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IN FOCUS

February 21, 2025

The Evolution of P.L. 86-272's State Income Tax Immunity for Income Derived from Interstate Commerce

Enacted in 1959, P.L. 86-272, 73 Stat. 555 (codified at 15 U.S.C. §§ 381-384), limits the power of states to impose a net income tax on out-of-state sellers who have limited business activities within the state. To fall within P.L. 86-272's protection, an out-of-state seller's in-state business activity must generally be limited to the "solicitation of orders" for the sale of tangible goods, provided that the orders are sent to a location outside the taxing state for approval and the orders are filled by shipment or delivery from a location outside the taxing state. The U.S. Supreme Court has stated that P.L. 86-272's "minimum standards" for when a state can impose a tax on net income derived from interstate commerce are "somewhat less than entirely clear." The Court last interpreted these "minimum standards" in 1992, in *Wisconsin Department of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214 (1992). In *Wrigley*, the Court held that an out-of-state seller would not "forfeit" the tax immunity conferred by P.L. 86-272 if the seller's only in-state activities consisted of the solicitation of orders, activities "entirely ancillary" to solicitation, and de minimis activities. While *Wrigley* addressed a range of issues, states, interstate businesses, and tax commentators recognize a growing disagreement about how P.L. 86-272 should apply to modern business activities, such as an out-of-state seller's interactions with in-state customers over the internet.

This In Focus provides an overview of P.L. 86-272's legislative history, summarizes *Wrigley*, and discusses challenges post-*Wrigley*.

Legislative History

Congressional committees reporting on the bills that served as a basis for P.L. 86-272 described their provisions as "temporary solutions" to the problems arising from three U.S. Supreme Court actions. These actions were a decision in a pair of cases, *Northwestern States Portland Cement Co. v. Minnesota* and *Williams v. Stockham Valves & Fittings, Inc.*, 358 U.S. 450 (1959) (collectively *Northwestern States*); a grant of a motion to dismiss and a denial of certiorari in *Brown-Forman Distillers Corp. v. Collector of Revenue*, 234 La. 651 (1958), *appeal dismissed*, 369 U.S. 28 (1959); and a denial of certiorari in *International Shoe Co. v. Fontenot*, 236 La. 279 (1958), *cert. denied*, 359 U.S. 984 (1959). In *Northwestern States*, the Court ruled that

> net income from the interstate operations of [an out-of-state business] may be subjected to state taxation provided the levy is not discriminatory and is properly apportioned to local activities within the taxing State forming sufficient nexus to support the same.

The Senate Finance Committee explained that the Court's broad language in *Northwestern States* created "considerable concern and uncertainty" as to the type and amount of in-state activities that would be regarded as grounds for a state to impose a tax on an out-of-state seller's income from interstate commerce. The House Judiciary Committee expressed that, although *Northwestern States* might be strictly construed as permitting states to tax an out-of-state seller's income from interstate commerce when the seller had "an office or other fixed business activity within the taxing State," the developments in *Brown-Forman* and *International Shoe* could provide for "solicitation alone [to be] sufficient activity."

Within a year of the Court's actions, P.L. 86-272 became law. P.L. 86-272 provides

> [n]o State . . . shall have power to impose, for any taxable year . . . , 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 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).

It also extends immunity to out-of-state businesses that hire independent contractors with offices in the taxing state to solicit sales or *make sales* of tangible personal property.

Wrigley

The U.S. Supreme Court last addressed the scope of P.L. 86-272 immunity in *Wrigley* in 1991. In *Wrigley*, the Court determined (1) the extent to which the term "solicitation of orders" conferred immunity to out-of-state businesses whose in-state activities "neither explicitly nor implicitly propose[d] a sale" and (2) whether there was a de minimis exception providing state income tax immunity to out-of-state businesses with some in-state activity other than solicitation of orders. The Court ultimately held that the phrase "solicitation of orders" in P.L. 86-272 affords tax immunity to out-of-state businesses performing in-state

activities that are (1) "strictly essential" to making requests for purchases and (2) "entirely ancillary" to requests for purchases. The Court explained "entirely ancillary" activities are "those that serve no independent business function apart from their connection to the soliciting of orders." The Court also ruled that there is not a de minimis exception for an out-of-state business's in-state nonsolicitation activities if those activities establish a "nontrivial additional connection with the taxing state" when "taken together."

In *Wrigley*, Wisconsin contended that six in-state activities were potential grounds to subject Wrigley to a net income tax: the sales representatives' replacement of stale gum; gum supplying through "agency stock checks"; gum, rack, and promotional material storage; storage space rental; "the regional managers' recruitment, training, and evaluation of employees; and the regional managers' intervention in credit disputes." The Court determined that none of these activities "c[ould] reasonably be viewed as requests for orders." However, in-state recruitment, training, and evaluation of sales representatives; the use of in-state hotels and homes for sales-related meetings; and a regional sales manager's intervention in credit disputes were ancillary to solicitation because they facilitated requests for purchases.

The Court ruled for Wisconsin because it found the remaining three in-state activities were not ancillary to solicitation or de minimis. Replacement of stale gum was not ancillary because replacing a spoiled product served an independent business function unrelated to requesting orders. The supplying of gum through agency stock checks, in which Wrigley made retailers pay for the gum supplied, was also not ancillary to solicitation because it served an independent business function—making "actual sales" to consumers rather than soliciting consumers. As the "vast majority" of gum stored in Wisconsin was for replacing stale gum and agency stock checks, the Court held that the storage of gum was not ancillary to solicitation. The activities not ancillary to solicitation fell outside the de minimis exception also, because, when taken together, they "constituted a nontrivial additional connection with the State." The Court reached this conclusion even though the gum sales through agency stock checks accounted for only 0.00007% of annual Wisconsin sales and totaled only several hundred dollars per year.

Post-*Wrigley*

In 2021, the Multistate Tax Commission (MTC), an intergovernmental state tax commission whose mission includes the promotion of "uniform and consistent tax policy and administration among the states," issued an update to its *Statement of Information Concerning Practices of the Multistate Tax Commission and Supporting States Under Public Law 86-272*. The updates to the statement generally provide that out-of-state businesses' interactions with in-state customers via the internet should be considered in-state business activity for the purpose of P.L. 86-272. Some tax commentators contend P.L. 86-272 immunity is eroding as states begin to "effectively follow[] the MTC's approach." They emphasize that the updated statement designates an internet seller's "commonplace activities" as in-state business activities that defeat P.L. 86-272 immunity. These activities include providing post-sale product use assistance to in-state customers via electronic chat or email; inviting in-state website viewers to apply for nonsales positions; using "cookies [to] gather customer search information" to adjust production and inventory; and remotely fixing or upgrading products in-state customers previously purchased by transmitting code or electronic instructions over the internet.

Some recent state supreme court cases might also be viewed as narrowing P.L. 86-272 immunity. In 2024, the U.S. Supreme Court declined to hear the appeal of an Oregon Supreme Court's decision in *Sante Fe Natural Tobacco Company v. Department of Revenue*, 372 Or. 509 (2024). The Oregon Supreme Court held a New Mexico tobacco business's in-state business activities relating to its incentive agreements with wholesalers were not ancillary to solicitation or de minimis. Under the incentive agreements, wholesalers were "contractually obligated to accept and process" orders that the New Mexico business's in-state representatives collected from in-state retailers. In *Uline, Inc. v. Commissioner of Revenue*, 10 N.W.3d 170 (Minn. 2024), the Minnesota Supreme Court ruled that market research activities performed by in-state representatives of a Wisconsin industrial and packaging products business were not ancillary to solicitation or de minimis. The in-state representatives recorded information about competitors, competitors' products bought by their customers, and their customers' "special delivery needs, bulk pricing requests, complaints about product or service quality, [and] need for certain products." Then, they shared that information with the corporate sales department and other departments.

Considerations for Congress

Congress has introduced several legislative measures to clarify the scope of P.L. 86-272 immunity. The Business Activity Tax Simplification Act (BATSA) has been introduced multiple times. BATSA would have extended P.L. 86-272's protection to digital goods and prohibited a state from taxing income derived from interstate commerce unless the business had a physical presence in the taxing state or was domiciled there. The Interstate Commerce Simplification Act would have expanded the definition of "solicitation of orders" to include an activity that facilitates solicitation even if that activity also serves an "independently valuable business function apart from solicitation." Congress might also consider legislation that responds to specific provisions, in the MTC's updated statement, that designate certain activities, including activities conducted over the internet, as not protected under P.L. 86-272.

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