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Subject: Internet Retailer Acting Through Agent Must Collect California Use Tax
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To Our Clients and Friends:

A recent decision by the California Court of Appeals, Borders Online, LLC v. State Board of Equalization, May 31, 2005, illustrates how a state may subject an out-of-state entity to tax based on the activities of an in-state affiliate. As the case shows, affiliate nexus principles continue to produce nonfiling exposure for many taxpayers, particularly in light of technological advances in the way business is conducted.

Borders Online, LLC (hereinafter "Online"), a Delaware company with a Michigan headquarters, did not maintain contacts in California sufficient to directly establish nexus. During the years at issue, Online sold more than \$1.5 million in merchandise over the internet to California customers without collecting or paying California sales or use tax. Per company policy, Online's customers could return purchases to any location of its affiliate, which had stores throughout California.

The court held that the affiliate was performing selling activities on behalf of Online in California because the taking of returns represented an important part of Online's sales process. Moreover, the activities of Online's affiliate (which also included some cross-marketing with Online) were significantly associated with Online's ability to establish and maintain a market in California for Online's sales. Thus, through its affiliate, Online had a sufficient presence in California to justify the imposition of a sales and use tax collection responsibility under the Commerce Clause of the United States Constitution.

The Borders case is a reminder that taxpayers often modify the type or level of activities conducted in a jurisdiction without considering the nexus implications. This can result in a taxpayer unknowingly establishing nexus in a jurisdiction where nexus did not previously exist.

If you have any questions regarding the within, or would like to discuss the application of nexus principles to your company's activities (including the quantification of potential nexus exposure and the benefit that can be obtained by voluntary disclosure), please do not hesitate to contact me.

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