SCHOLASTIC BOOK CLUBS, INC. 2931 E. MCCARTY STREET JEFFERSON CITY, MO 65101-4431,	§	STATE OF ALABAMA ALABAMA TAX TRIBUNAL
Taxpayer,	§	DOCKET NO. S. 14-374
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

FINAL ORDER

The Department of Revenue assessed Scholastic Book Clubs, Inc. ("Taxpayer") for use tax for April 2007 through March 2013. The Taxpayer appealed to the Tax Tribunal pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. The parties submitted a joint stipulation of facts on August 13, 2015. Additional evidence was introduced at an August 27, 2015 hearing. Chris Grissom, Jimmy Long, Anne Torregrossa, and David Bertoni represented the Taxpayer. Assistant Counsel Ralph Clements, Christy Edwards, and Mary Martin Mitchell represented the Revenue Department.

ISSUES

The Taxpayer is an out-of-state retailer that sold books and other tangible personal property at retail to various Alabama customers during the period in issue. The two disputed issues are:

(1) Was the Taxpayer required to collect, report, and remit Alabama use tax to the Revenue Department during the subject period pursuant to Alabama's use tax statutes, Code of Ala. 1975, §40-23-60, et seq.; and,

(2) Is the Department barred from assessing the Taxpayer by the Due Process Clause of the Fourteenth Amendment and/or the Commerce Clause, Art. 1, §8, cl. 3, of the U.S. Constitution.

FACTS

The facts are undisputed. The Taxpayer is headquartered in Missouri, and sells books and other educational materials in Alabama and throughout the United States.

The Taxpayer has no retail stores or offices in Alabama, owns no property and has no employees in Alabama, is not registered to do business in Alabama, does not have a mailing address or telephone number in Alabama, and does not own or control another entity doing business in Alabama.

The Taxpayer conducts business in all 50 states in the same manner. Specifically, each month during the school year, the Taxpayer mails catalogs, order forms, and promotional coupons to early childhood development centers, primary and secondary schools, and to households in which children are homeschooled by their parents, i.e., parent educators. If the materials are sent to a school, the school distributes the materials to the classroom teachers in the school. The classroom teachers then have the option to either discard the materials, or distribute them to their students.

If a teacher elects to distribute the materials, the teacher thereafter gathers the completed order forms and consolidates the orders on a master order form. The teacher may also order books and materials on the master order form. The teacher then mails the completed master order form, and the money for the orders, to the Taxpayer in Missouri.

After receiving the master order form, the Taxpayer ships the purchased items to the school by common carrier, to the attention of the teacher that submitted the order form. The teacher thereafter distributes the items to the appropriate individuals. If there are

discrepancies and/or complaints concerning the items, the teacher communicates with the Taxpayer concerning the discrepancies and/or complaints.

The Taxpayer awards bonus points to classrooms and parent educators based on the dollar value of the items ordered by the classroom or parent educator. The classroom teachers and parent educators may use the bonus points to purchase items from the Taxpayer, or they may use them to obtain $25 gift certificates from Target, Staples, or Michaels. The bonus points stay with the classroom if a teacher retires or is transferred. The Taxpayer's stated intent is that all items purchased using the bonus points should be used for classroom purposes, but the Taxpayer has no way of monitoring, controlling, or otherwise knowing how the items may be used.

The number of Alabama schools, including home schools, that placed orders with the Taxpayer during the years in issue ranged from 1,834 to 1,955 per year. The number of individual classrooms that ordered items ranged from 9,518 to 13,977 per year. The fair market value of the goods purchased with or distributed as a result of bonus point redemptions ranged from $424,069 to $961,330 per year during those years.

Scholastic, Inc. is the Taxpayer's parent corporation. Scholastic, Inc. contracted with the Alabama Board of Education to furnish certain text books and programs during the period June 2012 through May 2018.

Scholastic Book Fairs, Inc. is also a subsidiary of Scholastic, Inc. Scholastic Book Fair, Inc. is based in Florida, and supplied books for book fairs held in Alabama and elsewhere during the period in issue.

The Taxpayer failed to file Alabama sales or use tax returns during the period in issue. The Department audited the Taxpayer for use tax for the period and determined

that the Taxpayer was statutorily subject to Alabama use tax, and that it also had contacts or nexus with Alabama sufficient to require it to report and remit the use tax due on its sales in Alabama. It assessed the Taxpayer accordingly. This appeal followed.

Other relevant facts are set out in the following analysis.

ANALYSIS

Issue (1). Was the Taxpayer subject to Alabama use tax under Alabama's use tax statutes?

Code of Ala. 1975, §40-23-61(a) levies a use tax on tangible personal property that is purchased at retail for use, storage, or consumption in Alabama.[1] See generally, *In re Culverhouse, Inc.*, 358 B.R. 806 (M.D. Ala. 2006, affirmed 214 Fed. App. 921). The seller is required to collect the tax from the purchaser, Code of Ala. 1975, §40-23-67, and is thereafter required to file use tax returns and remit the tax to the Department. Code of Ala. 1975, §40-23-68.

It is undisputed that the Taxpayer sold the books and other materials at retail to its Alabama customers during the subject period, and that the items were intended for use, storage, or consumption in Alabama. The §40-23-61(a) use tax levy thus applied to the items sold by the Taxpayer to Alabama customers during the assessment period.

As indicated, §40-23-68 also requires taxpayers subject to Alabama use tax to file returns and remit the tax due to the Department. Section 40-23-68(b) includes nine specific activities that, if engaged in by a seller, would statutorily require the seller to file

[1] If the retail sale is in Alabama, and the seller collects Alabama sales tax on the sale and remits the tax to the Department, the subsequent use, storage, or consumption of the property in Alabama is exempted from the use tax. Code of Ala. 1975, §40-23-62(1).

Alabama use tax returns and remit the tax to the Department. See, §40-23-68(b)(1), (2),

(3), (4), (5), (6), (7), (8), and (10). For example, subparagraph (b)(1) requires a seller to report and pay use tax if the seller "[m]aintains, occupies, or uses . . . an office, place of distribution, sales or sample room or place, warehouse, or storage or other place of business" in Alabama. Subparagraph (b)(6) requires a seller to report and pay use tax if it has "under a franchise or licensing arrangement or contract, a franchisee or licensee operating under its trade name" in Alabama. The subparagraphs in §40-23-68(b) apply in the alternative. Consequently, a seller is required to report and remit use tax to the Department if any one of the subparagraphs apply.

The Taxpayer argues that it was not required to report and remit Alabama use tax to the Department pursuant to §40-23-68(b) during the period in issue because it was not engaged in Alabama in any of the activities specified in the above nine subparagraphs. It specifically addresses subparagraph (b)(3), which requires a seller to report and pay use tax if the seller "[e]mploys or retains under contract any representative, agent, salesman . . . operating in this state under the authority (of the seller) for the purpose of selling" tangible personal property in Alabama. It contends that subparagraph (b)(3) does not apply because the Alabama teachers were not employed by or under contract as representatives or agents of the Taxpayer.

I agree that subparagraph (b)(3) does not apply to the Taxpayer because the Alabama teachers were not employed by or under contract with the Taxpayer during the subject period. The Taxpayer may, however, still be required to report and remit use tax to the Department pursuant to subparagraph (b)(9). That catchall provision requires a seller to report and pay Alabama use tax if it "[m]aintains any other contact with this state that would allow this state to require the seller to collect and remit the tax due under the

provisions of the Constitution and laws of the United States." That is, all out-of-state sellers selling tangible personal property at retail for use, storage, or consumption in Alabama are statutorily required to report and remit Alabama use tax, unless they are constitutionally protected from doing so.

The Taxpayer argues that the Legislature provided clear guidance in the nine subparagraphs in §40-23-68(b) other than subparagraph (b)(9) as to when or under what specific circumstances a seller would be required to report and remit Alabama use tax. It contends that if subparagraph (b)(9) is allowed to control, it would "render subsection (b)(3) of the statute a nullity." Taxpayer's Brief at 12.

I agree that by enacting the nine subparagraphs in §40-23-68(b) other than subparagraph (9), the Legislature provided specific examples of activities that would statutorily require a seller to collect and remit Alabama use tax to the State.[2] But the examples were not intended to be and are not all-inclusive. That is why the Legislature included catchall subparagraph (b)(9).

The Taxpayer correctly argues that "[t]he fundamental rule of statutory construction is that this Court is to ascertain and effectuate the legislative intent as expressed in the statute." Taxpayer's Brief at 13. Applying that rule of construction, the Legislature clearly intended when it enacted subparagraph (b)(9) to require any seller that sells tangible

[2] While a retailer engaged in an activity described in the §40-23-68(b) subparagraphs would be statutorily required to report and remit use tax to the Department, the activities described in various of those subparagraphs are not sufficient to establish Commerce Clause nexus. For example, subparagraphs (b)(4), (5), (7), and (8) require a seller to collect and remit use tax if the seller solicits, by various means, orders from Alabama customers. As discussed below, the solicitation of orders, by itself and without a physical presence in the taxing state, is insufficient to establish Commerce Clause nexus. See generally, *Quill Corp. v. North Dakota*, 112 S. Ct. 1904 (1992).

personal property at retail for use, storage, or consumption in Alabama to report and remit the use tax due to the State, unless the seller is protected by the Due Process Clause and/or Commerce Clause of the U.S. Constitution. The Taxpayer was thus statutorily required to collect, report, and remit use tax to the Department on the items it sold to Alabama customers during the assessment period, unless it was constitutionally protected from doing so.[3]

Issue (2). Does the Due Process Clause and/or the Commerce Clause prevent the Department from assessing the Taxpayer for the use tax in issue?

In *Complete Auto Transit, Inc. v. Brady*, 97 S. Ct. 1076 (1977), the U.S. Supreme Court opined that a state may assess a tax against an out-of-state vendor only "when the tax is applied to an activity with a substantial nexus with the taxing State. . . ." *Complete Auto*, 97 S. Ct. at 1079. In *Quill Corp.*, supra, the Supreme Court for the first time distinguished between due process nexus and Commerce Clause nexus. For due process purposes, the Court held "that a taxpayer has sufficient nexus with a taxing state for due process purposes if the taxpayer purposely directs its activities towards the residents of the state and avails itself of the economic benefits of the state." *Quill*, 112 S. Ct. at 1910, 1911.

[3] The Department also argues that the Taxpayer had nexus with Alabama pursuant to Alabama's remote entity nexus statute, Code of Ala. 1975, §40-23-190, and that it was also required to collect and remit use tax pursuant to Code of Ala. 1975, §41-4-116 because its parent, Scholastic, Inc., had a contract with the Alabama Department of Education during a part of the period in issue. See, Department's Prehearing Brief at 8 – 11. A discussion of those issues is, however, pretermitted by the above holding that the Taxpayer was otherwise statutorily required to collect and remit use tax on the tangible personal property it sold in Alabama during the subject period.

The Taxpayer clearly directed its sales activities towards Alabama residents during the period in issue when it mailed its catalogs, order forms, and promotional materials to thousands of school teachers and parent educators in Alabama every month of the school year during the period. It also availed itself of Alabama's economic market by making over $17,877,000 in sales to Alabama customers during the period.[4] The Taxpayer thus clearly had due process nexus with Alabama during the assessment period.

The harder question, of course, is whether the Taxpayer also had Commerce Clause nexus with Alabama. In *Quill*, supra, the Court held that for Commerce Clause purposes, an out-of-state vendor has nexus with the taxing state only if the vendor has a physical presence in the state. The issue thus is whether the teachers' activities in Alabama relating to the Taxpayer's sales of its books and other materials in Alabama during the subject period established a physical presence for the Taxpayer in Alabama sufficient to satisfy the *Quill* Commerce Clause nexus standard.

Courts in several other states have decided the Commerce Clause nexus issue in cases involving the Taxpayer or other taxpayers conducting similar business activities. In Michigan, Arkansas, and Ohio, the courts found that the teachers' activities on behalf of the out-of-state retailer were not sufficient to create Commerce Clause nexus. See, *Scholastic Book Clubs, Inc. v. Michigan Revenue Division*, 567 N.W.2d 692 (Mich. 1997); *Pledger v.*

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[4] The parties did not stipulate as to the amount of the Taxpayer's sales in Alabama during the assessment period, nor was the amount submitted into evidence at the August 27, 2015 hearing. The parties agree, however, that the amount of the final assessment is correctly based on the Taxpayer's sales in Alabama during the period. The Alabama use tax rate is four percent of the sales price. Consequently, the tax of $715,089 included in the final assessment is based on total sales of $17,877,225. ($715,089 x 25 = $17,877,225).

Troll Book Clubs, Inc., 871 S.W.2d 389 (Ark. 1994); *Troll Book Clubs, Inc. v. Tracy*, Ohio Bd. Of Tax Appeals, No. 92-Z-590 (Aug. 19, 1994), respectively. In Connecticut, California, Kansas, and Tennessee, the courts found nexus. See, *Scholastic Book Clubs, Inc. v. Comm'r of Revenue Servs.*, 38 A.3d 1183 (Conn. 2012); *Scholastic Book Clubs, Inc. v. Board of Equalization*, 207 Cal. App. 3d 734 (1989); *In re Scholastic Book Clubs, Inc.*, 920 P.2d 947 (1996); *Scholastic Book Club, Inc. v. Farr*, 373 S.W.3d 558 (Tenn. Ct. App. 2012), respectively.

I have reviewed the above cases, and I find that the courts that found nexus applied the better rationale. Although the Taxpayer asserts that the decision by the Connecticut Supreme Court cited above is "so opaque as to offer little meaningful guidance," Taxpayer's Post-Trial Brief at 18, I find the Court's rationale compelling, and accordingly adopt it, as follows:

> COMMERCE CLAUSE CLAIM
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> The commissioner next claims that the trial court incorrectly concluded that there is no "substantial nexus" between the plaintiff and the state under the commerce clause of the United States constitution that would justify imposition of sales or use taxes. The commissioner claims that the trial court improperly focused on the technical label ascribed to the teachers but that the United States Supreme Court has stated that the facts under a substantial nexus analysis must be examined functionally from the perspective of the out-of-state retailer, focusing on the nature and extent of the activities of the in-state provider and whether those activities are significantly associated with the retailer's ability to establish and maintain a market in the state for the sale of its products. The commissioner also claims that, under the foregoing analysis, the teachers' activities in the present case satisfy that standard. The plaintiff responds that the tax assessments are barred under the commerce clause because the plaintiff does not occupy the bright-line physical presence in Connecticut required under the substantial nexus test affirmed by the United States Supreme Court in *Quill Corp. v. North Dakota ex rel. Heitkamp*, 504 U.S. 298, 315, 112 S. Ct. 1904, 119 L. Ed. 2d 91 (1992) (*Quill*). The plaintiff contends that the imposition of tax

liability on the basis of the activities of the schoolteachers would blur the United States Supreme Court's rule, with dramatic implications for direct marketers, who would be deprived of any intelligible definitions or principles to determine where *Quill*'s bright line lies. We agree with the commissioner.

* * *

We begin with *Scripto, Inc. v. Carson*, 362 U.S. 207, 207-10, 80 S. Ct. 619, 4 L. Ed. 2d 660 (1960) (*Scripto*), in which the court considered whether Florida could constitutionally impose a state use tax on a Georgia retailer for the sale of goods shipped to purchasers in Florida. Noting that there must be "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax"; (internal quotation marks omitted) id., 210-11; the court concluded that, because the seller had "[ten] wholesalers, jobbers, or 'salesmen' conducting continuous local solicitation in Florida and forwarding the resulting orders from that [s]tate to [Georgia] for shipment of the ordered goods," the required nexus was present. Id., 211. The court reasoned that, although the "salesmen" had written contracts describing them as "independent contractor[s]," were paid on commission and did not work exclusively for the seller; (internal quotation marks omitted) id., 209; the fact that they were "not regular employees of [the seller] devoting full time to its service . . . [was] a fine distinction . . . without constitutional significance. The formal shift in the contractual tagging of the salesman as 'independent' neither results in changing his local function of solicitation nor bears [on] its effectiveness in securing a substantial flow of goods into Florida. . . . To permit such formal 'contractual shifts' to make a constitutional difference would open the gates to a stampede of tax avoidance. . . . The test is simply the nature and extent of the activities of the [seller] in Florida." (Citations omitted.) Id., 211-12.

A few years later, the court determined in *National Bellas Hess, Inc. v. Dept. of Revenue*, 386 U.S. 753, 754-55, 758, 87 S. Ct. 1389, 18 L. Ed. 2d 505 (1967) (*Bellas Hess*), that an Illinois statute taxing goods purchased within the state from a mail order house in Missouri created an unconstitutional burden on interstate commerce where the seller had no outlets or sales representatives in the state and its only connection with its Illinois customers was by common carrier or the United States mail. In reaching that conclusion, the court explained that it had no intention of obliterating the "sharp distinction" generally recognized by state taxing authorities "between mail order sellers with retail outlets, solicitors, or property within a [s]tate, and those who do no more than communicate with customers in the [s]tate by mail or common carrier as part of a general interstate business." Id., 758.

The court subsequently articulated a four part test in

Inc. v. Brady, 430 U.S. 274, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977) (*Complete Auto Transit*), to be used in considering commerce clause challenges to state taxation authority, stating that such challenges will be upheld if "the tax is applied to an activity with a substantial nexus with the taxing [s]tate, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the [s]tate." Id., 279. The court described the test as a "practical analysis"; id.; and added in *Tyler Pipe Industries, Inc. v. Dept. of Revenue*, 483 U.S. 232, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987), that "the crucial factor governing nexus is whether the activities performed in [the] state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in [the] state for the sales." (Internal quotation marks omitted.) Id., 250.

Thereafter, in *Quill Corp. v. North Dakota ex rel. Heitkamp*, supra, 504 U.S. 301-302, the court revisited the question of whether a mail order house that had no outlets or sales representatives in the state could be required to pay a use tax on goods purchased by in-state users after the North Dakota Supreme Court decided not to follow *Bellas Hess* because of subsequent changes in the economic, commercial and retail environment. Surveying its precedent, the court noted that *Bellas Hess* was not inconsistent with *Complete Auto Transit* because *Bellas Hess* concerned only the first prong of the test and stood for the proposition that "a vendor whose only contacts with the taxing [s]tate are by mail or common carrier lacks the 'substantial nexus' required by the [c]ommerce [c]lause." Id., 311. The court emphasized the continuing validity of the '"sharp distinction [articulated in *Bellas Hess*] between mail-order sellers with [a physical presence in the taxing] [s]tate and those . . . who do no more than communicate with customers in the [s]tate by mail or common carrier as part of a general interstate business'"; id.; explaining that "[w]hether or not a [s]tate may compel a vendor to collect a sales or use tax may turn on the presence in the taxing [s]tate of a small sales force, plant, or office." Id., 315. The court concluded that the "bright line" rule articulated in *Bellas Hess* "firmly establishes the boundaries of legitimate state authority to impose a duty to collect sales and use taxes and reduces litigation concerning those taxes." Id.

On the basis of these principles, at least two jurisdictions concluded in circumstances like those in the present case that a substantial nexus existed between Scholastic and the state under a commerce clause analysis. In *Scholastic Book Clubs, Inc. v. Board of Equalization*, 207 Cal. App. 3d 734, 255 Cal. Rptr. 77 (1989), a California appeals court described the case as "more analogous to *Scripto* than to . . . *Bellas* [*Hess*]"; id., 739; observing that, although the teachers did not have "written agency agreements with [Scholastic], they serve[d] the same function as did the Florida jobbers in

Scripto—obtaining sales within California from local customers for a foreign corporation. In fact, they do more. Unlike the Florida jobbers, the California teachers collect payment from the purchasers, and receive and distribute the merchandise. [Scholastic] not only relies . . . but in fact depends on the teachers to act as its conduit to the students. Moreover, there is an implied contract between [Scholastic] and the teachers [because Scholastic] rewards them with the bonus points for merchandise if they obtain and process the orders. The bonus points are similar to the Florida jobbers' commissions in *Scripto*; the more sales the teachers make, the more bonus points they earn." Id., 739-40.

"[N]either the form of the remuneration, the amount thereof, nor the fact that the teachers . . . were not formally employed by, or dependent [on Scholastic] for their primary income has any legal significance in determining whether they acted as . . . representatives in soliciting orders for [Scholastic's] products in California. Further, unlike the Illinois customers in . . . *Bellas* [*Hess*], the students . . . are not solicited directly through the mail. The only way a student can order books is through a local intermediary—his or her teacher. [Scholastic] is thus exploiting or enjoying the benefit of California's schools and employees to obtain sales." Id., 740. Accordingly, the court concluded that Scholastic and the teachers had an implied agency relationship under California law that justified imposition of the California sales and use tax. Id.

Seven years later, the Kansas Supreme Court examined United States Supreme Court precedent and cases from other jurisdictions and found the reasoning in the California case persuasive. See *In re Scholastic Book Clubs, Inc*., 260 Kan. 528, 920 P.2d 947 (1996). The Kansas court explained: "The facts are similar to the case at bar. . . . Scholastic clearly has more of a connection with Kansas than catalog sales through the mail or by common carrier. Applying the test stated in . . . *Bellas Hess* and *Quill*, Scholastic's use of the Kansas teachers to sell its product to Kansas students provides a substantial nexus with the state of Kansas. Scholastic is a retailer doing business in Kansas. Application of the [Kansas Compensating Tax Act] does not violate the [c]ommerce [c]lause." Id., 546. Like the California court, the Kansas court concluded that, because Scholastic had an implied agency relationship with the teachers, there was no violation of the commerce clause. Id., 541.

The California and Kansas courts concluded that a substantial nexus existed between the retailer and the state because the retailer had an "implied" agency relationship with the teachers. *Scholastic Book Clubs, Inc. v. Board of Equalization*, supra, 207 Cal. App. 3d 737-38; *In re Scholastic Book Clubs, Inc*., supra, 260 Kan. 541. In the present case, we conclude that a

substantial nexus exists between the plaintiff and the state because the teachers are the plaintiff's representatives. The difference in terminology does not affect our analysis. See *Scripto, Inc. v. Carson*, supra, 362 U.S. 211 (contractual tagging of salesmen as "'independent'" had no bearing on their local function of soliciting sales for retailer, the test being nature and extent of retailer's activities). The out-of-state retailer in this case, as well as the California and Kansas cases, is Scholastic, and the facts in all three cases are essentially the same. The trial court in the present case found that approximately 14,000 Connecticut schoolteachers receive and distribute the plaintiff's marketing materials to schoolchildren throughout the state and provide essential administrative services by (1) receiving, compiling and sending all orders and payments to the plaintiff, (2) receiving the plaintiff's products and distributing them to the students, and (3) resolving all complaints and problems arising following delivery of the plaintiff's products. Thus, because the teachers who participate in the program serve as the only means through which the plaintiff communicates with Connecticut schoolchildren, they provide the substantial nexus required to permit imposition of sales and use taxes under the bright-line physical presence rule established in *Bellas Hess* and *Quill*. See *Tyler Pipe Industries, Inc. v. Dept. of Revenue*, supra, 483 U.S. 250 ("activities performed in [the] state on behalf of the taxpayer [must be] significantly associated with the taxpayer's ability to establish and maintain a market in [the] state for the sales" [internal quotation marks omitted]).

* * *

The plaintiff contends that the facts in three cases in which the United States Supreme Court found a substantial nexus underscore the lack of a substantial nexus in the present case. The plaintiff notes that, in *Standard Pressed Steel Co. v. Dept. of Revenue*, 419 U.S. 560, 561, 95 S. Ct. 706, 42 L. Ed. 2d 719 (1975), the vendor had an employee residing in the state of Washington and using a home office as a base of operations to visit in-state customers, and that the employee was assisted by a group of the taxpayer's engineers who visited Washington three days every six weeks, that, in *Scripto, Inc. v. Carson*, supra, 362 U.S. 209, the vendor's commissioned sales agents were operating within the state under the vendor's authority, and that, in *Tyler Pipe Industries, Inc. v. Dept. of Revenue*, supra, 483 U.S. 249, the vendor's in-state sales representatives called on its customers and solicited orders on a daily basis. The plaintiff further notes that *Scripto* was viewed by the court in *Bellas Hess* and *Quill* as representing "[t]he furthest extension of [the state's taxing] power" under the federal constitution; *Quill Corp. v. North Dakota ex rel. Heitkamp*, supra, 504 U.S. 306; see also *National Bellas Hess, Inc. v. Dept. of Revenue*, supra, 386 U.S. 757 ("the case . . . which represents the furthest constitutional reach . . . of a [s]tate's

power to deputize an out-of-state retailer as its collection agent for a use tax is *Scripto*"); and argues that it is not logical to extend the reasoning of *Scripto* to schoolteachers who have no oral or written agreement with the plaintiff to act as sellers of the plaintiff's products and who receive no compensation from the plaintiff for their efforts. We are not persuaded.

We first observe that the language in *Bellas Hess* and *Quill* describing *Scripto* as representing the "furthest" extension of the state's taxing power was no more than an observation concerning the state of the law at that time, and was not necessarily intended to mean that a substantial nexus between the out-of-state retailer and the state could not be found in other, as of yet undefined, circumstances. We also emphasize that the test involves a "practical analysis"; *Complete Auto Transit, Inc. v. Brady*, supra, 430 U.S. 279; and that the court viewed the evolution of its case law as "a retreat from the formalistic constrictions of a stringent physical presence test in favor of a more flexible substantive approach . . . ." (Internal quotation marks omitted.) *Quill Corp. v. North Dakota ex rel. Heitkamp*, supra, 504 U.S. 314. Under this approach, in which we consider the "nature and extent of the activities" of the seller; *Scripto, Inc. v. Carson*, supra, 362 U.S. 211; and whether "the activities performed in [the] state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in [the] state"; *Tyler Pipe Industries, Inc. v. Dept. of Revenue*, supra, 483 U.S. 250; it is clear that Connecticut schoolteachers provide the substantial nexus required under the commerce clause to permit imposition of the taxes at issue in the present case. The fact that there is no oral or written agreement compelling the teachers to serve as agents or sellers of the plaintiff's products and that they receive no direct compensation from the plaintiff is not dispositive. The nature of the program necessarily places the teachers in a position in which they are functioning in much the same way as salesmen, in that they are bringing the plaintiff's products to the attention of the students and are providing them with the means to order, pay for and receive delivery of those products. Moreover, the teachers derive benefits from the program because they earn bonus points that enable them to purchase other items of value from the plaintiff's catalog. Accordingly, under the bright-line rule established in *Bellas Hess* and *Quill* and the "practical analysis" required by United States Supreme Court precedent, we conclude that the activities of the Connecticut schoolteachers who participate in the plaintiff's program provide the requisite nexus under the commerce clause to justify imposition of the taxes at issue in this case.

Scholastic Book Clubs, 38 A.3d at 1194 – 1201.

The Connecticut Supreme Court found that the teachers were representatives of the Taxpayer, whereas the California and Kansas courts found that the teachers were implied agents of the Taxpayer. *Scripto* holds, however, that the technical title given to in-state individuals that perform activities on behalf of or that benefit an out-of-state retailer is irrelevant and "without constitutional significance." *Scripto*, 80 S. Ct. at 621. Rather, "the crucial factor governing nexus is whether the activities performed in (the) state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in (the) state for the sales." *Tyler Pipe*, 107 S. Ct. at 2821. The teachers' activities in Alabama were clearly and significantly associated with the Taxpayer's ability to establish and maintain a market for its sales in Alabama.

In *State of Alabama v. Newbern*, 239 So.2d 792 (Ala. 1970), over 100 individuals in Alabama solicited orders from Alabama customers on behalf of an out-of-state taxpayer. One issue was whether the individuals were agents or salesmen of the taxpayer within the meaning of Title 51, §792, Code of Ala. 1958, the predecessor statute to §40-23-68. That statute required a seller to report and remit use tax to the Department if it "solicits and receives purchases or orders by (an) agent or salesman" operating in Alabama.

The taxpayer argued that the individuals in issue were not its agents or salesmen because they had no technical legal relationship with the taxpayer. The Alabama Supreme Court disagreed:

> We do not think the statute requires a "legal relationship" between seller and solicitor. The main thrust of title 51, §792(c), supra, seems to us simply to require solicitation of orders for the seller by persons within the state who are characterized as 'agents or salesmen." We do not think that the legislature intended a seller conducting such solicitation to avoid collecting the use tax merely by showing that its salesmen failed to come within some technical

> definition of "salesman" or lacked some legal relationship with the out-of-state seller not articulated in the statute.

Newbern, 239 So.2d at 352.

The above holding in *Newbern* follows the U.S. Supreme Court's holding in *Scripto* that the presence of individuals in a state that perform activities associated with and that enhance an out-of-state seller's ability to establish and maintain a market for the seller's sales in the state is sufficient to establish a physical presence nexus, regardless of what name or designation the individuals are given or not given.

In any case, as in the California and Kansas cases involving the Taxpayer, the Alabama teachers were also implied agents of the Taxpayer under Alabama law. In *Graduate Supply House, Inc. v. State of Alabama*, Docket S. 05-751 (Admin. Law Div. Third P.O. 11/20/2007), the taxpayer, a Mississippi corporation, rented caps and gowns in Alabama. The taxpayer did not own property or have employees in Alabama. Four employees of an unrelated business, Balfour, did, however, assist the taxpayer in the rental of the caps and gowns to Alabama students. Specifically, the four employees measured the Alabama students for the caps and gowns, provided the students with the taxpayer's order forms, and collected and remitted the order forms to the taxpayer. Given those facts, the Administrative Law Division, now the Tax Tribunal, held that the employees were implied agents of the taxpayer, thus giving the taxpayer nexus with Alabama.

> The Taxpayer argues that the individuals that measure the students and then submit the completed order forms to the Taxpayer are Balfour representatives, and are not associated with or acting on behalf of the Taxpayer. I disagree.
>
> A written agency agreement is not required in Alabama for an agency relationship to exist. Rather, an agency relationship may be expressed,

> implied, or apparent, and the existence of an agency relationship is a question of fact to be determined under the specifics of each case. *Lawler Mobile Homes, Inc. v. Tarver*, 492 So.2d 297 (Ala. 1986).
>
> Although there is no written agency agreement between the Taxpayer and the Balfour representatives, the facts establish that the representatives are de facto or implied agents of the Taxpayer. They measure the students for the caps and gowns. They also provide the students (or the schools) with the Taxpayer's order forms. They collect the completed order forms and submit them to the Taxpayer. The representatives are clearly acting on behalf of the Taxpayer when performing those duties. The representatives' actions are also tacitly approved by the Taxpayer because approximately 95 percent of the Taxpayer's rentals in Alabama are through the Balfour representatives.
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> * * *
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> In summary, the Balfour representatives and the Taxpayer have at least a tacit agreement or understanding whereby the representatives perform various activities on behalf of the Taxpayer in Alabama. They in turn receive a commission for their activities. The representatives are acting as agents of the Taxpayer, and their actions on behalf of the Taxpayer in Alabama allow the Taxpayer to establish and maintain its business of renting caps and gowns in Alabama. Stated differently, the activities of the Balfour representatives are "significantly associated with the [T]axpayer's ability to establish and maintain a market in (Alabama). . . ." *Tyler Pipe*, 107 S. Ct. at 2821. The Taxpayer thus has nexus with Alabama under the rationale of *Tyler Pipe* and *Scripto*.

Graduate Supply House at 5 – 6.

In *Graduate Supply House*, the Administrative Law Division briefly discussed the Michigan, Kansas, and California cases that involved the Taxpayer, and also other factually similar book club cases. The Division distinguished the facts in *Graduate Supply House* from the facts in the book club cases because while the Balfour representatives received commissions for their activities on behalf of the taxpayer, "the teachers were not compensated by the out-of-state retailers for their activities on behalf of the retailers." *Graduate Supply House* at 8. Upon further review, however, and as discussed below, the

Alabama teachers and parent educators may have financially benefitted, i.e., been compensated, for their activities on behalf of the Taxpayer by receiving the bonus points, which they could use either for the classroom or personally. In any case, and again as discussed below, whether the teachers and parent educators benefitted is irrelevant to the issue. As discussed, what is relevant is that the teachers' activities were essential, necessary, and directly related to the Taxpayer's ability to make sales to customers in Alabama.

The Taxpayer submitted affidavits from three Alabama teachers in support of its position. The teachers assert that they were not agents of the Taxpayer, that they did not consider the bonus points to be compensation to them, and that they participated in the Taxpayer's sales program only because it benefitted the children in their class – "what I do in the classroom is strictly on behalf of my students and for the benefit of the classroom." Munn Affidavit at ¶8.

I do not doubt that most all of the teachers that participate in the Taxpayer's sales program do so primarily if not exclusively for the benefit of their students. But the teachers' reasons or motivations for participating is also irrelevant to the issue. I agree with the Connecticut Supreme Court that "it is the effect of the in-state (teachers') participation in fostering the out-of-state retailer's goal of selling its products, not the (teachers') motivation," that is controlling. *Scholastic Book Club*, 38 A.3d at 1191.

In the California case involving the Taxpayer, the court opined that "[t]he bonus points are similar to the Florida jobbers' commissions in *Scripto*; the more sales the teachers make, the more bonus points they earn." *Scholastic Book*, 207 Cal. App. 3d at

740. The analogy is loose, at best, because there is evidence that at least some of the Alabama teachers used the bonus points exclusively for the benefit of their classroom and their students.

But some teachers may use the points for personal gain or benefit. This is especially true concerning the parent educators that homeschool their children. The Taxpayer admittedly cannot monitor or control how a teacher or a parent educator may use the points. Consequently, a parent educator could easily use the points to purchase $25 gift certificates at Target, Staples, or Michaels, and then use the gift certificates to purchase items unrelated to their children's education. And even if a parent educator used the bonus points to purchase education-related items, the parent educator would still benefit financially because but for the points, the parent educator would have been required to pay for the items purchased using their own money.

In any case, like the teachers' motivation in participating in the Taxpayer's sales program, whether the teachers or parent educators financially benefitted from the bonus points is irrelevant. Again, what is relevant and controlling is whether the teachers' activities in Alabama were significantly associated with the Taxpayer's ability to establish and maintain a market for its sales in Alabama. Clearly they were because but for the teachers' activities in Alabama on behalf of the Taxpayer, the Taxpayer would have had no sales in Alabama.

To summarize, by agreeing to distribute the Taxpayer's materials to their students, the teachers are in substance soliciting or at least promoting sales on behalf of the Taxpayer. The fact that the teachers are not required to do so, may not personally benefit from their Taxpayer-related activities, may also purchase items from the Taxpayer, and are

motivated to help their students and not the Taxpayer, is irrelevant. The teachers also do substantially more than just distribute the Taxpayer's materials. They gather the completed order forms and compile them on a master order form. They then mail the master form and the purchase money to the Taxpayer, receive and distribute the items purchased to the appropriate parties, and then communicate and work with the Taxpayer to resolve any problems that may arise concerning the transactions. The teachers are in substance a voluntary sales force whose activities in Alabama are essential and necessary for the Taxpayer to make sales in Alabama. The presence and activities of the teachers on behalf of or that benefit the Taxpayer thus established a physical presence for the Taxpayer in Alabama sufficient to establish Commerce Clause nexus under existing U.S. Supreme Court guidelines.

The final assessment in issue is affirmed. Judgment is entered against the Taxpayer for use tax and interest of $815,346.79, plus applicable interest from the date the final assessment was entered, February 25, 2014.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2B-2(m).

Entered March 25, 2016.

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BILL THOMPSON
Chief Tax Tribunal Judge

bt:dr
cc: Christy O. Edwards, Esq.
Mary Martin Majors, Esq.
Ralph M. Clements, III, Esq.
Christopher R. Grissom, Esq.
James E. Long, Jr., Esq.
Anne M. Torregrossa, Esq.

David W. Bertoni, Esq.