstate commerce. If gross receipts—the very objective of interstate commerce—by themselves serve as the basis for a state's power to tax (or regulate) persons engaged in such commerce, then the Commerce Clause is no restriction on state authority, at all.

Moreover, it is no answer that R.C. 5751.01(I)(3) sets a threshold of $500,000 in annual gross receipts as the basis for "bright-line presence" in Ohio under the CAT statute. The

[9] The Court in *dicta* stated that the physical presence rule of *Quill* does not extend to a state income tax. *Couchot*, 74 Ohio St.3d at 425. As discussed in Section F, that statement has no application here, and this Court has never again cited *Couchot* in addressing a challenge under the Commerce Clause.

minimum level of required gross receipts set by the statute is simply a matter of state legislative choice. The General Assembly might reduce the level of required receipts at any time if it concludes, for example, that state budget difficulties require an extension of CAT liability to ever smaller companies. There is, moreover, nothing to prevent another state or locality that chooses to follow Ohio's lead from selecting a lower threshold for purported "presence" in the state. The amount of sales chosen by the State itself cannot validate the nexus standard as a matter of constitutional requirements. A decision upholding a standard of "substantial nexus" based on gross receipts would, therefore, be fundamentally at odds with the principles of the dormant Commerce Clause.

Further, the gross receipts nexus standard of the CAT statute would obliterate the established distinction between a State's jurisdiction to tax under the Due Process Clause, and the limitations on a state's power over interstate commerce under the Commerce Clause. In *Quill*, the Court expressly found that "while a state may, consistent with the Due Process Clause, have the authority to tax a particular taxpayer, imposition of the tax may nonetheless violate the Commerce Clause." 504 U.S. at 305. In *Wynne* the Court recently quoted with approval the above passage from *Quill* (135 S.Ct. at 1788) and reaffirmed the *Quill* principle that the Commerce Clause sets a higher standard than does the Due Process Clause for state authority to tax interstate commerce. *See* 135 S.Ct. at 1789 ("the fact that a State has the jurisdictional power to impose a tax says nothing about whether that tax violates the Commerce Clause").[10] In this case, the CAT statute's gross receipts nexus standard requires only that an out-of-state company have customers in the state, a standard akin to the "minimum contacts" analysis applicable to the Due Process Clause. *See Quill*, 504 U.S. at 306-308 (solicitation of sales from outside the state

[10] Five justices joined in the majority opinion. In addition, the dissenting opinion of three Justices—Ginsburg, Scalia and Kagan—cited *Quill* with approval for the proposition that the Commerce Clause sets a higher standard than does the Due Process Clause. 135 S.Ct. at 1818.

may be adequate to satisfy the Due Process standard). The Court, however, has expressly rejected such a formulation of an "economic presence" standard as sufficient to meet the requirements of the Commerce Clause. *Id.* at 304, 311-312 (describing the lower court's conclusion that Quill's "economic presence" was sufficient to require use tax collection, and rejecting the lower court's analysis regarding the Commerce Clause). The CAT's expansive "gross receipts" nexus standard likewise fails to survive scrutiny under the Commerce Clause.

I. Fundamental Principles Regarding The Regulation Of Interstate Commerce Require Rejection Of The CAT Statute's Novel Gross Receipts Standard Of Nexus.

1. The In-State Presence Standard Of Substantial Nexus Is Grounded In The Core Principles Of The Commerce Clause.

In *Quill*, the Supreme Court explained, at length, how the physical presence rule of *Bellas Hess* is consistent with, and grounded in, the principles that underlie the "substantial nexus" requirement of the Commerce Clause. 504 U.S. at 311-314 (physical presence standard "furthers the ends of the dormant Commerce Clause."). In particular, the in-state presence requirement of substantial nexus serves as "a means for limiting state burdens on interstate commerce." *Id.* at 313. The substantial nexus test thus derives from the core objectives of the dormant Commerce Clause and is informed "by structural concerns about the effects of state regulation on the national economy," rather than concerns about fairness to any individual company. *Id.* at 312.

As the Court recognized in *Quill*, the danger of inconsistent state laws across numerous state and local taxing jurisdictions in the United States justifies the in-state presence standard of nexus reaffirmed by the Court time and again. *Id.* at 313 n.6. While state and local gross receipts taxes are less common than sales and use taxes, the expansive gross receipts "bright-line presence" standard of the CAT statute could readily be adopted in states and localities throughout the country. Indeed, in the 2015 state legislative season, at least three states adopted

or expanded a tax reporting requirement based on gross receipts. *See* Nevada S.B. 483 (enacted June 9, 2015), available at http://leg.state.nv.us/Session/78th2015/Bills/SB/SB483_EN.pdf (adopting the new "Commerce Tax" on gross revenue from engaging in business in the state); Tennessee H.B. 644 (2015), codified at Tenn. Code. Ann. § 67-4-702(27)(A)(iv)(a) ("substantial nexus in the state" includes having gross receipts in excess of $500,000 for purposes of the "Business Tax Act"); and Washington Subst. S.B. 6138 (enacted July 2, 2015), available at http://lawfilesext.leg.wa.gov/biennium/2015-16/Pdf/Bills/Session%20Laws/Senate/6138-S.SL.pdf (amending R.C.W. 82.04.066 to apply "gross receipts" nexus provision to wholesale sales for purposes of the B&O tax). Texas also has a form of gross receipts tax that is measured by a company's total revenues adjusted for certain factors. Tex. Tax Code § 171.101. Although Texas has not yet adopted a "gross receipts" nexus standard, a number of other states use a gross receipts threshold for reporting of the state's corporate income-based tax. *E.g.,* Cal. Rev. & Tax. Code § 23101(b)(2); 1 Colo. Code Regs. 201-2:39-22-301.1(2)(b)(iii); Michigan (Mich. Comp. Laws § 206.621(1); N.Y. Tax Law § 209(1)(b).

In addition, there are numerous local jurisdictions throughout the United States, including many major municipalities, with gross receipts taxes that could soon follow suit and seek to compel tax reporting by businesses with no connection other than customers residing in the city. *See, e.g.*, San Francisco Business and Tax Regulations Code, § 953 (2014) (San Francisco Gross Receipts Tax) ("every person engaging in business within the City shall pay an annual gross receipts tax measured by the person's gross receipts from all taxable business activities attributable to the City"); Los Angeles Municipal Code, § 21.43(e) (Los Angeles Business Tax) (gross receipts tax on retail sales); City of Philadelphia Business Privilege Tax Regulations, § 103(A) (2015) ("A taxpayer is subject to the Gross Receipts portion of the BPT when it has sufficient contact with the City to be taxed without violating the United States Constitution.").

Thus, the very same "structural concerns" that support the in-state activity or presence requirement of *Quill* and *Tyler Pipe* apply with equal force to the gross receipts nexus provision of the CAT statute, R.C. 5751.01(I)(3). Indeed, if Ohio is free to impose tax obligations on remote sellers based on nothing more than making sales to customers in the state, then "so can every other State, and so, indeed, can every municipality, every school district, and every other political subdivision throughout the Nation" with power to impose such taxes, resulting in precisely the kinds of "local entanglements" and burdens on interstate commerce that the Commerce Clause is designed to prevent. *Bellas Hess*, 386 U.S. at 759-760.

2. Changes In Standards For Requiring Tax Reporting By Remote Sellers Are Properly The Purview Of Congress, Not State Legislatures.

The need to safeguard the national economic interests secured by the Commerce Clause and inherent to remote sales transactions has only increased in the years since *Tyler Pipe* and *Quill* were decided, with the growth of electronic commerce conducted over the Internet. The physical presence requirement adopted in *Bellas Hess* and reaffirmed in *Quill* was based in part on the Supreme Court's conclusion that "it is difficult to conceive of commercial transactions more exclusively interstate in character than the mail order transactions here involved." *See Natl. Bellas Hess*, 386 U.S. at 759. Today, the majority of remote sales are conducted online, an even more intensely interstate environment.

The goal of a single national marketplace is precisely why the framers reserved for Congress the power to regulate commerce "among the several States." *See Wynne,* 135 S.Ct. at 1794 (quoting *Hughes v. Oklahoma*, 441 U.S. 322, 325-326, 99 S.Ct. 1727, 60 L.Ed.2d 250 (1979) (the underlying concern for adoption of the Commerce Clause was the "immediate reason for calling the Constitutional Convention: the conviction that in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued relations

among the Colonies and later among the States under the Articles of Confederation.")) As *Quill* makes clear, Congress, rather than individual states or the courts, including the U.S. Supreme Court, is "better qualified to resolve" the underlying tension between the state interest in levying taxes on remote sellers and the potential burdens imposed by such tax obligations on interstate commerce. 504 U.S. at 316. In fact, there is a bill currently before Congress that would strike such a balance, including the adoption of a nexus standard with respect to state business activity taxes imposed on out-of-state companies. *See* H.R. 2584, Business Activity Tax Simplification Act of 2015, 114th Cong. (2015-2016), available at https://www.congress.gov/bill/114th-congress/house-bill/2584/text. The bill was reported out favorably by the House Judiciary Committee to the full House of Representatives on June 17, 2015. *See* https://www.congress.gov/bill/114th-congress/house-bill/2584/all-actions. Since Congress is considering the issue, "it may be that 'the better part of both wisdom and valor is to respect the judgment of [Congress]" with regard to state taxation of interstate commerce generally, and remote sellers in particular. (Internal citation omitted.) *Quill*, 504 U.S. at 318-319.

3. The Doctrine Of *Stare Decisis* Supports The Conclusion That The Gross Receipts Nexus Provision Of R.C. 5751.01(I)(3) Is Unconstitutional.

In the area of interstate commerce, the "settled expectations" of businesses regarding their state tax obligations is a significant factor with regard to applying the principles of the Commerce Clause. *Quill*, 504 U.S. at 316. Like the physical presence standard of *Quill,* the in-state activities rule of *Tyler Pipe* "has engendered substantial reliance and has become part of the basic framework of a sizable industry." *See id.* In that regard, the "interest in stability and orderly development of the law that undergirds the doctrine of *stare decisis"* strongly supports continued adherence to the *Tyler Pipe* rule. (Internal citation omitted.) *Id.* Indeed, even critics of dormant Commerce Clause jurisprudence in general, such as Justice Scalia, support reliance

on *stare decisis* with regard to prior decisions applying the doctrine. *See, e.g.*, *Wynne*, 135 S.Ct. at 1811 (Scalia, J., dissenting) (stating that *stare decisis* properly applies where a challenged tax is not distinguishable from a tax the Court has already held unconstitutional). Companies engaged in the interstate sale of goods, such as Newegg, have been (and remain) justified, for purposes of planning and conducting their commercial activities, in relying upon *Tyler Pipe* and its predecessor decisions as establishing the limits of the states' power to tax gross receipts. *See id.* at 315 (whatever "artificiality" may exist in specific applications of the physical presence standard, it has the demonstrable, and overriding, benefit of creating a clear rule that "firmly establishes the boundaries" of legitimate state tax authority).

> **Proposition of Law 2**: The CAT statute is unconstitutional as-applied to Newegg by the Commissioner. Imposition of the CAT against Newegg, a company with no in-state presence in Ohio, violates the "substantial nexus" standard of the Commerce Clause as established under numerous decisions of the United States Supreme Court. *E.g., Tyler Pipe*, 483 U.S. at 250-251; *Commonwealth Edison*, 453 U.S. at 626; *Std. Pressed Steel*, 419 U.S. at 562; *Gen. Motors*, 377 U.S. at 447-448. Merely obtaining gross receipts in excess of $500,000 annually does not establish constitutional "substantial nexus" under long-standing Supreme Court authority, so applying the CAT based solely on Newegg's gross receipts from sales of goods delivered to Ohio customers violates the Constitution. In addition, because Newegg engaged in no business activities within the State of Ohio sufficient to satisfy the constitutional "substantial nexus" standard, application of the CAT to Newegg on any other basis, whether separate from or together with its gross receipts, is also unconstitutional.

A. Newegg Satisfies The Clear And Convincing Standard For An As-Applied Challenge.

Newegg has consistently asserted that the CAT statute, as applied to Newegg, is unconstitutional because Newegg lacks the necessary in-state activities required under the Commerce Clause. Appx. 2-3, 9-10, Notice of Appeal at 2-3, 9-10.

A party challenging a statute as applied to it alleges that "the application of the statute in the particular context in which he has acted, or in which he proposes to act, would be unconstitutional." (Internal quotation and citation omitted.) *Wymsylo v. Bartec, Inc.*, 132 Ohio

St.3d 167, 2012-Ohio-2187, 970 N.E.2d 898, ¶ 22. The party making the as-applied challenge bears the burden of presenting clear and convincing evidence of a set of facts that makes the statute unconstitutional when applied to those facts. *Harrold v. Collier*, 107 Ohio St.3d 44, 2005-Ohio-5334, 836 N.E.2d. 1165, ¶ 38.

The evidence presented before the Board establishes that application of the CAT to Newegg is unconstitutional. Newegg had no facilities, property, employees, or representatives in Ohio, and no activities were performed by Newegg, or on its behalf, in Ohio, let alone activities associated with making or maintaining a market in the state.

Before the Board, the Commissioner argued that Newegg's Internet marketing activities were sufficient to satisfy the Commerce Clause substantial nexus requirement. Such an argument, if presented before this Court, is not only at odds with the in-state activities requirement of substantial nexus under *Tyler Pipe* and numerous other cases, but also lacks support in the record. All of Newegg's online marketing, whether by Newegg itself or by third-party vendors providing services for Newegg, was performed at locations outside of Ohio. Furthermore, the Supreme Court has long rejected the notion that state tax obligations can arise based on mere advertising delivered to recipients in a state. *See Natl. Bellas* Hess, 386 U.S. at 758 and n.11 (explaining that state tax administrators "have generally considered an advertising nexus insufficient" to require a seller to "participate in the tax collection system," and citing *State v. Lane Bryant, Inc.*, 277 Ala. 385, 171 So.2d 91 (1965)).

In addition, any argument by the Commissioner that Newegg had the "functional equivalent" of in-state presence through its marketing activities is without any support in any reported decision by any Court, let alone the United State Supreme Court. Any suggestion that Newegg has a constitutionally sufficient presence as a result of electronic downloads performed

by Internet users through their computers or mobile devices is equally without factual basis or supporting precedent.

Indeed, the Commissioner's theory that using the Internet is the functional equivalent of in-person solicitation misses the point. The Commerce Clause test looks not at the objective or effect of making sales, but to the nature and location of the activities that led to the sale. Upholding the Commissioner's unprecedented theory would create substantial nexus in every state where a consumer chooses to pick up a telephone to call Newegg to place an order or to use his or her computer to access a remote website. In both cases, Newegg does not own, control, or select the device chosen by the consumer to initiate communication with the company, *e.g.*, a laptop computer or a telephone, and the consumer is free to use the technology of his or her choice to access a call center or website. In both instances, Newegg does nothing more than receive and respond to interstate communication with a prospective customer.

> **Proposition of Law 3**: The assessments against Newegg are invalid under the CAT statute, when its terms are properly construed to avoid constitutional infirmities. Multiple provisions of the CAT statute may be reasonably construed so as to prevent the application of the CAT to Newegg, an out-of-state retailer with no physical presence in Ohio, including R.C. 5751.02(A), R.C. 5751.01(H)(3) and (I)(3), and R.C. 5751.01(F)(2)(jj).

A. Newegg Is Not "Doing Business In This State" Within The Meaning Of R.C. 5751.02(A) And 5751.01(H).

The CAT is a tax levied against companies that are "doing business in this state." R.C. 5751.02(A) provides, in pertinent part:

> For the purpose of funding the needs of this state and its local governments, there is hereby levied a commercial activity tax on each person with taxable gross receipts for the *privilege of doing business in this state*. For the purposes of this chapter, *"doing business" means engaging in any activity* * * *. (Emphasis added.)

Under this provision, therefore, the CAT is imposed on any person that is "engaging in any activity in this state." *Id.* Newegg is not engaged in any activity in Ohio. This interpretation of

R.C. 5751.02(A) is consistent with the constitutional principle, as discussed in support of Proposition of Law 1, that a company is not subject to a state tax measured by gross receipts unless the company, or third-party representatives acting on its behalf, is performing activities in the state that assist the company to make and maintain a market for sales in the state. *Tyler Pipe*, 483 U.S. at 250. As the Court explained in *General Motors*, "[w]here, as in the instant case, the taxing State is not the domiciliary State, we look to the taxpayer's business activities within the State" to determine the constitutionality of a gross receipts tax. 377 U.S. at 441.

The Commissioner interprets the remaining language of R.C. 5751.02(A)—which provides that "[p]ersons on which the commercial activity tax is levied include, but are not limited to, persons with substantial nexus with this state"—as superseding the fundamental requirement of "engaging in any activity" in the state, quoted above. According to the Commissioner, through the interplay of R.C. 5751.01(H)(3) (defining substantial nexus to mean "a bright line presence in this state") and 5751.01(I)(3) (defining bright line presence in this state to include taxable gross receipts of at least $500,000 per year), Newegg has substantial nexus under R.C. 5751.02(A) because its sales to Ohio customers exceed $500,000 even if it engages in no activity in the state. The Commissioner's interpretation would read out of the statute the primary, in-state activities requirement of R.C. 5751.02(A), and must yield to a better reading that is consistent with the language of the CAT statute as a whole.[11]

B. The CAT Statute Itself Excludes Gross Receipts That Cannot Be Taxed Consistent With The Constitutional Limitations On The State's Authority.

In fact, the CAT statute itself includes an exclusionary provision that may also reasonably be construed to avoid serious constitutional infirmities under the "substantial nexus" requirement of the Commerce Clause. Under R.C. 5751.01(F)(2)(jj), excluded from the definition of "gross

[11] Moreover, any ambiguity in the statute must be interpreted in favor of the taxpayer, Newegg. *E.g., Gulf Oil Corp. v. Kosydar*, 44 Ohio St.2d 208, 218, 339 N.E.2d 820 (1975) (franchise tax on the privilege of doing business in the state construed in favor of the taxpayer).

receipts" are "any receipts for which the tax imposed by this chapter is prohibited by the constitution or laws of the United States * * *." The only reasonable interpretation of the exclusion is that the General Assembly wished to avoid conflict with all limitations on the State's authority to impose a tax measured by gross receipts, including restrictions arising under the substantial nexus requirement of the dormant Commerce Clause. *See* R.C. 1.47(A); *SFA Folio*, 73 Ohio St.3d at 122 (interpreting statute that imposed tax "in accordance with the Constitution of the United States" to conform to Commerce Clause requirements); *Buchman*, 73 Ohio St.3d at 269. The exclusion of R.C. 5751.01(F)(2)(jj) thereby permits an interpretation that preserves the statute by limiting its reach in accordance with the dictates of the Commerce Clause.

> **Proposition of Law 4**: No other provision of the CAT statute applies to Newegg. The evidence presented before the Board clearly established that Newegg lacked statutory "substantial nexus with this state" under the other provisions of R.C. 5751.01(H) and lacked "bright-line presence" in Ohio under the other provisions of R.C. 5751.01(I).

A. No Other Provisions Of The CAT Statute Required Newegg To Pay The CAT.

In issuing and affirming the CAT assessments against Newegg, the Commissioner relied strictly on Newegg's annual gross receipts from sales to Ohio customers in excess of $500,000. Appx. 28-30, Final Determination at 1, 3. While Newegg has demonstrated the numerous and fundamental errors with the Commissioner's reliance on the gross receipts "bright-line presence" provision, the evidence presented to the Board also proved that Newegg is also not subject to the CAT under any other provision of the statute.

Newegg did not own or use "part or all of its capital in this state" and did not "otherwise [have] nexus in this state * * * under the Constitution of the United States." R.C. 5751.01(H)(1), (4). Newegg likewise had no "certificate of compliance with the laws of this state authorizing [it] to do business in this state." R.C. 5751.01(H)(2). Nor did Newegg have in Ohio, at any

time, property with a value of at least $50,000, payroll of at least $50,000, or twenty-five percent (25%) of its total property, total payroll or total receipts. R.C. 5751.01(H)(3), (I)(1), (2), (4). Nor did Newegg ever have domicile in Ohio for any purpose. R.C. 5751.01(I)(5). In sum, Newegg is not subject to the CAT.

B. Any Claim By The Commissioner That Newegg Is Subject To The CAT Under The Constitutional Catch-All Provision Of R.C. 5751.01(H)(4) Is Clearly Refuted By The Evidence.

No activities were performed in Ohio on behalf of Newegg that are significantly associated with Newegg's ability to establish and maintain a market in Ohio. As discussed under Proposition of Laws 1 and 2, Newegg therefore does not otherwise have nexus under the Commerce Clause of the U.S. Constitution. Therefore, the catch-all provision of R.C. 5751.01(H)(4) does not apply.

V. CONCLUSION

For the foregoing reasons, Newegg respectfully requests that the Court reject the Commissioner's imposition of the CAT against Newegg, reverse the decision of the Board of Tax Appeals that affirmed the Commissioner's assessments of CAT against Newegg, and order that the CAT assessments against Newegg be eliminated in their entirety.

Respectfully submitted,

/s Martin I Eisenstein

Martin I. Eisenstein (PHV 1095-2015)
(Counsel of Record)
Matthew P. Schaefer (PHV 2399-2015)
BRANN & ISAACSON
184 Main Street
P.O. Box 3070
Lewiston, ME 04243-3070
Tel.: (207) 786-3566
Fax: (207) 783-9325
Email: meisenstein@brannlaw.com
mschaefer@brannlaw.com
AND

Edward J. Bernert (0025808)
BAKER HOSTETLER
Capital Square, Suite 2100
65 East State Street
Columbus, OH 43215-4260
Tel.: (614) 462-2687
Fax: (614) 462-2616
Email: ebernert@bakerlaw.com

Counsel for Appellant
Newegg, Inc.

CERTIFICATE OF SERVICE

This is to certify that a true copy of the foregoing Appellant Newegg, Inc.'s Merit Brief was served by U.S. and electronic mail to counsel of record for Appellee Tax Commissioner, Daniel W. Fausey and Christine T. Mesirow, Assistant Attorneys General, State of Ohio, 30 East Broad Street, 25th Floor, Columbus, Ohio 43215–3428, on this 31st day of August, 2015.

/s Edward J. Bernert
Edward J. Bernert (0025808)
One of the Attorneys for Appellant
Newegg Inc.

NOTICE OF APPEAL FROM THE OHIO BOARD OF TAX APPEALS

In the Supreme Court of Ohio

Newegg, Inc.,	:	Case No. 15-0483
Appellant,	:	
v.	:	Appeal from the Ohio Board of Tax Appeals
Joseph W. Testa, Tax Commissioner of Ohio,	:	
Appellee.	:	BTA Case No. 2012-234

NOTICE OF APPEAL OF APPELLANT NEWEGG, INC.

Martin I. Eisenstein (PHV 1095-2015)
(Counsel of Record)
Matthew P. Schaefer (PHV 2399-2015)
BRANN & ISAACSON
184 Main Street
P.O. Box 3070
Lewiston, ME 04243-3070
Tel. (207) 786-3566
Fax (207) 783-9325
Email: meisenstein@brannlaw.com
mschaefer@brannlaw.com

AND

Edward J. Bernert (0025808)
BAKER HOSTETLER
Capitol Square, Suite 2100
65 East State Street
Columbus, OH 43215-4260
Tel: (614) 462-2687
Fax: (614) 462-2616
Email: ebernert@bakerlaw.com

Counsel for Appellant,
Newegg, Inc.

Mike DeWine (0009181)
Attorney General of Ohio
Christine T. Mesirow (0015590)
Daniel W. Fausey (0079928)
Assistant Attorneys General
Office of the Attorney General
Taxation Section, 25th Floor
Rhodes Tower
30 East Broad Street
Columbus, OH 43215
Tel. (614) 466-5967
Fax (614) 466-8226
christine.mesirow@ohioattorneygeneral.gov

Counsel for Appellee,
Tax Commissioner of Ohio

RECEIVED
MAR 25 2015
Attorney General's Office
Taxation Section

FILED
MAR 25 2015
CLERK OF COURT
SUPREME COURT OF OHIO

FILED/RECEIVED
BOARD OF TAX APPEALS
2015 MAR 25 PM 2:20

NOTICE OF APPEAL OF APPELLANT NEWEGG, INC.

Appellant Newegg, Inc. ("Newegg") hereby gives notice of its appeal as of right, pursuant to R.C. 5717.04, to the Supreme Court of Ohio, from the Decision and Order ("Decision") of the Board of Tax Appeals ("Board") journalized on February 26, 2015, in *Newegg, Inc. v. Joseph W. Testa, Tax Commissioner of Ohio*, being BTA Case No. 2012-234. A true copy of the Decision being appealed is attached hereto and incorporated by reference herein.

INTRODUCTION

In this case, the Tax Commissioner of Ohio (the "Commissioner") assessed Appellant, Newegg, Inc., the state's commercial activity tax (the "CAT"), even though neither Newegg, nor any other person acting on its behalf, conducted any activities in Ohio during the relevant period. As the Board explained it in its decision, the Commissioner imposed the CAT strictly because "the [C]ommissioner determined that Newegg had [statutory] substantial nexus with this state, *i.e.*, a 'bright line presence' in the state because it had at least $500,000 [per year] 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 section were numbered in July 2005)." [Decision at 4 (brackets added)]. The Board concluded that, with the statutory sales threshold met and nothing more, imposition of the CAT was obligatory. [Decision at 4 ("[W]e are constrained to follow the mandate of the General Assembly in concluding that appellant, an out-of-state seller, has [statutory] substantial nexus within this state by virtue of its gross receipts for the reporting periods in question.") (second bracketed term added)].

In proceedings below, Newegg did not dispute, nor does it dispute here, that its gross receipts from interstate sales to Ohio consumers exceeded the statutory threshold of $500,000 annually. Newegg's challenge—as asserted in its petition for reassessment before the

Commissioner, in its appeal to the Board, and now—is based upon the Commerce Clause of the United States Constitution.

Newegg has consistently asserted that, as applied to Newegg, the CAT statute violates Commerce Clause principles, because Newegg lacks "substantial nexus" with Ohio under the standards established by the Supreme Court in cases involving gross receipts taxes like the CAT, including, but not limited to, *Standard Pressed Steel, Inc. v. Wash. Dep't of Revenue*, 419 U.S. 560 (1975), and *Tyler Pipe Indus., Inc. v. Wash. Dep't of Revenue*, 483 U.S. 232 (1987). This "as applied" challenge was properly raised below. [*See* Decision at 3 (quoting para. 6 of Newegg's notice of appeal) ("*Application of the CAT to Newegg would violate principles of the Commerce Clause of the United States Constitution*..." (italics added).][1]

As a corollary to its "as applied" constitutional challenge, Newegg has consistently urged both the Commissioner and the Board that, in order to preserve the CAT statute's constitutionality, the statute should be interpreted, in the first instance, so that it does not apply to Newegg. *See, e.g., Buchman v. Board of Educ.*, 73 Ohio St. 3d 260, 269 (1995) ("where a statute reasonably allows for more than a single construction or interpretation, it is the duty of the court to choose that construction or interpretation which will avoid rather than raise serious questions as to its constitutionality"). Newegg offered interpretations of multiple provisions of the CAT that could be reasonably interpreted by the Commissioner and the Board to avoid causing the CAT statute to violate the Constitution by imposing tax on a business—Newegg—that lacked "substantial nexus" with the state. [*See* Decision at 2-3 (quoting paras. 1-5 of Newegg's notice of appeal).] Under these interpretations, Newegg would not be liable for the CAT.

[1] Any assertion that Newegg did not present an as-applied challenge to the Commissioner and the Board would be frivolous.

Citing its limited role in cases involving constitutional challenges, the Board declined to rule on either the constitutional issues or the related statutory interpretation arguments raised by Newegg below. Instead, the Board explained that the parties "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." [Decision at 3 (citation omitted).]

It is well-established that the Board's role is to receive evidence for constitutional challenges and that it may not declare a statute unconstitutional. *See, e.g., MCI Telecommunications Corp. v. Limbach*, 68 Ohio St.3d 195, 197-98 (1995).[2] However, Newegg's statutory interpretation contentions would have permitted the Board to resolve the appeal *without* declaring the CAT unconstitutional on its face or as applied, consistent with the Board's duty to construe the statute in a manner to preserve its constitutionality. *E.g., Buchman*, 73 Ohio St. 3d at 269 (duty of tribunal to choose a construction of a statute that will avoid serious constitutional questions). Nevertheless, the Board concluded that the terms of the CAT statute are unambiguous and require resolution of Newegg's appeal by this Court through a declaration concerning the statute's constitutionality. [Decision at 4 ("[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").] In declining to give the CAT statute a reasonable interpretation consistent with the Constitution, the Board erred.

[2] In that regard, the Board over-stepped its authority in one respect in its Decision. It determined that the pertinent CAT statutes, "under the plain language set forth therein," do not require that a company have an in-state presence in order to be subject to the CAT. [Decision at 4.] Such a reading interprets the CAT in a manner which is at odds with the limitations on state taxing power under the Commerce Clause, necessarily rendering the CAT unconstitutional.

The Board also failed to recognize that it has the authority to apply binding precedent regarding the constitutionality of state statutes. *See Marysville Exempted Village Sch. Dist. Bd. of Educ. v. Union County Bd. of Revision*, 2013 Ohio 3077, ¶ 15, 136 Ohio St. 3d 146, 150 (limits on Board's jurisdiction over constitutional questions do not preclude it from giving effect to binding precedent). Because the United States Supreme Court has held in multiple cases that gross receipts taxes like the CAT are subject to the constitutional standards of "substantial nexus," including specifically the "physical presence" requirement described by the Court, the Board should have applied such clear authority to invalidate the CAT assessment against Newegg. *See, e.g., Standard Pressed Steel,* 419 U.S. 560 (1975) and *Tyler Pipe*, 483 U.S. 232 (1987). The Board's failure to reverse the final determination of the Commissioner was error.

As a result of the proceedings below, this case arrives at the Supreme Court of Ohio with a complete evidentiary record from the Board—including exhibits and live testimony from fact witnesses and experts—on Newegg's constitutional and related statutory arguments. The Court now properly has jurisdiction to determine the necessary facts and resolve all of the as-applied constitutional issues and questions of statutory interpretation presented by Newegg's appeal, despite the Board's Decision not to make any findings or rulings below.

In addition, Newegg hereby invokes the jurisdiction of the Court to determine whether the gross receipts "bright line presence" provision of the CAT statute, R.C. 5751.01(I)(3), on its face, violates the Commerce Clause of the Constitution. No extrinsic facts are required to make such a determination. Newegg's standing as a company that satisfies the threshold of $500,000 in annual gross receipts is alone enough to establish this Court's authority to consider the issue. *See, e.g., Global Knowledge Training, L.L.C. v. Levin*, 2010 Ohio 4411, ¶¶ 16, 17, 127 Ohio St.3d 34, 38 (a facial challenge to the constitutionality of a statute, which is made without regard to extrinsic facts, may be raised initially on appeal before the Ohio Supreme Court); *Palazzi v.*

Estate of Gardner, 32 Ohio St. 3d 169, 175 (1987) (a party within the class to whom the statute applies has standing to challenge its constitutionality).

ERRORS TO BE REVIEWED AND PROPOSITIONS OF LAW PRESENTED

Newegg complains of the following errors in the Board's Decision, and sets forth the following propositions of law concerning the constitutional and other questions as to which this Court has jurisdiction, but which the Board declined to address. Newegg also asserts a facial challenge to R.C. 5751.01(I)(3).

1. The Board erred by upholding the final determination of the Commissioner against Newegg because the evidence presented to the Board established that the CAT could not be imposed upon Newegg consistent with the requirements of the Commerce Clause of the United States Constitution, under long-standing and binding precedent of the United States Supreme Court, including, but not limited to, *Tyler Pipe,* 483 U.S. 232 (1987), and *Standard Pressed Steel*, 419 U.S. 560 (1975). Consistent with these binding precedents, Newegg lacked the in-state business activities necessary to establish the "substantial nexus" required for the State of Ohio to have constitutional authority to impose the CAT on Newegg. The Board had jurisdiction and authority to apply such precedents. *Marysville Exempted Village Sch. Dist.*, 2013 Ohio 3077, ¶ 15, 136 Ohio St. 3d 146, 150 (Board may give effect to binding precedent on constitutional issues).

2. The Board erred by upholding the final determination against Newegg because the evidence presented to the Board established that the CAT assessments against Newegg are not supported by the terms of the CAT statute, when the statute is properly construed to avoid constitutional infirmities. The Board erred in not interpreting the CAT statute to avoid presenting serious constitutional questions regarding the statute. *See Buchman*, 73 Ohio St. 3d at 269. Multiple provisions of the CAT statute may be reasonably construed so as to prevent its

application to Newegg, a company that lacked the in-state presence required by the Commerce Clause to permit the imposition of the CAT on its gross receipts under long-standing Supreme Court precedent, including:

(a) R.C.5751.02: Because the evidence showed that Newegg engaged in no activity within Ohio, and neither owns nor leases property in the state, the company was not "doing business in this state" within the meaning of R.C. 5751.02;

(b) R.C. 5751.01(H)(3) & (I)(3): Although Newegg had gross receipts from sales to Ohio residents in excess of $500,000 annually, such receipts are not "taxable gross receipts" within the meaning of R.C. 5751.01(I)(3), in that none of its gross receipts are subject to taxation in Ohio because the Commissioner lacks the authority to impose the CAT on Newegg, so that Newegg lacks "bright line presence" in the state under R.C. 5751.01(H)(3);

(c) R.C. 5751.01(F)(2)(jj) (formerly codified at R.C. 5751.01(F)(2)(aa)): Newegg's receipts from sales to Ohio residents are not subject to the CAT because the term "gross receipts" under R.C. 5751.01(F)(2)(jj) excludes "[a]ny receipts for which the tax imposed by this chapter is prohibited by the constitution or laws of the United States." Because the Commissioner lacks the authority to impose the CAT on Newegg, taxation of its receipts from sales to Ohio residents is prohibited by the Constitution.

These provisions of the CAT statute should be interpreted to avoid the imposition of the CAT on Newegg. While the Board had jurisdiction to enter such an order because it would not have involved a declaration that the CAT statute is unconstitutional, this Court now has the necessary

jurisdiction and authority to interpret the CAT statute to avoid serious constitutional infirmities in the law.

3. The Board likewise erred by upholding the final determination against Newegg because the evidence presented to the Board established that the CAT assessments against Newegg are not supported by any of the other provisions of the CAT statute, nor did the Commissioner allege that such provisions supported the final determination. In particular, the evidence established that the following provisions did not apply to Newegg:

(a) R.C. 5751.01(H)(1), (2) and (4): Newegg lacked statutory "substantial nexus with this state" under R.C. 5751.01(H)(1), (2) and (4), in that Newegg did not own or use "part or all of its capital in this state," lacked a "certificate of compliance with the laws of this state authorizing [it] to do business in this state," and did not "otherwise [have] nexus in this state . . . under the Constitution of the United States."

(b) R.C. 5751.01(H)(3) and 5751.01(I)(1), (2), (4) & (5): Newegg lacked statutory "'bright line presence' in this state" under R.C. 5751.01(H)(3) and 5751.01(I)(1), (2), (4) & (5) in that Newegg did not have in Ohio at any time (i) property with an aggregate value of at least fifty thousand dollars, (ii) payroll of at least $50,000, (iii) twenty-five or more percent of its total property, total payroll or total receipts, or (iv) domicile for corporate, commercial or other business purposes.

If any of these provisions is asserted by the Commissioner before this Court as a basis for upholding the final determination or the Board's Decision, this Court has jurisdiction and authority to rule that none of these provisions is a basis for sustaining the assessments, final determination or Decision.

3. The Board's Decision affirming the final determination should be reversed, and the assessments cancelled, because the CAT statute is unconstitutional as applied to Newegg. In particular, if interpreted to require the imposition of the CAT against Newegg, R.C. 5751.01(H)(3), (I)(3), (I)(4) & (F)(2)(jj), and R.C. 5751.02, or any of them, are unconstitutional as applied. Imposition of the CAT on Newegg violates the "substantial nexus" standards of the Commerce Clause of the U.S. Constitution, as established by the Supreme Court in numerous decisions. *See, e.g., Tyler Pipe*, 483 U.S. 232; *Standard Pressed Steel*, 419 U.S. 560; *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977); *National Bellas Hess v. Ill. Dep't of Revenue*, 386 U.S. 753 (1967); *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 617, 626 (1981); *Goldberg v. Sweet*, 488 U.S. 252, 263 (1989); *Norton Co. v. Ill. Dep't of Revenue,* 340 U.S. 534, 537 (1951). Merely obtaining gross receipts in excess of $500,000 annually does not establish constitutional "substantial nexus" under long-standing Supreme Court authority, so applying the CAT statute based solely on Newegg's gross receipts violates the Constitution. Furthermore, because the evidence shows that Newegg engaged in no business activities within the State of Ohio sufficient to satisfy the constitutional "substantial nexus" standards established by the Supreme Court, application of the CAT to Newegg on any other basis, whether separate from or together with its gross receipts, is also unconstitutional. This Court has the jurisdiction and authority to make the necessary findings of fact and rulings of law to declare the CAT statute unconstitutional as applied to Newegg. *E.g., MCI Telecommunications Corp.*, 68 Ohio St.3d 197-98 (Board of Tax Appeals receives evidence for an as applied challenge, but this Court determines the facts and resolves the constitutional questions).

4. The Board's Decision affirming the final determination against Newegg should be reversed, and the assessments cancelled, because the Ohio CAT statute is unconstitutional on its

face, without regard to any extrinsic facts. By operation of the CAT statute according to its plain terms, the gross receipts "bright line" presence provision set forth in R.C. 5751.01(I)(3) requires the CAT to be imposed on a company solely because the company meets a statutory threshold of $500,000 in annual gross receipts from interstate sales to Ohio consumers, irrespective of whether the company has the in-state presence required under the "substantial nexus" standards established by the Supreme Court under the Commerce Clause. A declaration by this Court that R.C. 5751.01(I)(3) is unconstitutional and unenforceable, on its face, and a ruling striking it from the statute, will eliminate the constitutional defect in the CAT statute. The Court has jurisdiction over Newegg's facial challenge. *E.g., Global Knowledge Training*, 2010 Ohio 4411, ¶¶ 16, 17, 127 Ohio St.3d 34, 38 (Court has jurisdiction to consider facial challenges presented to it).

5. Finally, in its Decision, the Board stated as follows: "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." [Decision at 3.] Newegg understands this sentence to mean that the Board believed Newegg was not presenting to the Board a *facial* constitutional challenge to the CAT, but was asserting—as plainly stated in paragraph 6 of its notice of appeal to the Board—that the *application* of the CAT to Newegg violates ("is prohibited by") the Constitution. If, however, the above-quoted sentence from the Decision means that Newegg did not assert an as-applied challenge before the Board, that conclusion is clearly erroneous. [*See* Decision at 3 (quoting Newegg's notice of appeal, para. 6) ("*Application of the CAT to Newegg would violate the Company's rights under the Commerce Clause* . . .") (italics added).] As noted in paragraph 4, above, Newegg asserts before this Court a facial challenge, in addition to its as-applied challenge to the CAT under the Commerce Clause.

CONCLUSION

For all of the foregoing reasons, Newegg respectfully requests that the Decision of the Board be reversed. Newegg requests that final judgment be entered in its favor voiding the Board's Decision and the CAT assessments at issue in this appeal.

Respectfully submitted,

Martin I. Eisenstein esq

Martin I. Eisenstein (PHV 1095-2015)
(Counsel of Record)
Matthew P. Schaefer (PHV 2399-2015)
BRANN & ISAACSON
184 Main Street
P.O. Box 3070
Lewiston, ME 04243-3070
Tel. (207) 786-3566
Fax (207) 783-9325
Email: meisenstein@brannlaw.com
mschaefer@brannlaw.com

AND

Edward J. Bernert (0025808)
BAKER HOSTETLER
Capital Square, Suite 2100
65 East State Street
Columbus, OH 43215-4260
Tel: (614) 462-2687
Fax: (614) 462-2616
Email: ebernert@bakerlaw.com

Counsel for Appellant
Newegg, Inc.

BEFORE THE BOARD OF TAX APPEALS
STATE OF OHIO

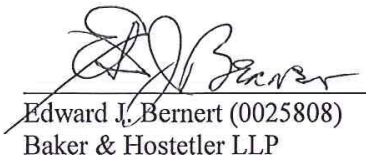
Newegg, Inc.,	:	
	:	Case No. _____
	:	
Appellant,	:	
	:	Appeal from the Ohio
v.	:	Board of Tax Appeals
	:	
Joseph W. Testa,	:	
Tax Commissioner of Ohio,	:	
	:	BTA Case No. 2012-234
Appellee.	:	

PRAECIPE

TO THE OHIO BOARD OF TAX APPEALS

Demand is hereby made that the Ohio Board of Tax Appeals ("Board") prepare, transmit and file with the Supreme Court of Ohio a certified transcript of the records and proceedings of the Board pertaining to its Order in the above-styled matter; including in said certified transcript, the Board's Order, the original papers in the case or a transcript thereof, and all evidence with originals or copies of all exhibits as adduced in said proceeding considered by the Board in making its Order.

Respectfully submitted,



Edward J. Bernert (0025808)
Baker & Hostetler LLP
65 East State Street, Suite 2100
Columbus, Ohio 43215
(614) 228-1541

One of the Attorneys for Appellant
Newegg, Inc.

PROOF OF SERVICE UPON OHIO BOARD OF TAX APPEALS

This is to certify that the Notice of Appeal of Newegg, Inc., was filed by hand delivery with the Ohio Board of Tax Appeals, State Office Tower, 30 East Broad Street, 24th Floor, Columbus, Ohio as evidenced by its date stamp as set forth hereon.

Edward J. Bernert (0025808)
One of the Attorneys for Appellant
Newegg, Inc.

CERTIFICATE OF SERVICE

This is to certify that a true copy of the foregoing Notice of Appeal of Appellant Newegg, Inc. was sent by certified U.S. mail to Appellee Joseph W. Testa, Tax Commissioner of Ohio, 30 East Broad Street, 22nd Floor, Columbus, Ohio 43215; and to counsel of record for Appellee Tax Commissioner, by certified mail and hand delivery to The Honorable Mike DeWine, Attorney General of Ohio, Christine T. Mesirow and Daniel W. Fausey, Assistant Attorneys General, State of Ohio, 30 East Broad Street, 25th Floor, Columbus, Ohio 43215–3428, on this 25th day of March, 2015.

Edward J. Bernert (0025808)
One of the Attorneys for Appellant
Newegg, Inc.

606085978.1

OHIO BOARD OF TAX APPEALS

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

Appellant(s),

vs.

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

Appellee(s).

CASE NO(S). 2012-234

(COMMERCIAL ACTIVITY TAX)

DECISION AND ORDER

APPEARANCES:

For the Appellant(s) - NEWEGG, INC.
Represented by:
MARTIN EISENSTEIN
BRANN & ISAACSON
P.O. BOX 3070
184 MAIN STREET
LEWISTON, ME 04243-3070

STEVEN L. SMISECK
VORYS, SATER, SEYMOUR AND PEASE LLP
52 EAST GAY STREET, P.O. BOX 1008
COLUMBUS, OH 43216

For the Appellee(s) - JOSEPH W. TESTA, TAX COMMISSIONER OF OHIO
Represented by:
CHRISTINE T. MESIROW
ASSISTANT ATTORNEY GENERAL
OFFICE OF OHIO ATTORNEY GENERAL
30 EAST BROAD STREET, 25TH FLOOR
COLUMBUS, OH 43215

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

RECEIVED
JAN 19 2012
DEPT. OF TAXATION OF OHIO
OFFICE OF TAX COMMISSIONER

BEFORE THE OHIO BOARD OF TAX APPEALS

NEWEGG, INC., 16839 E. Gale Avenue City of Industry, CA 91745 Appellant, vs. **JOSEPH W. TESTA,** Tax Commissioner of Ohio 30 East Broad Street, 22nd Floor Columbus, OH 43215, Appellee.	)	BTA Case No._____ (COMMERCIAL ACTIVITY TAX) Amount in Controversy: Approximately $1,160,000 in Tax, Penalties, and Pre-Assessment Interest, Plus Post-Assessment Interest.

RECEIVED
BOARD OF TAX APPEALS
2012 JAN 19 PM 12:47

NOTICE OF APPEAL

Martin I. Eisenstein (Maine Reg. 003027)
Matthew P. Schaefer (Maine Reg. 007992)

BRANN & ISAACSON
184 Main Street
P.O. Box 3070
Lewiston, ME 04243-3070
Tel. (207) 786-3566
Fax (207) 783-9325
Email: meisenstein@brannlaw.com
mschaefer@brannlaw.com

LEGAL COUNSEL FOR APPELLANT,
NEWEGG, INC.

Raymond D. Anderson (0015196)
Steven L. Smiseck (0061615)

VORYS, SATER, SEYMOUR & PEASE LLP
52 East Gay Street
P.O. Box 1008
Columbus, OH 43216-1008
Tel: (614) 464-6447
Fax: (614) 719-4856
Email: rdanderson@vorys.com
slsmiseck@vorys.com

LEGAL COUNSEL FOR APPELLANT,
NEWEGG, INC.

Pursuant to Section 5717.02 of the Ohio Revised Code ("R.C."), Newegg, Inc. ("Newegg" or the "Company") hereby gives notice of appeal to the Ohio Board of Tax Appeals ("the Board") from a final determination dated November 22, 2011 ("Determination") issued by Joseph W. Testa, Tax Commissioner of the State of Ohio ("Commissioner") that affirmed assessments of Ohio Commercial Activity Tax ("CAT") against Newegg with respect to the following tax periods: (1) July 1, 2005 through December 31, 2009; (2) January 1, 2010 through March 31, 2010 (including 2010 estimated tax); (3) April 1, 2010 through June 30, 2010; (4) July 1, 2010 through September 30, 2010; (5) October 1, 2010 through December 31, 2010; and (6) January 1, 2011 through March 31, 2011 (including 2011 estimated tax) (together, the "Tax Periods"). A copy of the Determination is attached hereto as required by statute. *See* Exhibit A.

BACKGROUND

1. Newegg is an online retailer with no physical presence in the State of Ohio. It sells its goods through the Internet from locations entirely outside of the state.

2. While some of Newegg's customers reside in Ohio, Newegg itself has no personnel, agents, representatives, or property of any kind in Ohio, and makes no sales from within the State of Ohio.

3. As a result, Newegg is protected from imposition of the Commercial Activity Tax ("CAT") under the Commerce Clause of the United States Constitution. The United States Supreme Court has made clear that a state lacks the power under the Commerce Clause to impose a gross receipts tax on a company with no physical presence in the state. *Tyler Pipe Industries, Inc. v. Wash. Dep't of Revenue*, 483 U.S. 232, 250 (1987). This "bright line," physical presence standard derives from constitutional principles and authorities set forth by the

Court in *National Bellas Hess v. Ill. Dep't of Revenue*, 386 U.S. 753 (1967), and subsequently reaffirmed in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

4. As it applies to gross receipts taxes like the CAT, the Supreme Court has held that the physical presence standard is only satisfied through in-state activities by, or on behalf of, the taxpayer that are significantly associated with its ability to establish and maintain a market in the state. *Tyler Pipe,* 483 U.S. at 250; *Standard Pressed Steel, Inc. v. Wash. Dep't of Revenue*, 419 U.S. 560, 562-64 (1975) (sufficient nexus for gross receipts tax established through presence of full-time employee in the state calling on customers); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 617, 626 (1981) (citing *Bellas Hess* for threshold of state taxing power for gross receipts tax purposes, and finding sufficient presence); *see also Norton Co. v. Ill. Dep't of Revenue,* 340 U.S. 534, 537 (state lacks authority to impose gross receipts tax on a company with no "local incident" in the state). The Supreme Court relied upon *Tyler Pipe, Standard Pressed Steel*, and *Commonwealth Edison* in upholding the physical presence test for sales and use taxes in *Quill*, and the Court has never held that a state has the power under the Commerce Clause to impose gross receipts tax on a company based on any lesser, or different standard than the "bright line," physical presence test of *Tyler Pipe* and *Quill*. Because Newegg lacks the necessary physical presence in Ohio required under the Commerce Clause, it is not subject to the CAT, and the assessments against it should be cancelled.

5. In addition to its constitutional protections, Newegg also submits that it does not satisfy the statutory requirements for imposition of Ohio's Commercial Activity Tax (the "CAT") inasmuch as it does not satisfy the in-state activity requirements that underpin the imposition of such tax.

6. Read as a whole, the CAT seeks to tax in-state business activities, not those between Ohio residents and those companies, like Newegg, having no in-state presence

whatsoever. Moreover, even if it were to be held that the CAT statutes were ambiguous as to their application to out-of-state companies like Newegg, "there is one fundamental precept which still obtains in the interpretation of taxation statutes, to wit, that in case of doubt, such doubt is to be resolved in favor of the taxpayer." *Stephens v. Glander*, 151 Ohio St. 62, 84 N.E.2d 279, 281 (1949).

7. Newegg submits that, when all doubts are resolved in its favor as required by law, the Determination against it should be vacated in its entirety and the assessment cancelled.

8. Further, Newegg submits that any penalty sought to be imposed on the Company should be rescinded because: (1) it was reasonable for Newegg to conclude that Ohio's attempt to export a domestic tax to a foreign corporation with no in-state presence violated state and federal law; and (2) Newegg's reliance on well established legal principles, including the United States Supreme Court bright-line "substantial nexus" rule was justified and appropriate in light of Ohio's unprecedented attempt to impose the CAT on non-resident mail order and Internet sellers.

THE FINAL DETERMINATION

9. In support of his finding that Newegg was subject to the CAT, despite its lack of physical presence in Ohio, for each of the Tax Periods, the Commissioner rested the Determination on the following grounds:

10. First, the Determination concluded that Newegg had "substantial nexus" with Ohio as that term is defined in the statute [*see* R.C. 5751.01(H)], based on the "bright-line presence" test set forth in R.C. 5751.03(I)(3). [Determination at 3.] The Commissioner stated that Newegg "had annual sales sitused to Ohio in excess of $500,000.00 and, therefore, met the bright-line presence requirement subjecting it to the commercial activity tax." [*Id.*]

11. There was no other "bright-line" statutory basis for the Determination's conclusion that Newegg owed CAT for the Tax Period.

12. At the same time, the Commissioner found that there is no ambiguity in the application of the CAT to an out-of-state retailer with no physical presence in the State of Ohio, such as Newegg. According to the Commissioner, despite the physical presence requirement of the Commerce Clause, the terms of the CAT dictate that it applies to Newegg, based solely on Newegg's annual gross receipts from sales to Ohio purchasers. [*Id.*]

13. Finally, the Commissioner stated that "[u]nder established Commerce Clause jurisprudence, the imposition of the tax measured by those receipts is not prohibited by the laws or the Constitution of either the United States or Ohio." [*Id.*]

14. Each of the grounds given by the Commissioner for the Determination is in error.

ASSIGNMENTS OF ERROR

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 this 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 [sic] 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, as discussed below. It is the duty of those charged with interpreting and applying a law to construe it so as to "prevent a declaration of unconstitutionality." *Conold v. Stern*, 138 Ohio St. 352, 25 N.E.2d 133, 143 (1941) (citation omitted). Only by excluding Newegg from the reach of the CAT can the constitutionality of the tax be preserved.

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. The Supreme Court has made clear that a state lacks the power under the Commerce Clause to impose a gross receipts tax on a company with no physical presence in the state. *Tyler Pipe*, 483 U.S. at 250 (1987) ("the crucial factor governing nexus is whether <u>the activities performed in this state on behalf of the taxpayer</u> are significantly associated with the taxpayer's ability to establish and maintain a market in this State") (internal citation omitted and emphasis added); *Standard Pressed Steel*, 419 U.S. at 562-64 (1975)

(sufficient nexus for gross receipts tax established through presence of full-time employee in the state calling on customers); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981) (applying the bright-line rule to a general revenue tax on the value of coal extracted from the state, and finding that "the interstate business must have a substantial nexus with the State before any tax may be levied on it"). This physical presence standard derives from constitutional principles and authorities set forth by the Court in *National Bellas Hess* and subsequently reaffirmed in *Quill*. The Supreme Court relied upon *Tyler Pipe, Standard Pressed Steel*, and *Commonwealth Edison* in upholding the physical presence test for sales and use taxes in *Quill*, and the Court has never held that a state has the power under the Commerce Clause to impose gross receipts tax on a company based on any lesser, or different standard than physical presence test of *Tyler Pipe* and *Quill*. 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 asserting 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.

REQUEST FOR HEARING

Appellant Newegg requests that the Board of Tax Appeals or its attorney examiners conduct a *de novo* hearing in Columbus, Ohio in connection with these assignments of error.

REQUEST FOR RELIEF

Newegg respectfully asks that the Determination be vacated in its entirety, that the assessments against Newegg for the Tax Periods cancelled, that the Commissioner be barred from asserting CAT liability against Newegg for the Tax Periods, and that Newegg be awarded such other relief as is just and equitable.

Respectfully submitted,

Martin I. Eisenstein by RDA per e-mail authorization on 1/19/12

Martin I. Eisenstein (Maine Reg. 0017878)
Matthew P. Schaefer (Maine Reg. 007992)
BRANN & ISAACSON
184 Main Street
P.O. Box 3070
Lewiston, ME 04243-3070
Tel. (207) 786-3566
Fax (207) 783-9325
Email: meisenstein@brannlaw.com
mschaefer@brannlaw.com

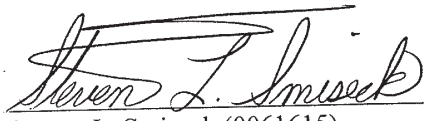
and

Raymond D. Anderson (0015196)
Steven L. Smiseck (0061615)
VORYS, SATER, SEYMOUR & PEASE LLP
52 East Gay Street
P.O. Box 1008
Columbus, OH 43216-1008
Tel: (614) 464-6447
Fax: (614) 719-4856
Email: rdanderson@vorys.com
slsmiseck@vorys.com

LEGAL COUNSEL FOR APPELLANT,
NEWEGG, INC.

CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of this Notice of Appeal has been filed, via hand delivery, with Joseph W. Testa, Tax Commissioner of Ohio, 30 East Broad Street, 22nd Floor, Columbus, Ohio, on this 19th day of January, 2012.



Steven L. Smiseck (0061615)

Ohio Department of TAXATION
Office of the Tax Commissioner
30 E. Broad St., 22nd Floor • Columbus, OH 43215

NOV 28 2011

1000000034

FINAL DETERMINATION

Date: NOV 22 2011

Newegg Inc.
16839 E. Gale Avenue
City of Industry, CA 91745

Re: Six Assessments
Commercial Activity Tax

This is the final determination of the Tax Commissioner with regard to the petitions for reassessment under R.C. 5751.09 concerning the following commercial activity tax assessments:

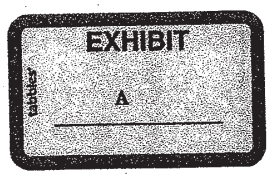
Assessment No.	Period	Tax	Interest	Late Filing Penalty	Late Payment Penalty	Total
17201034126112	7/1/2005 - 12/31/2009	$447,580.00	$54,081.00	$156,655.00	$111,895.00	$770,211.00
17201034427316	2010 1st quarter/2010 estimate	$50,000.00	$1,117.81	$17,500.00	$10,000.00	$78,617.81
17201034427317	2010 2nd quarter	$50,000.00	$630.14	$17,500.00	$10,000.00	$78,130.14
17201034427318	2010 3rd quarter	$50,000.00	$126.03	$17,500.00	$10,000.00	$77,626.03
17201106110042	2010 4th quarter	$50,000.00	$71.23	$17,500.00	$10,000.00	$77,571.23
17201114476189	2011 1st quarter/2011 estimate	$50,000.00	$38.36	$17,500.00	$10,000.00	$77,538.36

The petitioner was assessed as the result of an audit which was commenced because it failed to register for the Ohio commercial activity tax. The petitioner is the second largest on-line only retailer in the United States selling information technology and consumer electronic products. Most orders are fulfilled through on-line processing centers in California and New Jersey. The petitioner conducts the majority of its marketing efforts on-line through targeted marketing via affiliates, search engines, shopping comparison sites and e-mail programs. Its off-line marketing activities include advertisements in various technology publications, print and electronic catalogs, box inserts, event participation, public relations and targeted broadcast and major media print and broadcast activities designed to increase its brand awareness. The petitioner fulfills its orders from warehouses located in New Jersey and Tennessee.

The audit results clearly determined that the petitioner had more than $500,000 in sales to customers in Ohio. Consequently, it was required to file and pay the commercial activity tax required by R.C. 5751.02(A) which it failed to do. The petitioner was assessed and it submitted petitions for reassessment, requesting a hearing which was duly held.

The petitioner makes the following contention:

> * * * Newegg is protected from imposition of the Commercial Activity Tax ("CAT") under the Commerce Clause of the United States Constitution. The Supreme Court has made clear that a state lacks the power under the Commerce Clause to impose a gross receipts tax on a company with no physical presence in the state. *Tyler Pipe Industries,*



1000000035
NOV 22 2011

> *Inc. v. Wash. Dep't of Revenue*, 483 U.S. 232, 250 (1987). * * * In addition to its constitutional protections, Newegg also submits that it does not satisfy the statutory requirements for imposition of Ohio's Commercial Activity Tax (the "CAT") inasmuch as it does not satisfy the in-state activity requirements that underpin the imposition of such tax. Read as a whole, the CAT seeks to tax in-state business activities, not those between Ohio residents and those companies like Newegg, having no in-state presence whatsoever. Moreover, even if it were to be held that the CAT statutes were ambiguous as to their application to out-of-state companies like Newegg, "there is one fundamental precept which still obtains in the interpretation of taxation statutes, to wit, that in case of doubt, such doubt is to be resolved in favor of the taxpayer." *Stephens v. Glander*, 151 Ohio St. 62, 84 N.E.2nd 279, 281 (1949).

While the petitioner has customers in Ohio to which it sells and ships goods, it asserts that it has no activities or contacts in Ohio which rise to the level necessary for Ohio to constitutionally impose the tax.

The petitioner's contention is not well taken. The petitioner is subject to the tax because it has "substantial nexus with this state," as that phrase is defined in R.C. 5751.01(H). The petitioner satisfies the third condition in that division, and therefore is a person on whom the tax is levied.

Effective June 30, 2005, R.C. 5751.02(A) levies the commercial activity tax

> * * * on each person with taxable gross receipts for the privilege of doing business in this state. For the purposes of this chapter, "doing business" means engaging in any activity, whether legal or illegal, that is conducted for, or results in, gain, profit, or income, at any time during the calendar year. Persons on which the commercial activity tax is levied include, but are not limited to, persons with substantial nexus with this state.

Pursuant to R.C. 5751.01(H), a person has "substantial nexus with this state" if the person meets any of the following conditions:

(1) Owns or uses a part or all of its capital in this state;
(2) Holds a certificate of compliance with the laws of this state authorizing the person to do business in this state;
(3) Has bright-line presence in this state;
(4) Otherwise has nexus with this state to an extent that the person can be required to remit the tax imposed under this chapter under the Constitution of the United States.

Pursuant to R.C. 5751.01(I), a person "has bright-line presence" in this state for a reporting period if the person meets any of the following conditions:

(1) Has at any time during the calendar year property in this state with an aggregate value of at least fifty thousand dollars. * * *
(2) Has during the calendar year payroll in this state of at least fifty thousand dollars. * * *

1000000036
NOV 22 2011

(3) Has during the calendar year taxable gross receipts of at least five hundred thousand dollars.
(4) Has at any time during the calendar year within this state at least twenty-five percent of the person's total property, total payroll, or total gross receipts.
(5) Is domiciled in this state as an individual or for corporate, commercial, or other business purposes.

Division (F) of R.C. 5751.01 defines gross receipts as "the total amount realized by a person, without deduction for the cost of goods sold or other expenses incurred, that contributes to the production of gross income of the person * * * [including] [a]mounts realized from the sale, exchange, or other disposition of the taxpayer's property to or with another." Specifically excluded from gross receipts are "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." R.C. 5751.01(F)(2)(aa) (formerly R.C. 5751.01(F)(2)(z)).

"Taxable gross receipts" is defined as gross receipts sitused to this state under R.C. 5751.033. For purposes of the petitioner, division (E) applies:

> Gross receipts from the sale of tangible personal property shall be sitused to this state if the property is received in this state by the purchaser. In the case of delivery of tangible personal property by common carrier or by other means of transportation, the place at which such property is ultimately received after all transportation has completed shall be considered the place where the purchaser receives the property. * * *

There is no ambiguity. The petitioner had annual sales sitused to Ohio in excess of $500,000.00 and, therefore, met the bright-line presence requirement subjecting it to the commercial activity tax.

Further, gross receipts from the sale of tangible personal property are sitused to Ohio if "such property is ultimately received in Ohio after all transportation has been completed * * * regardless of where title passes or other conditions of sale." R.C. 5751.033(E). Consequently, the Ohio commercial activity tax requires the property to be sitused to Ohio because Ohio was the ultimate destination of the property. Therefore, the gross receipts were properly sitused to Ohio.

The petitioner has more than $500,000.00 in taxable gross receipts sitused to Ohio for periods assessed and, thus has "bright-line presence." As such, the petitioner has "substantial nexus" with Ohio. Under established Commerce Clause jurisprudence, the imposition of the tax measured by those receipts is not prohibited by the laws or Constitution of either the United States or Ohio.

The petitioner is a person doing business in Ohio and, therefore, subject to the Ohio Commercial Activity tax. R.C. 5751.02. The petitioner failed to provide any support to show otherwise nor did it provide actual Ohio gross receipts for the periods assessed.

Accordingly, the assessments are affirmed and will stand as issued.

0000000037
NOV 22 2011

Current records indicate that no payments have been made on these assessments. However, due to payment processing and posting time lags, payments may have been made that are not reflected in this final determination. **Any tax balances unpaid after the assessment dates bear post-assessment interest for the period between the assessment dates and payments as provided by law, which is in addition to the above totals.** Payments shall be made payable to "Ohio Treasurer Josh Mandel." Any payment made within sixty days of the date of this final determination should be forwarded to: Department of Taxation, Commercial Activity Tax Division, P.O. Box 16678, Columbus, Ohio 43216-6678.

THIS IS THE TAX COMMISSIONER'S FINAL DETERMINATION WITH REGARD TO THIS MATTER. UPON EXPIRATION OF THE SIXTY-DAY APPEAL PERIOD PRESCRIBED BY R.C. 5717.02, THIS MATTER WILL BE CONCLUDED AND THE FILE APPROPRIATELY CLOSED.

I CERTIFY THAT THIS IS A TRUE AND ACCURATE COPY OF THE FINAL DETERMINATION RECORDED IN THE TAX COMMISSIONER'S JOURNAL

JOSEPH W. TESTA
TAX COMMISSIONER

/s/ Joseph W. Testa

Joseph W. Testa
Tax Commissioner

COMMERCE CLAUSE

U.S. Const., art. I, § 8, cl. 3

The Congress shall have power *** [t]o regulate commerce with foreign nations, and among the several states, and with the Indian tribes; ***

DUE PROCESS CLAUSE

U.S. Const., amend. XIV, § 1

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the state wherein they reside. No state shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any state deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

5751.01 Definitions.

As used in this chapter:

(A) "Person" means, but is not limited to, individuals, combinations of individuals of any form, receivers, assignees, trustees in bankruptcy, firms, companies, joint-stock companies, business trusts, estates, partnerships, limited liability partnerships, limited liability companies, associations, joint ventures, clubs, societies, for-profit corporations, S corporations, qualified subchapter S subsidiaries, qualified subchapter S trusts, trusts, entities that are disregarded for federal income tax purposes, and any other entities.

(B) "Consolidated elected taxpayer" means a group of two or more persons treated as a single taxpayer for purposes of this chapter as the result of an election made under section 5751.011 of the Revised Code.

(C) "Combined taxpayer" means a group of two or more persons treated as a single taxpayer for purposes of this chapter under section 5751.012 of the Revised Code.

(D) "Taxpayer" means any person, or any group of persons in the case of a consolidated elected taxpayer or combined taxpayer treated as one taxpayer, required to register or pay tax under this chapter. "Taxpayer" does not include excluded persons.

(E) "Excluded person" means any of the following:

(1) Any person with not more than one hundred fifty thousand dollars of taxable gross receipts during the calendar year. Division (E)(1) of this section does not apply to a person that is a member of a consolidated elected taxpayer;

(2) A public utility that paid the excise tax imposed by section 5727.24 or 5727.30 of the Revised Code based on one or more measurement periods that include the entire tax period under this chapter, except that a public utility that is a combined company is a taxpayer with regard to the following gross receipts:

(a) Taxable gross receipts directly attributed to a public utility activity, but not directly attributed to an activity that is subject to the excise tax imposed by section 5727.24 or 5727.30 of the Revised Code;

(b) Taxable gross receipts that cannot be directly attributed to any activity, multiplied by a fraction whose numerator is the taxable gross receipts described in division (E)(2)(a) of this section and whose denominator is the total taxable gross receipts that can be directly attributed to any activity;

(c) Except for any differences resulting from the use of an accrual basis method of accounting for purposes of determining gross receipts under this chapter and the use of the cash basis method of accounting for purposes of determining gross receipts under section 5727.24 of the Revised Code, the gross receipts directly attributed to the activity of a natural gas company shall be determined in a manner consistent with division (D) of section 5727.03 of the Revised Code.

As used in division (E)(2) of this section, "combined company" and "public utility" have the same meanings as in section 5727.01 of the Revised Code.

(3) A financial institution, as defined in section 5726.01 of the Revised Code, that paid the tax imposed by section 5726.02 of the Revised Code based on one or more taxable years that include the entire tax period under this chapter;

(4) A person directly or indirectly owned by one or more financial institutions, as defined in section 5726.01 of the Revised Code, that paid the tax imposed by section 5726.02 of the Revised Code based on

one or more taxable years that include the entire tax period under this chapter.

For the purposes of division (E)(4) of this section, a person owns another person under the following circumstances:

(a) In the case of corporations issuing capital stock, one corporation owns another corporation if it owns fifty per cent or more of the other corporation's capital stock with current voting rights;

(b) In the case of a limited liability company, one person owns the company if that person's membership interest, as defined in section 1705.01 of the Revised Code, is fifty per cent or more of the combined membership interests of all persons owning such interests in the company;

(c) In the case of a partnership, trust, or other unincorporated business organization other than a limited liability company, one person owns the organization if, under the articles of organization or other instrument governing the affairs of the organization, that person has a beneficial interest in the organization's profits, surpluses, losses, or distributions of fifty per cent or more of the combined beneficial interests of all persons having such an interest in the organization.

(5) A domestic insurance company or foreign insurance company, as defined in section 5725.01 of the Revised Code, that paid the insurance company premiums tax imposed by section 5725.18 or Chapter 5729. of the Revised Code, or an unauthorized insurance company whose gross premiums are subject to tax under section 3905.36 of the Revised Code based on one or more measurement periods that include the entire tax period under this chapter;

(6) A person that solely facilitates or services one or more securitizations of phase-in-recovery property pursuant to a final financing order as those terms are defined in section 4928.23 of the Revised Code. For purposes of this division, "securitization" means transferring one or more assets to one or more persons and then issuing securities backed by the right to receive payment from the asset or assets so transferred.

(7) Except as otherwise provided in this division, a pre-income tax trust as defined in division (FF)(4) of section 5747.01 of the Revised Code and any pass-through entity of which such pre-income tax trust owns or controls, directly, indirectly, or constructively through related interests, more than five per cent of the ownership or equity interests. If the pre-income tax trust has made a qualifying pre-income tax trust election under division (FF)(3) of section 5747.01 of the Revised Code, then the trust and the pass-through entities of which it owns or controls, directly, indirectly, or constructively through related interests, more than five per cent of the ownership or equity interests, shall not be excluded persons for purposes of the tax imposed under section 5751.02 of the Revised Code.

(8) Nonprofit organizations or the state and its agencies, instrumentalities, or political subdivisions.

(F) Except as otherwise provided in divisions (F)(2), (3), and (4) of this section, "gross receipts" means the total amount realized by a person, without deduction for the cost of goods sold or other expenses incurred, that contributes to the production of gross income of the person, including the fair market value of any property and any services received, and any debt transferred or forgiven as consideration.

(1) The following are examples of gross receipts:

(a) Amounts realized from the sale, exchange, or other disposition of the taxpayer's property to or with another;

(b) Amounts realized from the taxpayer's performance of services for another;

(c) Amounts realized from another's use or possession of the taxpayer's property or capital;

(d) Any combination of the foregoing amounts.

(2) "Gross receipts" excludes the following amounts:

(a) Interest income except interest on credit sales;

(b) Dividends and distributions from corporations, and distributive or proportionate shares of receipts and income from a pass-through entity as defined under section 5733.04 of the Revised Code;

(c) Receipts from the sale, exchange, or other disposition of an asset described in section 1221 or 1231 of the Internal Revenue Code, without regard to the length of time the person held the asset. Notwithstanding section 1221 of the Internal Revenue Code, receipts from hedging transactions also are excluded to the extent the transactions are entered into primarily to protect a financial position, such as managing the risk of exposure to (i) foreign currency fluctuations that affect assets, liabilities, profits, losses, equity, or investments in foreign operations; (ii) interest rate fluctuations; or (iii) commodity price fluctuations. As used in division (F)(2)(c) of this section, "hedging transaction" has the same meaning as used in section 1221 of the Internal Revenue Code and also includes transactions accorded hedge accounting treatment under statement of financial accounting standards number 133 of the financial accounting standards board. For the purposes of division (F)(2)(c) of this section, the actual transfer of title of real or tangible personal property to another entity is not a hedging transaction.

(d) Proceeds received attributable to the repayment, maturity, or redemption of the principal of a loan, bond, mutual fund, certificate of deposit, or marketable instrument;

(e) The principal amount received under a repurchase agreement or on account of any transaction properly characterized as a loan to the person;

(f) Contributions received by a trust, plan, or other arrangement, any of which is described in section 501(a) of the Internal Revenue Code, or to which Title 26, Subtitle A, Chapter 1, Subchapter (D) of the Internal Revenue Code applies;

(g) Compensation, whether current or deferred, and whether in cash or in kind, received or to be received by an employee, former employee, or the employee's legal successor for services rendered to or for an employer, including reimbursements received by or for an individual for medical or education expenses, health insurance premiums, or employee expenses, or on account of a dependent care spending account, legal services plan, any cafeteria plan described in section 125 of the Internal Revenue Code, or any similar employee reimbursement;

(h) Proceeds received from the issuance of the taxpayer's own stock, options, warrants, puts, or calls, or from the sale of the taxpayer's treasury stock;

(i) Proceeds received on the account of payments from insurance policies, except those proceeds received for the loss of business revenue;

(j) Gifts or charitable contributions received; membership dues received by trade, professional, homeowners', or condominium associations; and payments received for educational courses, meetings, meals, or similar payments to a trade, professional, or other similar association; and fundraising receipts received by any person when any excess receipts are donated or used exclusively for charitable purposes;

(k) Damages received as the result of litigation in excess of amounts that, if received without litigation,

would be gross receipts;

(l) Property, money, and other amounts received or acquired by an agent on behalf of another in excess of the agent's commission, fee, or other remuneration;

(m) Tax refunds, other tax benefit recoveries, and reimbursements for the tax imposed under this chapter made by entities that are part of the same combined taxpayer or consolidated elected taxpayer group, and reimbursements made by entities that are not members of a combined taxpayer or consolidated elected taxpayer group that are required to be made for economic parity among multiple owners of an entity whose tax obligation under this chapter is required to be reported and paid entirely by one owner, pursuant to the requirements of sections 5751.011 and 5751.012 of the Revised Code;

(n) Pension reversions;

(o) Contributions to capital;

(p) Sales or use taxes collected as a vendor or an out-of-state seller on behalf of the taxing jurisdiction from a consumer or other taxes the taxpayer is required by law to collect directly from a purchaser and remit to a local, state, or federal tax authority;

(q) In the case of receipts from the sale of cigarettes or tobacco products by a wholesale dealer, retail dealer, distributor, manufacturer, or seller, all as defined in section 5743.01 of the Revised Code, an amount equal to the federal and state excise taxes paid by any person on or for such cigarettes or tobacco products under subtitle E of the Internal Revenue Code or Chapter 5743. of the Revised Code;

(r) **[Applicable to tax periods beginning before 7/1/2015]**Receipts from the sale, transfer, exchange, or other disposition of motor fuel as "motor fuel" is defined in section 5736.01 of the Revised Code;

(r) **[Applicable to tax periods beginning 7/1/2015]** In the case of receipts from the sale, transfer, exchange, or other disposition of motor fuel as "motor fuel" is defined in section 5736.01 of the Revised Code, an amount equal to the value of the motor fuel, including federal and state motor fuel excise taxes and receipts from billing or invoicing the tax imposed under section 5736.02 of the Revised Code to another person;

(s) In the case of receipts from the sale of beer or intoxicating liquor, as defined in section 4301.01 of the Revised Code, by a person holding a permit issued under Chapter 4301. or 4303. of the Revised Code, an amount equal to federal and state excise taxes paid by any person on or for such beer or intoxicating liquor under subtitle E of the Internal Revenue Code or Chapter 4301. or 4305. of the Revised Code;

(t) Receipts realized by a new motor vehicle dealer or used motor vehicle dealer, as defined in section 4517.01 of the Revised Code, from the sale or other transfer of a motor vehicle, as defined in that section, to another motor vehicle dealer for the purpose of resale by the transferee motor vehicle dealer, but only if the sale or other transfer was based upon the transferee's need to meet a specific customer's preference for a motor vehicle;

(u) Receipts from a financial institution described in division (E)(3) of this section for services provided to the financial institution in connection with the issuance, processing, servicing, and management of loans or credit accounts, if such financial institution and the recipient of such receipts have at least fifty per cent of their ownership interests owned or controlled, directly or constructively through related interests, by common owners;

(v) Receipts realized from administering anti-neoplastic drugs and other cancer chemotherapy, biologicals, therapeutic agents, and supportive drugs in a physician's office to patients with cancer;

(w) Funds received or used by a mortgage broker that is not a dealer in intangibles, other than fees or other consideration, pursuant to a table-funding mortgage loan or warehouse-lending mortgage loan. Terms used in division (F)(2)(w) of this section have the same meanings as in section 1322.01 of the Revised Code, except "mortgage broker" means a person assisting a buyer in obtaining a mortgage loan for a fee or other consideration paid by the buyer or a lender, or a person engaged in table-funding or warehouse-lending mortgage loans that are first lien mortgage loans.

(x) Property, money, and other amounts received by a professional employer organization, as defined in section 4125.01 of the Revised Code, from a client employer, as defined in that section, in excess of the administrative fee charged by the professional employer organization to the client employer;

(y) In the case of amounts retained as commissions by a permit holder under Chapter 3769. of the Revised Code, an amount equal to the amounts specified under that chapter that must be paid to or collected by the tax commissioner as a tax and the amounts specified under that chapter to be used as purse money;

(z) Qualifying distribution center receipts.

(i) For purposes of division (F)(2)(z) of this section:

(I) "Qualifying distribution center receipts" means receipts of a supplier from qualified property that is delivered to a qualified distribution center, multiplied by a quantity that equals one minus the Ohio delivery percentage. If the qualified distribution center is a refining facility, "supplier" includes all dealers, brokers, processors, sellers, vendors, cosigners, and distributors of qualified property.

(II) "Qualified property" means tangible personal property delivered to a qualified distribution center that is shipped to that qualified distribution center solely for further shipping by the qualified distribution center to another location in this state or elsewhere or, in the case of gold, silver, platinum, or palladium delivered to a refining facility solely for refining to a grade and fineness acceptable for delivery to a registered commodities exchange. "Further shipping" includes storing and repackaging property into smaller or larger bundles, so long as the property is not subject to further manufacturing or processing. "Refining" is limited to extracting impurities from gold, silver, platinum, or palladium through smelting or some other process at a refining facility.

(III) "Qualified distribution center" means a warehouse, a facility similar to a warehouse, or a refining facility in this state that, for the qualifying year, is operated by a person that is not part of a combined taxpayer group and that has a qualifying certificate. All warehouses or facilities similar to warehouses that are operated by persons in the same taxpayer group and that are located within one mile of each other shall be treated as one qualified distribution center. All refining facilities that are operated by persons in the same taxpayer group and that are located in the same or adjacent counties may be treated as one qualified distribution center.

(IV) "Qualifying year" means the calendar year to which the qualifying certificate applies.

(V) "Qualifying period" means the period of the first day of July of the second year preceding the qualifying year through the thirtieth day of June of the year preceding the qualifying year.

(VI) "Qualifying certificate" means the certificate issued by the tax commissioner after the operator of a

distribution center files an annual application with the commissioner. The application and annual fee shall be filed and paid for each qualified distribution center on or before the first day of September before the qualifying year or within forty-five days after the distribution center opens, whichever is later.

The applicant must substantiate to the commissioner's satisfaction that, for the qualifying period, all persons operating the distribution center have more than fifty per cent of the cost of the qualified property shipped to a location such that it would be sitused outside this state under the provisions of division (E) of section 5751.033 of the Revised Code. The applicant must also substantiate that the distribution center cumulatively had costs from its suppliers equal to or exceeding five hundred million dollars during the qualifying period. (For purposes of division (F)(2)(z)(i)(VI) of this section, "supplier" excludes any person that is part of the consolidated elected taxpayer group, if applicable, of the operator of the qualified distribution center.) The commissioner may require the applicant to have an independent certified public accountant certify that the calculation of the minimum thresholds required for a qualified distribution center by the operator of a distribution center has been made in accordance with generally accepted accounting principles. The commissioner shall issue or deny the issuance of a certificate within sixty days after the receipt of the application. A denial is subject to appeal under section 5717.02 of the Revised Code. If the operator files a timely appeal under section 5717.02 of the Revised Code, the operator shall be granted a qualifying certificate effective for the remainder of the qualifying year or until the appeal is finalized, whichever is earlier. If the operator does not prevail in the appeal, the operator shall pay the ineligible operator's supplier tax liability.

(VII) "Ohio delivery percentage" means the proportion of the total property delivered to a destination inside Ohio from the qualified distribution center during the qualifying period compared with total deliveries from such distribution center everywhere during the qualifying period.

(VIII) "Refining facility" means one or more buildings located in a county in the Appalachian region of this state as defined by section 107.21 of the Revised Code and utilized for refining or smelting gold, silver, platinum, or palladium to a grade and fineness acceptable for delivery to a registered commodities exchange.

(IX) "Registered commodities exchange" means a board of trade, such as New York mercantile exchange, inc. or commodity exchange, inc., designated as a contract market by the commodity futures trading commission under the "Commodity Exchange Act," 7 U.S.C. 1 et seq., as amended.

(X) "Ineligible operator's supplier tax liability" means an amount equal to the tax liability of all suppliers of a distribution center had the distribution center not been issued a qualifying certificate for the qualifying year. Ineligible operator's supplier tax liability shall not include interest or penalties. The tax commissioner shall determine an ineligible operator's supplier tax liability based on information that the commissioner may request from the operator of the distribution center. An operator shall provide a list of all suppliers of the distribution center and the corresponding costs of qualified property for the qualifying year at issue within sixty days of a request by the commissioner under this division.

(ii)

(I) If the distribution center is new and was not open for the entire qualifying period, the operator of the distribution center may request that the commissioner grant a qualifying certificate. If the certificate is granted and it is later determined that more than fifty per cent of the qualified property during that year was not shipped to a location such that it would be sitused outside of this state under the provisions of division (E) of section 5751.033 of the Revised Code or if it is later determined that the person that operates the distribution center had average monthly costs from its suppliers of less than forty million

dollars during that year, then the operator of the distribution center shall pay the ineligible operator's supplier tax liability. (For purposes of division (F)(2)(z)(ii) of this section, "supplier" excludes any person that is part of the consolidated elected taxpayer group, if applicable, of the operator of the qualified distribution center.)

(II) The commissioner may grant a qualifying certificate to a distribution center that does not qualify as a qualified distribution center for an entire qualifying period if the operator of the distribution center demonstrates that the business operations of the distribution center have changed or will change such that the distribution center will qualify as a qualified distribution center within thirty-six months after the date the operator first applies for a certificate. If, at the end of that thirty-six-month period, the business operations of the distribution center have not changed such that the distribution center qualifies as a qualified distribution center, the operator of the distribution center shall pay the ineligible operator's supplier tax liability for each year that the distribution center received a certificate but did not qualify as a qualified distribution center. For each year the distribution center receives a certificate under division (F)(2)(z)(ii)(II) of this section, the distribution center shall pay all applicable fees required under division (F)(2)(z) of this section and shall submit an updated business plan showing the progress the distribution center made toward qualifying as a qualified distribution center during the preceding year.

(III) An operator may appeal a determination under division (F)(2)(z)(ii)(I) or (II) of this section that the ineligible operator is liable for the operator's supplier tax liability as a result of not qualifying as a qualified distribution center, as provided in section 5717.02 of the Revised Code.

(iii) When filing an application for a qualifying certificate under division (F)(2)(z)(i)(VI) of this section, the operator of a qualified distribution center also shall provide documentation, as the commissioner requires, for the commissioner to ascertain the Ohio delivery percentage. The commissioner, upon issuing the qualifying certificate, also shall certify the Ohio delivery percentage. The operator of the qualified distribution center may appeal the commissioner's certification of the Ohio delivery percentage in the same manner as an appeal is taken from the denial of a qualifying certificate under division (F)(2)(z)(i)(VI) of this section.

(iv)

(I) In the case where the distribution center is new and not open for the entire qualifying period, the operator shall make a good faith estimate of an Ohio delivery percentage for use by suppliers in their reports of taxable gross receipts for the remainder of the qualifying period. The operator of the facility shall disclose to the suppliers that such Ohio delivery percentage is an estimate and is subject to recalculation. By the due date of the next application for a qualifying certificate, the operator shall determine the actual Ohio delivery percentage for the estimated qualifying period and proceed as provided in division (F)(2)(z)(iii) of this section with respect to the calculation and recalculation of the Ohio delivery percentage. The supplier is required to file, within sixty days after receiving notice from the operator of the qualified distribution center, amended reports for the impacted calendar quarter or quarters or calendar year, whichever the case may be. Any additional tax liability or tax overpayment shall be subject to interest but shall not be subject to the imposition of any penalty so long as the amended returns are timely filed.

(II) The operator of a distribution center that receives a qualifying certificate under division (F)(2)(z)(ii)(II) of this section shall make a good faith estimate of the Ohio delivery percentage that the operator estimates will apply to the distribution center at the end of the thirty-six-month period after the operator first applied for a qualifying certificate under that division. The result of the estimate shall be multiplied by a factor of one and seventy-five one-hundredths. The product of that calculation shall be the Ohio delivery

percentage used by suppliers in their reports of taxable gross receipts for each qualifying year that the distribution center receives a qualifying certificate under division (F)(2)(z)(ii)(II) of this section, except that, if the product is less than five per cent, the Ohio delivery percentage used shall be five per cent and that, if the product exceeds forty-nine per cent, the Ohio delivery percentage used shall be forty-nine per cent.

(v) Qualifying certificates and Ohio delivery percentages issued by the commissioner shall be open to public inspection and shall be timely published by the commissioner. A supplier relying in good faith on a certificate issued under this division shall not be subject to tax on the qualifying distribution center receipts under division (F)(2)(z) of this section. An operator receiving a qualifying certificate is liable for the ineligible operator's supplier tax liability for each year the operator received a certificate but did not qualify as a qualified distribution center.

(vi) The annual fee for a qualifying certificate shall be one hundred thousand dollars for each qualified distribution center. If a qualifying certificate is not issued, the annual fee is subject to refund after the exhaustion of all appeals provided for in division (F)(2)(z)(i)(VI) of this section. The first one hundred thousand dollars of the annual application fees collected each calendar year shall be credited to the revenue enhancement fund. The remainder of the annual application fees collected shall be distributed in the same manner required under section 5751.20 of the Revised Code.

(vii) The tax commissioner may require that adequate security be posted by the operator of the distribution center on appeal when the commissioner disagrees that the applicant has met the minimum thresholds for a qualified distribution center as set forth in division (F)(2)(z) of this section.

(aa) Receipts of an employer from payroll deductions relating to the reimbursement of the employer for advancing moneys to an unrelated third party on an employee's behalf;

(bb) Cash discounts allowed and taken;

(cc) Returns and allowances;

(dd) Bad debts from receipts on the basis of which the tax imposed by this chapter was paid in a prior quarterly tax payment period. For the purpose of this division, "bad debts" means any debts that have become worthless or uncollectible between the preceding and current quarterly tax payment periods, have been uncollected for at least six months, and that may be claimed as a deduction under section 166 of the Internal Revenue Code and the regulations adopted under that section, or that could be claimed as such if the taxpayer kept its accounts on the accrual basis. "Bad debts" does not include repossessed property, uncollectible amounts on property that remains in the possession of the taxpayer until the full purchase price is paid, or expenses in attempting to collect any account receivable or for any portion of the debt recovered;

(ee) Any amount realized from the sale of an account receivable to the extent the receipts from the underlying transaction giving rise to the account receivable were included in the gross receipts of the taxpayer;

(ff) Any receipts directly attributed to a transfer agreement or to the enterprise transferred under that agreement under section 4313.02 of the Revised Code.

(gg)

(i) As used in this division:

(I) "Qualified uranium receipts" means receipts from the sale, exchange, lease, loan, production, processing, or other disposition of uranium within a uranium enrichment zone certified by the tax commissioner under division (F)(2)(gg)(ii) of this section. "Qualified uranium receipts" does not include any receipts with a situs in this state outside a uranium enrichment zone certified by the tax commissioner under division (F)(2)(gg)(ii) of this section.

(II) "Uranium enrichment zone" means all real property that is part of a uranium enrichment facility licensed by the United States nuclear regulatory commission and that was or is owned or controlled by the United States department of energy or its successor.

(ii) Any person that owns, leases, or operates real or tangible personal property constituting or located within a uranium enrichment zone may apply to the tax commissioner to have the uranium enrichment zone certified for the purpose of excluding qualified uranium receipts under division (F)(2)(gg) of this section. The application shall include such information that the tax commissioner prescribes. Within sixty days after receiving the application, the tax commissioner shall certify the zone for that purpose if the commissioner determines that the property qualifies as a uranium enrichment zone as defined in division (F)(2)(gg) of this section, or, if the tax commissioner determines that the property does not qualify, the commissioner shall deny the application or request additional information from the applicant. If the tax commissioner denies an application, the commissioner shall state the reasons for the denial. The applicant may appeal the denial of an application to the board of tax appeals pursuant to section 5717.02 of the Revised Code. If the applicant files a timely appeal, the tax commissioner shall conditionally certify the applicant's property. The conditional certification shall expire when all of the applicant's appeals are exhausted. Until final resolution of the appeal, the applicant shall retain the applicant's records in accordance with section 5751.12 of the Revised Code, notwithstanding any time limit on the preservation of records under that section.

(hh) In the case of amounts collected by a licensed casino operator from casino gaming, amounts in excess of the casino operator's gross casino revenue. In this division, "casino operator" and "casino gaming" have the meanings defined in section 3772.01 of the Revised Code, and "gross casino revenue" has the meaning defined in section 5753.01 of the Revised Code.

(ii) Receipts realized from the sale of agricultural commodities by an agricultural commodity handler, both as defined in section 926.01 of the Revised Code, that is licensed by the director of agriculture to handle agricultural commodities in this state.

(jj) 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 this state.

(3) In the case of a taxpayer when acting as a real estate broker, "gross receipts" includes only the portion of any fee for the service of a real estate broker, or service of a real estate salesperson associated with that broker, that is retained by the broker and not paid to an associated real estate salesperson or another real estate broker. For the purposes of this division, "real estate broker" and "real estate salesperson" have the same meanings as in section 4735.01 of the Revised Code.

(4) A taxpayer's method of accounting for gross receipts for a tax period shall be the same as the taxpayer's method of accounting for federal income tax purposes for the taxpayer's federal taxable year that includes the tax period. If a taxpayer's method of accounting for federal income tax purposes changes, its method of accounting for gross receipts under this chapter shall be changed accordingly.

(G) "Taxable gross receipts" means gross receipts sitused to this state under section 5751.033 of the

Revised Code.

(H) A person has "substantial nexus with this state" if any of the following applies. The person:

(1) Owns or uses a part or all of its capital in this state;

(2) Holds a certificate of compliance with the laws of this state authorizing the person to do business in this state;

(3) Has bright-line presence in this state;

(4) Otherwise has nexus with this state to an extent that the person can be required to remit the tax imposed under this chapter under the Constitution of the United States.

(I) A person has "bright-line presence" in this state for a reporting period and for the remaining portion of the calendar year if any of the following applies. The person:

(1) Has at any time during the calendar year property in this state with an aggregate value of at least fifty thousand dollars. For the purpose of division (I)(1) of this section, owned property is valued at original cost and rented property is valued at eight times the net annual rental charge.

(2) Has during the calendar year payroll in this state of at least fifty thousand dollars. Payroll in this state includes all of the following:

(a) Any amount subject to withholding by the person under section 5747.06 of the Revised Code;

(b) Any other amount the person pays as compensation to an individual under the supervision or control of the person for work done in this state; and

(c) Any amount the person pays for services performed in this state on its behalf by another.

(3) Has during the calendar year taxable gross receipts of at least five hundred thousand dollars.

(4) Has at any time during the calendar year within this state at least twenty-five per cent of the person's total property, total payroll, or total gross receipts.

(5) Is domiciled in this state as an individual or for corporate, commercial, or other business purposes.

(J) "Tangible personal property" has the same meaning as in section 5739.01 of the Revised Code.

(K) "Internal Revenue Code" means the Internal Revenue Code of 1986, 100 Stat. 2085, 26 U.S.C. 1, as amended. Any term used in this chapter that is not otherwise defined has the same meaning as when used in a comparable context in the laws of the United States relating to federal income taxes unless a different meaning is clearly required. Any reference in this chapter to the Internal Revenue Code includes other laws of the United States relating to federal income taxes.

(L) "Calendar quarter" means a three-month period ending on the thirty-first day of March, the thirtieth day of June, the thirtieth day of September, or the thirty-first day of December.

(M) "Tax period" means the calendar quarter or calendar year on the basis of which a taxpayer is required to pay the tax imposed under this chapter.

(N) "Calendar year taxpayer" means a taxpayer for which the tax period is a calendar year.

(O) "Calendar quarter taxpayer" means a taxpayer for which the tax period is a calendar quarter.

(P) "Agent" means a person authorized by another person to act on its behalf to undertake a transaction for the other, including any of the following:

(1) A person receiving a fee to sell financial instruments;

(2) A person retaining only a commission from a transaction with the other proceeds from the transaction being remitted to another person;

(3) A person issuing licenses and permits under section 1533.13 of the Revised Code;

(4) A lottery sales agent holding a valid license issued under section 3770.05 of the Revised Code;

(5) A person acting as an agent of the division of liquor control under section 4301.17 of the Revised Code.

(Q) "Received" includes amounts accrued under the accrual method of accounting.

(R) "Reporting person" means a person in a consolidated elected taxpayer or combined taxpayer group that is designated by that group to legally bind the group for all filings and tax liabilities and to receive all legal notices with respect to matters under this chapter, or, for the purposes of section 5751.04 of the Revised Code, a separate taxpayer that is not a member of such a group.

Amended by 130th General Assembly File No. TBD, HB 492, §1, eff. 9/17/2014.

Amended by 130th General Assembly File No. 41, HB 72, §3, eff. 1/30/2014.

Amended by 130th General Assembly File No. 25, HB 59, §101.01, eff. 9/29/2013 and 7/1/2014.

Amended by 130th General Assembly File No. 7, HB 51, §101.01, eff. 7/1/2013.

Amended by 130th General Assembly File No. 2, SB 28, §1, eff. 3/22/2013.

Amended by 129th General AssemblyFile No.186, HB 510, §1, eff. 3/27/2013, applicable to tax periods beginning on or after January 1, 2014 except for a taxpayer that is a corporation or any other person directly or indirectly owned by one or more insurance companies subject to the tax imposed by section 5725.18 or Chapter 5729. of the Revised Code; for such taxpayers, the amendment applies to tax periods beginning on or after January 1, 2013.

Amended by 129th General AssemblyFile No.188, HB 472, §1, eff. 12/20/2012.

Amended by 129th General AssemblyFile No.125, SB 315, §101.01, eff. 9/10/2012.

Amended by 129th General AssemblyFile No.117, HB 508, §1, eff. 9/6/2012.

Amended by 129th General AssemblyFile No.28, HB 153, §101.01, eff. 9/29/2011.

Amended by 129th General AssemblyFile No.44, HB 277, §1, eff. 10/17/2011.

Amended by 129th General AssemblyFile No.7, HB 114, §101.01, eff. 6/29/2011.

Amended by 128th General AssemblyFile No.9, HB 1, §101.01, eff. 10/16/2009.

Effective Date: 06-30-2005; 03-30-2006; 2006 HB699 03-29-2007

Related Legislative Provision: *See 130th General Assembly File No. TBD, HB 492, §4.*

See 130th General Assembly File No. 41, HB 72, §3.

See 130th General Assembly File No. 25, HB 59, §803.90.

See 129th General AssemblyFile No.186, HB 510, §5

See 129th General AssemblyFile No.186, HB 510, §4

5751.02 Commercial activity tax levied on taxable gross receipts.

(A) For the purpose of funding the needs of this state and its local governments , there is hereby levied a commercial activity tax on each person with taxable gross receipts for the privilege of doing business in this state. For the purposes of this chapter, "doing business" means engaging in any activity, whether legal or illegal, that is conducted for, or results in, gain, profit, or income, at any time during a calendar year. Persons on which the commercial activity tax is levied include, but are not limited to, persons with substantial nexus with this state. The tax imposed under this section is not a transactional tax and is not subject to Public Law No. 86-272, 73 Stat. 555. The tax imposed under this section is in addition to any other taxes or fees imposed under the Revised Code. The tax levied under this section is imposed on the person receiving the gross receipts and is not a tax imposed directly on a purchaser. The tax imposed by this section is an annual privilege tax for the calendar year that, in the case of calendar year taxpayers, is the annual tax period and, in the case of calendar quarter taxpayers, contains all quarterly tax periods in the calendar year. A taxpayer is subject to the annual privilege tax for doing business during any portion of such calendar year.

(B) The tax imposed by this section is a tax on the taxpayer and shall not be billed or invoiced to another person. Even if the tax or any portion thereof is billed or invoiced and separately stated, such amounts remain part of the price for purposes of the sales and use taxes levied under Chapters 5739. and 5741. of the Revised Code. Nothing in division (B) of this section prohibits:

(1) A person from including in the price charged for a good or service an amount sufficient to recover the tax imposed by this section; or

(2) A lessor from including an amount sufficient to recover the tax imposed by this section in a lease payment charged, or from including such an amount on a billing or invoice pursuant to the terms of a written lease agreement providing for the recovery of the lessor's tax costs. The recovery of such costs shall be based on an estimate of the total tax cost of the lessor during the tax period, as the tax liability of the lessor cannot be calculated until the end of that period.

Amended by 130th General Assembly File No. 25, HB 59, §101.01, eff. 7/1/2014.

Amended by 130th General Assembly File No. 7, HB 51, §101.01, eff. 7/1/2013.

Amended by 128th General AssemblyFile No.9, HB 1, §101.01, eff. 10/16/2009.

Effective Date: 06-30-2005

Related Legislative Provision: *See 130th General Assembly File No. 25, HB 59, §803.90.*

See 130th General Assembly File No. 7, HB 51, §812.20.20.

See 129th General AssemblyFile No.186, HB 510, §5

See 128th General AssemblyFile No.9, HB 1, §803.70.

5751.033 Situsing of gross receipts to Ohio.

For the purposes of this chapter, gross receipts shall be sitused to this state as follows:

(A) Gross rents and royalties from real property located in this state shall be sitused to this state.

(B) Gross rents and royalties from tangible personal property shall be sitused to this state to the extent the tangible personal property is located or used in this state.

(C) Gross receipts from the sale of electricity and electric transmission and distribution services shall be sitused to this state in the manner provided under section 5733.059 of the Revised Code.

(D) Gross receipts from the sale of real property located in this state shall be sitused to this state.

(E) Gross receipts from the sale of tangible personal property shall be sitused to this state if the property is received in this state by the purchaser. In the case of delivery of tangible personal property by motor carrier or by other means of transportation, the place at which such property is ultimately received after all transportation has been completed shall be considered the place where the purchaser receives the property. For purposes of this section, the phrase "delivery of tangible personal property by motor carrier or by other means of transportation" includes the situation in which a purchaser accepts the property in this state and then transports the property directly or by other means to a location outside this state. Direct delivery in this state, other than for purposes of transportation, to a person or firm designated by a purchaser constitutes delivery to the purchaser in this state, and direct delivery outside this state to a person or firm designated by a purchaser does not constitute delivery to the purchaser in this state, regardless of where title passes or other conditions of sale.

(F) Gross receipts from the sale, exchange, disposition, or other grant of the right to use trademarks, trade names, patents, copyrights, and similar intellectual property shall be sitused to this state to the extent that the receipts are based on the amount of use of the property in this state. If the receipts are not based on the amount of use of the property, but rather on the right to use the property, and the payor has the right to use the property in this state, then the receipts from the sale, exchange, disposition, or other grant of the right to use such property shall be sitused to this state to the extent the receipts are based on the right to use the property in this state.

(G) Gross receipts from the sale of transportation services by a motor carrier shall be sitused to this state in proportion to the mileage traveled by the carrier during the tax period on roadways, waterways, airways, and railways in this state to the mileage traveled by the carrier during the tax period on roadways, waterways, airways, and railways everywhere. With prior written approval of the tax commissioner, a motor carrier may use an alternative situsing procedure for transportation services.

(H) Gross receipts from dividends, interest, and other sources of income from financial instruments described in divisions (F)(4), (5), (6), (7), (8), (9), (10), (11), and (13) of section 5733.056 of the Revised Code shall be sitused to this state in accordance with the situsing provisions set forth in those divisions. When applying the provisions of divisions (F)(6), (8), and (13) of section 5733.056 of the Revised Code, "gross receipts" shall be substituted for "net gains" wherever "net gains" appears in those divisions. Nothing in this division limits or modifies the exclusions enumerated in divisions (E) and (F)(2) of section 5751.01 of the Revised Code. The tax commissioner may promulgate rules to further specify the manner in which to situs gross receipts subject to this division.

(I) Gross receipts from the sale of all other services, and all other gross receipts not otherwise sitused

under this section, shall be sitused to this state in the proportion that the purchaser's benefit in this state with respect to what was purchased bears to the purchaser's benefit everywhere with respect to what was purchased. The physical location where the purchaser ultimately uses or receives the benefit of what was purchased shall be paramount in determining the proportion of the benefit in this state to the benefit everywhere. If a taxpayer's records do not allow the taxpayer to determine that location, the taxpayer may use an alternative method to situs gross receipts under this division if the alternative method is reasonable, is consistently and uniformly applied, and is supported by the taxpayer's records as the records exist when the service is provided or within a reasonable period of time thereafter.

(J) If the situsing provisions of divisions (A) to (H) of this section do not fairly represent the extent of a person's activity in this state, the person may request, or the tax commissioner may require or permit, an alternative method. Such request by a person must be made within the applicable statute of limitations set forth in this chapter.

(K) The tax commissioner may adopt rules to provide additional guidance to the application of this section, and provide alternative methods of situsing gross receipts that apply to all persons, or subset of persons, that are engaged in similar business or trade activities.

(L) As used in this section, "motor carrier" has the same meaning as in section 4923.01 of the Revised Code.

Amended by 129th General AssemblyFile No.127, HB 487, §101.01, eff. 6/11/2012.

Effective Date: 06-30-2005; 2006 HB699 03-29-2007

5751.31 Direct appeal on constitutional issues to supreme court.

Notwithstanding any section of law to the contrary, the tax commissioner may issue one or more final determinations under section 5703.60 of the Revised Code for which any appeal must be made directly to the supreme court within thirty days after the date the commissioner issued the determination if the primary issue raised by the petitioner is the constitutionality of division (H)(3) of section 5751.01 of the Revised Code or an issue arising under Section 3, 5a, or 13 of Article XII, Ohio Constitution. Such final determination shall clearly indicate that any appeal thereof must be made directly to the supreme court within the thirty-day period prescribed in this division.

Effective Date: 06-30-2005