No. 06-1228

IN THE

Supreme Court of the United States

FIA CARD SERVICES, N.A.,
fka MBNA AMERICA BANK, N.A.,
Petitioner,

v.

TAX COMMISSIONER OF THE STATE OF WEST VIRGINIA,
Respondent.

On Petition for Writ of Certiorari to the West Virginia Supreme Court of Appeals

BRIEF OF TAX FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

Kyle O. Sollie*
Reed Smith LLP
2500 One Liberty Place
1650 Market Street
Philadelphia, PA 19103
(215) 851-8852

Christopher Atkins
Staff Attorney
Tax Foundation
2001 L Street NW,
Suite 1050
Washington, DC 20036
(202) 464-6200

* Counsel of Record

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D.C. 20002

QUESTION PRESENTED

Can a State impose direct taxes, in this case franchise and corporate net income taxes, on a corporate person with no physical connection, no tangible property, and no employees within that State?

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INTEREST OF THE *AMICUS CURIAE*

The Tax Foundation submits this brief as *amicus curiae* in support of Petitioner in the above-captioned matter.[1]

[1] No counsel for a party authored this brief in whole or in part, and no person or entity, other than *amicus curiae*, has made a monetary contribution to the preparation or submission of this brief. Written consent of the Petitioner and Respondent have been obtained and filed with the Clerk of the Court.

The Tax Foundation is a non-profit research organization formed in 1937 to educate taxpayers about sound tax policy. In this regard, the Tax Foundation disseminates information on taxes and promotes tax systems that are simple, fair, and favor economic growth. The Tax Foundation works to further this mission by educating the legal community on economic issues relating to tax law, by educating lawmakers and the public on tax law issues in an understandable and relevant manner, and by advocating that judicial decisions on tax law promote principled tax policy. Accordingly, the Tax Foundation has a direct stake in the outcome of this case.

SUMMARY OF ARGUMENT

No doubt the parties and various *amici* will fully explore the split in authorities—including a split in the highest State courts of appeal on the precise issue in this case. This brief, therefore, will not. Instead, this brief will emphasize the importance of this case to our nation's economy, especially to our financial system and money system. This brief will also discuss what will result if this Court does not hear this case—economic effects that have been studied and reported by economists, commentators, congressional committees and the Board of Governors of the Federal Reserve System itself. This brief will show that, to avoid these effects, this Court should take this case and resolve the issue—indeed, we will show that it is unlikely that Congress will do so. Even if this Court decides not to resolve the tax nexus issue, this Court should take this case and clarify its role, vis-à-vis Congress, in articulating standards for State taxation of interstate commerce.

ARGUMENT

I. UNLESS THIS COURT REAFFIRMS A SINGLE STATE-TAX NEXUS STANDARD, UNCERTAINTY WILL BURDEN INTERSTATE COMMERCE AND ECONOMIC GROWTH.

The parties and other *amici* will undoubtedly elaborate on the split in the authority concerning the question in issue in this case. We will not. As for the split, suffice it to say that with its holding that West Virginia may impose franchise and income taxes on MBNA, the West Virginia Supreme Court of Appeals has departed from a physical presence nexus standard articulated by this Court in *Quill v. North Dakota*, 504 U.S. 298 (1992) (reaffirming physical presence standard in the context of sales and use taxes). In departing from *Quill*, the West Virginia court's ruling conflicts with that of the Tennessee Court of Appeals in *J.C. Penney National Bank v. Johnson*, 19 S.W.3d 831 (Tenn. Ct. App. 1999), *cert. denied*, 531 U.S. 927 (2000) (holding that the State cannot impose franchise or excise taxes on a bank with no physical presence in the State). This conflict will lead to business uncertainty and, ultimately, stunted economic growth. We will focus on the economic effect of this conflict. Our conclusion is that this conflict has important economic consequences and that, as described more fully in Section II, it has been left to this Court to resolve the conflict.

A. The Commerce Clause has been held to prevent state-imposed burdens on commerce and drags on economic growth.

Congress's authority under the Commerce Clause is intended to temper the parochial interests of individual States

that adversely affect the national economy.[2] Indeed, Congress's authority under the Commerce Clause strips the States of authority to burden interstate commerce—even in the absence of congressional action. Congress's Commerce Clause power is intended to avoid tensions among individual States and thus promote the national economy.

With respect to State taxation, this Court has held that for a tax to overcome a Commerce Clause challenge, it must, among other things, be applied to an activity with a "substantial nexus" with the taxing State. *See Complete Auto Transit v. Brady*, 430 U.S. 274, 279 (1977). Under the nexus prong of *Complete Auto*, this Court has stressed that the "Commerce Clause and its nexus requirement are informed . . . by structural concerns about the effects of State regulation on the national economy." *Quill*, 504 U.S. at 312.

In light of this background, this Court articulated a bright-line nexus rule for sales and use taxes, which requires a company to have a physical presence in a State before the State may require the company to collect sales or use tax. "[A] vendor whose only contacts with the taxing State are by mail or common carrier lacks the 'substantial nexus' required by the Commerce Clause." *Id.* at 311. The ruling of the West Virginia Supreme Court of Appeals in this case represents a departure from that physical presence standard. *Tax Commissioner of the State of West Virginia v. MBNA*

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[2] The Commerce Clause of the United States Constitution authorizes Congress to "regulate Commerce … among the several States," U.S. CONST. art. I, sec. 8, cl. 3. There were no similar limitations of State power under the Articles of Confederation, and the resultant trade wars among the States were a significant impetus for the adoption of the Constitution. *See, e.g.*, James Madison, The Federalist No. 42, *in* JAMES MADISON: WRITINGS 235, 238 (Jack N. Rakove ed. 1999) ("A very material object of this power was the relief of the States which import and export through other States, from the improper contributions levied on them by the latter.").

America Bank, N.A., 640 S.E.2d 226, 236 (W.V. 2006) (Benjamin, J., dissenting) ("[T]he majority goes where no court has gone before . . . . "). Since the West Virginia court's ruling is inconsistent with this Court's holding in *Quill* and also conflicts with the rulings of courts in other States, this Court should grant certiorari in order to resolve the confusion over nexus which is affecting the investment decisions of those engaged in interstate commerce.

B. In our increasingly mobile modern economy, uncertainty about nexus rules will burden commerce and create a drag on economic growth.

Businesses throughout our nation's history could always ply their trade across State lines. Today, with new technologies, even the smallest businesses can sell their products and services in all fifty States through the Internet. If such sales can now expose these businesses to tax compliance and liability risks in States where they merely have customers, they will be less likely to expand their reach into those States. Unless this Court articulates a single nexus standard, the conflicting standards will impede the desire and ability of business to use new technology to expand, which harms the nation's economic growth potential.

As new technologies advance and improve, businesses can more easily reach across geographical borders; this makes a bright-line nexus rule regarding interstate commerce more and more important. While the American economy was once defined chiefly by the manufacturing and sales of tangible goods and services, the so-called "New Economy" is defined by enhancements in technology and information. *See, e.g.*, Michael J. Mandel, *You Ain't Seen Nothin' Yet*, BUSINESS WEEK, Aug. 24-31, 1998, at 60 ("There is growing evidence that the U.S. economy is in the early stages of a powerful new wave of innovation. The leading edge is the

information revolution, which permeates every sector of the economy."). This qualitative transformation is leading to a level of economic integration among States that is markedly greater than that in the past. *See, e.g.*, Daniel Shaviro, *An Economic and Political Look at Federalism in Taxation*, 90 MICH. L. REV. 895, 902 (1992) ("Today's far greater set of economic interrelationships among the States, founded above all on drastic reductions in the costs of travel and communication, suggest a far greater elasticity of response to locational tax disparities. Thus, the efficiency consequences of locational disparities probably have grown immensely."). This new wave of interstate economic integration has heavily impacted the financial services industry. "The range of products and services offered by banks and other financial institutions has grown tremendously over the last quarter-century." R. Todd Ervin, *State Taxation of Financial Institutions: Will Physical Presence or Economic Presence Win the Day?*, 19 VA. TAX REV. 515, 521 (2000).

Surprisingly, and counter-intuitively, the West Virginia Supreme Court of Appeals thought a bright-line rule was no longer appropriate for the same reason we think that it is vital—the transformation of the economy. The court stated a belief that the "physical presence test, articulated in 1967, makes little sense in today's world." *MBNA*, 640 S.E.2d at 234. The West Virginia court failed to understand that the importance of the Commerce Clause and its protections for interstate business is only enhanced in an age of economic integration. "Today's more integrated national economy presents far greater opportunities than existed in 1787 for States in effect to reach across their borders and tax nonconsenting nonbeneficiaries." Shaviro, 90 MICH L. REV. at 902.

Indeed, the Commerce Clause itself was fashioned during a period of economic transformation. In the immediate aftermath of the Revolutionary War, the U.S. economy

expanded. "Demand for goods, especially English goods, led to rising prices." Brannon P. Denning, *Confederation-Era Discrimination Against Interstate Commerce and the Legitimacy of the Dormant Commerce Clause*, 94 KY L.J. 37, 44 (2005). Increased trade led to increased State taxation and regulation of trade, which only increased when post-war economic growth later cooled. *See id.* at 40 ("The mid-1780's brought on a severe depression, during which States scrambled to raise revenue. Imposts and duties on commerce became popular, with nearly every State enacting some sort of impost or duty regime."). This economic tension between the States, and the lack of power in Congress to regulate it, led directly to calls for a new Constitution that would include a clear federal power to regulate interstate commerce.

The pressures that motivated the adoption of the Commerce Clause in the 1780s and the pressures that make it relevant in the 21st century are similar: need for revenue caused by either an increase in demand for State services or by lackluster economic growth. *See generally* Andrew Welsh-Huggins, *States Look to Tax on Business for Cash*, ASSOCIATED PRESS, Feb. 17, 2007 (reporting that States are looking to increase taxes on businesses that are "doing business" in their State as a way to raise money for programs). Furthermore, economic transformation and integration has always been a feature of the American economy, even back to the period of the Founding. "Colossal technological bounds, global interdependence, and sustained high growth aren't exceptional. Through most of America's economic history, they've proved the rule." Keith H. Hammonds, *The Optimists Have it Right*, BUSINESS WEEK, Aug. 24-31, 1998, at 146. Regrettably, because economic integration is greater now than it was in 1780, the economic costs of nexus uncertainty are also greater today and can ripple through the economy much more quickly.

This economic transformation means that a failure to

resolve the nexus issue will have adverse impacts on interstate commerce. As some States follow the physical presence rule, and others follow some iteration of the economic presence rule adopted by the West Virginia Supreme Court of Appeals, compliance costs for businesses engaged in interstate commerce will increase. Businesses that merely expand their sales into States that follow the economic presence principle will have to file tax returns in those States, which will require them to understand the local tax base, any applicable tax rates, available tax incentives, and differing apportionment formulas. Most importantly, many State revenue agencies and courts have not adopted one approach or the other, leaving businesses to guess about whether to file and pay taxes or not.

Contrary to the assertion of the West Virginia Supreme Court of Appeals, complying with State business tax systems is no easy task. Though many State and local governments follow some federal rules, "enough differences remain, along with legal or factual issues and compliance requirements unique to the State and local level, to create substantial added compliance costs." Shaviro, 90 MICH. L. REV. at 921. Widespread adoption of vague economic presence standards would only expand these tax compliance costs. *See, e.g.*, Douglas L. Lindholm, *"Old Economy" Tax Systems On A "New Economy" Stage: The Continuing Vitality of the "Physical Presence" Nexus Requirement*, COUNCIL ON STATE TAXATION (Feb. 2003) 1, 28 ("If an economic presence rule were truly in effect today, it would create a compliance burden of truly Brobdingnagian complexity.").[3]

[3] According to statistics from the Internal Revenue Service, all businesses spent 3,078,352,769 man-hours to comply with the federal tax system in 2005. Small businesses accounted for over 1,000,000,000 of these man-hours. *See* J. Scott Moody, Wendy Warcholik, & Scott A. Hodge, *The Rising Cost of Complying with the Federal Income Tax*, TAX FOUNDATION SPECIAL REPORT NO. 138, 1, 8 (Table 5) (Dec. 2005).

This cost of complying with multiple State tax systems, and the resulting economic harm, was at the heart of the *Quill* decision. The Court specifically recognized that economic harm that would come from requiring *Quill* to potentially collect tax in over 6,000 separate tax jurisdictions, all with different tax systems. *See Quill*, 504 U.S. at 313 fn.6. Members of the business community have shared the Court's concern. "[A]ggressive States will always seek to stretch the limits and to impose their own creative definitions to justify taxation most citizens would consider unjust. No small business can possibly cope with the widely varying and ever-changing laws of 50 States, the administrative burdens of keeping records by State, or the costs of preparing and filing multiple returns, nor can we afford to pay inflated tax claims or legal fees required to defend against them." *Business Activity Tax Simplification Act of 2005: Hearing on H.R. 1956 Before the H. Committee on the Judiciary, Subcommittee on Commercial and Administrative Law*, 109th Cong. 24 (2005) (Statement of Carey J. "Bo" Horne, President, ProHelp Systems, Inc.).

Such concerns are equally pressing in this case, where uncertainty over nexus rules will either lead to a decrease in economic expansion or a lower rate of return for those that choose to press ahead. This Court can—and should—act to ensure that interstate commerce is not unduly burdened by this confusion.

C. Confusion over nexus rules entices States to export their tax burden to nonresidents and may lead to retaliation by other States, creating a further drag on the economy.

There are many reasons why West Virginia seeks to tax the income of those who, like the petitioner, have no physical presence there. West Virginia's action is part of a larger trend in State and local tax policy: an attempt to export the tax

burden to non-residents and non-voters. *See, e.g.*, Herbert Kaylor, *The Experience of Several Cities in Implementing a Commuter Tax*, 2004 STATE TAX TODAY 133-2, at 117 (Jul. 12, 2004). Utilizing a wide scope of mechanisms—from increases in rental car taxes, to the rediscovery of gross receipts taxes, to economic nexus schemes like those employed in this case by West Virginia—States are increasingly trying to place more of the tax burden on outsiders.

Exporting the tax burden is not a new idea. States were attempting to do so in the 1780's when the Constitution was adopted. For example, States' unwillingness to cede control over the levying of imposts and duties during that era was "due to the fact that such measures were a way to raise revenue without directly taxing their citizens." Denning, 94 KY. L.J. at 53. However, even if exporting the tax burden constitutes good local politics, the national economy must take precedence. Thus, the courts should "more consistently and coherently bar [unconstitutional] tax exportation." Shaviro, 90 MICH. L. REV. at 897. Unless this Court grants certiorari and resolves the uncertainty over nexus, States will be emboldened in their effort to tax outsiders and retaliate against other States doing the same.

II. CONGRESS HAS DETERMINED THAT THE QUESTION PRESENTED IN THIS CASE IS IMPORTANT, ESPECIALLY IN THE CONTEXT OF A NATIONAL BANK, BUT HAS INDICATED THAT THIS COURT SHOULD DECIDE IT.

In addition to general economic principles, studies authorized by Congress counsel against a nexus rule such as the one articulated by the West Virginia Supreme Court of Appeals. More than simply revealing the adverse impact that such a rule would have, however, this legislative history

exposes Congress's position on this very issue—which is that it should be decided by the courts. This Court should grant certiorari, if not to address the merits of the issue, then to define its own role in regulating interstate commerce *vis-à-vis* Congress.

A. Congressional committees and the Federal Reserve Board agree this is an important question that should be resolved.

In 1969, Congress began to lift historical restrictions on State taxation of national banks.[4] In doing so, Congress feared the consequences for expansive tax nexus for out-of-State financial institutions. *See* S.R. REP. NO. 91-530 (1969), *reprinted in* 1969 U.S.C.C.A.N. 1594, 1596-98 (discussing the "very serious concern" voiced with regard to the scope of State taxation on out-of-State banks). As a result, Congress imposed a seven-year moratorium prohibiting States from imposing any tax on earnings or capital—such as the taxes at issue here—on out-of-State banks.[5] In explaining its

[4] H.R. 7491, 91st Cong. (1969). Prior to 1969, Congress had heavily limited State taxation of national banks in other ways in order to protect them from unfair treatment in comparison to State banks. *See* R.S. § 5219, Mar. 4, 1923, ch. 297; 42 Stat. 1499, Mar. 25, 1926, ch. 88; S.R. REP. NO. 91-530 (1969), *reprinted in* 1969 U.S.C.C.A.N. 1594, 1595 (discussing background and basis for legislation); REPORT OF THE ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, *State Taxation of Banks: Issues and Options*, M-168, Dec. 1989, available at http://www.library.unt.edu/gpo/ACIR/Reports/information/M-168.pdf. However, the cumbersome regulation led to heavy litigation, and by 1969, it was clear that the legislation had backfired. By that time, federal banks actually enjoyed preferential treatment over similar State institutions. *See* S.R. REP. NO. 91-530 (1969), *reprinted in* 1969 U.S.C.C.A.N. 1594, 1595 (discussing background and basis for legislation).

[5] Pub. L. No. 91-156 at § 1(b), 83 Stat. 434 (1969), which continued to restrict States from taxing out-of-State federal banks based on income. In 1973, Congress enacted, until 1976, a prohibition against States imposing "doing business" taxes, including earned income taxes, on any out-of-State banks, both State and federal. Pub. L. No. 93-100 at §7, 87 Stat. 342 (1973). Interestingly, the moratorium did not apply to sales and use taxes, presumably because Congress determined that those taxes would not have such a negative effect on interstate commerce and the

affirmative restrictions, Congress expressed concern that "the expanded taxing powers might be used in a way which could impair the mobility of capital or the economic efficiency of the banking system." H.R. REP. NO. 91-728 (1965) (Conf. Rep.), *reprinted in* 1969 U.S.C.C.A.N. 1601, 1603.

During the moratorium, Congress authorized several studies on the impact that State taxation of out-of-State financial institutions would have on the economy, banking, and money. In doing so, the Senate recognized that "taxation of the transactions of out-of-State depositories raises a number of difficult legal questions as well as operating and administrative problems." S.R. REP. NO. 93-149 (1973), *reprinted in* 1973 U.S.C.C.A.N. 2014, 2020. Imposition of income and franchise taxes on financial institutions could cause "lendable funds to dry up in the taxing State." *Id.* In addition, compliance burdens would be significant. Specifically, the Senate noted that "serious problems" could result "when two or more States claiming jurisdiction to tax use different rules and require different kinds of reports and records." *Id.*

Thus, Congress first authorized a study by the Federal Reserve Board on the "probable effects on the banking systems of the imposition on banks of intangible personal property taxes and those taxes imposed by States on banks whose principal offices are located outside their boundaries." Pub. L. No. 91-156 at § 4, 83 Stat. 434 (1969). Upon review of the Federal Reserve Board report, REPORT OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE BOARD ON STATE AND LOCAL TAXATION OF BANKS (1972) (hereinafter "FEDERAL RESERVE REPORT"), Congress authorized further study by the Advisory Commission on Intergovernmental

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national economy. *Id.* Accordingly, it would be truly bizarre if the nexus standard that applies to sales and use taxes would be more restrictive than the standard that applies to "doing business" taxes like the taxes assessed against MBNA in this case.

Relations ("ACIR"). Pub. L. No. 93-100 at § 7, 87 Stat. 342 (1973) (requiring a study by the ACIR on the "application of State 'doing business' taxes on out-of-State commercial banks, mutual savings banks, and savings and loan associations.").

Both reports cautioned that there would be serious economic consequences if States began to exercise taxing jurisdiction over out-of-State financial institutions the way West Virginia has exercised taxing jurisdiction over MBNA.

It is important to recognize that at the time Congress authorized these studies, the scope of State jurisdiction to tax out-of-State financial institutions was unclear. Both the Federal Reserve Report and the ACIR report acknowledged this ambiguity in the law and predicted that States would assert taxing jurisdiction over entities with no physical connection to the taxing State. In its survey of State tax administrators, the Federal Reserve Board found that once the moratorium was removed, "most States would continue to assert jurisdiction if the out-of-State bank maintained an office in the State, but . . . that jurisdiction might be asserted if lending activity is carried on, even if loans are solicited by traveling personnel from outside the State and are subject to out-of-State approval."[6] FEDERAL RESERVE REPORT at 21-22 (1972). In fact, the Board reported, "Several State tax administrators indicated in response to the Board's survey that, if the question arose, in all likelihood their States would claim to have jurisdiction to tax out-of-State banks on types of lending typically done by banks across State lines." *Id.* at 33, 46. *See also* Supplementary Note to Appendix 10.

In its 1975 report, the ACIR echoed these fears, reporting:

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[6] Notably, the committee apparently believed that, at a bare minimum, the presence of "traveling personnel" was necessary. The West Virginia Supreme Court of Appeals has not required even this thin connection.

> Nearly all depositories engage from time to time in transactions that cross State lines, and many could be subject potentially to out-of-State tax claims under net income or other 'doing business' taxes. The frequency of future exposures may increase, particularly in light of the spreading use of new technologies for customer-bank communications and fund transfers from remote locations.

S. COMM. ON BANKING, HOUSING AND URBAN AFFAIRS, 94TH CONG., REPORT OF THE ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS ON STATE AND LOCAL 'DOING BUSINESS' TAXES ON OUT-OF-STATE FINANCIAL DEPOSITORIES 23 (Comm. Print 1975) (hereinafter "ACIR REPORT"). Both reports detail the real consequences that such expansive taxing jurisdiction would have on the efficient functioning of the nation's banking system. For example, such taxes would create "artificial barriers that will impede the free mobility of capital among the States." FEDERAL RESERVE REPORT at 23. The Board referenced the banking system as a "highly efficient mechanism through which savings accumulated in one part of the country are channeled to borrowers in other parts of the country," *id.*, and explained that "out-of-State banks are able to assist in financing projects in States where, because of legal loan limits or other factors, local resources are insufficient." *Id.* at 24. "Broadly stated, the role of financial institutions is to gather savings from economic units with surpluses and lend them to those needing additional funds." *Id.* at 25. The Board determined that "[a]ll types of financial institutions contribute importantly to the provision of geographic mobility to savings, moving them from localities or regions where they are relatively plentiful and rates of return are low, to areas where they are scarce and rates of return are higher." *Id.* at 27. These flows of funds have "played a strategic role .

. . in promoting overall growth in our economy." *Id.*

In light of this sensitive ebb and flow, the Board determined that, faced with taxes based on any "slight contact with the State," financial institutions might pass the cost of high tax burdens onto customers or curtail multi-State operations, which would threaten to reallocate financing. *See id.* at 23. Such taxes would "tend to divert credit flows away from potential users in those States" and "have an inhibiting effect on the volume of capital investment and on the level of economic activity in those States." *Id.* at 30. The Board feared a "substantial exodus of financing" from particular States. *Id.* at 48.

The Board also cautioned against the presumption that States would consider such consequences before imposing broad-based taxes. "[T]he pressing needs of the States for revenue, however, may prevent adequate consideration of the economic consequences of each new tax proposal." *Id.* at 49. In other words, States would look out for their current parochial interests, not the long-term national interests. "Moreover, once a few States had begun to levy such taxes, this would tend to stimulate enactment of similar taxes in other States as well." *Id.*

Furthermore, uncertainty itself would have negative consequences. The Board reported that for the financial services industry, there is "no clear standard . . . for determining which States….have jurisdiction to tax any given enterprise or activity." *Id.* at 60. The effects of uncertainty and additional compliance costs "may be substantial" and "may become an important factor in decisions to make particular loans or investments." *Id.* at 58. Particularly, unclear taxation of out-of-State banks would likely result in "higher interest rates for borrowers in certain States and a lower volume of total financing." *Id.* at 24. Thus, even the uncertainty surrounding the jurisdictional parameters would lead to an upset in the nation's economic

equilibrium.

As a result, the Federal Reserve Board concluded that legislation would be beneficial to define the limitations of State taxing jurisdiction on financial institutions. It recommended a "substantial tie" test, such that States could tax banks headquartered in their State or with branches in their State. It clarified that its proposal contemplated State taxation of an enterprise which "establishes facilities or maintains staff in a State."[7] *Id.* at 62.

Similarly, the ACIR Report also called for a jurisdictional test based on physical presence within the taxing State. *See* ACIR REPORT at 50-51. Echoing the Board's concerns, the ACIR explained that the proposal was meant to "safeguard the inter-State mobility of credit, savings, and depository investments" and afford financial institutions "a large measure of certainty about the circumstances in which they might be subject to taxation outside their headquarters State." *Id.* at 89-90.

In sum, the studies conducted for Congress over six years in the 1970's warned of the consequences to the economy that would ensue from a lack of clear nexus standards regarding State taxation of out-of-State financial institutions.

B. Congress has determined to leave the question to the courts.

Despite the abundance of evidence establishing the importance of the issue to the national economy, on September 12, 1976, Congress allowed the moratorium on State taxation of out-of-State financial institutions to lapse

[7] The Federal Reserve Board's selection of the phrase "substantial tie" is interesting. Semantically, it is indistinguishable from this Court's "substantial nexus" formulation, which is the subject of this litigation. The Board understood that formulation not merely to be some physical presence, but to be some *permanent* physical presence.

without providing any guidance. At that time, Section 548 of Title 12 went into effect as proposed in 1969. It simply states:

> For the purposes of any tax law enacted under the authority of the United States or any State, a national bank shall be treated as a bank organized and existing under the laws of the State or other jurisdiction in which its principal office is located.

12 U.S.C. § 548. Subsequent bills calling for nexus guidelines were tabled and never enacted. For example, the Interstate Taxation of Depositories Act of 1976, S. 3368, 94th Cong. (1976), was referred to the Senate Committee on Banking, Housing and Urban Affairs on May 4, 1976 and never resurfaced. The Business Activity Tax Simplification Act of 2005, H.R. 1956, 109th Cong. (2005), has similarly stalled, with the last consideration of the bill occurring in July 2006.

C. The courts, including this Court, have stepped into the void; the resulting decisions have correctly favored a physical presence standard, especially for financial institutions.

The courts have filled the void. As discussed above, in 1992, this Court in *Quill* reaffirmed that, under the Commerce Clause, a State may require a corporation to collect sales and use tax only if the corporation has a physical presence in the State. "[T]he *Bellas Hess* rule has engendered substantial reliance and has become part of the basic framework of a sizable industry. The 'interest in stability and orderly development of the law' that undergirds the doctrine of stare decisis, therefore counsels adherence to settled precedent." *Quill*, 504 U.S. at 317, *quoting Runyon v. McCrary*, 427 U.S. 160, 190-91 (1976) (Stevens, J., concurring); *see also National Bellas Hess, Inc. v. Illinois*

Revenue Dept., 386 U.S. 753 (1967).

Two years after *Quill*, Congress passed a significant piece of banking legislation—the Reigle-Neal Interstate Banking and Branching Efficiency Act of 1994. Pub. L. 103-28, 108 Stat. 2338 (1994). That Act allowed banks to branch across State lines, bringing to the fore once again the question of State taxation of financial institutions. Declining the opportunity to impose guidelines in the wake of *Quill* and the Federal Reserve and ACIR reports, Congress explicitly deferred to the courts. Specifically, Congress added subsection (b) to 12 U.S.C. § 1846, providing that States could tax national banks "to the extent that such tax or tax method is otherwise permissible by or under the Constitution of the United States or other Federal law." *Id.* Of course, "otherwise permissible" rules are those that have been, for the most part, set by the courts, especially this Court. Accordingly, Congress affirmatively turned to the courts to define the limits of State taxing jurisdiction over financial institutions. *Cf. Quill*, 504 U.S.at 309 ("[T]he Commerce Clause is more than an affirmative grant of power; it has a negative sweep as well. The Clause, in Justice Stone's phrasing, 'by its own force' prohibits certain State actions that interfere with interstate commerce.") (internal citations omitted).

Following this lead, the Tennessee Court of Appeals, explicitly relying on *Quill*, held in 1999 that J.C. Penney National Bank did not have nexus based solely on borrowers in the State. *J.C. Penney*, 19 S.W.3d 831 (Tenn. Ct. App. 1999), *cert. denied*, 531 U.S. 927 (2000). *But see Lanco, Inc. v. Director, Div. of Taxation*, 908 A.2d 176 (N.J. 2006) (holding that the physical presence standard does not apply with regard to an intangible holding company); *A&F Trademark, Inc. v. Tolson*, 605 S.E.2d 187 (N.C. App. 2004), *cert. denied*, --- U.S. ----, 126 S. Ct. 353 (2005) (same); *Geoffrey, Inc. v. South Carolina Tax Commission*, 437 S.E.2d

13 (S.C. 1993), *cert. denied*, 510 U.S. 992 (1993) (same). Relying on *Quill* and *J.C. Penney*, companies and financial institutions have been operating under the assumption and expectation that they are only subject to tax in a State if they are physically present in the State.

D. A lack of resolution by this Court will disrupt the assumptions and expectations of financial services providers.

Now, four decades after Congress studied the implications of this issue, the fears of the Federal Reserve Board are coming true. States are assessing tax on out-of-State financial institutions whose only in-State activity is lending, such as in *MBNA*. The resulting rules concerning "tax nexus" are unclear and the effects of uncertainty and additional compliance costs will "become an important factor in decisions to make particular loans or investments." FEDERAL RESERVE REPORT at 58. *See also* Lindholm, *"Old Economy" Tax Systems On A "New Economy" Stage: The Continuing Vitality of the "Physical Presence" Nexus Requirement*, at 29-30 ("[C]ompliance with State business activity taxes, particularly corporate income taxes, requires a series of value judgments—usually different from State to State—that create immense complexities for taxpayers and tax administrators alike."). Yet we anticipate that Congress will likely remain silent in the face of this uncertainty, as they have in the past.

Accordingly, this Court should grant the petition for writ of certiorari and resolve the uncertainty regarding this important question.

CONCLUSION

For the foregoing reasons, *Amicus* respectfully requests that this Court grant the petition for writ of certiorari.

Respectfully submitted,

Kyle O. Sollie*
Reed Smith LLP
2500 One Liberty Place
1650 Market Street
Philadelphia, PA 19103
(215) 851-8852

Christopher Atkins
Staff Attorney
Tax Foundation
2001 L Street NW,
Suite 1050
Washington, DC 20036
(202) 464-6200

* Counsel of Record

May 8, 2007