

NOTES

PUTTING THE NEXUS INTO PUBLIC LAW 86-272

Scholars and policymakers frequently debate¹ the states' authority to tax the net income of foreign corporations.² This debate often centers on Public Law 86-272.³ Congress enacted this legislation to exempt foreign corporations from paying net income taxes in states where their activities are limited to "solicitation".⁴ Congress, however, failed to specify in the statute when this exemption applies.⁵ By default, the state courts assumed this burden.⁶ In determining when the "solicitation" exemption applies, courts focus on the type of activities carried out by a foreign corporation within the taxing state.⁷ Quite often, this emphasis on *categorizing* activities generates conflicting interpretations.⁸ As a result, cor-

1. During the last quarter century, state governments increasingly have looked to corporations as a source of needed tax revenues. C. MCLURE, *ECONOMIC PERSPECTIVES ON STATE TAXATION OF MULTIJURISDICTIONAL CORPORATIONS* 7 (1986). The problem of generating revenues has become especially acute under the Reagan Administration, with the relative decrease in the size of the federal government. Of particular importance to the states is the authority to tax the net income of foreign corporations engaged in interstate commerce.

Two primary issues are implicated when a state seeks to tax the net income of a foreign corporation. First, does the corporation have sufficient contacts with the taxing state to permit the state to impose a tax? Second, assuming the state has authority to tax, how should the state "apportion" the corporation's revenues to the activities carried out within the state? Tatarowicz, *State Judicial and Administrative Interpretations of U.S. Public Law 86-272*, 38 *TAX LAWYER* 293, 294 (1985). This Note focuses on the former; the latter is beyond the scope of this Note. In general, a corporation's net income is "apportioned" (divided among states in which the corporation is engaged in business) on the basis of the corporation's sales, property and payroll attributable to a particular state. For a summary of the apportionment methods utilized by the states, see J. HELLERSTEIN, *STATE TAXATION* (1983) [hereinafter HELLERSTEIN]; HARTMAN, *FEDERAL LIMITS ON STATE AND LOCAL TAXATION* §§ 9:16-9:29 (1981) [hereinafter HARTMAN].

2. For the purposes of this Note, a "foreign corporation" is defined as a business incorporated in a state other than that seeking to impose the tax, which business does not maintain its principal place of business inside the taxing state, nor carry out sufficient activities within that state to require it to be "qualified to do business," but which, nevertheless, engages in some business activities within the taxing state. States generally tax the net income of foreign corporations as a measure of the benefits the corporations derive from the state. *See generally* P. HARTMAN, *STATE AND LOCAL GOVERNMENT TAXATION* 63-64 (1953).

3. *See infra* note 58.

4. *See infra* notes 66-71 and accompanying text.

5. Tatarowicz, *supra* note 1, at 293.

6. *Id.*

7. *See infra* notes 63-71 and accompanying text.

8. *See infra* notes 72-74 and accompanying text.

porations engaged in or contemplating multistate business operations face uncertainty when speculating whether states' will tax their net income.⁹

In contrast, foreign corporations seemingly face little uncertainty when anticipating whether a state will tax their gross receipts.¹⁰ In the absence of legislation, the Supreme Court has developed rudimentary guidelines for reviewing the legality of a state's gross receipts tax.¹¹ The Court looks to see whether a sufficient "nexus" exists between the foreign corporation and a taxing state.¹² Specifically, the Court allows the tax if the corporation's *activities as a whole* constitute an established market within the state.¹³ Unlike the state court decisions under Public Law 86-272, the Court's nexus analysis does not focus on the *type* of activities carried out by the foreign corporation. Thus, the Court avoids the ambiguity inherent in categorizing activities.

This Note calls for Congress to amend Public Law 86-272's analysis of state net income taxes by incorporating the nexus test that the Supreme Court uses for state gross receipts taxes. Part I reviews the history of the states' authority to impose a net income tax on foreign corporations and the state court interpretations under Public Law 86-272. Part II exam-

9. In the words of one commentator, "The unfortunate result . . . is that taxpayers are left without an intelligible standard to follow in planning their multistate activities so as to minimize their tax and administrative burdens." Tatarowicz, *supra* note 1, at 324-35. One noted scholar describes the problem of states' authority to tax the net income of corporations engaged exclusively in interstate commerce as "a riddle wrapped in an enigma inside a mystery." Sweeney, *State Taxation of Interstate Commerce Under Public Law 86-272: "A Riddle Wrapped in an Enigma Inside a Mystery,"* 1984 B.Y.U. L. REV. 169, 170 n.5 (1984) (quoting Rep. Emanuel Celler, 105 CONG. REC. 17, 771 (1959)).

Corporations engaged in interstate commerce face the burden of paying taxes in multiple states, as well as keeping abreast of the intricacies of multiple state tax laws. This latter burden may prove to be the more cumbersome, as the time and expense of preparing the tax returns in numerous states may outweigh the incremental income derived from interstate operations. For additional commentary regarding the uncertainty faced by corporations engaged in interstate operations see Sweeney, *supra* at 169; HELLERSTEIN, *supra* note 1, ¶¶ 6.8-.18.

10. For the purposes of this Note, "gross receipts" tax is defined as one imposed by a State on every dollar of sales derived by a foreign corporation from activities carried out within the taxing State.

Prior to 1976, the Supreme Court repeatedly refused to permit the states to tax the gross receipts of a foreign corporation. See *infra* notes 78-108 and accompanying text. Subsequent to 1976, foreign corporations have faced little uncertainty regarding the applicability of a state's gross receipts tax, arguably because the Court has articulated a clear standard for reviewing the legality of such a tax. See *infra* notes 119-28 and accompanying text.

11. See *infra* notes 119-22 and accompanying text.

12. *Id.*

13. *Id.*

ines the Supreme Court's treatment of state gross receipts taxes and summarizes the nexus test adopted by the Court. Part III proposes that Congress amend Public Law 86-272 to incorporate the nexus analysis.

I. TAXING CORPORATE NET INCOME

A. *The Early Focus: Whether States May Tax Corporate Income Derived Exclusively from Interstate Commerce?*

The states' authority to tax the net income of foreign corporations evolved from a series of Supreme Court decisions beginning in 1918. In *Peck & Co. v. Lowe*¹⁴ the Court upheld a federal tax imposed on domestic corporations' net income derived from international commerce.¹⁵ Peck & Co., a domestic corporation engaged in buying goods in the states and reselling them in foreign countries, challenged the tax as unconstitutionally taxing the exportation of goods.¹⁶ In upholding the tax, the Court stated that the Constitution prohibited only taxes imposed directly on the exportation process.¹⁷ Because this net income tax applied at the conclusion of the exportation process, the Court viewed it as a mere indirect tax on the exportation of goods, and therefore legitimate.¹⁸

In *United States Glue Co. v. Oak Creek*¹⁹ the Court broadened *Peck & Co.* to permit states to tax net income of domestic corporations engaged in interstate commerce.²⁰ United objected to a Wisconsin tax on the

14. 247 U.S. 165 (1918).

15. *Id.* at 175. The Federal government subjected every domestic corporation to a tax on a specified per centum of its "entire net income arising or accruing from all sources during the preceding calendar year." Act of October 3, 1913, c. 16, section II, 38 Stat. 166, 172.

16. The corporation based its challenge on article 1, § 9 which includes in part: "No Tax or Duty shall be laid on Articles exported from any State . . ." U.S. CONST. art. 1, § 9, cl. 5.

17. 247 U.S. at 175.

18. *Id.* The *Peck* Court interpreted the Constitution as banning all taxes imposed during the exportation process. While the Court did not define when this process began and ended, it did indicate that taxes levied on activities leading up to exportation (such as a manufacturing tax levied on the value of goods produced in the state) were exempt from the prohibition, as were taxes imposed on post-exportation results (i.e., net income). The Court held that a net income tax "is levied after exportation is completed, after all expenses are paid and losses adjusted, and after the recipient of the income is free to use it as he chooses." *Id.* This holding explained the Court's early distinction between net income taxes and gross receipts taxes imposed on revenues derived by corporations while engaging in business that crossed the state's borders. The Court upheld the net income tax for the aforementioned reason, yet deemed illegal the gross receipts taxes because they were imposed while goods were still in the exportation process.

19. 247 U.S. 321 (1918).

20. *Id.* at 329.

company's net income,²¹ which included receipts from the sale of goods in interstate commerce.²² The company contended that Wisconsin's tax amounted to an unconstitutional interference with commerce between the states.²³ The Court rejected this challenge, holding that Wisconsin's tax entailed only "indirect" and "incidental" burdens on interstate commerce.²⁴

Applying the *United States Glue* rationale, the California Supreme Court, in *West Publishing Co. v. McClogan*²⁵ held that a state may "unquestionably" tax the income of a foreign corporation engaged exclusively in interstate commerce.²⁶ West, a Minnesota based publisher, employed representatives in California to solicit orders, collect payments and handle customer complaints.²⁷ The company bartered for office

21. *Id.* at 323. United States Glue had its principle place of business in Wisconsin. The State of Wisconsin sought to "apportion" (*see supra* note 1) the company's net income on the basis of activities carried out within the state. United States Glue contended that its net income was derived exclusively from interstate commerce, and therefore, that a state could not subject the income to apportionment.

22. *Id.* at 325-26.

23. *Id.* at 323. *See supra* note 21.

24. *Id.* at 329. The Court's holding refined the distinction noted earlier in *Peck & Co.* regarding the legality of the net income tax versus the gross receipts tax. In *Peck & Co.*, the Court distinguished the taxes on the basis of the "direct" burden the gross receipts tax imposed on the "exportation process." *See supra* note 18. In *United States Glue Co.* the Court also focused on the direct versus indirect nature of the burdens imposed by the respective taxes on interstate commerce. Unlike the *Peck & Co.* Court, however, this Court articulated the burden in terms of inhibiting commerce between the states. The Court felt that the gross receipts tax placed an immediate deterrent on businesses engaged in interstate commerce, and that the tax was therefore illegal. In contrast, the state imposed the net income tax after the interstate transactions were completed, and after the corporation had derived a profit. In this situation, the Court found no unconstitutional interference with interstate commerce by the statute. 247 U.S. at 328. This distinction by the Court in its treatment of state net income taxes and gross receipts taxes remained intact until the Court's decision in *Spector Motor Service, Inc. v. O'Connor*, 340 U.S. 602 (1951). For further discussion of *Spector* see *infra* note 101.

25. 27 Cal. 2d 705, 166 P.2d 861, *aff'd per curiam*, 328 U.S. 823 (1946).

26. 27 Cal. 2d at 715, 166 P.2d at 867.

27. 27 Cal. 2d at 705, 166 P.2d at 862. Because West was neither incorporated nor had its principle place of business in California, this case is distinguishable on the facts from *Peck & Co.* and *United States Glue Co.* *See supra* notes 13-21 and accompanying text. As such, the Court's decision to uphold the tax underscores the development of the states' taxing authority since these earlier decisions. Both *Peck & Co.* and *United States Glue Co.* had their principle places of business in the state imposing the tax. The issue in those cases was whether the state could tax revenues derived outside the state by domestic corporations. In contrast, in *West Publishing Co.*, California sought to tax the net income of a "foreign corporation": a business incorporated in Minnesota, and not "qualified" (*see supra* note 1) to do business within California. California's argument for imposing the tax was that West had engaged in substantial income-producing activities within California which were

space in California, but did not lease or own real property in the State.²⁸ West refused to file net income tax returns in California. The company alleged that California's tax unfairly burdened interstate commerce and denied West due process.²⁹ Speaking for a unanimous court, Justice Traynor cited considerable Supreme Court precedent to find that California's net income tax only indirectly affected interstate commerce.³⁰ The court also rejected West's due process challenge.³¹ Concluding that the state provided a market in which West was able to engage in substantial income-producing activities, the court held that these activities fairly subjected the company to taxation within the state.³²

B. The Modern Focus: Whether a Corporation has Sufficient Contacts with the Taxing State to Subject it to the State's Net Income Tax?

The early Court decisions focused on whether a state could tax the net income of foreign corporations engaged in activities within the state.³³

made possible because of the benefits provided by the state (e.g., a court system, protection of persons and property, and a transportation system).

28. 27 Cal. 2d at 707, 166 P.2d at 862.

29. 27 Cal. 2d at 708-09, 166 P.2d at 863, West contended the tax violated the due process clauses on the grounds that the state did not furnish such "protection, opportunities or benefits that would justify a tax." 27 Cal. 2d at 713, 166 P.2d at 866.

30. *Id.* The court reiterated the distinction between net income taxes and gross receipts taxes developed in *United States Glue Co. v. Oak Creek*. See *supra* note 26.

31. 27 Cal. 2d at 713-15, 166 P.2d at 866-67.

32. *Id.* The court quoted extensively from the Supreme Court's decision in *International Shoe Co. v. Washington*, 326 U.S. 310, 321 (1945), in finding that West's activities established such a "presence" as to "subject it alike to taxation by the state and to suit to recover the tax." Specifically, the court found that California provided a market in which West competed with local publishers, the same protection for West's agents as agents carrying on business activities for a principal engaged in intrastate commerce, and a court system in which West could enforce payment for the sale of its publications.

Interestingly, the California Supreme Court's focus on the "substantiality" of West's activities is virtually identical to the test that the Supreme Court subsequently adopted for reviewing the legality of the gross receipts tax. See *Complete Auto Transit v. Brady*, 430 U.S. 274 (1976); and *Tyler Pipe Inds. v. Dept. of Revenue*, 107 S. Ct. 2810 (1987). For further discussion see *infra* notes 111-27 and accompanying text. The Court in *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959), also focused on the "substantiality" of a foreign corporation's activities in upholding a net income tax. See *infra* notes 36-45 and accompanying text. This focus on the corporation's activities as a whole, however, disappeared from the Court's language when Congress enacted Public Law 86-272 in 1959, see *infra* notes 58-75 and accompanying text, and did not resurface until *Complete Auto Transit* in 1976, see *infra* notes 111-20 and accompanying text.

33. See *supra* notes 14-32 and accompanying text.

With this issue answered in the affirmative by *West Publishing*,³⁴ the courts and Congress turned their attention to the question of whether a corporation has sufficient contacts within a State to subject it to state taxation.³⁵

1. *Nexus Under Northwestern*

In *Northwestern States Portland Cement Co. v. Minnesota*³⁶ the Supreme Court identified a pattern of activity which justly subjected the foreign corporation to Minnesota's net income tax.³⁷ In that case, Northwestern, an Iowa corporation, limited its activities in Minnesota to the regular solicitation of orders for the sale of its cement products.³⁸ These orders were transmitted to Iowa for acceptance and, if approved, were filled and delivered from Iowa.³⁹ To further the solicitation process, Northwestern maintained a leased sales office in Minnesota.⁴⁰ However, the company did not own real estate in Minnesota and did not warehouse merchandise in the state.⁴¹ The Court nonetheless upheld Minnesota's power to tax Northwestern. The Court found that the tax was not discriminatory and that the state properly apportioned the tax to local activities within the tax state.⁴² The Court's analysis concentrated on finding a sufficient nexus between the taxing state and the corpora-

34. See *supra* text accompanying notes 25-32.

35. A 1940 Supreme Court decision provided a framework for this analysis. In *Wisconsin v. J.C. Penney*, 311 U.S. 435 (1940), the Court acknowledged that corporations must pay to engage in commerce within a state. The Court held that to determine when a state may justifiably impose a tax, courts must simply ask "whether the state has given anything for which it can ask [a] return." *Id.* at 444. While this question is helpful because it provides a framework to determine if a corporation's contacts with a state are sufficient to justify taxation, it leaves unanswered the more difficult question of exactly what conduct justifies taxation.

36. 358 U.S. 450 (1959). The court decided this case together with *Williams, State Revenue Commissioner v. Stockham Valves & Fittings*. 213 Ga. 713, 101 S.E.2d 197 (1958). Because the facts of the consolidated cases are virtually identical, all references in this Note are to the facts of *Northwestern States*.

37. The Court in *Northwestern* boldly set out to reduce the confusion and controversy that had developed in the wake of some three hundred opinions regarding the taxing power of the states. *Northwestern States*, 358 U.S. at 457-58. The Court accredited this "quagmire" to Congress "not having undertaken to regulate taxation [between the States] . . . and the states having understandably persisted in their efforts to get some return for the substantial benefits they have afforded [interstate commerce]." *Id.* at 457. Despite this admirable objective, the decision in *Northwestern States* sparked a tremendous backlash in Congress. See *infra* notes 55-57 and accompanying text.

38. *Id.* at 454.

39. *Id.*

40. *Id.*

41. *Id.*

42. *Id.* at 452.

tion.⁴³ The Court found such a nexus because Northwestern maintained an office in Minnesota and engaged in regular "solicitation" within the state.⁴⁴

A liberal reading of *Northwestern States* suggests that any state could tax a foreign corporation that carries out regular "solicitation".⁴⁵ This position gained further credibility when the Court denied certiorari for two state Supreme Court cases involving Louisiana's corporate net income tax.⁴⁶ In *Brown-Forman Distillers Corp. v. Collector of Revenue*⁴⁷ and *International Shoe Co. v. Fontenot*⁴⁸ the Louisiana Supreme Court extended the state's power to tax the interstate income of foreign corporations. Both *Brown-Forman* and *International Shoe* maintained representatives in Louisiana.⁴⁹ The representatives for *International Shoe* were responsible for soliciting product orders,⁵⁰ while the representatives in *Brown-Forman* assisted wholesale customers with product marketing.⁵¹ Neither corporation maintained property in Louisiana, authorized its salesmen to accept or reject orders, or made its deliveries from inside the state. Yet, the Louisiana Court sustained the tax.⁵² Several scholars have argued that by denying certiorari for these two cases, the Supreme Court implicitly validated state taxes on foreign corporations whenever the corporations engaged in repeated solicitation within the state.⁵³

2. *Congressional Reaction: Public Law 86-272* (the "Solicitation Law")

The Court's decision in *Northwestern States*, coupled with its subsequent denial of certiorari in *Brown-Forman* and *International Shoe*,

43. *Id.* at 464. The Court looked to the "vigorous and continuous sales campaigns" carried out in the taxing states as evidence of a sufficient nexus to justify the state imposing a tax. *Id.* at 464-65. These campaigns included "the usual sales activities . . . regular solicitation, receipt and forwarding of orders . . . and the promotion of business and good will." *Id.* at 456.

44. Sweeney, *supra* note 9, at 171.

45. See, e.g., Hartman, *Solicitation and Delivery Under P.L. 86-272: An Unchartered Course*, 29 VAND. L. REV. 353, 358 (1976).

46. *Id.*

47. 234 La. 651, 101 So.2d 70 (1958), *cert. denied*, 357 U.S. 28 (1959).

48. 236 La. 279, 107 So.2d 640 (1959), *cert. denied*, 359 U.S. 984 (1959).

49. *Brown-Forman*, 231 La. at 653, 101 So. 2d at 72; *International Shoe*, 236 La. at 289, 106 So. 2d at 640.

50. *International Shoe*, 236 La. at 280, 107 So. 2d at 640.

51. *Brown-Forman*, 231 La. at 653-54, 101 So. 2d at 70.

52. *Brown-Forman*, 231 La. at 659, 101 So. 2d at 72; *International Shoe*, 236 La. at 282, 107 So. 2d at 641.

53. See *supra* note 49. See also Tatarowicz, *supra* note 1, at 296.

prompted a sharp reaction from the business community.⁵⁴ Corporate leaders lobbied Congress for minimum jurisdictional standards to limit the states' power to tax the net income of interstate corporations.⁵⁵ Small and moderate sized corporations in particular contended that the expense of keeping abreast of numerous state tax laws would chill their interest in interstate operations.⁵⁶

Congress responded swiftly by enacting Public Law 86-272.⁵⁷ Voted into law less than a year after the Courts decision in *Northwestern States*, Congress enacted the statute as a "stopgap" measure until it could develop more comprehensive guidelines.⁵⁸

54. Tatarowicz, *supra* note 1, at 296; Sweeney, *supra* note 9, at 172. See also *State Taxation of Interstate Commerce*, 1959: *Hearings Before the Senate Select Committee on Small Business*, 86th Cong., 1st Sess. 1-356; SENATE COMM. ON FINANCE, STATE TAXATION OF INCOME DERIVED FROM INTERSTATE COMMERCE, S. REP. NO. 658, 86th Cong., 1st Sess. 1-3, reprinted in 1959 U.S. CODE CONG. & ADMIN. NEWS 2548, 2549.

55. Hartman, *supra* note 45, at 359 (1976).

56. Tatarowicz, *supra* note 1, at 297. Justice Frankfurter was the first to espouse this opinion in his dissent to *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 476 (1959). Frankfurter believed that the result of *Northwestern* would be to subject small or medium sized corporations doing exclusively interstate business to the burden of filing tax returns in many additional states. This requirement would in turn require corporations to stay informed of the tax laws of all of the states in which they did business. Justice Frankfurter called for the development of a Congressional policy to address the problems posed by the states expanding their taxing power.

57. Pub. L. No. 86-272, Title I, § 101, Sept. 14, 1959, 73 Stat. 555 (codified as amended at 15 U.S.C. § 381 (1982)).

58. Sweeney, *supra* note 9, at 175. The legislative history of Public Law 86-272 suggests that Congress intended to adopt the holding in *Northwestern States*, but rejected the reach of the Louisiana Supreme Court's decisions in *Brown-Forman* and *International Shoe*. See 105 CONG. REC. 16354 (1959); 1959 U.S. CODE CONG. & ADMIN. NEWS 2548; 1 SPECIAL SUBCOMM. HOUSE JUDICIARY COMM., STATE TAXATION OF INTERSTATE COMMERCE, H.R. REP. NO. 1480, 88th Cong., 2d Sess. 438-39 (1964) [hereinafter the *Willis Report*] § 201 and § 202 of Public Law 86-272 provided for a study by the Committee on the Judiciary of the House of Representatives and the Committee on Finance of the United States Senate pertaining to the taxation of interstate commerce by the states. This commission conducted an exhaustive five year analysis of the states' taxing authority. Despite this comprehensive undertaking, Congress failed to adopt the amendments recommended by the commission. This Title was repealed by Pub. L. No. 94-455, § 2121(a), 90 Stat. 1914 (1976). See 15 U.S.C. § 381 (1976), Historical Note. Numerous attempts have been made to either amend the language of Public Law 86-272, or to enact new state tax legislation, including bills proposing restrictions on State and local income, franchise, capital stock, gross receipts, and sales and use taxes. HELLERSTEIN, *supra* note 1, ¶ 6.17. For a summary of proposed legislation see Kust, *State Taxation of Interstate Business - An Obdurate Issue*, 25 TAX EXECUTIVE 143 (1973); Hellerstein, *State Taxation Under the Commerce Clause: An Historical Perspective*, 29 VAND. L. REV. 335 (1976); Mathias Comm., *Interstate Taxation: Hearings on S.2173 Before the Senate Comm. on the Judiciary*, 95th Cong., 1st & 2d Sess. (1977-78); Byrd Comm., *State Taxation of Interstate Commerce and Worldwide Corporate Income: Hearings on S.983 and S.1688 Before the Subcomm. on Taxation and Debt Management Generally of the Senate Comm. on Finance*, 96th Cong., 2d Sess. (1980).

Rather than enumerating the activities that subject a foreign corporation to a state's taxing authority, Public Law 86-272 provides a minimal jurisdictional standard below which the states may not impose a net income tax.⁵⁹ Under the broad language of the statute, states may not tax foreign corporations engaged exclusively in interstate commerce as long as the corporation:

- 1) limits its activities to the "solicitation of orders";
- 2) sends its orders out of state for approval; and
- 3) makes all deliveries from outside the state.⁶⁰

If the corporation fails to satisfy any of these standards or if the corporation owns or leases real property in the state, then the state may tax the corporation.⁶¹

The immunity provided by Public Law 86-272 depends largely on the construction of the term "solicitation of orders".⁶² In the absence of more explicit Congressional guidelines, the state courts have assumed the

59. Called the "solicitation law," this statute used what the Senate Report refers to as "a 'minimum activities' type of approach." (Citing, S. REP. NO. 658, 86th Cong., 1st Sess. 2 (1959)). See Sweeney, *supra* note 9, at 180 n.61.

Note also, that the subtitle for the first section of Public Law 86-272 is "Minimum Standards."

60. 15 U.S.C. § 381(a)(1) (1982). See *supra* note 66.

61. One scholar cautions:

"if a company does not obtain immunity from state taxation through Public Law 86-272, the state may not automatically subject the company to taxation. Rather, the courts must decide, based on established federal and state case law, whether the state can subject the company's income derived from interstate commerce to taxation."

Sweeney, *supra* note 9, at 180-81.

62. HELLERSTEIN, *supra* note 1, ¶ 6.11.

The controversy stemming from Public Law 86-272 is due primarily to the statute's lack of guidance in defining when the "solicitation" exemption applies. See Tatarowicz, *supra* note 1, at 293.

As noted above, see *supra* note 59, a congressionally authorized commission prepared recommendations to provide guidelines for making these determinations. Unfortunately, this effort went for naught, as the recommendations were never adopted. The following is a summary of the recommendations contained in the *Willis Report*:

Activities which will not result in State income tax liability for a foreign corporation:

Usual or frequent activity in the State by employers soliciting orders *without* authority to accept them, or engaging in some form of promotional activity, but not soliciting or taking orders; solicitation activity by nonemployee representatives conducted through an office or other business location in the State or usual or frequent solicitation activity by nonemployee representatives; delivery of goods in the State in company-operated vehicles, regardless of frequency.

Activities which will result in state income tax liability for a foreign corporation:

Usual or frequent activity in the state by employees soliciting orders *with* authority to accept them, or usual or frequent activity in the State by employees engaged in purchasing activity or in the performance of services; the maintenance of any business location in the State, including any kind of office; the ownership of real property in the State, or a stock of goods in a public warehouse or in the hands of a distributor if used to fill orders for the owner's account; the operation of mobile stores in the State.

burden of providing the construction.⁶³ Predictably, the courts are divided over the Act's proper interpretation.⁶⁴ Court decisions in Pennsylvania and Indiana are representative of a "broad" construction.⁶⁵ "Solicitation" under these holdings exempts a corporation from a state's net income tax when the corporation's activities in the state are limited to requests for orders,⁶⁶ acts "incidental" to such requests,⁶⁷ and acts preceding requests.⁶⁸ Conversely, Oregon narrowly interprets "solicitation"⁶⁹ to exempt a corporation only when its activities are limited to

HELLERSTEIN, *supra* note 1, ¶ 6.10 (quoting the *Willis Report*, *supra* note 59).

The *Willis Report* essentially expanded on the Court's holding in *Northwestern*, incorporating much of the factual background of that opinion. See *supra* notes 36-47 and accompanying text. However, these recommendations retained the underlying focus of Public Law 86-272, which is to categorize a business' activities, and to exempt that business from state net income tax if the business does not engage in any "prohibited" activities. To a large degree, the state courts have created judicial guidelines paralleling the recommendations of the *Willis Report*. However, the dividing line between approved and prohibited activities varies from state to state, accounting for much of the uncertainty surrounding Public Law 86-272; see *infra* notes 65-73 and accompanying text.

63. Tatarowicz, *supra* note 1, at 293.

64. "[T]he state court decisions have wound a tortuous and serpentine path in defining 'solicitation' and 'delivery.'" HARTMAN, *supra* note 1, ¶ 9:10 (1981). For a thorough listing and discussion of such cases see Tatarowicz, *supra* note 1, at 303-28.

The state court decisions can be categorized into a "broad" or "narrow" interpretation of the term solicitation. Tatarowicz, *supra* note 1, at 303. Under the "broad" interpretation, the state courts liberally interpret the immunity granted to corporations under the "solicitation law." In contrast, the courts adopting a narrowing interpretation strictly construe the exemption.

65. See *United States Tobacco Co. v. Commonwealth*, 478 Pa. 125, 386 A.2d 471, *cert. denied*, 439 U.S. 880 (1979); see also *Indiana Dep't. of Revenue v. Kimberly-Clark Corp.*, 275 Ind. 378, 416 N.E.2d 1264 (1981), *rev'g*, 375 N.E.2d 1146 (Ind. 1978); but *cf.* *Indiana Dep't. of Revenue v. Continental Steel Corp.*, 399 N.E.2d 754 (Ind. App. 1980).

66. In *United States Tobacco Co. v. Commonwealth*, 478 Pa. 125, 386 A.2d 471 (1979), the Supreme Court of Pennsylvania exempted a New Jersey corporation engaged in the interstate sale of tobacco products from Pennsylvania's corporate income tax. U.S. Tobacco Company maintained missionary representatives in the state to call on wholesalers and retailers of the company's products. These representatives forwarded orders from wholesalers to the company's office in Connecticut and assisted retailers with displays. The company did not own or lease real property in the state. The court held that "solicitation" is not restricted to the act of asking a customer to purchase a product. Activities "inextricably related to solicitation" or "incidental" to asking for an order also fall within the Pennsylvania court's rubric of the "solicitation laws" exemption. 478 Pa. at 140-41, 386 A.2d at 140-41.

67. *Id.*

68. The court in *Indiana Dep't. of Revenue v. Continental Steel Corp.* limited the "solicitation" exemption to "those acts which lead to the placing of orders," 399 N.E.2d at 759. However, the Supreme Court of Indiana implicitly adopted the holding of *U.S. Tobacco Co.* in its more recent decision in *Indiana Dep't. of Revenue v. Kimberly-Clark*.

69. Oregon has played the leading role in developing a narrow interpretation of "solicitation." Powers, *P.L. 86-272 and the Oregon Connection*, 1 INTERSTATE TAX REPORT 3 (1981). Since 1965, Oregon has issued seven opinions under the "solicitation law": *Miles Laboratories, Inc. v. Depart-*

requests for orders.⁷⁰

The ironic result of the enactment of Public Law 86-272 and Congress' subsequent failure to adopt proposed amendments has been a "diversity of interpretations of a federal statute enacted to secure some semblance of certainty."⁷¹ Commentators have called for Congress to provide multistate corporations with strict guidelines so they can anticipate state income tax consequences.⁷² Despite the uncertainty and confusion surrounding Public Law 86-272, both Congress and the Supreme Court have preferred to let the state courts individually fashion these guidelines.⁷³ Although Public Law 86-272 remains intact despite a quarter century of criticism, the deficiencies of the statute are pressing and demand attention.⁷⁴

II. TAXING A CORPORATION'S GROSS RECEIPTS

A. *The Spector Doctrine*

In contrast with its treatment of net income taxes, the Supreme Court has only recently permitted states to tax the gross receipts of foreign corporations.⁷⁵ States historically imposed the gross receipts tax on corpo-

ment of Revenue, 274 Or. 395, 546 P.2d 1081 (1976); *Olympia Brewing Co. v. Department of Revenue*, 277 Or. 309, 511 P.2d 837 (1973), *cert. denied*, 415 U.S. 976 (1974); *Iron Fireman Mfg. Co. v. State Tax Comm'n*, 251 Or. 227, 445 P.2d 126 (1968); *Briggs & Stratton Co. v. State Tax Comm'n*, 3 Or. T.R. 174 (1968); *Hergg Jones Co. v. State Tax Comm'n*, 247 Or. 404, 430 P.2d 998 (1967); *Cal-Roof Wholesale, Inc. v. State Tax Comm'n*, 242 Or. 435, 410 P.2d 233 (1966); *Smith Kline & French Laboratories v. State Tax Comm'n*, 241 Or. 50, 403 P.2d 375 (1965). *Smith Kline, Hergg Jones, Briggs and Olympia* involved foreign corporations engaging in activities in Oregon that sought exemptions from Oregon's net income tax. The other three cases involved Oregon corporations that sought to have their income apportioned in Washington on the basis that their activities in Washington exceeded "solicitation."

70. "[S]olicitation should be limited to those generally accepted or customary acts in the industry which lead to the placing of orders, not those which follow as a natural result of the transaction . . ." *Miles Laboratories, Inc. v. Department of Revenue*, 274 Or. 395, 400, 546 P.2d 1081, 1082 (1976). Oregon distinguished exempt "solicitation" from non-exempt "solicitation" on the basis of pre-sale versus post-sale activities.

71. Hartman, *supra* note 45, at 353. For a summary of the state judicial and administrative interpretations of the "solicitation law," see Tatarowicz, *supra* note 1, at 293. See also HARTMAN, *supra* note 1, ¶¶ 9.11-9.14.

72. See, e.g., Sweeney, *supra* note 9, at 194-99.

73. Hartman, *supra* note 46, at 362; Tatarowicz, *supra* note 1, at 293.

74. See *infra* notes 128-39 and accompanying text.

75. See *infra* note 111 and accompanying text. The gross receipts tax is referred to as a "transaction" tax. States began to use transaction taxes in volume after 1932, in response to increasing demands upon government. Dunham, *Gross Receipts Taxes on Interstate Transactions*, 47 COLUM. L. REV. 211, 215 (1947).

rations in exchange for the privilege of engaging in business activities within the state.⁷⁶ However, until 1976, the Supreme Court consistently refused to permit states to expressly extend this tax to foreign corporations.⁷⁷

One may trace the Court's initial aversion to gross receipts taxes imposed on corporations engaged in interstate commerce to its decisions in *Fargo v. Michigan*⁷⁸ and *Philadelphia Steamship Co. v. Pennsylvania*.⁷⁹ In *Steamship* the State of Pennsylvania imposed a gross receipts tax on the revenues Steamship Co. derived from transporting freight between states.⁸⁰ The Court found the tax invalid (despite Steamship being incorporated in Pennsylvania) because it conflicted with Congress' exclusive power to regulate commerce between the states.⁸¹ For similar reasons, the Court in *Fargo* invalidated a tax imposed by the State of Michigan.⁸² Michigan sought to impose a tax on the gross receipts Fargo derived from engaging in business within the state.⁸³ The court found that imposing the tax on Fargo, a New York based corporation shipping goods into Michigan, unduly burdened interstate commerce.⁸⁴ These decisions established the principle that gross receipts taxes levied on corporations engaged in interstate commerce imposed a direct and impermissible burden on commerce between the states.

Some sixty years later, the Court in *Freeman v. Hewitt*⁸⁵ forcefully reaffirmed its opposition to the gross receipts tax imposed on foreign corporations. The *Freeman* court recognized that subsequent to *Fargo* and *Steamship*, the Court upheld a variety of taxes as legitimate means for a state to recover the cost of enabling corporations to engage in business in the taxing state.⁸⁶ During this period, the Court affirmed states' authority to tax manufacturing,⁸⁷ property,⁸⁸ net income,⁸⁹ consumption⁹⁰ and

76. See, e.g., *Atlantic and Pacific Tele. Co. v. Philadelphia*, 190 U.S. 160, 162 (1903).

77. See *infra* notes 79-110 and accompanying text.

78. 121 U.S. 230 (1887).

79. 122 U.S. 326 (1887).

80. *Steamship*, 122 U.S. at 327.

81. *Id.* at 347.

82. *Fargo*, 121 U.S. at 247.

83. *Id.* at 232.

84. *Id.* at 240.

85. 324 U.S. 249 (1946).

86. *Id.* at 255.

87. *Utah Power & Light Co. v. Post*, 286 U.S. 165 (1932); *American Mfg. Co. v. St. Louis*, 250 U.S. 459 (1919).

88. *Virginia v. Imperial Sales Co.*, 293 U.S. 15, 19 (1934).

licensees.⁹¹ Consequently, in *Freeman*, Indiana sought to analogize to these decisions to permit the imposition of a gross receipts tax on income derived from interstate commerce.⁹² The Court rejected Indiana's effort by distinguishing the gross receipts tax from those taxes previously upheld.⁹³ The Court based this distinction on its belief that the gross receipts tax imposed a direct burden on interstate commerce, while the other taxes imposed only indirect burdens.⁹⁴

In *Spector Motor Service, Inc. v. O'Connor*⁹⁵ the Supreme Court again invalidated a gross receipts tax, but offered a varied rationale. In *Spector* the State of Connecticut levied a gross receipts tax on a Missouri corporation engaged exclusively in the business of interstate freight transportation.⁹⁶ Spector Motor objected to the tax, arguing that it violated the Commerce Clause.⁹⁷ The Court invalidated the tax not because it imposed an economic burden on interstate commerce, but because Connecticut levied it for the "privilege" of engaging in activities which were part of interstate commerce.⁹⁸ Implicitly, the Court held that the gross receipts tax unconstitutionally permitted the states to regulate the basic right of persons to engage in interstate commerce.⁹⁹ Ironically, this shift in reasoning away from reliance on the economic burden on interstate commerce ultimately led to the Court upholding the gross receipts tax.¹⁰⁰

89. See *supra* notes 14-32 and accompanying text.

90. *McGoldrick v. Berwind-White Co.*, 309 U.S. 33, 58 (1940).

91. *Cheney Brothers Co. v. Massachusetts*, 246 U.S. 147 (1919); *St. Louis S.W. Ry. v. Arkansas*, 235 U.S. 350, 364 (1914).

92. 329 U.S. at 255-58.

93. *Id.* at 256-59.

94. *Id.* at 256-57: "What makes the tax invalid is the fact that there is interference by a State with the freedom of interstate commerce." This recognition that gross receipts taxes impose a direct burden on interstate commerce was first noted by the Court in *United States Glue Co. v. Oak Creek*, 247 U.S. 321 (1918). The Court in *United States Glue* differentiated between the gross receipts tax and the net income tax because states imposed the latter tax after interstate transactions were completed, while the former was imposed on the actual transaction (i.e., on every dollar of sales). See *supra* note 24. After *Freeman*, this distinction was short-lived. See *infra* notes 96-101 and accompanying text.

95. 340 U.S. 602 (1951).

96. *Id.* at 603.

97. *Id.* at 604. Spector Motor also objected to the tax on due process grounds. However, the Court invalidated the tax under the commerce clause without addressing the due process issue.

98. *Id.* at 603, 607-10.

99. *Id.* at 610.

100. Prior to *Spector*, the only obstacle preventing the Court from upholding the gross receipts tax was its belief that the tax imposed a direct burden on interstate commerce. See *supra* note 24.

B. *Narrowing the Spector Doctrine*

Implicit in the Court's decisions following *Spector* was the realization that states could make corporations pay their way when engaging in interstate commerce.¹⁰¹ This realization required the Court to balance a corporation's interest in freely engaging in interstate commerce against the states' need to be compensated for enabling the commerce to take place. As a result, the Court began to narrow the *Spector* doctrine to one of draftsmanship and phraseology.¹⁰² The Court increasingly upheld state legislation that in form did not inhibit interstate commerce, but in substance paralleled the taxes invalidated in *Freeman* and *Spector*.¹⁰³ Most notably, in *Railway Express Agency v. Virginia (Railway I)*,¹⁰⁴ the Court invalidated a "privilege" tax levied by Virginia on the gross receipts of interstate corporations.¹⁰⁵ In response, the Virginia legislature reworded the statute to remove the appearance of a tax on the privilege of engaging in interstate commerce.¹⁰⁶ The amended statute imposed a tax on the value of a foreign corporation's "intangible property" within the state, measured by the corporation's gross receipts. The apparent effect of this statute was to continue to tax the corporation's gross receipts.¹⁰⁷ Nevertheless, the Court upheld the statute in *Railway Express*

While the Court acknowledged during this era that states were justified in seeking to recover from foreign corporations the cost of enabling interstate commerce to take place, *see e.g.*, *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938) ("it was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of the state tax burden . . ."), the Court required that recovery take the form of an indirect burden on commerce between the states. In *Spector*, the Court unwittingly enabled itself, a quarter of a century later, to overcome this direct burden obstacle. By focusing on the taxes' interference with the basic privilege to engage in interstate commerce, rather than on its supposed economic burden on such commerce, the Court implicitly shifted the analysis away from the commerce clause to the due process clause. Once this shift became apparent, the Court began to uphold gross receipts taxes whenever taxes were fairly apportioned and did not discriminate against interstate commerce. *See infra* note 110 and accompanying text. However, it was not until *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1976), that the Court expressly overruled *Spector* and gave its official blessing to gross receipts taxes. *See infra* notes 111-20 and accompanying text.

101. *See Complete Auto Transit v. Brady*, 430 U.S. 274, 281 (1976); *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938).

102. *Complete Auto*, 430 U.S. at 281 (citing *Memphis Gas Co. v. Stone*, 335 U.S. 80 (1948)).

103. State legislatures began to enact laws that levied taxes either on property maintained in the taxing state by a foreign corporation (such as railroad cars), or on purely intrastate transactions (such as the transportation of freight by an interstate railroad between two points within the state).

104. 347 U.S. 359 (1954).

105. *Id.* at 369.

106. *See Complete Auto*, 430 U.S. at 284.

107. *Id.* at 284.

Agency, Inc. v. Virginia (Railway II).¹⁰⁸

C. *The Demise of Spector and the Rebirth of Nexus*

During the two decades following *Spector*, the Court increasingly upheld carefully worded gross receipts taxes but stopped short of disaffirming the *Spector* doctrine.¹⁰⁹ This reluctance yielded in *Complete Auto Transit, Inc. v. Brady*¹¹⁰ when a unanimous Court rejected the holding in *Spector* that a state tax on the privilege of doing business is *per se* unconstitutional when applied to interstate commerce.¹¹¹ In *Complete Auto* Mississippi sought to impose a gross receipts tax on a Michigan corporation engaged in the transportation of motor vehicles.¹¹² The motor vehicles were manufactured in Michigan and shipped by rail to Mississippi.¹¹³ From there, Complete Auto transported the vehicles to dealerships in Mississippi.¹¹⁴ Complete Auto claimed that because its transport was only one part of an interstate movement, Mississippi's tax violated *Spector's* prohibition against taxing the privilege of engaging in interstate commerce.¹¹⁵

The Court in *Complete Auto* harshly criticized *Spector* and its progeny, finding that the formalism of *Spector* obscured the "question whether the tax produces a forbidden effect."¹¹⁶ However, the Court implicitly¹¹⁷ ap-

108. 358 U.S. 434, 441 (1959) (*Railway II*). The Court in *Railway II* recognized that the *Spector* doctrine had created a situation where an "otherwise constitutional levy" could be "disable[d]" by the improper use of words or labels. *Id.*

109. See, e.g., *Colonial Pipeline Co. v. Traigle*, 421 U.S. 100, 114 (1975) ("The tax cannot be said to be imposed . . . merely or solely for the privilege of doing interstate business . . . It is, a fairly apportioned and nondiscriminatory means of requiring appellant to pay it's just share of the cost of state government . . ."); *Standard Pressed Steel Co. v. Dep't. of Revenue of Washington*, 419 U.S. 560, 562 (1975) (Court found that the question posed in *Wisconsin v. J.C. Penney*, 311 U.S. 435 (1940), in the present case verged on the "frivolous". See *supra* note 35 for a discussion *J.C. Penney*); *General Motors Corp. v. Washington*, 377 U.S. 436, 440 (1964) ("it is well established that taxation measured by gross receipts is constitutionally proper if it is fairly apportioned." The Court distinguished *Spector* by implying that the State of Washington did not impose its tax for the privilege of doing interstate commerce. *Id.* at 447).

110. 430 U.S. 274 (1976).

111. *Id.* at 288.

112. *Id.* at 276-77.

113. *Id.* at 276.

114. *Id.*

115. *Id.* at 277-78.

116. *Id.* at 288. The Court found that under the *Spector* doctrine, there was no relationship between the decisions of the courts and the economic realities of the taxes under review. *Id.* at 279.

117. The Court's analysis did not proceed beyond the reversal of *Spector* because Complete Auto alleged only that the tax was invalid based on the holding in *Spector*. *Id.* at 288.

proved of the use of a four-part test to review the legality of gross receipts taxes.¹¹⁸ This test focuses primarily on whether a nexus sufficient to justify imposing a tax exists between the foreign corporation and the taxing state. The Court declined to decide whether such a nexus was present in *Complete Auto*.¹¹⁹ However, its reference to this test implied that future decisions reviewing the legality of gross receipts taxes would entail an inquiry into the corporations's *activities as a whole* within the taxing state.

D. Tyler Pipe: *A Further Articulation of the Nexus Test*

In *Tyler Pipe Industries, Inc. v. Dept. of Revenue*¹²⁰ the Court articulated its definition of "nexus": "[W]hether the activities performed in this state on behalf of the taxpayer are *significantly* associated with the taxpayer's ability to establish and maintain a market in this state for the sales"¹²¹ (emphasis added). Tyler, a Texas based manufacturer of steel pipe, conducted business in the State of Washington through an independent contractor.¹²² Tyler did not maintain an inventory of pipe in Washington,¹²³ nor did it own or lease property in the state.¹²⁴ Tyler did, however, derive revenue in excess of \$22 million from the state.¹²⁵ The Court found that the activities engaged in by Tyler's independent contractors were so *significant*, and so *substantial* that they justified Washington's imposition of a gross receipts tax.¹²⁶ This focus on the

118. *Id.* at 287. The four elements of this test are: 1) whether the foreign corporation has a sufficient nexus with the state; 2) whether the tax discriminates against interstate commerce; 3) whether the tax is unfairly apportioned; and 4) whether the tax is unrelated to services provided by the state. For the origins of these factors, respectively, see *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318 (1977); *General Motors Corp. v. Washington*, 377 U.S. 436 (1964); *Illinois Central R. Co. v. Minnesota*, 309 U.S. 157 (1940); *Ingels v. Morf*, 300 U.S. 290 (1937).

119. 430 U.S. at 287. The Court noted *Complete Auto* did not allege that its activities were not "sufficiently connected to the State to justify a tax, or that the tax [was] not fairly related to the benefits provided the taxpayer, or that the tax discriminate[d] against interstate commerce, or that the tax [was] not fairly apportioned." *Id.*

120. 107 S. Ct. 2810 (1987).

121. *Id.* at 215.

122. Brief for Appellant at 3-9, *Tyler Pipe Industries v. Department of Revenue*, 107 S. Ct. 2810 (1987).

123. *Id.*

124. *Tyler Pipe*, 107 S. Ct. at 2821.

125. Brief for Appellant at 3.

126. *Tyler Pipe*, 107 S. Ct. at 2821-22. The activities carried out by the independent contractors on behalf of Tyler which apparently formed this nexus included: 1) keeping track of and advising Tyler about the local market conditions in Washington; 2) calling on wholesalers of Tyler's products and soliciting orders from these wholesalers; 3) handling customer complaints; 4) evaluating a pro-

corporation's *activities as a whole* (rather than on the *type* of activity, as the courts apply under Public Law 86-272) established a straightforward approach to determine when the imposition of a gross receipts tax is justified.

III. PROPOSAL

The state courts' conflicting interpretations under Public Law 86-272 prevent corporate administrators from accurately predicting whether a state has the authority to tax corporate net income. This confusion and uncertainty would be reduced by incorporating into the statute the "nexus" test articulated by the Supreme Court. Essentially, the Court upheld the gross receipts tax in *Complete Auto* for the same reason it sanctioned the net income tax in *Northwestern States Cement*; the Court recognized that it is only fair that foreign corporations be made to pay for the right to engage in interstate business.¹²⁷ Given these complimentary rationales, it is inconsistent for the courts to focus on a corporation's *activities as a whole* when evaluating whether a state may impose a gross receipts tax, while focusing on the *type* of activities when evaluating whether a state may tax net income.

The inability of Public Law 86-272 to address the concerns expressed by Congress in enacting the law is demonstrated by the following hypotheticals. Consider foreign corporation "X", a large business engaged in interstate commerce involving state "Y". Assume state Y imposes a tax on the net income of corporations carrying out business within its borders. Under Public Law 86-272, corporation X may avoid state Y's net income tax by carefully restricting the scope of its salesman's activities to "solicitation",¹²⁸ as defined by that state's judiciary. Theoretically, corporation X may derive millions of dollars of revenue as a result of activities carried out in the state, and yet, if the corporation carefully engineers its agents activities, it will be under no obligation to pay state Y's income tax.

Consider next foreign corporation "Z", a small business engaging in an insignificant volume of transactions within state Y. If the business owns or leases a small office in the state, permits salesmen to approve orders while soliciting in the state, or even makes customer deliveries

spective customer's financial position; and 5) maintaining valuable customer relationships. Brief for Appellant at 3-9, *Tyler Pipe Indus., Inc. v. Department of Revenue*, 107 S. Ct. 2810 (1987).

127. See *supra* note 102 and accompanying text.

128. See *supra* notes 63-71 and accompanying text.

from an inventory pool located within the state,¹²⁹ *Z*'s activities may exceed *Y*'s definition of "solicitation" and *Y* will tax *Z*.

The above hypotheticals point out the problems with Public Law 86-272. Under the Law, a large corporation such as *X* can use its superior financial resources and legal advice to protect itself from the state taxes that Congress intended it to pay.¹³⁰ Conversely, the small business such as *Z*, the very individual Congress sought to protect by enacting Public Law 86-272,¹³¹ generally will not have such resources. As a result, a state may legitimately tax a business which derives only incidental benefits from the state, yet a business which derives significant and substantial revenues from the state (an indice of benefit) may completely avoid that same tax.

In enacting Public Law 86-272, Congress also was concerned with the burden on small businesses of filing multiple state tax returns.¹³² Congress' solution was to exempt corporations engaged in mere "solicitation" from state net income taxation.¹³³ As the above hypotheticals indicate, Public Law 86-272 may not alleviate the burden imposed on small businesses engaging in interstate commerce, because these businesses lack the financial resources to interpret the law in a cost efficient manner. What Public Law 86-272 did accomplish, however, was to create a loophole through which carefully counseled corporations can avoid multistate net income taxation.

The development of tax guidelines focusing on a corporation's activities as a whole within the state, as opposed to an inquiry into the type of activities, would more adequately address congressional concerns with respect to small businesses. The test that courts should use to review the legality of both the gross receipts as well as net income taxes is whether a foreign corporation has engaged in such activities within a state that it may legitimately require the corporation to compensate the state.¹³⁴ If a corporation's activities as a whole have been so significant and so substantial as to enable it to establish a market in the taxing state, then the state should have authority to tax the corporation's receipts and net income.

129. See *supra* note 66.

130. Sweeney, *supra* note 9, at 173-75.

131. *Id.*

132. See *supra* note 57; see also Sweeney, *supra* note 9, at 173-75.

133. See *supra* notes 58-62 and accompanying text.

134. This test should adopt the language of the Court's opinion in *Tyler Pipe*. See *supra* notes 121-27 and accompanying text.

Numerous commentators have called for revisions to the "solicitation law."¹³⁵ None of these commentators have focused on incorporating the nexus standard articulated by the Supreme Court for gross receipts taxation. To reduce the confusion surrounding the "solicitation law" since its enactment, this Note calls for such a revision. Specifically:

1. Congress should revise Public Law 86-272 to expressly authorize the states to tax both net income and gross receipts of corporations engaged purely in interstate commerce;
2. Congress should replace the statute's focus on the type of activity (providing an exemption for mere solicitation) with language focusing on frequency of activity, measured by whether a sufficient nexus exists between the corporation and the state;
3. The language of the statute should underscore the Court's rationale in permitting the states to tax the gross receipts and net income, which is to compensate the states for enabling interstate commerce to take place.

The above recommendations provide only rudimentary guidelines. Congress should supplement these guidelines with examples of activities which it deems so substantial and so significant as to justify imposition of either a gross receipts tax or a net income tax.¹³⁶ To address the concerns of small businesses, Congress should also consider incorporating into the statute an exemption from a state's net income tax for those businesses which derive less than a set amount of revenues.¹³⁷ By adopt-

135. See, e.g., Sweeney, *supra* note 9, at 194-99; Hartman, *supra* note 45. As an alternative to amending the language of P.L. 86-272 to achieve more certainty in state taxation of foreign corporations, a more equitable approach to resolving this uncertainty may be to focus on enunciating workable guidelines for *allocating* taxable income among various states. While there is merit to this approach, this author believes the lack of progress made by the states in recent years in agreeing to such guidelines brings into question the states willingness to sacrifice *any* degree of their taxing autonomy.

136. The factors enumerated in *Tyler Pipe*, see *supra* note 127, should provide the framework for these proposed guidelines. Congress should also give consideration to the recommendations of the *Willis Report*, *supra* note 59. In short, these guidelines must emphasize the corporation's activities as a whole, in contrast with the current emphasis on the type of activities engaged in by the corporation.

Of course, challenges made to a state's net income tax under the proposed revisions to Public Law 86-272 will be resolved on a case-by-case basis, as they are today. However, by providing more comprehensive guidelines regarding the state's authority to tax, this author believes that the frequency of these disputes will be reduced.

137. For the sake of analysis, assume that Congress establishes such a floor at \$100,000. If a business grossing just under \$100,000 a year in a state (which taxes net income at a rate of 5%) was exempt from that state's taxing authority, the loss to the state would be approximately \$500.00 (assuming the business operates on a 10% profit margin). The insignificance of this loss is reflected in the fact that this business will probably have expended many thousands of dollars in the state (with retailers, merchants, suppliers, advertisers, etc.) in order to generate that \$100,000 in revenue.

ing these recommendations, Congress will enable a corporate tax planner to better anticipate when his corporation will be subject to a state's taxing authority.

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These expenditures provide a much more immediate benefit to the citizens of the state than a mere \$500.00 in tax revenue.