

Letter of Findings Number: 07-0582
Income Tax
For Tax Year 2003

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ISSUE

I. Income Tax—Corporate.

Authority: IC § 6-8.1-5-1; [45 IAC 3.1-1-52](#); [45 IAC 3.1-1-55](#).

Taxpayer protests the assessment of corporate income tax.

STATEMENT OF FACTS

Taxpayer is in the business of producing and distributing films and television shows nationally and internationally. As the result of an audit, the Indiana Department of Revenue ("Department") issued proposed assessment for Indiana income tax for the tax year 2003. Taxpayer protests the proposed assessment. An administrative hearing was held and this Letter of Findings results. Further facts will be supplied as required.

I. Income Tax—Corporate.

DISCUSSION

Taxpayer protests the imposition of income tax on certain activities for the tax year 2003. The Department determined that Taxpayer had properly reported income from activities such as renting or leasing films to Indiana theaters or syndicating television shows to Indiana television stations. The Department determined that Taxpayer had not properly reported income from licensing films and television shows to broadcast and cable networks which were then viewed on those networks by Indiana residents in their homes. Taxpayer protests that these activities should not be reported to Indiana, but rather should be reported to the states in which the respective networks have their commercial domiciles. None of the networks in question are commercially domiciled or headquartered in Indiana. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The Department refers to [45 IAC 3.1-1-52](#), which states:

The numerator of the sales factor generally includes gross receipts from sales attributable to this state, and includes all interest income, service charges, carrying charges, or time-price differential charges incidental to such sales regardless of the place where the accounting records are maintained or the location of the contract or other evidence of indebtedness. The numerator shall not include sales between members of an affiliated group filing consolidated returns under [IC 6-3-4-14](#).

The Department also refers to Letter of Findings 04-0398 ("LOF 04-0398"), which was issued to an unrelated third party which also was involved in producing and licensing programming for the cable television industry. LOF 04-0398 determined that the taxpayer in that case was in a unitary relationship with several subsidiaries each of which had its own business situs in Indiana. LOF 04-0398 then determined that, since the taxpayer was in a unitary relationship with the Indiana-sitused subsidiaries and should be filing a combined return with those subsidiaries, the income of that taxpayer was partially attributable to viewers in Indiana viewing advertisements on those cable networks. The Department determined an apportionment formula for that taxpayer and applied a similar apportionment formula to Taxpayer in the instant case.

Taxpayer states that its facts are materially different from the taxpayer in LOF 04-0398. Taxpayer explains that it has no subsidiaries in Indiana and that it is not in a unitary relationship with the networks in question.

Taxpayer refers to [45 IAC 3.1-1-55](#), which states in relevant part:

Gross receipts from transactions other than sales of tangible personal property shall be included in the numerator of the sales factor if the income-producing activity which gave rise to the receipts is performed wholly within this state. *Except as provided below if the income producing activity is performed within and without this state such receipts are attributed to this state if the greater proportion of the income producing activity is performed here, based on costs of performance.*

The term "income producing activity" means the act or acts directly engaged in by the taxpayer for the ultimate purpose of obtaining gains or profit. Such activity does not include activities performed on behalf of the taxpayer, such as those conducted on its behalf by an independent contractor. Accordingly, "income producing activity" includes but is not limited to the following: (1) The rendering of personal services by employees or the utilization of tangible and intangible property by the taxpayer in performing a service. (2) The sale, rental, leasing, or licensing the use of or other use of tangible personal property. (3) The sale, licensing the use of or other use of intangible personal property.

Income producing activity is deemed performed at the situs of real, tangible and intangible personal property or the place where personal services are rendered. The situs of real and tangible personal property is at its

physical location. *The situs of intangible personal property is the commercial domicile of the taxpayer (i.e., the principal place from which trade or business of the taxpayer is directed or managed), unless the property has acquired a "business situs" elsewhere. "Business situs" is the place at which intangible personal property is employed as capital; or the place where the property is located if possession and control of the property is localized in connection with a trade or business so that substantial use or value attaches to the property.*

Example:

Taxpayer, a corporation whose principal business activity is the manufacture and sale of hot water heaters, obtains notes for the sale of such water heaters in connection with its Indiana business activity. The property has a business situs in this state, therefore, interest income derived from such notes is attributable to this state.

The term "costs of performance" means direct costs determined in a manner consistent with generally accepted accounting principles and in accordance with accepted conditions or practices in the trade or business of the taxpayer.

....

(*Emphasis added.*)

In the instant case, the intangible personal property is the films and television shows which Taxpayer licenses to the various cable and broadcast networks. Taxpayer is commercially domiciled in California, not in Indiana. The networks are commercially domiciled and headquartered in other states, not in Indiana. When Taxpayer licenses its programming to a network, the situs of the intangible personal property is where the network "possesses and controls" the intangible personal property, as described by [45 IAC 3.1-1-55](#). That possession and control occurs at either the network's headquarters or commercial domicile.

Therefore, Taxpayer is correct that the intangible personal property is situated either at its commercial domicile in a state other than Indiana or at the business situs outside Indiana where the networks use the intangible personal property. The Department's reliance on the reasoning of LOF 04-0398 is misplaced. The taxpayer in that case had a unitary relationship with related corporations, each of which had an Indiana business situs, thereby making that taxpayer subject to apportionment of income derived from those licensing arrangements.

In the instant case, the Department conducted the audit on Taxpayer alone, without discussing any other taxpayers. The subject of whether or not Taxpayer was in a unitary relationship with any of the networks involved was not raised and so is not an issue in this Letter of Findings. While the networks which license the programming from Taxpayer would be subject to the apportionment method discussed in LOF 04-0398 by virtue of their direct contact with Indiana customers, Taxpayer itself is one step removed from liability for Indiana income taxation on these transactions, as provided by [45 IAC 3.1-1-55](#). Taxpayer has met the burden imposed by IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is sustained.

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