

## Oregon Considers Controversial Tax Rules for Internet Sellers

The Oregon Department of Revenue (“Department”) is considering a controversial policy from the Multistate Tax Commission (“MTC”) eroding a longstanding federal law limiting the reach of state income taxes for businesses shipping goods to another state. The Department is convening a rules advisory committee (“RAC”) to gauge the reaction of stakeholders.

### Takeaway

- Oregon may become the first state in the country to formally adopt a sweeping change to the way states tax out-of-state businesses.
- Federal Public Law 86-272 insulates out-of-state businesses from state income taxes if their only activity is soliciting tangible property sales.
- The proposed state policy, originating from the Multistate Tax Commission, asserts the federal law no longer applies to a company with a functional website engaging with its customers.
- In a public meeting on Tuesday, Aug. 23, stakeholders questioned whether it is appropriate for the Oregon Department of Revenue to adopt the expansive policy change via rule.

### Background

Public Law (“PL”) 86-272, also known as the Interstate Income Tax Act of 1959, insulates a business from state income taxes if its only connection to the state is soliciting tangible property sales. In other words, an out-of-state online retailer is not subject to state tax obligations in the customer’s state if their only activity is soliciting sales and shipping orders.

The federal law has driven substantial tax controversy in recent decades, especially with the emergence of digital commerce. For decades, state tax agencies mostly respected the federal law and acknowledged it to shield small businesses from tax obligations if their only activity in the state was fulfilling orders. In recent years, however, state tax agencies have sought to create hurdles and traps for businesses that whittle away the distinction between out-of-state and in-state activities.

### Multistate Tax Commission’s “Revised Statement” on PL 86-272

In 2021, the MTC, an intergovernmental state tax agency comprised of state taxing authorities, [revised its statement](#) interpreting PL 86-272 for activities conducted over the Internet. In its

statement, the MTC says, “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.” Under the new interpretation, the MTC asserts the federal law no longer applies to a company with a functional website engaging with its customers. Since a functional website is crucial to running an online business, the policy unilaterally eviscerates the immunity.

The policy relies on an impractical notion that a business offering assistance over the Internet is comparable to sending an employee to the customer’s location for tax purposes. That position contradicts longstanding practices and case law governing the immunity from state tax obligations. For example, the courts have long held that a business can provide customer support over the phone without triggering state tax obligations. Notably, the MTC guidance maintains the protections for activities over the telephone but not the same activities over digital communication. The result is vastly different tax rules for effectively the same activity.

### **Most States Have Not Acted on the MTC’s Policy**

Currently, California and New York are the only states to take official actions to adopt the MTC’s controversial policy. It is worth noting that neither of those states provided a public forum for businesses and tax practitioners to air their grievances with the policy. Conversely, Oregon is seeking input from stakeholders before drafting a formal rule, providing the first real opportunity for parties to engage over the issue.

### **Stakeholders Question Oregon’s Authority to Adopt Policy by Rule**

During the first meeting of the RAC on Tuesday, Aug. 23, RAC members raised abundant questions about Oregon’s adoption of the MTC policy. In particular, **does the Department even have the statutory authority to adopt the policy by rule?** With only a few words in the governing statutes for the state’s corporate activity tax, Oregon law is utterly silent on the tax immunity provided by PL 86-272. Additionally, the Department has never adopted a regulation articulating the law’s protected or unprotected business activities. Since the policy is a broad departure from current practice, stakeholders questioned whether it is appropriate for the Department to make such a drastic policy change with its regulatory powers.

RAC members also questioned whether the change is appropriate on policy grounds. Many state tax codes provide a readily ascertainable threshold to determine if the state’s business payroll, property, or sales are substantial enough to trigger state tax obligations. This policy, also known as factor-presence nexus, is recommended by the MTC. Oregon does not include a factor-presence nexus rule in its tax statutes. If Oregon adopted the MTC’s new interpretation of PL 86-272, any online retailer selling a good in the state could trigger state tax obligations with a single sale, including small retailers on platforms like Etsy and eBay.

Additionally, stakeholders raised concerns about the coexistence of the MTC policy and existing laws. Under current law, Oregon requires in-state companies to treat sales made in other states that are not taxable as if they were sales made in Oregon under a policy known as “throwback.” If Oregon adopts the MTC policy, it must eliminate the throwback requirement to make its tax system legally consistent. Although repealing the throwback policy is a preferred

reform for many taxpayers, the Department does not have the authority to create or revoke a tax statute.

Finally, the Department was asked to reconsider the appropriateness of state action, either a rule or legislation, nullifying a federal law and the judicial risks accompanying such an aggressive position. Since very few states have adopted the policy and there is no case law dictating its constitutionality, does Oregon want to put a target on its back for the next contentious state tax controversy? RAC members advised that if the MTC or states believe the immunity protections are outdated and need revisions to reflect contemporary business practices, they should lobby Congress to change the statute.

The Department has scheduled two additional meetings of the RAC. These meetings are currently scheduled for Sept. 7 and 20. You can find more information about these meetings on the [Department's website](#).