WALMART.COM:
A CASE STUDY IN ENTITY ISOLATION

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INTRODUCTION

[2] As a result of constitutional concerns surrounding the imposition of burdens on interstate commerce, local and state governments are generally prevented from forcing out-of-state retailers to charge and collect sales and use taxes unless these retailers maintain a physical presence within the taxing state./1/ It is estimated that local and state governments are currently losing billions of dollars in revenues each year due to their inability to tax many remote consumer sales./2/ While this revenue loss is still a relatively small piece of the overall state and local revenue pie, the advent of the Internet and an increase in remote sales activity suggests that the loss may one day become significant./3/

[3] Further, the physical presence requirement has led to a tax-planning strategy that contributes to the growing revenue loss. Employing so-called "entity isolation" strategies, retailers sometimes incorporate a separate affiliate company in order to shelter this company from sales and use tax collection obligations that are imposed in states where the parent corporation maintains a physical presence./4/ In particular, large retailers with traditional retail outlets throughout the United States have an incentive to incorporate an affiliate for their online retail operations in order to level the playing field with pure online retailers who do not have use tax collection obligations outside of the state where they are physically based.

[4] This report discusses how Wal-Mart Stores Inc., the largest retailer in the world with annual sales exceeding $ 121 billion,/5/ has attempted to ensure that its online subsidiary, Walmart.com, does not have to charge and collect sales or use taxes on electronic-commerce transactions in many circumstances. Part 1 sets out the case study of Walmart.com's entity isolation strategy by reviewing publicly available information, including SEC filings, press releases, and Web site disclosures. The case study suggests that Walmart.com may be acting as the retail agent of its parent company or that the two companies are operationally tied to each other in significant ways. Part 2 briefly discusses how state tax authorities and courts could employ so-called "attributional nexus theory" to combat entity isolation strategies employed by companies such as Wal-Mart Stores Inc. Part 3 discusses how, in order to reduce sales tax base erosion in the longer term it is likely necessary to replace physical presence requirements with economic presence tests such as the one contemplated by the Streamlined Sales Tax Project, which permit states to impose collection obligations on remote retailers. This part also discusses the importance of assuaging tax compliance concerns to help convince Congress that interstate commerce will not be unduly harmed if states are permitted to extend their tax jurisdiction over remote vendors.

1. WALMART.COM CASE STUDY

1.1. ENTITY ISOLATION AND THE DOCTRINE OF CORPORATE SEPARATENESS

[5] In January 2000, Wal-Mart Stores Inc. announced that the company intended to create, in partnership with a venture capital firm, a corporate affiliate called Walmart.com Inc. (operating under the business name Walmart.com) to be headquartered in the San Francisco Bay area./6/ At its Web site, Walmart.com is described as an "independent company,"/7/ although the same Web site indicates that Wal-Mart Stores Inc. is the majority owner of the corporation that operates under the business name Walmart.com./8/

[6] Wal-Mart Stores Inc. maintains "more than 3,000 stores and offices across the United States."/9/ The question that remains is whether Walmart.com can, under current constitutional principles, be forced to charge and collect sales taxes on sales to jurisdictions where Wal-Mart Stores Inc. maintains physical outlets.

[7] In response to an e-mail inquiry from the author, Walmart.com maintained that the law only compels Walmart.com to collect sales taxes from residents of states where Walmart.com maintains a physical presence./10/ In other words, Walmart.com maintains that the company (or its parent company) does not have to collect sales taxes on online transactions with consumers within states where Wal-Mart Stores Inc. alone maintains its traditional retail outlets.

[8] But has Walmart.com effectively shielded itself from the reach of state and local tax authorities? Wal-Mart Stores Inc. maintains that Walmart.com is an independent company, yet Wal-Mart Stores Inc. owns 100 percent of Walmart.com/11/ and additionally maintains a majority interest on Walmart.com's board of directors. Under general corporate governance principles, as articulated by Delaware corporate law where Wal-Mart Stores Inc. is incorporated, Wal-Mart Stores Inc. has de jure (legal) control over its online affiliate./12/ Nevertheless, courts have generally respected the doctrine of corporate separateness and have asserted that it is unconstitutional to force a corporate affiliate that does not maintain a physical presence within a state to collect sales taxes simply because the affiliate's parent company maintains a physical presence within the state./13/

[9] Other courts, however, have attacked entity isolation strategies in the ground that, under so-called attributional nexus theory, there is sufficient nexus between two related companies to warrant the imposition of sales tax obligations on a company that lacks a physical presence within the taxing state./14/ For example, state courts have held that attribution nexus exists if the affiliate is acting as the agent of its corporate parent or is operationally tied in a significant way to the parent./15/ The Supreme Court has not yet considered whether entity isolation techniques pass constitutional muster./16/

1.2. IS WALMART.COM OPERATIONALLY INDEPENDENT FROM ITS PARENT?

[10] Do the two companies maintain operational independence? In its initial press release, Wal-Mart Stores Inc. indicated: "This new company is expected to greatly accelerate the development of Wal- Mart's Internet retail site, Walmart.com, and to further complement efforts to attract offline customers to the Internet via the trusted Wal-Mart brand."/17/ In other words, Wal-Mart Stores Inc. understandably wants to tap into its goodwill in order to enhance sales through Walmart.com. At least one court has scrutinized the mixing of brand names and other intellectual property but nevertheless let a corporate affiliate off the sales tax hook because there was insufficient evidence that the affiliate was operationally dependent on the parent company./18/

[11] On August 2, 2000, Wal-Mart Stores Inc. announced that it would build a distribution center in Georgia in order to house and ship products ordered by Walmart.com customers./19/ According to the press release, Wal-Mart Stores Inc. and Walmart.com entered into the distribution agreement in order for Walmart.com to "leverage years of logistical expertise and fully take advantage of the many efficiencies that allow Wal-Mart to pass tremendous savings on to customers."/20/

[12] Further, Walmart.com's Web site suggests that the two companies enjoy ties that benefit each other, including "excellent vendor relationships, highly efficient back-office systems, [and] an unswerving commitment to Sam Walton's 'Always low prices' philosophy."/21/ Wal-Mart Stores Inc. may argue that the parent deals with its online affiliate on an arm's length (that is, independent) basis. However, the public disclosures suggest that the two companies are combining their efforts to take advantage of operational synergies. Wal-Mart Stores Inc. is able to charge "always low prices" due at least in part to its vast supply network, where the company leverages its purchasing power in order to reduce the prices charged by suppliers. Further, a Walmart.com press release asserts that Wal-Mart Stores Inc. purchased the minority interest in Walmart.com owned by its venture capital partner in order to "establish the deepest integration possible between its online and offline programs."/22/

[13] A truly independent company would charge an arm's length price (that is, fair market value) to its affiliate that included a markup to take into account the increased profit margin to which Wal- Mart Stores Inc. should be entitled. Accordingly, Walmart.com should be charged the same price Wal-Mart Stores Inc. would charge to supply Target or another similarly situated retailer. If Wal-Mart Stores Inc. charged Walmart.com the price that Walmart.com would pay a truly independent supplier, however, then Walmart.com would presumably not be able to charge the "low prices" available at Wal-Mart Stores Inc.

1.3. IS WALMART.COM ACTING AS THE AGENT OF ITS PARENT?

[14] Does a dot.com affiliate of a so-called bricks-and-mortar (that is, a company with traditional retail offices) act as the agent or alter ego of its corporate parent? Walmart.com arguably acts like a retail arm or agent of Wal-Mart Stores Inc. and not like an independent retail outlet. For instance, the Wal-Mart Stores Inc. Web site does not support any retail activity, but acts as a corporate Web site for employees, suppliers, and investors./23/ In its 2001 Annual Report filed with the Securities and Exchange Commission, Wal-Mart Stores Inc. lists www.walmart.com as

its "Retail Internet Site." Further, the Annual Report indicates that Walmart.com "was formed in fiscal 2000 to further develop the Company's e-commerce initiative and [I]nternet business."/24/

[15] For federal securities disclosure purposes, Wal-Mart Stores Inc. did not disclose the amount of revenues generated by Walmart.com because sales generated by the dot.com affiliate are lumped together with the traditional Wal-Mart Stores discount stores and super-centers into one category called "Wal-Mart Stores,"/25/ making it impossible to estimate sales tax revenue losses, if any, resulting from the fact that Walmart.com does not charge and collect sales taxes outside of a few states. Sales from Walmart.com may not be material from a securities law perspective and, hence, are not required to be reported.

[16] Further, the Walmart.com Web site includes a number of statements that would suggest to a potential customer that the online affiliate and the parent company are one and the same (or at least acting on each other's behalf)./26/ For example, the Walmart.com Web page contains a "Store Finder" service where Web site visitors can enter their ZIP codes in order to find the closest Wal-Mart store./27/

[17] In its Web site privacy disclosure, the company defines the term "we" to be Wal-Mart Stores Inc. and Wal-Mart.com Inc. (which operates under the business name Walmart.com)./28/ The privacy disclosure further indicates that "we" will not sell personal information on Web site visitors to anyone,/29/ but the inference is left that Walmart.com shares all of the information that it collects with its parent, presumably in order to enhance the parent company's own market research concerning the buying habits of its customers. Wal-Mart also advertises a Wal-Mart credit card that can be used for online purchases, as well as purchases through the traditional physical sales outlets./30/ Further, items purchased online via www.walmart.com can be returned to any Wal-Mart store./31/

2. SHORT-TERM SOLUTIONS: ATTACKING ENTITY ISOLATION THROUGH ATTRIBUTIONAL NEXUS THEORY

[18] The previous analysis suggests that Walmart.com may not be operationally independent from its parent company, Wal-Mart Stores Inc., or that the online affiliate is acting as the agent or alter ego of its parent. Accordingly, it may be constitutionally permissible under attributional nexus theory for local and state governments to force Walmart.com to charge and collect use taxes on sales to consumers where Wal-Mart Stores Inc. maintains a physical presence, which is every state within the United States./32/

[19] Even if Walmart.com has not crossed the line, it may not make sense to apply a body of sales tax law that was developed for the mail-order industry. In the public's mind, a dot.com affiliate of a well-branded retail chain, such as Wal-Mart, will almost invariably act as the Internet retail arm for the traditional store. Further, these large traditional retailers have the resources and knowledge to comply with all relevant local and state sales tax laws because they maintain stores throughout the country.

[20] Michael McIntyre suggests that, in determining whether a particular entity isolation strategy is effective, courts should take into account the real relationship between the related corporations in order to determine whether the imposition of a sales tax collection obligation on the remote seller would be an unreasonable burden on interstate commerce./33/ Alternatively, he suggests that states may be able to impose the collection obligation directly on the parent for its online affiliate sales./34/ The parent would be forced to instruct its subsidiary to charge and collect sales taxes in order to discharge this responsibility./35/

[21] John A. Swain similarly argues that existing judicial precedents support the ability of courts and state tax authorities to impose use tax collection obligations on remote sellers with affiliates within the taxing state, as long as the corporate group to which the affiliate belongs form a single business enterprise./36/ These sorts of theories will likely be tested by courts in the near future to the extent that state and local tax authorities challenge the practices of dot.com affiliates of traditional retail chains./37/

[22] In any event, Wal-Mart's entity isolation strategy may merely reflect the inevitable result of maintaining tax-free status over many Internet transactions while continuing to apply taxes to traditional economic activity. Wal-Mart is attempting to convert its otherwise taxable online sales into nontaxable sales through tax planning in order to level the competitive playing field with pure dot.coms that do not have to charge and collect sales taxes on out- of-state sales. Wal-Mart, as the largest traditional retailer within the United States, would hence likely benefit from a legal rule change that forced online companies to collect sales taxes from remote customers. Further, there are many more large retailers that are attempting to use similar entity isolation strategies./38/

3. Long-Term Solutions: Developing Economic Presence Tests

3.1. REPLACING PHYSICAL PRESENCE REQUIREMENTS

[23] As a result of the difficulties associated with taxing remote sales, some commentators have proposed reform efforts that focus instead on an economic presence test at the location of consumption (for example, the geographic location where the purchaser of an e-commerce good or service resides). An economic presence test would replace the traditional physical presence test by permitting state and local tax authorities to impose tax collection obligations on remote sellers if, for example, the seller exceeds a specified threshold of economic activity (for example, sales of over $ 100,000) within the taxing state. A threshold test is probably necessary to lower compliance concerns for small remote retailers with fewer resources; otherwise an undue burden may be placed on interstate commerce. The purpose of the economic presence test is to reduce revenue losses, discourage market distortions, and level the competitive playing field between traditional retailers and remote retailers./39/

[24] For example, Charles E. McLure Jr. has proposed that remote sales should be taxed by the state where consumption takes place, regardless of whether a business maintains a physical presence within the taxing state./40/ He asserts that, in order to achieve a workable solution, states will need to radically simplify and unify their tax bases./41/ Similarly, Walter Hellerstein

has advocated extending the reach of state tax authorities over the location of consumption for remote sales by focusing on the billing address of the consumer./42/ As a result of the difficulties that often arise in determining the location of consumption regarding e-commerce activities, additional rules have been suggested to impose the tax when it is not possible to determine the location where the purchaser resides./43/

3.2. THE STREAMLINED SALES TAX PROJECT

[25] These views have at least partly been adopted by the Streamlined Sales Tax Project (SSTP), the most ambitious effort yet by state tax authorities to simplify and unify their disparate sales and use tax systems. In order to encourage neutral tax treatment between traditional commercial activities and e-commerce, the SSTP's proposals would apply to all forms of commerce. These legislative efforts are based on a model state sales tax law (the Uniform Sales Tax Act) and uniform agreement (the SSTP Uniform Agreement) for participating states that was adopted on December 22, 2000 (and subsequently amended on January 24, 2001)./44/

[26] Through the SSTP Uniform Agreement, participating states agree to adopt a destination-based sales tax system where sales will be generally sourced to where a product has been received by a consumer (for example, the delivery address, which for digital products would generally coincide with the consumer's billing address)./45/ For digital goods, if the location of consumption cannot be determined, then the product would be taxed at the rate of the state and local jurisdiction where the product was first available for transmission (for example, the online vendor's normal place of business)./46/ Participation by remote sellers without a physical presence within a taxing state is voluntary until Congress overturns existing nexus requirements.

[27] The thrust of the SSTP is to greatly simplify and unify state and local sales and use taxes. Importantly, all local governments would have to use the same tax base as the one chosen by the state./47/ Further, participating states would administer all local sales and use taxes./48/ The remote vendors hence would be required to register only with the state tax authority and remit revenues to this central authority, which in turn would distribute the relevant revenues to local governments./49/ Finally, as subsequently discussed, Internet vendors would be encouraged to adopt technological platforms that automate the tax collection process. These steps should help to alleviate compliance costs associated with complying with different tax laws.

3.3. SSTP HURDLES: STATE FISCAL SOVEREIGNTY AND FEDERAL LEGISLATIVE RELUCTANCE

[28] The fate of the SSTP remains unclear. By boldly moving to simplify and unify their sales tax systems, state tax authorities have run squarely into fiscal sovereignty concerns reflected by state legislators. A special task force of the National Conference of State Legislatures (NCSL), on January 27, 2001, voted to approve the Uniform Sales Tax Act and SSTP Uniform Agreement, but modified the model act and agreement in a number of important ways./50/ The NCSL task force voted to: (a) permit states to have more flexibility in determining tax rates for certain goods (for example, clothing and food);/51/ (b) delete components of the SSTP Uniform Agreement, such as the definition of "sales tax bases";/52/ and (c) relegate the SSTP to the status of an advisory group, with no authority to change legislation./53/

[29] According to an NCSL spokesperson, the changes were necessary in order to ensure a realistic chance of success of final passage with state legislators./54/ These state legislators must deal with a diverse set of constituents, including businesses that want to make sure they are not subjected to discriminatory tax treatment (or that lobby to maintain tax preferences) and social groups that want to maintain a zero tax rate on certain items, such as food./55/ As of June 17, 2002, 33 states and the District of Columbia had adopted legislation based on the SSTP or NCSL efforts, while 2 additional states have introduced legislation pending further consideration./56/

[30] Concerns surrounding burdensome compliance costs will increase to the extent that the SSTP's harmonization and simplification efforts are reduced by the NCSL or other bodies. A practical political compromise could involve permitting states to maintain a certain amount of control over their sales tax systems, but prohibiting local governments from taxing out-of-state businesses./57/ As commentators have noted, the real complexity (and higher potential compliance cost) lies in the thousands of local sales and use tax rules and not with the 45 states that impose sales taxes./58/

[31] Further, the SSTP Uniform Agreement should be amended to exempt from registration small retailers with de minimis out- of-state sales in order to reduce compliance concerns for companies with few resources./59/ This is the approach adopted by the European Union (EU), which proposes to force non-EU companies to collect value added taxes on online sales to EU consumers as long as total sales into the EU exceed 100,000 Euros./60/ Alternatively, the states could agree that small retailers with below-threshold gross sales would not have to register for collection obligations on remote sales: This would be similar to the approach employed under Canada's goods and services tax (GST), under which companies with annual gross worldwide revenues of C $ 30,000 or less are exempt from GST registration requirements./61/ A threshold test in the sales tax context might help states convince Congress that interstate commerce would not be overly harmed by the imposition of collection obligations on remote retailers because small retailers would still be able to sell online goods to out-of-state residents without having to incur burdensome tax compliance costs.

[32] In any event, it is clear that for an economic presence test to be workable, steps must be taken to dramatically reduce the complexity in state sales taxes as well as uniformity in how these taxes will be administratively applied to transactions. The ultimate solution will likely require a compromised effort driven by a mix of bottom-up (state and local governments) and top-down (Congress) political institutions in order to assuage compliance concerns and circumvent constitutional hurdles surrounding burdens on interstate commerce./62/ For example, the Multistate Tax Commission, through its efforts with the Streamlined Sales Tax Project, calls on Congress to pass legislation to force remote sellers to charge and collect sales and use taxes once the states have simplified and unified their sales tax systems./63/ Federal legislators, however, currently show little enthusiasm for these developments and, in fact, have passed legislation that prevents states from imposing new or discriminatory taxes on e-commerce./64/

3.4. EASING THE COMPLIANCE BURDEN THROUGH TECHNOLOGY

[33] Tax compliance issues are clearly among the greatest hurdles to overcome in order to convince federal legislators that interstate commerce would not be unduly interfered with if remote sellers are forced to comply with collection obligations. In a previous work, I outlined a two-stage process for tax authorities seeking to address tax policy challenges presented by the Internet./65/ First, tax authorities should identify the critical values they wish to see preserved such as the desire to maintain their ability to effectively collect taxes to pay for public goods. Second, the regulators should look to see whether Internet technological solutions can help to preserve these values.

[34] The SSTP represents the most comprehensive attempt yet to employ Internet technologies in the tax collection process. The SSTP Uniform Agreement sets out a number of measures that would encourage technological solutions to the daunting compliance issues surrounding remote online sales to consumers. At this point, the adoption of software tax collection technologies by companies is voluntary as a result of Commerce Clause concerns. A pilot project is being conducted by four states (Kansas, Michigan, North Carolina, and Wisconsin) that have agreed to implement and test the technological solutions./66/

[35] The SSTP proposes that online vendors (or any remote vendors) should be able to register online once with a central registration system (remote vendors must currently register with each state through a paper registration system)./67/ Vendors can adopt automated Internet tax collection systems under three options: (a) Sellers can contract with a Certified Service Provider (that is, an unrelated online company that acts as a tax intermediary) that can fulfill the sellers' collection obligations; (b) sellers can adopt an approved software tax collection program to automatically charge and collect sales taxes; or (c) large sellers (that is, generally sellers with more than $ 500 million in annual sales) are permitted to use their own customized tax collection software program./68/

[36] The states will maintain an online database with all relevant tax rates (assigned to ZIP codes) that can be accessed by the online intermediaries or the software programs employed by the remote vendors./69/ In order to ease the compliance burden, online vendors will be permitted to be compensated by keeping a specified portion of the taxes collected./70/

[37] Automated online tax collection, however, needs to take into consideration the nature of cyberspace and its evolving values: the Internet can be analogized with a "digital biosphere," an online forum characterized by tremendous internal diversity where both commercial and non-commercial (for example, chat rooms, e-mail, or Usenet groups) overlap in an environment of rapid technological evolution. Even efficient technological solutions will be unacceptable to e-commerce participants to the extent they intrude on cyberspace values, including the desire to maintain transactional privacy and anonymity.

[38] The SSTP suggests steps to protect online consumer privacy./71/ For example, the automated tax collection system must be designed so that "the fundamental precept of anonymity is respected, and that personally identifiable information is only used when necessary" for the administration of the collection system./72/ Further, the Certified Service Providers must

"provide such technical, physical, and administrative safeguards so as to protect personally identifiable information from unauthorized access and disclosure."/73/ Nevertheless, it remains to be seen whether consumers will accept automated tax collection mechanisms that may come to be perceived as an unwarranted intrusion into their online experiences.

CONCLUSION

[39] Sales and use tax rules that emphasize the need for a physical presence within the taxing state provide an incentive for companies like Wal-Mart to engage in entity isolation strategies with their online affiliate corporations. The increased reliance on "independent" online affiliates adds to the growing revenue loss for state and local governments, reducing their ability to fund important public goods. In the short term, state tax authorities can challenge entity isolation strategies under attributional nexus theory by arguing, inter alia, that the affiliate is operationally tied to its parent corporation or that the affiliate acts as the retail agent for the parent company.

[40] In the longer term, the preferred alternative is to replace physical presence requirements with economic presence tests that permit states to impose collection obligations on remote retailers. The Streamlined Sales Tax Project represents the best chance for movement in this direction, although these efforts continue to face two daunting hurdles: the desire by many state governments to preserve control over their sales tax policy hence diluting the simplification and unification aspects of the SSTP and the apparent lack of enthusiasm by many federal legislators to overturn the Commerce Clause restrictions that mandate the physical presence tests. While state fiscal sovereignty concerns are clearly important, state governments may need to take additional steps to reduce tax compliance concerns for businesses in order to convince Congress that interstate commerce will not be unduly harmed if states are permitted to extend their tax jurisdiction over remote sellers.

/1/ See Quill Corp. v. North Dakota, 504 U.S. 298, 315 (1992). Under the "bright-line" physical presence test espoused by the U.S. Supreme Court, mail-order companies that do not maintain sales offices or sales forces within target states cannot be forced to collect use taxes by state or local governments. The Court recognized that this principle influences business and tax strategies: "Indeed, it is not unlikely that the mail-order industry's dramatic growth over the last quarter century is due in part to the bright-line exemption from state taxation created in [an earlier Court decision] Bellas Hess." Id. at 316. The Court emphasized that Congress could overturn this physical presence test under its authority to change the Commerce Clause. Id. at 318.

/2/ See Gen. Accounting Office, Sales Taxes: Electronic Commerce Growth Presents Challenges; Revenue Losses Are Uncertain 20-21 (June 2000) (estimating state and local revenue losses of up to $ 12 billion a year by 2003); Donald Bruce and William F. Fox, "State and Local Sales Tax Revenue Losses From E- Commerce: Updated Estimates" (estimating state and local government revenue losses of $ 13.3 billion for 2001). State Tax Notes, Oct 15, 2001, p. 203; 2001 STT 207-39; or 2001- 26150 (11 original pages).

/3/ In 1999, sales taxes provided roughly 25 percent of tax revenues or appromixately $ 237 billion to states and local governments. See Advisory Commission on Electronic Commerce, Report to Congress 18 (April 2000). For a discussion of trends surrounding increased remote sales in the context of cross-border income taxes, see Arthur J. Cockfield, "Balancing National Interests in the Taxation of Electronic Commerce Business Profits," 74 Tul. L. Rev. 133, 153-159 (1999).

/4/ For discussion, see Charles E. McLure Jr., "Taxation of Electronic Commerce: Economic Objectives, Technological Constraints, and Tax Laws," 52 Tax L. Rev. 269, 403 (1997) (arguing that entity isolation strategies lead to detrimental results for state and local governments).

/5/ Wal-Mart Stores Inc., Annual Report 2 (2001). Wal- Mart employs more than 885,000 employees in the United States and 255,000 employees internationally. Id at 7.

/6/ Press Release, Wal-Mart Stores Inc., Wal-Mart, Accel Partners to Launch Walmart.com, a New Independent Company Based in Silicon Valley (Jan 6, 2000), available at http://www.walmart.com/cservice/aw_pr_010600_01.gsp [hereinafter Wal-Mart, Accel Partners to Launch].

/7/ Id.

/8/ Id.

/9/ Id.

/10/ The author's full e-mail message read: "I have a question about sales taxes. If I buy a product from Walmart.com, do I have to pay sales taxes? Does it matter where I live? Thanks, Art Cockfield." E-mail from Arthur J. Cockfield, assistant professor, Queen's University Faculty of Law, to Walmart.com, Inc. (Jun 5, 2001, 14:34 EST). Walmart.com sent a (presumably) automated reply to the message on the same date at 2:49 p.m., which read in relevant part:

> We are writing in response to your question about sales tax. Current law requires online stores such as Walmart.com to charge sales tax only in the state or states where the online company maintains a physical presence. We currently charge sales tax in Arkansas, California, Ohio and Utah. All other states are exempt from this tax.

E-mail from Walmart.com Inc. to Arthur J. Cockfield (Jun 5, 2001, 14:49 EST). Copies of all e-mails and Web sites on file with Connecticut Law Review.

/11/ Wal-Mart Stores Inc., Annual Report, Exhibit 21 Subsidiaries of Wal-Mart Stores Inc. (2001). Wal-Mart Stores Inc. initially owned 88 percent of Walmart.com, but subsequently bought out the 12 percent interest owned by Accel Partners, its venture capital partner.

/12/ By maintaining the ability to appoint or fire the board of directors, Wal-Mart Stores Inc. is indirectly permitted to manage the affairs of its subsidiary: Directors are given the authority to manage the affairs of the corporation. Del. Code Ann. tit. 8, section 141 (1991).

/13/ See, for example, Current Inc. v. State Bd. of Equalization, 24 Cal. Rptr. 2d 407, 407 (Ct. App. 1994) (holding that a state could not force a mail-order company to collect sales tax because the company was not an agent or alter ego for its parent corporation based in Minnesota); Bloomingdale's By Mail Ltd. v. Commonwealth, 567 A.2d 773 (Pa. Commw. Ct. 1991) (holding that a state cannot force a mail-order company, Bloomingdale's by Mail, to collect use taxes because the parent company, Bloomingdale's, did not act as an agent for the mail-order company); SFA Folio Collections Inc. v. Tracy, 652 N.E. 2d 693 (Ohio 1995) (holding that the presence of a sister corporation in the same state did not establish substantial nexus). (For the full text of the Ohio Supreme Court's decision in SFA Folio Collections, see 95 STN 161-29.)

/14/ Several commentators have reviewed the law in this area in recent years. See generally Michael J. McIntyre, "Commentary: Taxing Electronic Commerce Fairly and Efficiently," 52 Tax L. Rev. 625 (1997); Karl Frieden, Cybertaxation 289-334 (2000); John A. Swain, "Cybertaxation and the Commerce Clause: Entity Isolation or Affiliate Nexus?" State Tax Notes, May 20, 2002, p. 723; 2002 STT 97-3; or Doc 2002-12073 (25 original pages).

/15/ For a discussion of state court decisions surrounding affiliate nexus issues, see Frieden, supra note 14, at 316-326, 323 (noting that "it is clear that, if an in-state affiliate performs certain activities on behalf of the out- of-state retailer that help the entity establish and maintain a market in the consumer's state, the more traditional attributional nexus rules will apply").

/16/ It is important to note that while the Supreme Court has yet to weigh in on the entity isolation issue, the Court has rejected formalism in the past in the context of state sales taxation. See Scripto Inc. v. Carson, 362 U.S. 207, 211 (1960) (asserting that it is constitutionally insignificant whether a remote seller characterizes its workers as employees or independent contractors, otherwise tax avoidance will result). Further, the Court ignored formalism in a case where National Geographic Society maintained a mail-order company out of the District of Columbia and sales offices for advertisements for its magazine in California. Nat'l Geographic Soc'y v. Cal. Bd. of Equalization, 430 U.S. 551, 551 (1977). The presence of the magazine ad sales office was found to be sufficient nexus for the imposition of the California sales tax because, for use tax purposes, substantial nexus is created between the taxing state and the business entity it seeks to tax. Id. at 554-56.

/17/ Wal-Mart, Accel Partners to Launch, supra note 6.

/18/ SFA Folio Collections Inc. v. Bannon, 217 Conn. 220, 229-30, 585 A.2d 666, 672 (1991). The court focused on the fact that Folio, a corporation operating a mail-order company, and Saks-Stamford, a corporation operating retail store, were "distinct corporate entities" (linked by a common corporate parent, Saks & Company) despite the fact that Folio catalogues were used at Saks-Stamford stores and Folio customers could use Saks- Stamford tailoring services. Id. at 230. The court additionally rejected the argument that "unitary nexus" was created by the shared corporate name, logo, or other intellectual property. The court refused to hold Folio responsible for use tax collection absent a showing that the corporate affiliates have ignored the formalities of corporate existence such as intermingling funds. Id. at 227-32.

/19/ Press Release, Wal-Mart Stores Inc., "New Wal-Mart Fulfillment Distribution Center to Provide Service to Wal- Mart.com" (Aug 2, 2000), available at http://www.walmart.com/cservice/aw_pr_080200_01.gsp.

/20/ Id. (quoting Jeanne Jackson, former CEO of Walmart.com Inc.).

/21/ Wal-Mart StoresInc., Walmart.com Background Information, available at http://www.walmart.com/cservice/aw_coinfo.gsp (last visited Nov. 12, 2001) (on file with the Connecticut Law Review). The passage on the Web site bears repeating in its entirety:

> With the support of Bentonville [the location in Arkansas where Wal-Mart Stores Inc. maintains its head office], we're able to tap into many of the things that have made Wal-Mart a universally known brand -- things like excellent supplier relationships, highly efficient back-office systems, an unswerving commitment to Sam Walton's "Always Low Prices" philosophy and an unrivaled group of experienced retailers who strive each day to make the customer number one.

In short, at Walmart.com, we're passionate about combining the best of two great worlds, technology and world-class retailing, to give our customers easy access to more things Wal-Mart: a wide assortment of their favorite products, Every Day Low Prices, guaranteed satisfaction, friendly service, convenient hours (24 hours, 7 days a week) and a great online shopping experience.

/22/ "Wal-Mart Announces New COO of Walmart.com," Nov 20, 2001, available at http://www.walmart.com/cservice/aw_pr_112001_01.gsp?NavMode=9.

/23/ Wal-Mart Stores Inc., Wal-Mart Stores, at
http://www.walmartstores.com/wmstore/wmstores/HomePage.jsp.

/24/ Wal-Mart Annual Report, supra note 5, at 3. The term "Company" had been previously defined as Wal-Mart Stores Inc. together with its subsidiaries. Id. at 2.

/25/ Id. at 3.

/26/ A California court held that separate corporate identity should be respected for sales tax purposes in part because neither company was held out to customers or potential customers as being the same, or an affiliate of, the other. Further, neither company exploited each other's marketing practices, customer lists, trade name, or goodwill. See Current Inc., 24 Cal. Rptr. 2d (Ct. App. 1994).

/27/ Wal-Mart Stores Inc., Store Finder, at http://www.walmart.com/cservice/ca_storefinder.gsp.

/28/ Wal-Mart Stores Inc., Security and Privacy, at
http://www.walmart.com/cservice/ca_securityprivacy.gsp.:

> Walmart.com Inc., and Wal-Mart Stores Inc., ("we") do not and will not sell or rent your personal information to anyone. You have the right to control your personal information as you see fit. We collect only the personal information you allow us to collect, and then it is used only to help us serve you better.

/29/ Id.

/30/ Wal-Mart Stores Inc., The Wal-Mart Credit Card, at
http://www.walmartcreditcard.com/index1.html.

/31/ Wal-Mart Stores, Inc., Quick Answers, at
http://www.walmart.com/cservice/ca_quickanswers.gsp.

/32/ The ultimate result would be determined by a court's interpretation of the statute employed by a particular state to try to force Walmart.com to collect use taxes. Accordingly, different state legislation may produce different judicial opinions concerning the viability of Walmart.com's entity isolation strategy.

/33/ McIntyre, supra note 14, at 651.

/34/ Id. at 652.

/35/ Id. at 651. In order for this alternative approach to be successful, courts would have to narrowly construe the holding in Quill to impose the bright-line physical presence test on use taxes on remote sellers who use a common carrier or the United States Postal Service to make sales into other states. Id. The Court appeared to suggest that the bright-line test applied generally to sales and use taxes, suggesting a more expansive interpretation. See Quill Corp. v. North Dakota, 504 U.S. 298, 314, 317 (1992). Still, the Court denied certiorari in a case that supports the proposition that economic presence is sufficient to create nexus. See Geoffrey Inc. v. Tax Comm'n, 437 S.E.2d 13, 16 (S.C. 1993). The South Carolina Supreme Court held that the presence within a state of intangible assets, such as licensing agreements or accounts receivable, could fulfill the nexus requirements for income tax purposes and would not unduly burden interstate commerce. Id. (For the full text of the South Carolina Supreme Court's decision in Geoffrey, see 93 STN 133-12.)

/36/ See Swain, supra note 14, at para. 121.

/37/ In 2001, the California Legislature introduced legislation that would force any Internet vendor to collect sales taxes if the corporation maintained an affiliate company with a physical presence within California. Cal. AB 81 (Apr 17, 2001). A subsequent amendment to the bill, however, deleted all references to Internet taxation. Cal. AB 81 (May 30, 2001). (For the full text of the April 17 version of AB 81, see Doc 2001-11236 (5 original pages) or 2001 STT 82-3.)

/38/ See, for example, Kim Peterson, "E- Commerce Two-Step," San Diego Union-Trib., May 13, 2001, at H1, LEXIS, News Library, Sdut File (discussing how Gateway Computers, based in San Diego, created a separate company based in Massachusetts for its online retail operations, so that it would only have to charge online sales tax to residents of Massachusetts).

/39/ One survey found that 58 percent of respondents considered it unfair for Internet businesses to have an artificial tax advantage over their "Main Street" counterparts. See Markle Foundation, Internet Survey: Frequency Questionaire 10 (November 2000).

/40/ Charles E. McLure Jr., "Rethinking State and Local Reliance on the Retail Sales Tax: Should We Fix the Sales Tax or Discard It?" 2000 BYU L. Rev. 77 (2000).

/41/ Id. at 89, 90.

/42/ See Walter Hellerstein, "State Taxation of Electronic Commerce," 52 Tax L. Rev. 425, 487-88 (1997).

/43/ For example, a "throwback" rule is suggested when a billing address cannot be determined, whereby the remote vendor will collect the sales tax at the tax rate imposed by the state where the vendor is located. Id. at 488. Alternatively, a "throwaround" rule is discussed whereby the vendor would impose an average tax rate reflecting previous e-commerce sales patterns and the resulting revenues would eventually be divided among the states in proportion to this historical sales pattern. Id. at 489-90.

/44/ The Uniform Sales and Use Tax Administration Act, once passed by a participating state, authorizes states to enter into the Streamlined Sales and Use Tax Agreement. Uniform Sales and Use Tax Administration Act section 4 (amended Jan 24, 2001) [hereinafter Uniform Sales Tax Act], available at http://www.geocities.com/streamlined2000. The agreement provides for the details to harmonize and simplify sales tax bases. Streamlined Sales and Use Tax Agreement (amended Jan 24, 2001) [hereinafter SSTP Uniform Agreement].

/45/ Id. at section 310.

/46/ This "throwback" rule is meant to avoid situations where the online vendor uses networking equipment based in zero-sales tax jurisdictions to transmit the digital good or service. Id. section 310(e), at 8 (indicating that any location that merely provided for the transmission of the digital product should be disregarded).

/47/ Id. section 304(a), at 4.

/48/ Id. section 306, at 4.

/49/ Id.

/50/ See Amendments by the NCSL Task Force on State and Local Taxation of Telecommunications and Electronic Commerce to the Uniform Sales and Use Tax Administration Act and the Streamlined Sales and Use Tax Agreement (Jan 27, 2001) [hereinafter NCSL Uniform Agreement].

/51/ Id. at sections 304 and 308.

/52/ Id. section 312.

/53/ Id. seciton 714.

/54/ See Dolores Whiskeyman, "State and Federal Officials, International Bodies Face Major Tax Issues," 6 Elec. Com. & L. Rep. 195, 196 (Feb 21, 2001).

/55/ For background on the NCSL and SSTP political process, see Doug Sheppard, "2000: The Rise of the Streamlined Project and the Fall of the Advisory Commission," State Tax Notes, Jan 1, 2001, p. 34; 2000 STT 251-25; or Doc 2001-309 (12 original pages) (discussing the urgency felt by the NCSL to act on sales tax unification and simplification as quickly as possible to stop federal efforts to preempt state tax authority).

/56/ Status of State Efforts on Streamlined Sales Tax Project, at http://www.geocities.com/streamlined2000/.

/57/ See, for example, Eugene F. Corrigan, "How Congress Can Help Remote Sellers and States," State Tax Notes, Mar 19, 2001, p. 965; 2001 STT 53-28; or Doc 2001-7790 (2 original pages). Eugene Corrigan, former executive director of the Multistate Tax Commission, agrees that states should be able to impose their sales tax on out-of-state vendors despite the absence of a physical presence within the taxing state. In his view, Congress should pass legislation to address Commerce Clause concerns so that the 45 states can extend their tax jurisdiction over remote sales.

/58/ Corrigan also notes that the real compliance complexity lies with the different local government sales and use taxes. Id. Accordingly, he argues that Congress should immunize all remote sellers from having to collect and remit any local use tax on any sale of goods shipped from outside the state. In addition to the thousands of existing local taxing jurisdictions, Corrigan also notes that there are approximately 30,000 additional local taxing jurisdictions that may choose to impose a sales and use tax. He also notes that "few if any" local governments currently collect significant sales or use tax revenues from sales to out-of-state consumers. In any event, he notes that the ability of states to tax remote sellers would generate more tax revenues and these revenues could be shared with local governments. Id. at 673.

/59/ The SSTP Uniform Agreement already contains an exemption for small retailers that collect less than $ 30,000 in sales taxes: These retailers cannot be forced to file more than one remittance per tax return. See SSTP Uniform Agreement, supra note 44, at section 320(a).

/60/ See "Commission Proposal for a Council Directive Amending Directive 77/388/EEC as Regards the Value Added Tax Arrangements Applicable to Certain Services Supplied by Electronic Means," COM (2000) 349. The EU has announced that this proposal, which was initially withdrawn, will become effective by July 2003.

/61/ See Excise Tax Act (Canada), R.S.C., c. E-13, section 148(1).

/62/ For discussion of the background behind federal and state reform efforts, see Frieden, supra note 14, at 189-206.

/63/ See, for example, Letter from Elizabeth Harchenko, Chair, Mutistate Tax Commission, to Sen. John McCain, R- Ariz., and Sen. Ernest F. Hollings, D-S.C., 2 (Mar 6, 2001).

/64/ See Internet Tax Freedom Act of 1998, Pub. L. No. 105-277, section 1101, 112 Stat. 2681 (1998); Internet Tax Nondiscrimination Act of 2000, H.R. 3709, 106th Cong. (2000) (extending the moratorium on new or discriminatory sales taxes through November 1, 2003).

/65/ See Arthur J. Cockfield, "Transforming the Internet Into a Taxable Forum: A Case Study in E-Commerce Taxation," 85 Minn. L. Rev. 1171, 1221, 1235-1237 (2001).

/66/ Streamlined Sales Tax Project, Pilot Status Report (May 2001), available at http://www.geocities.com/streamlined2000/.

/67/ SSTP Uniform Agreement, supra note 44, at sections 306 and 400.

/68/ Id. sections 404 and 500.

/69/ Id. section 308(b)(5).

/70/ Id. section 600.

/71/ Id. at section 318.

/72/ Id. section 318(c)(1).

/73/ Id. section 318(c)(4). When personally identifiable information is retained, individuals should be provided notice of such retention and the access to their own data and a right to correct inaccurately recorded data. Id. sections 318(c)(2) and (6).