ALABAMA DEPARTMENT OF REVENUE
REVENUE RULING 03-001

This document may not be used or cited as precedent. Code of Alabama 1975, §40-2A-5(a).

TO:

FROM: Dwight Carlisle
Commissioner of Revenue

DATE: August 4, 2003

FACTS

For purposes of this ruling, the requestor informed us and we have assumed without investigation that:

1. The requestor, Requestor, Inc, is a Delaware corporation.

2. Requestor, Inc. asserts that it has a mail order catalog business, which is conducted through a foreign state limited partnership, Catalog L.P. Mail order sales are made by the Catalog L.P. to Alabama residents by catalog solicitation and delivered to their customers in Alabama through the use of common carriers and the United States Postal Service.

3. Requestor, Inc. also asserts that it conducts a retail business through a separate entity, which is a foreign state limited liability company, Retail L.L.C. The Retail L.L.C. operates stores in foreign states A, B, C, D, E, F, G, H, I and J and is exploring the opportunity of opening a retail store in Alabama.

4. Requestor, Inc. asserts that it owns through various entities, both Catalog L.P. and Retail L.L.C.

REQUESTED REVENUE RULING

Requestor, Inc. requests a ruling that the conduct of a retail business in Alabama by Retail L.L.C. will not create nexus (commerce clause nexus) upon Catalog L.P. for sales/use tax withholding liability merely because both entities are owned by Requestor, Inc.

GENERAL DISCUSSION

The sale or use of tangible personal property in Alabama subjects the purchaser to Alabama's sales or use tax. As both Catalog L.P. and Retail L.L.C. are making retail sales in Alabama, the Alabama customers in these transactions have a tax burden to pay either sales or use taxes on these transactions, depending on circumstances not here important. While the tax burden is imposed on the retail consumer, Alabama law requires the entity making the sale to collect this tax from its customer under most circumstances and remit these tax collections to the appropriate taxing authorities within Alabama. These laws, while quite broad, are limited in application by the United States Constitution as the courts interpret this document from time to time to restrict a state, such as Alabama, in imposing an affirmative duty on interstate retailers to collect its sales and use tax.

The primary constitutional restriction important to this discussion is what is usually called the "dormant commerce clause". The United States Supreme Court has interpreted the authority that the U.S. Constitution grants to Congress to "regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes"[1] as limiting the taxing powers of the states, even in the absence of affirmative action by Congress. The Supreme Court's interpretation of this clause has evolved over many years.

In *Nat. Bellas Hess v. Dept. of Revenue*, 386 U.S. 753 (1967) and then in *Quill Corp. v. North Dakota By and Through Heitkamp*, 112 S.Ct. 1904 (1992), the United States Supreme Court determined that the dormant commerce clause of the United States Constitution precludes imposition of sales and use tax collection responsibilities upon an out-of-state mail-order firm whose only connection with customers of the taxing state is by common carrier or by United States mail. Most specifically, in *Quill*, the Court held that (1) mail-order businesses do not have to have a physical presence in the state in order to permit the state, consistent with the due process clause, to require it to collect use tax from its in-state customers, but (2) physical presence in the state is required for a business to have a "substantial nexus" with the taxing state, as required by the commerce clause. The "substantial nexus" language was taken from the Supreme Court's earlier decision in *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977), which required that the tax be applied to an activity with a substantial nexus with the taxing state. Thus, mail-order sellers with no retail outlets, solicitors or other types of property within the state are lacking a "substantial nexus" with the state and would not currently be subject to the Alabama requirements to collect sales or use tax on retail sales of tangible personal property purchased or used in Alabama.

---

[1] U.S. Const. Art. I, §8, cl.3.

It is conceded by the requestor that Retail L.L.C. would have a "substantial nexus" with Alabama based on its "physical presence" through the retail outlet. This entity would have to collect sales and use tax on all of its sales. Considered alone, Catalog L.P. would not appear to have a substantial nexus with Alabama and the catalog sales of tangible personal property at retail in Alabama would not subject Catalog L.P. to liability for failing to collect and remit sales and use tax on its Alabama sales. (Of course, the Alabama purchasers would still be liable for paying use tax on these transactions directly to Alabama.) The question of the requestor is whether or not a holding company owning one subsidiary in Alabama with "substantial nexus" necessarily creates "substantial nexus" on another distinct subsidiary of the holding company that would not otherwise be subject to collecting this tax. Stated differently, the question presented is whether or not the nexus of Retail LLC can be "transferred" to Catalog LP because they are owned by the same entity.

The Taxpayer cites *Current, Inc. v. State Board of Equalization*, 24 Cal. App. 4th 382 (1994), and other cases for the proposition that "where companies operate as separate and distinct entities, they will be treated (for sales/use tax collection liability purposes) as separate entities even though they may be owned by a common parent company." We read these cases to more precisely stand for the proposition that where two entities with a common parent do not have any integrated operations or management, are each organized and operated as separate and distinct corporate entities and neither being the alter ego, nominee or agent of the other for any purpose, they will be analyzed separately for dormant commerce clause nexus purposes. Merely having and operating separate legal entities is not enough to prevent Catalog LP from having nexus in this situation. If the two entities are conducting essentially the same business operation, offering essentially the same items for sale, using the same marketing or using the same trade name, the Commissioner will consider the actual facts presented by the situation and will make a determination of whether or not the two or more entities will be treated as one taxpayer for proper administration of Alabama's tax laws.

We note that this request essentially asks the Commissioner to state his current position on how the United States Constitution is interpreted by him for tax administration purposes. While we state this as our current position, this position could easily change as courts address this issue in the future. Many things that may influence further legislation and judicial interpretations are beginning to develop such as the various states adoption of some form of the Streamlined Sales and Use Tax Agreement from the Streamlined Sales Tax Project. Another important recent development is the passage of Act 2003-390, which is attached. Under this Act, if you choose to operate a retail entity in Alabama that is closely connected in its business operations[2] to another entity that has an economic presence in Alabama (such as the requestor's catalog company) both entities through their related ownership have consented to substantial nexus with Alabama (for the collection of sales or use taxes) even though such nexus might not otherwise exist for the out-of-state vendor alone. This remote entity nexus statute is a legislative application of already existing Alabama common law

[2] The Act uses terms including but not limited to the two entities use of "identical or substantially similar name, tradename, trademark, or goodwill, to develop, promote, or maintain sales."

remedies such as alter ego, nominee and piercing the corporate veil concepts that are within the Department's powers to prove substantial nexus with Alabama. Although the request does not address the use of this Act or common law applications to achieve substantial nexus, it appears that these remedies have direct application to the business relationship contemplated by the requestor. We suggest that the requestor review this Act in detail. It is the intent of the Commissioner in this ruling to state that Alabama will always enforce its sales and use tax laws to the fullest extent possible, limited only by legal restrictions or requirements as determined from time to time.

CONCLUSION

The Commissioner of the Department of Revenue grants the requested ruling on the limited question presented. Under current interpretations of law, if Retail L.L.C. and Catalog L.P. operate as completely separate and distinct businesses and meet all conditions detailed above, they will be treated (for sales/use tax collection liability purposes) as separate entities even though they are owned by a common parent company. However, merely having the entities formed as distinct legal entities will not ensure this treatment as outlined above.

_____

Dwight Carlisle
Commissioner of Revenue