In the Supreme Court of Ohio

MASON COMPANIES, INC.,	:	
	:	Case No. 15-0794
	:	
APPELLANT,	:	
	:	Appeal from the Ohio
v.	:	Board of Tax Appeals
	:	
JOSEPH W. TESTA,	:	
TAX COMMISSIONER OF OHIO,	:	
	:	BTA Case Nos. 2012-1169, 2012-2806
APPELLEE.	:	

BRIEF OF AMICI CURIAE THE BUCKEYE INSTITUTE FOR PUBLIC POLICY SOLUTIONS, MACKINAC CENTER FOR PUBLIC POLICY, NETCHOICE, AND AMERICAN CATALOG MAILERS ASSOCIATION, INC. IN SUPPORT OF APPELLANT MASON COMPANIES, INC.

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STATEMENT OF THE FACTS

The Buckeye Institute for Public Policy Solutions, Mackinac Center for Public Policy, NetChoice, and American Catalog Mailers Association, Inc. (the "Amici") adopt by reference the statement of the case and facts set forth in the Merits Brief of Mason Companies, Inc. ("Appellant").

STATEMENTS OF INTEREST OF AMICI CURIAE

The Buckeye Institute for Public Policy Solutions (the "Buckeye Institute") was founded in 1989 as an independent research and educational institution – a think tank – to formulate and promote free-market solutions for Ohio's most pressing public policy problems. The staff at the Buckeye Institute accomplish the organization's mission by performing timely and reliable research on key issues, compiling and synthesizing data, formulating free-market policies, and marketing those public policy solutions for implementation in Ohio and replication across the country. The Buckeye Institute is located directly across from the Ohio Statehouse on Capitol Square in Columbus, where it assists legislative and executive branch policymakers by providing ideas, research, and data to enable the lawmakers' effectiveness in advocating free-market public policy solutions. The Buckeye Institute is a non-partisan, nonprofit, tax-exempt organization, as defined by I.R.C. § 501(c)(3). Accordingly, it relies upon support from individuals, corporations, and foundations that share a commitment to individual liberty, economic freedom, personal responsibility, and limited government. The Buckeye Institute does not seek or accept government funding.

Founded in 1987, the Mackinac Center for Public Policy (the "Mackinac Center") is a Michigan-based nonprofit, non-partisan research and educational institute that advances policies fostering free markets, limited government, personal responsibility, and respect for private property. The Mackinac Center assists policy makers, scholars, business people, the media, and the public by providing objective analysis of Michigan issues. The goal of all Mackinac Center reports, commentaries and educational programs is to equip citizens and other decision makers to better evaluate policy options. The instant case concerns the Mackinac Center because it has published extensive research on taxation policy.

NetChoice is a trade association of leading e-commerce and online companies promoting the value, convenience, and choice of Internet business models. Members of NetChoice include online commerce platforms that bring together sellers and buyers from different states and nations. NetChoice members have a number of sellers, customers and users located in Ohio. NetChoice has a critical interest in ensuring that businesses can bring claims against states in court, particularly where the Internet enables these businesses to engage in commerce across state borders.

American Catalog Mailers Association, Inc. ("ACMA") is a nonprofit corporation under the laws of the District of Columbia and has its principal place of business in Providence, Rhode Island. ACMA advocates in matters directly affecting the catalog business, including publishers, suppliers and vendors. Its membership includes both large and small marketers across the country, including several companies that have significant business operations in Ohio. Founded in 2007 in response to postal policy decisions with serious negative repercussions for the catalog industry, ACMA now focuses on any material policy or regulatory issue specific to catalog marketing.

Each of the Amici has an enduring interest in fostering free markets and protecting interstate commerce from being unduly and unfairly burdened by state and local entanglements. The Amici are concerned that upholding the Tax Commissioner of Ohio's assessments in this case would expose Ohio businesses doing interstate business to tax liability in other states and localities that may follow Ohio's lead and require businesses with no presence in the state to report gross receipts tax. Accordingly, the Amici intervene in this case and urge the Court to hold that the application of the Ohio commercial activity tax (the "CAT") to nonresident businesses with no physical connection to the state would violate the "substantial nexus" requirement of the Commerce Clause of the United States Constitution.

ARGUMENT

PROPOSITION OF LAW: THE IMPOSITION OF OHIO'S COMMERCIAL ACTIVITY TAX ON A NONRESIDENT WITH NO PHYSICAL PRESENCE IN THE STATE VIOLATES THE SUBSTANTIAL NEXUS REQUIREMENT OF THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION.

I. Introduction

In 1992, the U.S. Supreme Court issued its seminal decision in *Quill Corp. v. North Dakota*, wherein the Court held that the "substantial nexus" requirement of the Commerce Clause requires that a nonresident have a non-trivial physical presence in the state in order to be subjected to sales/use taxes. 504 U.S. 298, 112 S.Ct. 1904, 119 L.Ed.2d 91 (1992). Ever since, a national debate has played out in state courts as to whether a similar physical presence standard also applies to other kinds of state taxes. *Compare J.C. Penney Nat'l Bank v. Johnson*, 19 S.W.3d 831 (Tenn. Ct. App. 1999) (holding that a physical presence requirement applies to income taxes); *Griffith v. ConAgra Brands, Inc.*, 229 W.Va. 190, 728 S.E.2d 74 (2012) (holding that a trademark licensor with no physical presence in the state had no "significant economic presence" in the state); *AccuZIP, Inc. v. Dir., Div. of Taxation,* 25 N.J. Tax 158 (2009) (holding that a state may not tax income generated in the state from selling *tangible* personal property when it lacks a physical presence in the state); *with A&F Trademark, Inc. v. Tolson*, 167 N.C.

App. 150, 605 S.E.2d 187 (2004) (holding that a state may tax income generated from intangible property, even when it lacks a physical presence in the state); *Lanco, Inc. v. Div. of Taxation*, 188 N.J. 380, 908 A.2d 176 (2006) (*dist. by AccuZIP, 25 N.J. Tax 158)* (holding that a state may tax income generated from *intangible* property, even when it lacks a physical presence in the state); *Tax Commissioner. v. MBNA Am. Bank, N.A.*, 220 W.Va. 163, 640 S.E.2d 226 (2006) , *cert. denied*, *FIA Card Servs., N.A., f.k.a. MBNA Am. Bank, N.A. v. Tax Commissioner.*, 551 U.S. 1141, 127 S.Ct. 2997, 168 L.Ed.2d 719 (2007), *limited by ConAgra* (holding that no physical presence requirement applies to income taxes in certain factual circumstances).

In the instant case, the Ohio Supreme Court is being asked to weigh in on this national debate and address whether the imposition of Ohio's CAT (a privilege tax measured by gross receipts) on a nonresident with no physical presence in the state violates the substantial nexus requirement of the Commerce Clause. As set out more fully below, arguments that a physical presence nexus standard only applies to state sales/use taxes are not well founded. Such arguments are based on several faulty premises: (i) that indirect taxes like sales taxes, which merely impose a collection obligation on the seller for which the seller is compensated by the state, impose a greater actual burden on interstate commerce than state taxes imposed directly on a taxpayer, (ii) that changes in business and technology have somehow lessened the burden of direct state taxes on interstate commerce, (iii) that the *Quill* Court's refusal to address facts and circumstances not in controversy in that case (*i.e.*, non-sales taxes) creates a negative implication as to the applicability of a physical presence standard to gross receipts taxes, and (iv) that an "economic presence" standard of nexus is somehow different than the "minimum contacts" standard of the Due Process Clause. More specifically, the CAT imposes unique practical burdens on interstate commerce such that the abandonment of a physical presence standard by

Ohio and similarly situated states would impose an undue burden on interstate commerce, thereby frustrating the purpose of the Commerce Clause.

II. Ohio is imposing the CAT on Appellant based on a de facto economic nexus standard

Ohio law imposes a CAT measured by gross receipts for the privilege of doing business in Ohio. R.C. 5751.02(A). The CAT is imposed on "persons with substantial nexus with this state." *Id*. A nonresident is deemed to have "substantial nexus with this state" if, amongst other factors, such person "has a bright-line presence" in the state. R.C. 5751.01(H). A person has a "bright line presence" in the state if their property, payroll or taxable sales in the state during the calendar year exceed a certain threshold – the threshold being $500,000 in the case of taxable sales. R.C. 5751.01(I)(3). Taxable sales are defined to include sales of tangible personal property that are received by purchasers in the state. R.C. 5751.01(G); R.C. 5751.033(E).

Accordingly, a nonresident that has absolutely no physical presence in the state may nevertheless be subject to Ohio CAT under the "bright-line presence" standard if it makes sales of property to residents in the state exceeding $500,000 in a calendar year. This is precisely the situation in the instant case, where Appellant is a remote internet seller whose sole contact with the state is making sales of tangible personal property delivered by common carrier to residents of the state. Therefore, the CAT is being imposed on Appellant solely based on income derived by Appellant from state residents (*i.e*., an "economic nexus" standard similar to the one set out by the South Carolina Supreme Court in *Geoffrey, Inc. v. South Carolina Tax Comm.*, 313 S.C. 15, 437 S.E.2d 13 (1993), *cert. denied,* 510 U.S. 992, 114 S. Ct. 550, 126 L.Ed. 2d 451 (1993).

III. Evolution of the "substantial nexus" requirement of the Commerce Clause and its application to sales/use taxes

Prior to the ratification of the U.S. Constitution, states' power over commerce, "guided by inexperience and jealousy, began to show itself in iniquitous laws and impolitic measures * * *, destructive to the harmony of States, and fatal to their commercial interests abroad. This was the immediate cause that led to the forming of a convention." *Gibbons v. Ogden*, 22 U.S. 1, 224, 9 Wheat. 1, 6 L.Ed. 23 (1824). As a result, the U.S. Constitution expressly authorized Congress to "regulate commerce with foreign nations, and among the several states." U.S. Constitution, Article I, Section 8, cl. 3.

The U.S. Supreme Court has long interpreted this language as not only involving an affirmative grant of power to Congress, but also having a negative implication as to the states' ability to tax interstate commerce (the "dormant" Commerce Clause). *Quill*, 504 U.S. at 309. The U.S. Supreme Court's "dormant" Commerce Clause jurisprudence evolved substantially over the years, starting with the notion that interstate commerce enjoyed a complete immunity from state taxation. *Leloup v. Port of Mobile*, (1888) 127 U.S. 640, 648, 8 S.Ct. 1380, 32 L.Ed. 311 (1888); *Freeman v. Hewit*, 329 U.S. 249, 252-3, 67 S.Ct. 274 (1946). Over time, the scope of this immunity waxed and waned, eventually evolving into the "Spector rule" as formulated in *Spector Motor Services v. O'Conner*, which focused on whether the incidence of the tax was on interstate or intrastate activities. 340 U.S. 602, 71 S.Ct. 508 (1951). The U.S. Supreme Court's view of the dormant Commerce Clause reached its current formulation in *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 97 S.Ct. 1076 (1977).

In *Complete Auto Transit*, the U.S. Supreme Court rejected its prior formalistic approach to the taxation of interstate commerce based on whether the incidence of the tax was directly or indirectly on interstate commerce (which could turn on how a statute was worded versus its actual impact on interstate commerce). *See Complete Auto Transit,* 430 U.S. at 284 (comparing *Ry. Express Agency, Inc. v. Virginia*, 347 U.S. 359 (1954) (*Railway Express I*) and *Ry. Express Agency, Inc. v. Virginia*, 358 U.S. 434 (1959)(*Railway Express II*)). Instead, the Court adopted a more pragmatic approach that focused on the actual impact of the tax on interstate commerce. *Complete Auto Transit* at 278-280.

Under this approach, a state may tax interstate commerce so long as the tax meets the following four criteria: (i) the tax must apply to an activity with substantial nexus with the state; (ii) the tax must be fairly apportioned; (iii) the tax does not discriminate against interstate commerce; and (iv) the tax must be fairly related to the services provided by the taxing state. *Complete Auto Transit*, 430 U.S. 274.

Following its seminal decision in *Complete Auto Transit*, the U.S. Supreme Court was called upon to apply this new standard in another seminal decision, *Quill Corp. v. North Dakota*, 504 U.S. 298. In *Quill*, a nonresident was engaged in catalog sales to residents of North Dakota but had no other meaningful contact with the state. North Dakota attempted to impose a sales/use tax collection obligation on the seller. The seller argued that North Dakota could not impose a sales/use tax upon a nonresident under the Commerce and Due Process Clauses of the U.S. Constitution absent a physical presence by the seller in the state.

The seller's position relied upon a decision of the Court issued 25 years earlier in *National Bellas Hess, Inc. v. Dept. of Revenue of State of Ill.* 386 U.S. 753, 87 S.Ct. 1389 (1967). In *Bellas Hess*, the Court had held that imposing sales/use taxes on a nonresident without a physical presence in the state would burden interstate commerce in a morass of complicated local obligations. Further, the state had no legitimate claim to impose "a fair share of the cost of the local government" on such a taxpayer because the taxpayer did not share the same benefits provided by the state as a taxpayer physically present in the state. *Id*. at 759-60.

In ruling for the state in the lower court decision, the North Dakota Supreme Court had declined to follow *Bellas Hess* under the rationale that "tremendous social, economic, commercial and legal innovations" had rendered the physical presence test obsolete. *Quill* at 301. The *Quill* Court reversed the North Dakota Supreme Court and upheld the physical presence standard of *Bellas Hess*.

The Quill Court upheld the physical presence test of *Bellas Hess* under several rationales. First, the Court for the first time clearly distinguished between the "minimum contacts" standard for nexus under the Due Process Clause and the "substantial nexus" standard of the Commerce Clause. *Quill*, 504 U.S. at 305. Due Process concerns the "fundamental fairness" of a state government exercising power over a taxpayer, and the Court has identified "notice" and "fair warning" as the analytic touchstones of Due Process nexus. *Id.* at 312. Under a Due Process analysis, the Court has held that "if a foreign corporation *purposefully avails itself of the benefits of an economic market in the forum State,* it may subject itself to the State's *in personam* jurisdiction even if it has no physical presence in the State." (Emphasis Added) *Id.* at 307. Therefore, economic nexus may be sufficient to create nexus under the Due Process Clause.

By contrast, the Commerce Clause is concerned with "structural concerns about the effects of state regulation on the national economy." *Quill*, 504 U.S. at 312. Therefore, "the 'substantial nexus' requirement is not, like [the] due process' 'minimum contacts' requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce." *Id*. at 313. "There may be more than sufficient factual connections, with economic and legal effects, between the taxing state to sustain the tax as against due process objections. Yet it may fall because of its burdening effect upon the commerce." *Id.* at 305 (quoting *Internatl. Harvester Co. v. Dept. of Treasury*, 322 U.S. 340, 353. 64 S.Ct. 1019, 88 L.Ed. 1313 (1944). Accordingly, although deriving income from customers in a state might be sufficient, in certain circumstances, to satisfy the minimum contacts standard of Due Process, something more is required to satisfy the substantial nexus requirement of the Commerce Clause.

The Court next examined whether imposition of sales/use tax on a nonresident with no physical presence in the state unduly burdened interstate commerce. In *Bellas Hess*, the Court had held that it would be unfair to impose a share of the cost of local government upon a nonresident that did not benefit from such services to the same extent as a business physically located in the state. The Court was less concerned with the notion that some business activities would escape taxation than it was in preventing states from unduly burdening interstate commerce. "Undue burdens on interstate commerce may be avoided not only on a case-by-case evaluation of the actual burdens imposed by particular regulations or taxes, but also * * * by the demarcation of a discrete realm of commercial activity that is free from interstate taxation." *Quill*, 504 U.S. at 315. In reaffirming *Bellas Hess*, the *Quill* Court upheld this rationale as well.

Finally, the Court based its decision on the principle of stare decisis. The Court noted that an entire industry had grown up in reliance on its holding in *Bellas Hess* and that overturning its decision would upset settled expectations. *Quill*, 504 U.S. at 316. In upholding a bright-line rule requiring physical presence for sales and use taxes, the Court sought to encourage settled expectations, which "fosters investment by businesses and individuals." *Id.*

IV. The physical presence standard upheld by *Quill* for sales/use taxes should apply equally to the CAT

A. <u>The CAT imposes a greater practical burden on interstate commerce than sales/use taxes</u>.

As stated by the Court in *Complete Auto Transit*, modern Commerce Clause analysis is focused on the practical burdens imposed by a state tax on interstate commerce. *Complete Auto Transit*, 430 U.S. at 284. In contrast to sales tax laws, which impose an administrative duty upon a seller to collect sales taxes from a buyer and remit such taxes to the state, the CAT is imposed directly on the seller. As stated by the Court in *Quill*, state sales and use taxes impose a "purely administrative duty of collecting and remitting" such taxes. *Quill*, 504 U.S. at 304. Not only are sales taxes merely an administrative duty, the state effectively pays the seller to act as its collection agent through the mechanism of allowing the seller to "keep" a portion of the taxes its collects as "vendor's compensation." Accordingly, sales taxes are indirect taxes whereas gross receipts taxes are direct taxes and therefore impose a greater actual burden on interstate commerce.

Following *Quill*, several state courts have held that a physical presence standard does not exist for state income taxes, in certain circumstances. However, the CAT is distinguishable from such cases because it is a gross receipts tax, not an income tax. *See, e.g., Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 98 S.Ct. 2340, 57 L.Ed.2d 197 (1978) (noting that gross receipts taxes are "inherently more burdensome" than income taxes). Whereas a seller only has an income tax liability when it is profitable, a seller has a tax liability under a gross receipts tax even if the company is losing money. Further, state income tax liability in one year may be offset by losses in another year by the carry forward or carry-back of net operating losses. In contrast, no such income-smoothing mechanism exists for gross receipts tax purposes. The seller is taxable no matter its profits or losses from one year to another.

Additionally, most state income taxes are apportioned to the state using a three factor formula comprised of some combination of the taxpayer's property, payroll and gross receipts in the state over its property, payroll and gross receipts everywhere. *See, e.g.*, Tenn. Code Ann. 67-4-2012. Under a multifactor apportionment formula, a nonresident with no physical presence in the state obtains some relief by having less of its income apportioned to the state. In contrast, the CAT is sitused based on gross receipts alone. This has the effect of burdening taxpayers who have directed no activity into the state at a disproportionate rate compared to taxpayers with a significant physical presence in the state. Although the Supreme Court has upheld the sourcing of income by a single-sales factor as not violating the external consistency requirement of the fair apportionment test of the Commerce Clause, it has never done so in the case where a taxpayer had no physical presence in the State. *See*, *Moorman,* 437 U.S. 267 (Brennan, J., Blackmun, J., and Powell, J., dissenting). In *Moorman,* which upheld an income tax apportioned by a single-sales factor on an out-of-state taxpayer with a physical presence in the State, the dissent admonished that "it is the commercial activity within the State, and not the sales volume, which determines the State's power to tax, and by which the tax must be apportioned." *Id.* at 281.

Furthermore, the CAT, as applied to out-of-state taxpayers with no physical presence in Ohio, shifts the burden of the tax to remote sellers like Appellant who, compared to resident brick and mortar taxpayers, do not receive the same protections and benefits offered by Ohio (*e.g.,* public education, fire and police protection, health and welfare benefits, state roads and other infrastructure) yet pay a disproportionate share of taxes compared to resident taxpayers. *See, e.g., Comptroller of the Treasury of Maryland v. Wynne,* ___ U.S. ___, 135 S.Ct. 1787, 1797, 191 L.Ed.2d 813 (2015). States have many incentives to create a competitive advantage for in-state taxpayers to the detriment of out-of-state taxpayers with no political representation in the state. The ability to shift the cost of government services to out-of-state taxpayers provides state legislators with a valuable political tool. As a check on this, the purpose of the Commerce Clause is to ensure a national economy free from undue state and local meddling.

For the foregoing reasons, the CAT is significantly more burdensome on interstate commerce than state sales/use or income taxes. Accordingly, there is an even greater need for a physical presence standard to be upheld for the CAT.

B. Although there have been significant economic, cultural, and technological changes since *Quill*, the burden imposed by gross receipts taxes on interstate commerce has not changed.

The dawn of e-commerce and its implications for state taxation echoes the situation in the 1980's and 1990's, when the mail order and catalog businesses experienced exponential growth. Partially owing to the limitations on state taxation outlined in *Quill*, businesses of all sizes, including small vendors, with geographically dispersed clientele have been able to compete and grow. The *Quill* Court found the argument for economic nexus unpersuasive then and would find it so now. The U.S. Supreme Court emphasized that the overarching concern was not that some transactions and taxpayers would escape taxation, but that states could not unduly burden interstate commerce.

Indeed, most of the state taxes that have been upheld at the state level against taxpayers with no physical presence have involved intangible holding companies, which are often viewed as special-purpose entities specifically designed to avoid state tax. *Compare A&F Trademark,* 167 N.C. App. 150 (holding that a state may tax income generated from intangible property, even when it lacks a physical presence in the state); *Lanco,* 188 N.J. 380 (holding that a state may tax income generated from *intangible* property, even when it lacks a physical presence in the state); with *AccuZIP,* 25 N.J. Tax 158 (holding that a state may not tax income generated in the state from selling *tangible* personal property when it lacks a physical presence in the state).

Of these cases, the only one that is factually similar to the instant case is *AccuZIP*, in which a state corporation business tax was struck down as applied to an out-of-state seller of tangible personal property with no physical presence in the state.

The West Virginia Supreme Court in *MBNA* took arguments for economic nexus to the extreme, suggesting that the Commerce Clause itself was obsolete: "The Framers' concept of commerce consisted of goods transported in horse-drawn, wooden-wheeled wagons or ships with sails. They lived in a world with no electricity, no indoor plumbing, * * * no iPods." *MBNA*, 220 W.Va. 163, 173, 640 S.E. 2d 226, 236 (Benjamin, J., dissenting). The *MBNA* court upheld corporate net income and business franchise taxes as applied to a credit card issuer on the basis of the presence of its customers in the state. The court strained to find justification for its finding of substantial nexus and offered no analysis of the effect of the taxes on interstate commerce as required under *Complete Auto Transit.* The dissent in *MBNA* offered a scathing rebuke of the decision, stating that "[t]here is no precedential support whatsoever for the conclusions reached by the majority decision. None. None at the state level. None at the federal level." *Id.* at 174. This decision has been not only roundly criticized but was also severely limited in a subsequent decision before the same court. *See ConAgra Brands*, 229 W.Va. 190 (Benjamin, J. concurring). Indeed, these cases are difficult to reconcile, and the concurrence suggested that *MBNA*, a decision from which he dissented, should be completely overruled.

Furthermore, each time the U.S. Supreme Court has reevaluated the concept of "substantial nexus," it has reaffirmed its holding that states cannot unduly burden interstate commerce and it has refused to uphold a tax in the absence of a physical presence by the taxpayer in the taxing state. Although some constitutional principles must be reexamined over time to apply them to new circumstances, the tenet that parochial state interests cannot burden interstate commerce remains a principle rooted in the creation of the Constitutional Convention.

Advocates for economic nexus have recognized its inherent problems by outlining model schemes with mitigating factors (*e.g.*, *de minimus* exceptions, simplified rates, uniform bases); nevertheless, the imposition of such factors are beyond the scope of judicial power. Unless Congress enacts national rules governing the taxation of interstate commerce, a requirement of physical presence is the governing rule for "substantial nexus" under the Commerce Clause.

C. The *Quill* Court's refusal to address whether a physical presence standard applies to non-sales taxes did not create a negative inference as to the applicability of this standard to such taxes.

Proponents of an economic nexus standard for non-sales taxes rely on the fact that the *Quill* Court did not explicitly apply the physical presence standard to other kinds of taxes. *See, MBNA,* 229 W. Va. at 169. Reliance on this omission is misplaced. The U.S. Supreme Court did not specifically address income or gross receipts taxes in *Quill* for a very simple reason: those facts and issues were not before the Court. As recently affirmed in the U.S. Supreme Court's holding in *Wynne,* the same Commerce Clause analysis should be applied to all state taxes. *Wynne*, 135 S.Ct. at 1795 (quoting *Complete Auto Transit*, 430 U.S. at 279)("[W]e must consider 'not the formal language of the tax statute but rather its practical effect.'").

Although the *Quill* Court did not directly address non-sales taxes, the U.S. Supreme Court did cite with approval a gross receipts tax case (*Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue*, (1987) 483 U.S. 232, 107 S.Ct. 2810, 97 L.Ed.2d 199 (1987) wherein the Court upheld a Commerce Clause nexus standard based on the performance of "activities within the state" that allow a nonresident to create or maintain a market in the state. *Quill,* 504 U.S. at 305. Further, the fact remains that the U.S. Supreme Court has NEVER upheld a gross receipts tax on a taxpayer without a physical presence in the taxing state. S*ee, Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 626, 101 S.Ct. 2946, 69 L.Ed. 884 (1981) ("the interstate business must have a substantial nexus with the State before *any* tax may be levied on 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); *General Motors Corp. v. Washington*, 377 U.S. 436, 447-48, 84 S.Ct. 1564, 12 L.Ed.2d 430 (1964), overruled, in part, on other grounds, *Tyler Pipe Industries, Inc. v. Washington State Dep't of Revenue*, 483 U.S. 232 (1987) (taxpayer's in-state activities were "decisive factors in establishing and holding the market"); *Field Ent., 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.Ed2d 39 (1956) (tax upheld based on the presence of a manager, employees and salespeople in the state). In its landmark decision in *Tyler Pipe*, the U.S. Supreme Court struck down a state business privilege tax measured by gross receipts. The crux of the Court's holding was 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 sales." (Emphasis added) 483 U.S. 232, 250-251.

Accordingly, in the context of non-sales taxes, the Supreme Court has repeatedly required a taxpayer's physical presence in the state before upholding a tax. As was the case in *Quill*, there has been significant reliance by businesses engaged in remote sales over the internet on these decisions. It would therefore disturb settled expectations to hold that no in-state activity/physical presence is required for a state to impose for gross receipts taxes on a nonresident.

Appellee also alleges that the Ohio Supreme Court has already upheld an "economic presence" standard for income taxes. *Couchot v. State Lottery Comm*. 74 Ohio St.3d 417, 659 N.E. 1125 (1996). Reliance on this case as authority in the instant case is also misplaced. First, although this court stated that there was "no indication" that the Supreme Court will extend the physical presence requirement of *Quill* to income-based taxes, this statement was dictum. *Id.* at 425. Such a determination was unnecessary to the disposition of the case because the taxpayers did, in fact, have a physical presence in the state. *Id.* In *Couchot*, non-Ohio residents came into the state to purchase lottery tickets, won the lottery, and re-entered the state to redeem the winning ticket. In upholding the withholding of Ohio personal income tax on the taxpayers' winnings, the court relied on the fact that the "entire income received by Couchot * * * is directly related to his physical presence in Ohio." *Id.* This conclusion obviated the need for a determination of whether a physical presence was necessary to subject Couchot to tax.

Couchot is further distinguishable from the instant case because the taxpayers in that case had multiple direct connections to the State. The Ohio Lottery is an event exclusively within the power, dominion, and control of Ohio. *Couchot* at 422, *see,* R.C. Chapter 3770 (as such sections were numbered in 1996). As this Court noted:

> It is operated by Ohio's State Lottery Commission and subject to Ohio regulation. The benefits, protections, and opportunities afforded by Ohio in this regard are undeniable. Only Ohio can provide for the existence of its lottery, and only Ohio can provide for and enforce the mechanisms for its operation. Also, the maintenance of the State Lottery Commission and the vast machinery employed, literally and figuratively, by the state in the operation of the lottery * * * are but part of the social and governmental costs incurred by Ohio in generating the income of which Couchot is the fortunate beneficiary. Certainly, the state of Ohio has given something for which it can ask return.

Couchot, 74 Ohio St.3d at 422. Indeed, Couchot not only did not suffer an undue burden from taxation by the State, he derived his income directly from an agency of the State that sought to tax him.

By contrast, the taxpayers in the instant case derived their income from individuals and businesses all over the country through sales conducted over the Internet. They had no offices, warehouses, sales agents, or even servers in Ohio. They derived no benefits from Ohio comparable to the ones received by *Couchot*. Accordingly, *Couchot* is factually distinguishable from the instant case in many critical ways – the most crucial being an absolute lack of physical presence in Ohio.

D. The adoption of an economic nexus standard is tantamount to adopting a minimum contacts standard under the Due Process Clause, a position expressly rejected by *Quill*.

The U.S. Supreme Court's requirement of a discrete analysis of Due Process nexus and Commerce Clause nexus applies to ALL taxes. As explained above, the Due Process Clause and the Commerce Clause serve different interests, and the Commerce Clause test for "substantial nexus" is more stringent than the Due Process Clause test for minimum contacts. Under the Due Process clause, the U.S. Supreme Court has held that "if a foreign corporation *purposefully avails itself of the benefits of an economic market in the forum State*, it may subject itself to the State's *in personam* jurisdiction even if it has no physical presence in the State." (Emphasis added) *Quill*, 504 U.S. at 307. When Ohio seeks to impose the CAT on a taxpayer with no physical presence in the state solely on the basis of deriving a certain amount of economic benefits from the state (a minimum of $500,000 in gross receipts), this smacks of a minimum contact standard of nexus – something the *Quill* Court explicitly rejected as being sufficient for substantial nexus under the Commerce Clause.

Rather than straining to carve out non-sales taxes from the holding of *Quill,* state courts would be better served by heeding the caution of Justice Scalia (joined in by Justices Kennedy and Thomas) in his concurrence in that case:

> If a precedent of this Court has direct application in a case, yet appears to rest on reasons rejected in some other line of decisions, [they] should follow the case which directly controls, leaving to this Court the prerogative of overruling its own decisions.

Quill, 504 U.S. at 321 (quoting *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477, 484, 109 S.Ct. 1917, 1921, 104 L.Ed.2d 256 (1989).

CONCLUSION

For the foregoing reasons, the Amici respectfully request this Court to reverse the decision of the Ohio Board of Tax Appeals.

Respectfully submitted,

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CERTIFICATE OF SERVICE

This is to certify that a true copy of the foregoing Brief of Amici Curiae The Buckeye Institute for Public Policy Solutions, Mackinac Center for Public Policy, NetChoice, and American Catalog Mailers Association, Inc. in Support of Appellant Mason Companies, Inc. was served by U.S. and electronic mail to counsel of record for Appellant Mason Companies, Inc., David W. Bertoni, 184 Main Street, P.O. Box 3070, Lewiston, ME 04243-3070, and Edward J. Bernert, Capitol Square, Suite 2100, 65 East State Street, Columbus, OH 43215-4260, and 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.

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