



FTB Publication 1050

Application and Interpretation of Public Law 86-272

Guide to Jurisdictional Standards Under the Uniform Division of Income Tax Purposes

Table of Contents

Introduction.....1

Article I Nature of Property Being Sold.....2

Article II Solicitation of Orders and Activities Ancillary to Solicitation.....2

Article III De Minimis Activities.....2

Article IV Specific Listing of Unprotected and Protected Activities.....4

 Section A -- Unprotected Activities

 Section B -- Protected Activities

 Section C -- Activities Conducted via the Internet

 1. Unprotected Activities Conducted Via the Internet

 2. Protected Activities Conducted Via the Internet

Article V Independent Contractors.....5

Article VI Application of Destination State Law in Case of Conflict.....5

Article VII Miscellaneous Practices.....5

 Section A -- Application to Foreign Commerce

 Section B -- Application to Corporation Incorporated in State or to Person Resident or Domiciled in State

 Section C -- Registration or Qualification to do Business

 Section D -- Loss of Protection for Conducting Unprotected Activity during Part of Taxable Year

 Section E -- Application of the Throwback Rule

Introduction

This Publication addresses the application of Public Law (PL) 86-272, 15 U.S.C. §§381-384, which Congress adopted in 1959. PL 86-272 prohibits a state from imposing a net income tax on the income of a person derived within the state from interstate commerce if the only business activities within the state conducted by or on behalf of the person consist of the solicitation of orders for sales of tangible personal property. The protections provided by PL 86-272 only apply to orders that are sent outside the state for acceptance or rejection. If the orders are accepted, they must be filled by shipment or delivery from a point outside the state to maintain PL 86-272 immunity.

In the decades since PL 86-272 was enacted, the way in which interstate business is conducted has changed significantly. Congress, however, has neither created a federal mechanism to provide administrative guidance to taxpayers nor has it updated the statute to indicate how it applies to new business activities. See *Wisconsin Department of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214, 223 (1992) (finding the statute’s minimum standard “to be somewhat less than entirely clear”). The contents of this Publication are intended to serve as general guidance to taxpayers and to provide notice as to how this state will apply the statute.

This Publication is guided by the principle that sovereign authority of states to impose tax will not be preempted unless it is the “clear and manifest purpose of Congress” to do so. *Department of Revenue of Oregon v. ACF*

Industries, Inc., 510 U.S. 332, 345 (1994). See also *Heublein, Inc. v. South Carolina Tax Comm’n*, 409 U.S. 275, 281-82 (1972) (noting that Congress must convey “its purpose clearly” or “it will not be deemed to have significantly changed the Federal-State balance”). The Supreme Court recently opined, in *South Dakota v. Wayfair, Inc.*, construing the Commerce Clause, that an Internet seller “may be present in a State in a meaningful way without that presence being physical in the traditional sense of the term.” 138 S. Ct. 2080, 2095 (2018). Although the *Wayfair* Court was not interpreting PL 86-272, this state considers the Court’s analysis as to virtual contacts to be relevant to the question of whether a seller is engaged in business activities in states where its customers are located for purposes of the statute.

This Publication does not attempt to take into account limitations on the application of business income taxes other than PL 86-272, including those limitations that may be provided under state law.

Finally, PL 86-272 not only affects the determination of whether a state into which tangible personal property is delivered (the “destination state”) may tax the income of the seller, but it also affects the determination of whether the state from which tangible personal property is shipped (the “origin state”) may subject the related receipts to that state’s throwback rule. This state intends to apply this Publication uniformly, irrespective of whether the destination state is determining if it can tax the income of the seller, or whether the origin state is determining if the related receipts are subject to that state’s throwback rule.

Article I. Nature of Property Being Sold

Only the solicitation to sell tangible personal property is afforded immunity under PL 86-272. Therefore, the leasing, renting, licensing or other disposition of tangible personal property, or transactions involving intangible property, such as franchises, patents, copyrights, trademarks, service marks and the like, or any other type of property are not protected activities under PL 86-272.

The sale or delivery, and the solicitation for the sale or delivery, of any type of service is not protected unless it is either: (1) entirely ancillary to solicitation of orders for sales of tangible personal property; or (2) otherwise set forth as a protected activity under Article IV, Section B, of this Publication.

Article II. Solicitation of Orders and Activities Ancillary to Solicitation

For in-state activity to be a protected activity under PL 86-272, it must be limited solely to solicitation (except for *de minimis* activities described in Article III, and those activities conducted by independent contractors described in Article V). Solicitation means (1) speech or conduct that explicitly or implicitly invites an order; and (2) activities that neither explicitly nor implicitly invite an order, but are entirely ancillary to requests for an order. See *Wisconsin Department of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214 (1992).

Ancillary activities are those activities that serve no independent business function for the seller apart from their connection to the solicitation of orders. Activities that a seller would engage in apart from soliciting orders are not ancillary to the solicitation of orders. The assignment of activities to sales personnel does not, merely by such assignment, make those activities ancillary to the solicitation of orders. Additionally, activities that seek to promote sales are not ancillary, because PL 86-272 does not protect activity that facilitates sales; it only protects ancillary activities that facilitate the request for an order. The conducting of activities that are not solicitation or entirely ancillary to solicitation will cause the company to lose its PL 86-272 protection, unless the disqualifying activities, taken together, are either *de minimis* (Article III) or permissible independent contractor activity (Article V).

Article III. De Minimis Activities

De minimis activities are those activities that, when taken together, establish only a trivial connection with the taxing state. An activity conducted within a taxing state on a regular or systematic basis or pursuant to a company policy (whether the policy is in writing or not) normally will not be considered trivial. Whether or not an activity consists of a trivial or nontrivial connection with the state is measured on both a qualitative and quantitative basis. If an activity either qualitatively or quantitatively creates a nontrivial connection with the

taxing state, and is otherwise not protected, then the activity exceeds the protection of PL 86-272.

Establishing that unprotected activities only account for a relatively small part of the business conducted within the taxing state is not determinative of whether the activities are *de minimis*. The relative economic importance of unprotected in-state activities, as compared to protected activities, does not determine whether the conduct of the unprotected activities causes the business to lose PL 86-272 protection.

Article IV. Specific Listing of Unprotected and Protected Activities

The following two lists – Sections A and B – set forth in-state activities that are presently treated by this state as “Unprotected Activities” or “Protected Activities.”

Section A. Unprotected Activities

The following in-state activities (assuming they are not *de minimis*) are not considered solicitation of orders for sales of tangible personal property, entirely ancillary to solicitation, or otherwise protected under PL 86-272:

1. Making repairs or providing maintenance or service to the property sold or to be sold.
2. Collecting current or delinquent accounts, whether directly or by third parties, through assignment or otherwise.
3. Investigating credit worthiness.
4. Installation or supervision of installation at or after shipment or delivery.
5. Conducting training courses, seminars, or lectures for personnel other than personnel involved only in solicitation.
6. Providing any kind of technical assistance or service including, but not limited to, engineering assistance or design service, when one of the purposes thereof is other than the facilitation of the solicitation of orders.
7. Investigating, handling, or otherwise assisting in resolving customer complaints, other than mediating direct customer complaints when the sole purpose of such mediation is to ingratiate the sales personnel with the customer.
8. Approving or accepting orders.
9. Repossessing property.
10. Securing deposits on sales.
11. Picking up or replacing damaged or returned property.
12. Hiring, training, or supervising personnel, other than personnel involved only in solicitation.
13. Using agency stock checks or any other instrument or process by which sales are made by sales personnel.
14. Maintaining a sample or display room in excess of two weeks (14 days) at any one location within the state during the taxable year.
15. Carrying samples for sale, exchange or distribution in any manner for consideration or other value.
16. Owning, leasing, using or maintaining any of the following facilities or property in-state:

- a. Repair shop.
 - b. Parts department.
 - c. Any kind of office other than an in-home office as permitted under Article IV, Sections A, No.18 and B, No.2.
 - d. Warehouse.
 - e. Meeting place for directors, officers, or employees.
 - f. Stock of goods other than samples for sales personnel or that are used entirely ancillary to solicitation.
 - g. Telephone answering service that is publicly attributed to the business or to employees or agents of the business in their representative status.
 - h. Mobile stores, vehicles with drivers who are sales personnel making sales from the vehicles.
 - i. Real property or fixtures to real property of any kind.
17. Consigning stock of goods or other tangible personal property to any person, including an independent contractor, for sale.
18. Maintaining an office or place of business of any kind by an employee or other representative. This does not include an in-home office as explained under Protected Activities (Article IV, Section B, No. 13). An in-home office is one that is located within the residence of the employee or representative that (i) is not publicly attributed to the business or to the employee or representative of the business in an employee or representative capacity, and (ii) so long as the use of such office is limited to soliciting and receiving orders from customers; for transmitting such orders outside the state for acceptance or rejection by the business; or for such other activities that are protected under PL 86-272.

A business will be considered to be maintaining an office or place of business in this state if: 1) there is a public listing within the state for the business or for an employee or representative of the business in such capacity; 2) if there is advertising or business literature that the business or its employee or representative can be contacted at a specific address within the state. However, the normal distribution and use of business cards and stationery identifying the employee's or representative's name, street address, email address, telephone, fax numbers and affiliation with the business shall not, by itself, be considered as advertising or otherwise publicly attributing an office to the business or its employee or representative.

The maintenance of any office or other place of business in this state that does not strictly qualify as an "in-home" office as described above will, by itself, cause the loss of protection.

For the purpose of this subsection it is not relevant whether the business pays directly, indirectly, or not at all for the cost of maintaining an in-home office.

- 19. Entering into franchising or licensing agreements; selling or otherwise disposing of franchises and licenses; or selling or otherwise transferring tangible personal property pursuant to such franchise or license by the franchisor or licensor to its franchisee or licensee within the state.
- 20. Activities performed by an employee who telecommutes on a regular basis from within the state, unless the activities constitute the solicitation of orders for sales of tangible personal property or are entirely ancillary to such solicitation.
- 21. Conducting an activity not listed in Protected Activities (Article IV, Section B), which is not entirely ancillary to facilitating the request for orders, even if the activity helps to increase purchases.

Section B. Protected Activities

The following in-state activities are protected:

- 1. Soliciting orders for sales of tangible personal property by any type of advertising.
- 2. Soliciting of orders for sales of tangible personal property by an in-state resident employee or representative of the business, so long as the employee or representative does not maintain or use any office or other place of business in the state other than an "in-home" office as described in Article IV, Section A, No. 18.
- 3. Carrying samples and promotional materials only for display or distribution without charge or other consideration.
- 4. Furnishing and setting up display racks and advising customers on the display of the business's products without charge or other consideration.
- 5. Providing automobiles to sales personnel for their use in conducting protected activities.
- 6. Passing orders, inquiries and complaints on to the home office.
- 7. Missionary sales activities; i.e., the solicitation of indirect customers for the business's goods. For example, a manufacturer's solicitation of retailers to buy the manufacturer's goods from the manufacturer's wholesale customers is protected if the-solicitation activity is otherwise immune.
- 8. Coordinating shipment or delivery without payment or other consideration and providing information relating thereto either prior or subsequent to the placement of an order.
- 9. Checking of customers' inventories without a charge therefore (for re-order, but not for other purposes such as quality control).
- 10. Maintaining a sample or display room for two weeks (14 days) or less at any one location within the state during the taxable year.
- 11. Recruiting, training or evaluating sales personnel, including occasionally using homes, hotels or similar places for meetings with sales personnel.
- 12. Mediating direct customer complaints when the purpose thereof is solely for ingratiating the sales

personnel with the customer and facilitating requests for orders.

13. Owning, leasing, using or maintaining personal property for use in the employee or representative's "in-home" office or automobile that is limited to the conducting of protected activities. Therefore, the use of personal property such as a cellular telephone, facsimile machine, duplicating equipment, personal computer, and computer software that is limited to the carrying on of protected solicitation and activity entirely ancillary to such solicitation will not, by itself, remove the protection.

Section C. Activities Conducted Via the Internet

To determine whether a seller of tangible personal property via the Internet is shielded from taxation by PL 86-272 requires the same general analysis as sellers of tangible personal property by other means. Thus, an Internet seller is shielded from taxation in the customer's state if the only business activity it engages in within that state is the solicitation of orders for sales of tangible personal property, which orders are sent outside that state for approval or rejection, and if approved, are shipped from a point outside of that state.

If the seller's activities within a state extend beyond solicitation of orders for sales of tangible personal property, and are neither entirely ancillary to solicitation nor de minimis, PL 86-272 does not shield the seller from taxation by the customer's state.

As a general rule, when a business interacts with a customer via the business's website or app, the business engages in a business activity within the customer's state. However, for purposes of this Publication, when a business presents static text or photos on its website, that presentation does not in itself constitute a business activity within those states where the business's customers are located.

Following are examples of activities conducted by a business that operates a website offering for sale only items of tangible personal property, unless otherwise indicated. In each case, customer orders are approved or rejected, and the products are shipped from a location outside of the customer's state. The business has no contacts with the customer's state other than what is indicated.

(a) Unprotected Activities Conducted Via the Internet

1. The business regularly provides post-sale assistance to in-state customers via either electronic chat or email that customers initiate by clicking on an icon on the business's website. For example, the business regularly advises customers on how to use products after they have been delivered. This in-state business activity defeats the business's PL 86-272 immunity in states where the customers are located because it does not

constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

2. The business solicits and receives on-line applications for its branded credit card via the business's website. The issued cards will generate interest income and fees for the business. This in-state business activity defeats the business's PL 86-272 immunity in states where the on-line application for cards is available to customers because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

3. The business's website invites viewers in a customer's state to apply for non-sales positions with the business. The website enables viewers to fill out and submit an electronic application, as well as to upload a cover letter and resume. This in-state business activity defeats the business's PL 86-272 immunity in the customer's state because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

4. The business places Internet "cookies" onto the computers or other electronic devices of in-state customers. These cookies gather customer search information that will be used to adjust production schedules and inventory amounts, develop new products, or identify new items to offer for sale. This in-state business activity defeats the business's PL 86-272 immunity because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

5. The business remotely fixes or upgrades products previously purchased by its in-state customers by transmitting code or other electronic instructions to those products via the Internet. This in-state business activity defeats the business's PL 86-272 immunity because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

6. The business offers and sells extended warranty plans via its website to in-state customers who purchase the business's products. Selling, or offering to sell, a service that is not entirely ancillary to the solicitation of orders for sales of tangible personal property, such as an extended warranty plan, defeats the business's PL 86-272 immunity—see Article I, Nature of Property Being Sold.

7. The business contracts with a marketplace facilitator that facilitates the sale of the business's products on the facilitator's on-line marketplace. The marketplace facilitator maintains inventory, including some of the business's products, at fulfillment centers in various

states where the business's customers are located. This maintenance of the business's products defeats the business's PL 86-272 immunity in those states where the fulfillment centers are located—see Article V, Independent Contractors.

8. The business contracts with in-state customers to stream videos and music to electronic devices for a charge. This in-state business activity defeats the business's PL 86-272 immunity because streaming does not constitute the sale of tangible personal property for purposes of PL 86-272—see Article I, Nature of Property Being Sold.

(b) Protected Activities Conducted Via the Internet

1. The business provides post-sale assistance to in-state customers by posting a list of static FAQs with answers on the business's website. This posting of the static FAQs does not defeat the business's PL 86-272 immunity because it does not constitute a business activity within the customers' state.

2. The business places Internet "cookies" onto the computers or other devices of in-state customers. These cookies gather customer information that is only used for purposes entirely ancillary to the solicitation of orders for tangible personal property, such as: to remember items that customers have placed in their shopping cart during a current web session, to store personal information customers have provided to avoid the need for the customers to re-input the information when they return to the seller's website, and to remind customers what products they have considered during previous sessions. The cookies perform no other function, and these are the only types of cookies delivered by the business to its customers' computers or other devices. This in-state business activity does not defeat the business's PL 86-272 immunity because it is entirely ancillary to the in-state solicitation of orders for sales of tangible personal property.

3. The business offers for sale only items of tangible personal property on its website. The website enables customers to search for items, read product descriptions, select items for purchase, choose among delivery options, and pay for the items. The business does not engage in any in-state business activities that are not described in this example, such as the activities described in Article IV, Section C, Unprotected Activities, examples a-h. This business activity does not defeat the business's PL 86-272 immunity because the business engages exclusively in in-state activities that either constitute solicitation of orders for sales of tangible personal property or are entirely ancillary to solicitation.

Article V. Independent Contractors

PL 86-272 provides protection to certain in-state activities if conducted by an independent contractor that

would not be afforded if performed by the business or its employees or other representatives. Independent contractors may engage in the following limited activities in the state without the business's loss of immunity:

1. Soliciting sales.
2. Making sales.
3. Maintaining an office.

Sales representatives and others who represent a single principal are not considered to be independent contractors.

Maintenance of a stock of goods in the state by the independent contractor under consignment or any other type of arrangement with the business, except for purposes of display and solicitation, removes the protection.

Performance of unprotected activities by an independent contractor on behalf of a seller, such as performing warranty work or accepting returns of products, also removes the statutory protection.

Article VI. Application of Destination State Law in Case of Conflict

In determining which state is to receive the assignment of the receipts at issue, preference is given to any clearly applicable law, regulation or written guideline that has been adopted by the destination state. However, except in the cases of the definition of what constitutes "tangible personal property," this state is not required by this Publication to follow any other state's (including the destination state's) law, regulation or written guideline if it determines that to do so (i) would conflict with its own laws, regulations, or written guidelines and (ii) would not clearly reflect the income-producing activity of the business within its borders.

Notwithstanding any provision set forth in this Publication to the contrary, this state will apply the destination state's definition of "tangible personal property" to determine the application of PL 86-272 as it relates to the origin state's throwback rule, if any. If the destination state lacks a definition that would enable a determination of whether the sale in question is a sale of "tangible personal property," then each state may treat the sale in any manner that would clearly reflect the activity of the business within its borders.

Article VII. Miscellaneous Practices

A. Application to Foreign Commerce.

PL 86-272 specifically applies, by its terms, to "interstate commerce" and does not directly apply to foreign commerce. For purposes of PL 86-272, "interstate commerce" includes commerce between the 50 states and The Commonwealth of Puerto Rico.

B. Application to Corporation Incorporated in State or to Person Resident or Domiciled in State.

The protection afforded by PL 86-272 does not apply to a corporation incorporated under the

laws of the taxing state or to a person who is a resident of or domiciled in the taxing state.

C. Registration or Qualification to do Business.

If a business's only connection to this state is that it registered or qualified to do business within this state, it will not forfeit the protection that may otherwise apply under PL 86-272 in this state. Seeking to use or protect any additional benefit under state law through engaging in other activity not protected under PL 86-272 (such as protecting a trade secret or corporate name) will forfeit the protection.

D. Loss of Protection for Conducting Unprotected Activity during Part of Taxable Year.

The protection afforded by PL 86-272 is determined on a taxable year by taxable year basis. Therefore, if at any time during a taxable year a business conducts activities that are not protected under PL 86-272, the business will not be considered protected under PL 86-272 for the entirety of that year.

E. Application of the **Throwback** Rule.

The Franchise Tax Board's multi-entity apportionment formula rules are as follows:

For taxable years beginning on or after April 22, 1999 and for taxable years beginning before January 1, 2011, California followed the administrative practice of applying the Joyce rule.

1. For purposes of determining which sales are included in the California sales factor numerator, sales of tangible personal property delivered or shipped to a purchaser in California will be included in the numerator only if the selling corporation is taxable in California.
2. Sales of tangible personal property delivered or shipped from California to other states are to be assigned to this state under the throwback rule only when the selling corporation is itself not taxable within the destination state.
3. The California property, payroll, and sales of those corporations within a unitary group (property, payroll, and single-weighted sales for certain entities with qualified business activities, see R&TC section 25128) that are taxable in this state will be taken into account in the apportionment of business income to this state.

For taxable years beginning on or after January 1, 2011, California applies the *Finnigan* rule (R&TC section 25135 (b).)

1. For purposes of determining which sales are included in the California sales factor numerator, sales of tangible personal property delivered or shipped to a purchaser in California will be included in the numerator if any member of the combined reporting group is taxable in California.

2. Sales of tangible personal property delivered or shipped from California to other states are to be assigned to this state under the throwback rule only when no member of the seller's unitary group is taxable within the destination state.

3. Treatment by Taxable Years:

- a. For taxable years beginning on or after January 1, 2011 and before January 1, 2013:
 - 1) For taxpayers not electing single-sales factor, the California property, payroll, and sales of each corporation within a unitary group (property, payroll and single-weighted sales for certain entities with qualified business activities, see R&TC section 25128) will be taken into account in the apportionment of business income to this state, including amounts attributable to entities exempt from taxation in this state because of PL 86-272. The total business income thus apportioned to California will be assigned to the individual corporations taxable by this state.
 - 2) For taxpayers electing single-sales factor, the California sales of each corporation within a unitary group (property, payroll and single-weighted sales for certain entities with qualified business activities, see R&TC section 25128) will be taken into account in the apportionment of business income to this state, including amounts attributable to entities exempt from taxation in this state because of PL 86-272. The total business income thus apportioned to California will be assigned to the individual corporations taxable by this state.
- b. For taxable years beginning on or after January 1, 2013, the California sales of each corporation within a unitary group (property, payroll and single-weighted sales for certain entities with qualified business activities, see R&TC section 25128) will be taken into account in the apportionment of business income to this state, including amounts attributable to entities exempt from taxation in this state because of PL 86-272. The total business income thus apportioned to California will be assigned to the individual corporations taxable by this state.

Connect With Us

Web: ftb.ca.gov

Phone: 800.852.5711 from 8 AM – 5 PM weekdays, except state holidays

916.845.6500 from outside the United States

California Relay Service: 711 or 800.735.2929 for persons with hearing or speaking limitation