

## Working Group Session II Issues

Relevant text of P.L. 86-272, 15 U.S.C. §381:

(a) **MINIMUM STANDARDS** No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

...

(c) **SALES OR SOLICITATION OF ORDERS FOR SALES BY INDEPENDENT CONTRACTORS**

For purposes of subsection (a), a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance, of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, or tangible personal property.

### **A. Selling tangible personal property over the internet**

The Statement of Information does not expressly address whether sales of tangible personal property over the internet are protected activity under P.L. 86-272.

Assume ordinary internet transactions where the buyer is located in the taxing state and makes a purchase by accessing the website of a remote seller and placing an order. Purchased items are delivered from a location outside of the purchaser's state.

Key questions:

1. Does the internet seller engage in "business activities" in the state where the purchaser is located and accesses the seller's website?

Possible relevant resources:

- (a) Justice Kennedy's concurrence in *Brohl*: sellers without physical presence "may be present in [the taxing] State in a meaningful way."
  - (b) *Wayfair* majority opinion: ". . . a company with a website accessible in South Dakota may be said to have a physical presence in the State via the customers' computers." The opinion also references the "pervasive virtual presence of retailers" in the purchaser's state and the retailer's "substantial virtual connections to the [taxing] State" and states that the South Dakota sales tax statute requires remote sellers to engage in "considerable business in the State."
  - (c) *Northwestern States Portland Cement Co.*, the S. Ct. case which triggered enactment of P.L. 86-272: We conclude that [under the Due Process Clause and the Commerce Clause] net income from the interstate operations of a foreign corporation may be subjected to state taxation provided that the levy is not discriminatory and is properly apportioned to local activities within the taxing State forming sufficient nexus to support the same.
2. If internet sellers engage in "business activities," do those activities extend beyond "the solicitation of orders" (and activities ancillary to the solicitation of orders)?

What are those activities?

Can it be said that internet orders are sent outside State A for approval or rejection if the retailer (or a computer) retains the right after the customer presses the order button to decline the transaction either because of credit/payment issues or for any other reason?

Possible relevant resources:

- (a) Floor statement by Rep. Miller, one of the House managers of the bill that became P.L. 86-272: "[This legislation] is very narrow, indeed. It covers only the single and simple area where a corporation does nothing more within a State than solicit orders."
- (b) *Heublein, Inc. v. South Carolina Tax Comm'n*: "In this statute [i.e., P.L. 86-272], Congress attempted to allay the apprehension of businessmen that 'mere solicitation' would subject them to state taxation."
- (c) Note the different language contained in subsection (a) and in subsection (c) of the statute. Subsection (a), which identifies protected activities of sellers, mentions only solicitation of orders, while subsection (c), which identifies protected activities when the activities are conducted by independent contractors on behalf of sellers, mentions not only solicitation but also "making sales."
- (d) Note that sellers' websites sometimes solicit and receive employment applications, receive and answer product questions after an item is purchased, facilitate product returns and exchanges, accept complaints and resolve disputes, investigate credit-

worthiness, provide information regarding product performance and repairs, provide information for prospective investors, etc. Various in-state activities described by the MTC Statement of Information as “Unprotected Activities” may now occur via sellers’ websites: (7) Investigating, handling or otherwise assisting in resolving customer complaints . . .; (10) Securing deposits on sales; and (12) Hiring, training or supervising personnel, other than personnel involved only in solicitation.

3. Does a seller’s property interest in and/or the use of in-state software (e.g., “apps”) and ancillary data (e.g., “cookies”) that are distributed to or stored on the computers or other physical communications devices of a vendor’s in-state customers exceed the protections of P.L. 86-272? Presumably, such software and cookies may be used to do more than solicit in-state sales.

### **B. Selling digital goods or licensing other intangible property over the internet**

Licensing property or transferring intangibles is already covered by the Statement of Information. Section I states that “[o]nly the solicitation to sell personal property is afforded immunity under P.L. 86-272; therefore, the leasing, renting, licensing or other disposition of tangible personal property, or transactions involving *intangibles*, such as franchises, patents, copyrights, trade marks, service marks and the like, or any *other* type of property are not protected activities under P.L. 86-272.” Section I also states that “[t]he sale or delivery and the solicitation for the sale or delivery of any type of service that is not either (1) ancillary to solicitation or (2) otherwise set forth as a protected activity . . . is not protected under Public Law 86-272 or this Statement.”

Key questions:

1. Should the Statement of Information address how “digital goods” should be characterized for purposes of P.L. 86-272 (i.e., as tangible or intangible personal property), or should this question be left to the states? Current Section VI of the Statement provides that signatory states agree to apply the definition of tangible personal property that exists in the state of destination.
2. How should the Statement of Information address the sale or other transfer of software?
3. What examples of internet transactions involving intangibles and/or services should be added to the Statement of Information?