STATE TAXATION OF MAIL ORDER INSURERS

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Because of new computer capabilities, the desire to reduce costs of operations, and in an effort to reach new and expanding markets, the mail order business has grown rapidly over the years. The insurance industry, particularly the life, accident and health lines, has also seen increasing use of direct mail methods to sell and service insurance policies. With the development of this phenomena, there has also evolved a complicated body of law delineating the states' powers to regulate and tax these direct mail insurance companies.

Most recently, the United States Supreme Court let stand a Wisconsin supreme court decision that decided two very important questions:

> [can] Wisconsin constitutionally impose a gross receipts tax on an unlicensed foreign insurance company engaged in selling insurance in a state solely through advertisements and use of U.S. mails, without any employees or property in that state. . . ;[1]

and whether the

> Wisconsin statute imposing on unauthorized foreign insurers a tax measured by premiums received for insuring subjects resident or located in Wisconsin, less premiums properly allocated or apportioned and reported as taxable premiums from any other state or states, is unconstitutional for failure to apportion tax on basis of activity conducted outside state that combined to produce the gross receipts upon which tax is levied.[2]

To understand completely what this decision means and how the courts arrived at this point, it is necessary to trace: (1) the development of state regulation and taxation of the insurance industry in general; (2) the evolution of the commerce and due process clauses; and (3) the way in which these areas have grown in conjunction with one another and have been applied to the direct mail insurers.

I. Regulation and Taxation of Insurance Companies: An Historical Background

The history of insurance company regulation in the United States is almost as old as the American insurance industry itself. The first insurance company began operations in 1768 in Pennsylvania, and that state began a form of insurance company regulation in 1794 when the first stock insurance company in America was formed. State taxation of insurance companies came shortly

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1. National Liberty Life Ins. Co. v. Wisconsin, 95 S. Ct. 1668 (1975).
2. Wisconsin v. National Liberty Life Ins. Co., 95 S. Ct. 1675 (1975).

thereafter when, in the early 1800's, New York began taxing insurance companies right along with other corporations. Then in 1824 that state imposed a 10 percent gross premiums tax on fire insurance companies. Although other types of taxes are often applied to insurance companies, the primary method of taxation by states over the years has been the premium tax.[3]

Generally, insurance regulation has been designed to achieve one or more of several goals: (1) to avoid overreaching by insurers; (2) to assure that rates and classifications are fair; and (3) to assure insurance company solvency.[4] The primary purposes of state taxation of insurance companies are (1) to assist in the regulation scheme, and (2) to raise revenue. These underlying motives need to be kept in mind throughout the ensuing discussion.

A. *Regulating "Foreign" Insurance Companies*

Historically, the problem of regulating foreign (out-of-state) insurance companies has been a difficult one. The federal-state dichotomy was temporarily resolved in the mid-1860's, when the United States Supreme Court ruled against an insurance agent named Paul who was asserting that Virginia's regulation of foreign insurers violated the commerce clause. *Paul v. Virginia*[5] made it clear that "issuing a policy of insurance is not a transaction of commerce," and that execution, through delivery, of a contract of insurance was subject, therefore, to local law.[6] For a considerable period of time thereafter, the federal government allowed the states to worry over the problems of regulating interstate insurance activity. Only due process requirements remained to limit somewhat the reach of a state's insurance commission and taxing authority.

For a while, the problem of regulating the mail order insurance business was left primarily to the state of the company's domicile, as opposed to the states where sales were solicited or risks covered. There were soon exceptions to this pattern, but to understand those exceptions, it is necessary to trace the unfolding of the due process clause.

B. *The Development of Due Process Requirements*

The foundation case in the due process area is the often-quoted *Pennoyer v. Neff*[7] decision, where it was held that to obtain valid jurisdiction and satisfy the due process clause, the defendant had to be "present" in the jurisdiction and properly served (or appearing voluntarily). Foreign corporations were found to be "present" in a jurisdiction if they were "doing business" there,[8] but the question of what acts constituted "doing business" was not an easy one.

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3. LONG & GREGG, PROPERTY AND LIABILITY INSURANCE HANDBOOK 999 (1965).
4. R. KEETON, INSURANCE LAW 554 (1st ed. 1971).
5. 75 U.S. 168 (1868).
6. Paul v. Virginia, 75 U.S. 168, 183 (1868).
7. 95 U.S. 714 (1877).
8. International Harvester Co. v. Kentucky, 234 U.S. 579 (1914).

The three cases which are repeatedly cited as the early examples of "doing *insurance* business" are *Allgeyer v. Louisiana*,[9] *St. Louis Cotton Compress Co. v. Arkansas*,[10] and *Connecticut General Life Insurance Co., v. Johnson*.[11] In these decisions the Supreme Court held that states did not have jurisdiction to impose premium taxes on insurance or reinsurance contracts that were entered into outside their jurisdiction, even though the covered risks were within their jurisdiction. In the *Connecticut General* case, for instance, California tried to tax reinsurance contracts entered into and to be performed outside the state. These contracts of reinsurance did affect risks within the state, but this was not enough for California to claim that Connecticut General was "present" and "doing business" there.

These early cases took a "conceptualistic approach" to the issue of what acts constituted "doing business". They looked at the place of the making of the contracts and the place of performance. The basic conclusion of this approach was summarized in *Minnesota Commercial Men's Association v. Benn*,[12] where the Court denied the risk state the power to tax an insurance company which, although insuring lives of people in that state, was not otherwise "present" there. This simply was not enough "doing business" to satisfy the "presence" test. The importance of physical presence was nowhere made clearer than in the case of *Compania General de Tabacos de Filipinas v. Collector*.[13] There a company domiciled in Spain and doing business in the Philippines bought fire insurance from an English company and marine insurance from a French company. The place of contracting and performance was Europe. While the English company was licensed and had an agent in the Philippines, the French company had no such presence there. The Court, using due process arguments, upheld a Philippine tax on the premiums paid to the English company, but not the French.

A final case which helped to clarify the "doing business" concept at that time was *Equitable Life Assurance Society v. Pennsylvania*,[14] where the Court found that Pennsylvania did not tax property beyond its jurisdiction by measuring a premium tax on the premiums sent directly to foreign insurance company offices *as well as* premiums received within the state of Pennsylvania. This case also represented one of the earliest efforts to evaluate a method of taxation for the requisite due process, by looking at the protections given by the taxing state to the insureds.

The *Equitable Life Assurance Society* case was only a hint of how the due process concept would change. A further expansion of state regulatory powers came in *Osborn v. Ozlin*,[15] only two years after *Connecticut General*. In *Osborn*,

9. 165 U.S. 578 (1897).
10. 260 U.S. 346 (1922).
11. 303 U.S. 77 (1938).
12. 261 U.S. 140 (1923).
13. 275 U.S. 87 (1927).
14. 238 U.S. 143 (1915).
15. 310 U.S. 53 (1940).

the insurance company had authorized agents in Virginia, and Virginia was attempting to require that all business conducted in that state be placed through these resident agents. The total regulatory plan was designed to assure that the policies would be serviced by a local agent, and, in return, the local agent was supposed to get part of the commission. The Supreme Court agreed that a state's total regulatory scheme may reach beyond state lines. The Court recognized "definable interests"[16] that a state could have in insurance business contracted and to be performed elsewhere.

Scarcely three years after *Osborn*, the court restated the "interest" theory in *Hoopeston Canning Co. v. Cullen*.[17] There, however, the state's interest in insurance contracted and performed outside the state was "protection of the citizen insured or the protection of the state from the incidents of loss."[18] While *Osborn* and *Hoopeston* were not radical departures from the "presence" test, they did illustrate a broadening view which eventually led to the "minimum contacts" rule of *International Shoe Co. v. Washington*:[19]

> Due process requires only that in order to subject a defendant to a judgment *in personam*, if he be not present within the territory of the forum, he have certain minimum contacts with it such that the maintenance of the suit does not offend "traditional notions of fair play and substantial justice."[20]

C. *Derailing the Regulation Train*

While this line of precedent was developing, the National Convention of Insurance Commissioners (NCIC) appointed a committee in the early 1880's to work on the problem of regulating unlicensed or unauthorized foreign insurance companies.[21] Their solution was for each state to require the insurance companies domiciled therein to also be licensed or authorized wherever they transacted business. This solution would have been acceptable but for a lack of uniformity in the way states reacted to the suggestion. Insurance commissioners were slow to impose regulations on local companies which would inure only to the benefit of other states, especially if reciprocity were uncertain. In 1938 and 1941, the NCIC and the National Association of Insurance Commissioners (NAIC, formerly the NCIC) proposed two more model acts to prohibit unauthorized insurers from doing business in the state where they lacked authority and to provide for a means of service of process on these unauthorized insurers, but these model bills had little time to catch on before the shocking landmark decision of *United States v. South-Eastern*

16. Osborn v. Ozlin, 310 U.S. 53 (1940).
17. 318 U.S. 313 (1943).
18. Hoopeston Canning Co. v. Cullen, 318 U.S. 313, 316 (1943).
19. 326 U.S. 310 (1945).
20. International Shoe Co. v. Washington, 326 U.S. 310, 316 (1945).
21. J. Manders, *Ministers Life & Casualty Union v. Haase: The New Trend in State Regulation of Unauthorized Mail-Order Insurance Companies*, 43 NOTRE DAME LAWYER 157, 158 (Dec. 1967).

Underwriters Association.[22] This decision reversed 75 years of precedent and found the business of insurance to be interstate commerce after all, thereby shifting the responsibility of controlling the industry from the state to the federal level.

The responsibility did not remain long with the federal government, however, and in less than a year the commerce clause powers, as applied to the insurance industry, were delegated back to the states by Public Law 15—the McCarran-Ferguson Act:[23]

> Sec. 1. The Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.
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> Sec. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business. . . .

D. *In the Wake of McCarran-Ferguson*

Following passage of the McCarran-Ferguson Act, a great deal of attention was focused on the legislative history of this bill to determine the intent of Congress. Was it the intention of Congress to grant states more or less power than existed prior to *South-Eastern Underwriters*? Congressional hearings seemed clear in that regard, and for a short time regulation and taxation of the insurance business was "frozen" within the limits of pre-*South-Eastern* cases. The House report read as follows:

> It is not the intention of Congress in the enactment of this legislation to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the South-Eastern Underwriters Association case. Briefly, your committee is of the opinion that we should provide for the continued regulation and taxation of insurance by the States, subject always, however, to the limitations set out in the controlling decisions of the United States Supreme Court, as for instance, in *Allgeyer v. Louisiana* (165 U.S. 578), *St. Louis Cotton Compress Co. v. Arkansas* (260 U.S. 346) and *Connecticut General Insurance Co. v. Johnson* (303 U.S. 77), which held, inter alia, that a State does not have power to tax contracts of insurance or reinsurance entered into outside its jurisdiction by individuals or corporations resident or domiciled therein covering risks within the State or to regulate such transactions in any way.[24]

In the case of *Prudential Insurance Co. v. Benjamin,*[25] the Supreme Court soon established that the McCarran Act had removed any commerce clause

22. 322 U.S. 533 (1944).
23. Act of Mar. 9, 1945, Pub. L. No. 79-15, 59 Stat. 33 (codified at 15 U.S.C. § 1011 (1970)). This law was approved nine months and three days after the *South-Eastern Underwriters* decision.
24. H.R. REP. No. 143, 79th Cong., 1st Sess. 3 (1945).
25. 328 U.S. 408 (1946).

restrictions on the regulation or taxation of insurance.[26] The Court did not, however, revert to a frozen concept of due process. In *Travelers Health Association v. Virginia*,[27] the trio of *Allgeyer*, *St. Louis Cotton*, and *Connecticut General* was rejected in favor of *Osborn*, *Hoopeston*, and *International Shoe*. The Court in *Travelers*, facing a fact situation similar to *Minnesota Commercial Men's Association v. Benn*,[28] broke the barrier of a strict "presence" test and allowed a scheme of substituted service and regulation for unauthorized direct mail insurance companies.[29] Ultimately, the expanding concept of due process in the area of substituted service found certain expression in *McGee v. International Life Insurance Company*:[30]

> It is sufficient for purposes of due process that the suit was based on a contract which had substantial connection with that state. . . . It cannot be denied that California has a manifest interest in providing effective means of redress for its residents when their insurers refuse to pay claims.[31]

E. *Taxation—A Tougher Test*

For jurisdictional and regulatory purposes, the "substantial connection" or "minimum contacts" theories of due process seem to suffice, but cases have made it clear that for taxation a greater "presence" is necessary. This dual standard was made perfectly clear in the companion cases of *McLeod v. Dillworth Co.*,[32] and *General Trading Co. v. State Tax Commission*.[33] In *McLeod*, Arkansas was prohibited from imposing a sales tax on a Tennessee corporation which solicited sales through the mails, by telephone, and through some Tennessee-based traveling salesmen. In *General Trading*, however, Iowa could require a Minnesota corporation to collect use taxes on a similar business. This was found to be regulation and not taxation, and "a state has power to make a tax collector of one whom it has no power to tax."

The stricter "presence" requirement for taxing purposes was best stated a couple of years later in *Freeman v. Hewit*:[34]

> Because the greater or more threatening burden of a direct tax on commerce is coupled with the lesser need to a State of a particular source of revenue, attempts at such taxation have always been more carefully scrutinized and more consistently resisted than police power regulations of aspects of such commerce.[35]

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26. *See also* Robertson v. California, 328 U.S. 440 (1946); North Little Rock Transp. Co. v. Casualty Reciprocal Exch., 181 F.2d 174 (8th Cir.), *cert. denied*, 340 U.S. 823 (1950); Darr v. Mutual Life Ins. Co., 169 F.2d 262 (2d Cir.), *cert. denied*, 335 U.S. 871 (1948).
27. 339 U.S. 643 (1950).
28. 261 U.S. 140 (1923).
29. *See also* Parmalee v. Iowa State Traveling Men's Ass'n, 206 F.2d 518 (5th Cir. 1953).
30. 355 U.S. 220 (1957).
31. McGee v. International Life Ins. Co., 355 U.S. 220, 223 (1957).
32. 322 U.S. 327 (1944).
33. 322 U.S. 335 (1944).
34. 329 U.S. 249 (1946).
35. Freeman v. Hewit, 329 U.S. 249, 254 (1946).

While the *Freeman* case talked in terms of "commerce clause" restrictions, *State Board of Insurance v. Todd Shipyards Corp.*,[36] seemed to extend strict "presence" requirements to due process concepts. In *Todd*, the Supreme Court determined that Texas could not impose premium taxes on out-of-state insurance contracts, where Todd Shipyards was doing business in Texas and bought insurance from an unauthorized alien insurance company to cover property located in Texas. The Court, reverting to an *Allgeyer, St. Louis Cotton, Connecticut General* "conceptualistic" standard, was unable to find sufficient contacts between the out-of-state insurer and Texas. While the *Todd* case may have appeared to be a step backward in the development of due process, the same result may very well have been reached by applying a "minimum contacts" rule.

Such was the case in *National Bellas Hess, Inc. v. Department of Revenue*,[37] where the Court could not find the requisite "minimum contacts" to satisfy "notions of fair play and substantial justice:"

> [National] does not maintain in Illinois any office, distribution house, sales house, warehouse or any other place of business; it does not have in Illinois any agent, salesman, canvasser, solicitor or . . . representative to sell or take orders, to deliver merchandise, to accept payments, or to service merchandise it sells; it does not own any tangible property, . . . it has not advertised . . . in newspapers, on billboards, or by radio or television in Illinois.[38]

By holding that Illinois could not regulate National Bellas Hess, a mail order seller, by requiring it to collect a use tax, the presumption would seemingly follow that Illinois couldn't have *taxed* such a business.

II. Beyond National Bellas Hess

While *National Bellas Hess* seemed to indicate that the Court was drawing a distinct line between use of the United States mail and other types of contacts in deciding the "nexus" question, several subsequent cases have raised new doubts.

A. *Ministers Life and Casualty*

In 1961, Wisconsin passed a statute which forbade the doing of business in Wisconsin by an unauthorized insurance company. A discriminatory three percent premium tax was placed on any unauthorized insurance; unauthorized insurers were prevented from enforcing such contracts in Wisconsin; penalties were imposed for transacting unauthorized acts of insurance; and the Wisconsin Commissioner of Insurance was to enforce the act through a substituted service of process procedure. The statute further provided that "doing business" included collecting premiums through the mail, even though no other contacts

36. 370 U.S. 451 (1962).
37. 386 U.S. 753 (1967).
38. National Bellas Hess, Inc. v. Department of Revenue, 386 U.S. 753, 754 (1967).

existed between the state and the insurance company. This meant that even if a direct mail insurance company stopped soliciting further contracts through the mail in Wisconsin, that company would still be subject to penalties for collecting premiums on existing business. The alternatives were to become licensed in Wisconsin, stop collecting premiums from Wisconsin business, or pay the penalties prescribed. Ministers Life and Casualty Union felt this was wrong, and they challenged the constitutionality of Wisconsin imposing taxes and penalties on the mere receipt of premiums (through the mail) on insurance written prior to the statute. The Wisconsin courts upheld the validity of the statute, and the United State Supreme Court dismissed for lack of a substantial federal question.[39]

After *Ministers*, there still remained some question about a state's jurisdiction to tax, because, in addition to using the mail, Ministers also selected group leaders, who lived within the state, to form the group and handle some of the administrative functions, such as collecting their group members' premiums and sending them all to Ministers. This one fact may have been thought to have distinguished *Ministers* from *Todd* where there were no contacts whatsoever by the insurer. The court in *Ministers* also correctly pointed out that Congress only cited *Allgeyer*, *St. Louis Cotton* and *Connecticut General* as examples of where the Supreme Court had gone before *South-Eastern Underwriters* and where they now must return and start anew. The *Ministers* court also cited the pre-*South-Eastern* cases of *Osborn* and *Hoopeston* as examples which Congress might just as well have used. The best indication, however, that the *Ministers* court was rejecting a frozen concept of pre-*South-Eastern* due process concepts came in the discussion of the *Benn* case:

> *Benn*'s 'presence concept' of doing business may be conceded to no longer have vitality in the field of jurisdiction for service of process in view of *International Shoe Co. v. Washington* . . . whose minimum-contact theory of jurisdiction was proclaimed only a few years after the decision in *Osborn* and *Hoopeston* in the related field of states' jurisdiction to tax and regulate.[40]

B. *United National Life—Another Step*

If the "presence concept" was not dead after *Ministers*, it was dealt a second seemingly fatal blow one year later in *People v. United National Life Insurance Co.*[41] In that case, three direct mail insurers, whose only contact with California was through the mails, were held to be subject to the jurisdiction of California and could be enjoined from doing business in that state without a license. The appeal from the California supreme court was dismissed by the United States Supreme Court for lack of a substantial federal question. Taken

39. Ministers Life & Cas. Union v. Haase, 30 Wis. 2d 339, 141 N.W.2d 287 (1966), *appeal dismissed*, 385 U.S. 205 (1967).
40. *Id.* at —, 141 N.W.2d at 294.
41. 66 Cal. 2d 577, 427 P.2d 199, 58 Cal. Rptr. 599, *appeal dismissed*, 389 U.S. 330 (1967).

together with *Ministers*, this leaves little doubt that a state has jurisdiction to regulate a direct mail insurance company whose only contact with the state is through the mail. Not so certain following these two cases was the question of a state's power to tax such mail order insurers.

C. *Strike Three; You're Out*

Finally, in 1974, the Wisconsin supreme court again grappled with their "Unauthorized Insurance Premium Tax."[42] This time the National Liberty Life Insurance Company presented an opportunity to look squarely at an out-of-state company whose only connection with Wisconsin came through the United States mail. There were no group leaders here, and this was a question of the state's power to tax, as well as regulate.

National argued that a "physical presence" was required and was lacking. They further asserted the notion that increasingly stricter presence tests were required for "service of process, police power regulation, and general revenue taxation,"[43] respectively. National's arguments relied heavily on *National Bellas Hess* and *Freeman*, and they attempted to distinguish the *Ministers* case because of the "physical presence" of group leaders in Wisconsin.

Justice Wilkie, writing the Wisconsin supreme court opinion in *National Liberty Life Insurance Co. v. Wisconsin*, began his reply to National's contentions with *Prudential Insurance Co. v. Benjamin*.[44] In interpreting the McCarran Act, that case "removed any objections to regulation or taxation of insurance based on the Commerce Clause."[45] Therefore, only the due process clause could restrict Wisconsin's taxation of National. Since the *Freeman* case relied on the commerce clause, it was not applicable to National. The *National Bellas Hess* case, although it was more difficult to deal with, was also explained away as a commerce clause *and* a due process clause case. Justice Wilkie then went on with an analysis which seemed to be saying that while *National Bellas Hess* talked in terms of due process, it was really the burden on interstate commerce that invalidated Illinois' attempt to make National Bellas Hess collect a use tax. Justice Wilkie seemed to be somewhat critical of the United States Supreme Court for its failure to distinguish between due process and interstate commerce concepts, and yet his efforts to contrast the two offered little to distinguish them. The two concepts are closely related.[46] With regard to the burden on commerce, the United States Supreme Court has said that state taxes cannot be justified unless designed to make "commerce bear a fair share of the cost of the local government whose protection it enjoys."[47] On the other hand, with regard

42. See *National Liberty Life Insurance Co. v. Wisconsin*, 62 Wis. 2d 347, 215 N.W. 2d 26, 27, n.1 (1974), for the pertinent statute.
43. *Id.* at 350, 215 N.W.2d at 29.
44. 328 U.S. 408 (1946).
45. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d 347, 351, 215 N.W.2d 26, 30 (1974).
46. *See* Central R.R. v. Pennsylvania, 370 U.S. 607 (1962).
47. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d 347, 351, 215 N.W.2d

to the due process clause the "simple but controlling question is whether the state has given anything for which it can ask return."[48] The questions seem more similar than dissimilar. However, even if *National Bellas Hess* cannot be neutralized with such a distinction, the dissenting view, that a large-scale, systematic, continuous solicitation and exploitation of a state's market is a sufficient nexus, would probably have prevailed had it not been for considerations of the burden Illinois was placing on interstate commerce.

Justice Wilkie was implying, furthermore, that even the commerce clause concepts had moved from "physical presence" concepts to a "minmum contacts" test, balanced additionally by the "burden on commerce" question:

> Here, too, the Constitution requires 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.'[49]

One further distinction was next pointed out in *National Liberty*. This Wisconsin tax on National Liberty is "not an isolated general revenue measure . . . [but] is part of a complex regulatory scheme. . . ."[50] Therefore, the *Osborn-Hoopeston-McGee* cases establish a better precedent because they affirm the manifest interest of a state in its total regulatory scheme:

> In determining the power of a state to apply its own regulatory laws to insurance business activities, the question in earlier cases became involved by conceptualistic discussion of theories of the place of contracting or of performance. More recently it has been recognized that a state may have substantial interests in the business of insurance of its people or property regardless of these isolated factors. This interest may be measured by highly realistic considerations such as the protection of the citizen insured or the protection of the state from the incidents of loss.[51]

When the more recent *Ministers* and *United National* cases were added to this string of precedent, there could be no other conclusion except "that state interest in the field of insurance is an important factor in determing whether the state can assert jurisdiction to regulate and tax consistent with due process."[52]

So it would seem that the steps to take in testing a state tax on insurance business are as follows: (1) are there certain "minimum contacts" so as not to offend notions of "fair play and substantial justice?";[53] (2) has the state "given

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26, 31 (1974), *citing* Northwestern Cement Co. v. Minnesota, 358 U.S. 450 (1959); Greyhound Lines v. Mealey, 334 U.S. 653 (1948); Freeman v. Hewit, 329 U.S. 249 (1946).

48. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d, 347, 351, 215 N.W.2d 25, 31 (1974), *citing* Standard Oil Co. v. Peck, 342 U.S. 382 (1952); Ott v. Mississippi Barge Line, 336 U.S. 169 (1949); Wisconsin v. J.C. Penney Co., 311 U.S. 435 (1940).

49. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d, 347, 351, 215 N.W.2d 26, 31 (1974), *citing* American Oil Co. v. Neill, 380 U.S. 451 (1965); Scripto, Inc. v. Carson, 362 U.S. 207 (1960); Miller Bros. Co. v. Maryland, 347 U.S. 340 (1954).

50. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d 347, 354, 215 N.W.2d 26, 32 (1974).

51. *Id.* at 354, 215 N.W.2d at 33, *quoting* Hoopeston Co. v. Cullen, 318 U.S. 313 (1943).

52. *Id.*

53. The test developed in *International Shoe Co. v. Washington*, 326 U.S. 310 (1945).

anything for which it can ask return?";[54] and (3) is the tax fairly apportioned to the activities within the taxing state? (This last question is the subject of the next section.)

The first question was answered here in the affirmative, despite *National Bellas Hess* and with the aid of the *Osborn-Hoopeston-McGee-Ministers-United National* chain. The answer to the second question was also yes:

> Anything which tends to lessen the danger of accidents, threats to life, and unhealthy conditions redounds to the benefit of companies engaged in either the life insurance or accident and health insurance business. Wisconsin provisions for public health, safety and welfare paid for out of general revenues are benefits enjoyed by National for which it would be fair to expect a contribution.[55]

Furthermore, these "benefits from an ordered society are much more directly related to National's business than to the retail sales involved in the *National Bellas Hess* case."[56]

III. Apportionment: "Watch Out For That Last Step!"

So it was that (1) National was found to have sufficient "minimum contacts" with Wisconsin so as not to offend notions of "substantial justice;" and (2) Wisconsin was found to have given something for which it could ask return; but (3) watch out for that last step! National contended that the taxing statute was still unconstitutional because it imposed a gross premiums tax disproportionate to National's activities in Wisconsin. In other words, the tax was not fairly apportioned.

Again the Wisconsin supreme court looked back for guidance from the United States Supreme Court, and again they were faced with a doubtful mix of commerce clause and due process clause cases. The whole issue of apportionment has been a difficult one to resolve over the years. Several methods have been tried, including: (1) specific allocation; (2) separate accounting; (3) single-factor formulas; and (4) multiple-factor formulas.

Specific allocation deals mostly with investment income and allocates gross or net receipts from a geographically-definable, specific transaction to tally to the state where the transaction is located. Separate accounting is an attempt to trace gross or net receipts to the states of their source by singling out a *part* of the corporation for which an income statement may be drawn detailing one state's activities, and then allowing that state to fully tax those receipts attributable to that separate and distinct part. Single-factor formulas apportion receipts on the basis of some factor, such as percentage of property, payroll or sales in the state; multiple-factor formulas combine two or more factors in computing the percentage to be taxed by a state.

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54. The test was cited in *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435 (1940).
55. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d 347, 356, 215 N.W.2d 26, 34 (1974).
56. *Id.*

Basically, Wisconsin's tax in the *National* case was unapportioned altogether. While separate accounting is sometimes used with conglomerates and for capital stock taxes, receipts taxes are not as adaptable to this method. Where goods and money cross state lines and services are performed in two or more states, the "source" of receipts is indeed complex. And although specific allocation works well in some situations with investment-type incomes, such as rents, that method is not readily adaptable to this type of gross receipts.

Wisconsin also might have contended that this was a single-factor formula based on sales within the state. Therefore, if National received $100,000 worth of total premiums from sales everywhere, and if they received $10,000 worth of premiums for Wisconsin residents, the formula would be $10,000/$100,000 X 3% (tax rate) X $100,000 (total premiums), which is the same thing as saying $10,000 (Wisconsin resident premiums) X 3%.

Even if it could have been argued that this was a single-factor formula, such measures are viewed with suspicion, and a single-factor apportionment has to achieve a just result. In *Greyhound Lines v. Mealey*,[57] therefore, a gross receipts tax based on mileage was approved only because it was found to be "constitutionally fair." The inequitable results of single-factor methods are illustrated in the earlier cases of *Ford Motor Co. v. Beauchamp*[58] and *Underwood Typewriter Co. v. Chamberlain*.[59] The first apportioned capital stock by reference to gross receipts and the latter apportioned a net income tax by using a property formula. Because of such inequities, single-factor methods are suspect, and multiple-factor formulas have been more acceptable.

In any case, Justice Wilkie made it clear that he considered Wisconsin's premium tax in the case, based solely on receipts, to be unapportioned. He also concluded that due process clause considerations, as well as commerce clause concepts, require that taxes be levied "only on that portion of the taxpayer's net income which arises from its activities within the taxing state."[60]

After an analysis of *General Motors v. Washington*[61] and *General Motors v. District of Columbia*,[62] it is apparent that, for both interstate commerce and due process purposes, the sales factor alone will not serve the purposes of apportionment without further connections with the taxing state being shown. Quoting from an article which this author found most informative, Justice Wilkie said:

> The premium tax is in effect a single factor apportionment formula based solely upon receipts. Although the receipts are the result of a chain of activities beginning in the domiciliary state and ending with

57. 334 U.S. 653 (1948).
58. 308 U.S. 331 (1939).
59. 254 U.S. 113 (1920).
60. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d 347, 358, 215 N.W.2d 26, 36 (1974), *citing* Northwestern Cement Co. v. Portland, 358 U.S. 450, 464 (1959).
61. 377 U.S. 436 (1964).
62. 380 U.S. 553 (1965).

> the capture of the premium in the risk state, the principal activities are at home. There are located the insurer's only office, all of its tangible properties and all of its employees. There is undertaken all of the study and research that leads to the writing of the policies, their form and content. There all the mortality and accident studies of an actuarial nature are made, and in effect the 'manufacture' of the insurance conducted. There the investment of the premiums is made and the reserves are accumulated out of which benefits are paid. The risk state premium tax, therefore, in focusing only upon the receipt of the premium, would seem to ignore by far the bulk of the activity involved![63]

Citing *Prudential Insurance Co. v. Benjamin*,[64] *Equitable Life Society v. Pennsylvania*,[65] and *Lincoln Life Insurance Co. v. Read*[66] as cases which dealt with premium taxes, but not the issue of apportionment, Justice Wilkie opined:

> These Supreme Court cases have established the constitutionality of gross premium taxes (if apportioned) as against the contention that they are an unfair burden on interstate commerce. However, if not apportioned the tax may be, as here, unconstitutional, as a violation of the due process clause.[67]

Certainly, in this case, National's activities in Wisconsin divided by their total activities everywhere would yield a much lower percentage than dividing Wisconsin-derived premiums by total premiums. Consider, too, the results of a Massachusetts-type, multiple-factor formula in a case like this. With no property in Wisconsin and no payroll there, the Wisconsin tax would only be one-third of what was charged here.

IV. Summary

On April 28, 1975, the United States Supreme Court denied a petition for certiorari in the case of *Wisconsin v. National Liberty Life Insurance Co.*[68] On the same day a conditional cross appeal was dismissed in the case of *National Liberty Life Insurance Co. v. Wisconsin.*[69] These cases will be printed in Volume 421, part one of the preliminary prints.

With this decision the Wisconsin supreme court, and by acquiescence the United States Supreme Court, determined that, in the case of direct mail, foreign, unauthorized insurance companies: (1) there are sufficient contacts; (2) the state is giving enough to justify asking some return; but (3) be careful

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63. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d 347, 358, 215 N.W.2d 26, 37 (1974), *citing* Patty, *State Premium Taxes On Mail Order Insurance Under the Due Process Clause*, 22 Tax Lawyer 363, 380 (1969).
64. 328 U.S. 408 (1946).
65. 238 U.S. 143 (1915).
66. 325 U.S. 673 (1945).
67. National Liberty Life Ins. Co. v. Wisconsin, 62 Wis. 2d 347, 358, 215 N.W.2d 26, 37 (1974).
68. 95 S. Ct. 1675 (1975).
69. 95 S. Ct. 1668 (1975).

to apportion premium taxes so as to accurately reflect the proportionate amount of activity in the state. Because of the inapplicability of the commerce clause to the regulation and taxation of insurance by a state, the National case is somewhat of a mutation.

V. Conclusion

Nevertheless,
National Bellas Hess,
Beware!