DEPARTMENT OF STATE REVENUE

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Letter of Findings Number: 08-0642
Adjusted Gross Income Tax
For the Years 2000-2002

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ISSUES

I. Adjusted Gross Income Tax–Throwback Sales.

Authority: IC § 6-3-2-2; 15 U.S.C. §§ 381-385.

Taxpayer protests the inclusion of sales to Indiana in its sales numerator as well as the inclusion of sales made from Indiana to customers in several other states.

II. Adjusted Gross Income Tax–Consolidated Returns.

Authority: IC § 6-3-2-2; IC § 6-3-4-14; IRC § 1504.

Taxpayer protests the inclusion of an affiliated corporation in its consolidated income tax return.

STATEMENT OF FACTS

Taxpayer is a corporation doing business in Indiana. Taxpayer filed a consolidated corporate income tax return on behalf of itself and two affiliated companies (collectively "Filing Group," and individually Taxpayer, Member A, and Member B). The members of Filing Group maintained at least five warehouses in Indiana during the tax years in question.

The Indiana Department of Revenue ("Department") conducted an audit of Taxpayer. The Department's audit determined that various sales made by Filing Group were made from Indiana to states and foreign countries in which Filing Group (or individual members of Filing Group) was not taxable. The auditor reattributed those sales from the respective states and foreign countries to Indiana.

In addition, the Department determined that two additional corporations should have been included in the consolidated tax return filed on behalf of Filing Group. Taxpayer protested the inclusion of one of these entities ("Excluded Corporation").

I. Adjusted Gross Income Tax–Throwback Sales.

DISCUSSION

Taxpayer protests the attribution of certain sales in Indiana's sales numerator. Filing Group sold their products to customers in several states and one foreign country. Taxpayer treated some of these sales as being "thrown back" to Indiana (i.e., the sales are shipped outside Indiana but treated as Indiana sales) and treated other sales as being sales to jurisdictions outside Indiana in determining Taxpayer's sales numerator. However, the Department determined that sales attributed to several jurisdictions should have been attributed to Indiana based on whether the particular member was subject to a net income tax in those particular jurisdictions ("throwback sales").

In general, IC § 6-3-2-2(e) provides that sales of tangible personal property are sourced to the state to which the tangible personal property is shipped. However, IC § 6-3-2-2(e)(2)(B) provides that sales shipped from Indiana are treated as Indiana sales for apportionment purposes if "the taxpayer is not taxable in the state of the purchaser." IC § 6-3-2-2(n) provides that a taxpayer is "taxable in another state" if:

(1) In that state the taxpayer is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporate stock tax; or

(2) that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not.

In addition, 15 U.S.C. §§ 381-385 (P.L. 86-272) provides that a state may not subject a taxpayer to a net income tax if the taxpayer's activities in that state do not exceed "mere solicitation." The question is whether a member of Filing Group is "taxable" in the states to which that member shipped its tangible personal property. If the member is taxable, the sales are not considered Indiana sales. If the member if not taxable and the property was shipped from Indiana, the sales are considered Indiana sales.

The sales can be divided into two categories: sales to foreign countries and sales to various states in the United States.

A. Indiana to Foreign Countries

Taxpayer raises three issues with regard to sales to foreign countries. First, Taxpayer argues that the Department used the incorrect amount of sales in determining the sales to be thrown back to Indiana. Second, Taxpayer argues that sales shipped from two warehouses are not subject to throwback to Indiana because the warehouses are not located in Indiana. Third, Taxpayer argues that it had an agent acting on Filing Group's behalf in the foreign countries ("Agent"). Therefore, because Agent's activities on behalf of Taxpayer exceeded solicitation, Taxpayer would be considered taxable in the foreign countries on at least a portion of Filing Group's

sales.

With regard to the sales figure used to determine throwback sales reattributable to Indiana, Taxpayer has provided sufficient information to substantiate a different amount of sales. Taxpayer has also provided sufficient information to conclude that sales from two of Filing Group's warehouses should not have been included in Indiana throwback sales.

With regard to the third issue–whether Agent's activities on behalf of the members of Filing Group are sufficient to make each member taxable in the foreign countries–15 U.S.C. § 381 provides:

(a) Minimum standards. No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after the date of the enactment of this Act [enacted Sept. 14, 1959], a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

. . .

(c) Sales or solicitation of orders for sales by independent contractors. For purposes of subsection (a), a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

(d) Definitions. For purposes of this section--

(1) the term "independent contractor" means a commission agent, broker, or other independent contractor who is engaged in selling, or soliciting orders for the sale of, tangible personal property for more than one principal and who holds himself out as such in the regular course of his business activities; and

(2) the term "representative" does not include an independent contractor.

Filing Group itself had no activities in the foreign countries. Agent likely exceeded the scope of activities in the United Kingdom that would make Filing Group's members taxable within the meaning of IC § 6-3-2-2(n) if Agent was an employee of those entities. Agent's activities in other foreign countries on behalf of Filing Group's members have not been discussed by Taxpayer.

However, Agent held itself out as providing its services on behalf of multiple book publishers. Because Agent provided services on behalf of more than one book publisher during the years in question, Agent was an independent contractor within the meaning of 15 U.S.C. § 381(d)(1).

Taxpayer has not provided–and the Department has not discovered–case law that holds that an independent contractor's activities in a jurisdiction on behalf of a principal are imputed to the principal for purposes of 15 U.S.C. § 381. Thus, the Department respectfully declines Taxpayer's protest.

B. Indiana to Other States

Taxpayer argues that the Department incorrectly determined that sales of tangible personal property shipped to other states should have been "thrown back" for purposes of determining Filing Group's Indiana sales.

Taxpayer, Member A, and/or Member B provided tax returns for several states. Wherever a member provided state tax returns filed in a particular state, sales shipped by that entity to that state were not thrown back to Indiana. However, if no state tax return was provided, the sales were thrown back.

Taxpayer provided information detailing the activities performed by sales representatives in the states in which sales were thrown back. Taxpayer has provided sufficient information regarding Filing Group's sales to Nevada, South Dakota, Washington, and Wyoming that establish that its sales to those jurisdictions should not be thrown back to Indiana.

However, Taxpayer (or Member A or Member B) has not filed state income tax returns in other states to which sales were thrown back. While the filing of a tax return in a particular state does not necessarily indicate that a taxpayer is doing business in that state, the lack of a tax return for a state that requires a return indicates that the taxpayer may have represented that it is not doing business in that state. Therefore, because Taxpayer (or Member A or Member B) has not demonstrated that it is doing business in several states because of its failure to file tax returns for the states, Taxpayer's protest is denied with respect to these states.

FINDING

Taxpayer's protest is sustained with regard to the amount of throwback sales to foreign countries. Taxpayer's protest is sustained with regard to the throwback sales from two warehouses. Taxpayer's protest is otherwise denied with regard to throwback sales to foreign countries.

Taxpayer's protest is sustained with regard to sales shipped to Nevada, South Dakota, Washington, and

Wyoming. Taxpayer's protest is denied with regard to throwback sales to all other states.

II. Adjusted Gross Income Tax–Consolidated Group.

DISCUSSION

Taxpayer protests the inclusion of Excluded Corporation with Filing Group. In particular, Taxpayer argues that IC § 6-3-2-2(p) precludes the Department from including a corporation in another corporation's income tax return absent a showing that income from Indiana sources is not fairly reflected by separately-filed returns and only after the methods specified in IC § 6-3-2-2(l) and (m) have been attempted.

Under Indiana adjusted gross income tax law, there are two types of returns which include multiple C corporations. The first type is a combined return. A combined return is filed on behalf of all entities that constitute a unitary group with a particular taxpayer, with certain exceptions. See IC § 6-3-2-2(o)-(q). A corporation included in a combined return may or may not be considered to conduct business if that corporation is viewed in isolation; nevertheless, the corporation's participation in a unitary business at least partially conducted in Indiana is sufficient to subject that corporation to Indiana's adjusted gross income tax.

The second type of return is a consolidated return under IC § 6-3-4-14. A consolidated return is filed on behalf of an affiliated group of corporations. The filing of a consolidated return is contingent upon "the condition that all corporations which at any time during the taxable year have been members of the affiliated group consent to all provisions of this section. . .." An affiliated group of corporations is defined by I.R.C. § 1504. An affiliated group of corporations needs only to meet the ownership and other statutory tests provided by I.R.C. § 1504; an affiliated group does not necessarily have to be a unitary group. A consolidated return for Indiana tax purposes is filed on behalf of those corporate members of an affiliated group which conduct business in Indiana. Only a member of the affiliated group that does not conduct business in Indiana, may be excluded from the consolidated return.

The Department did not require Excluded Corporation to be treated as part of a combined return. Thus, the provisions of IC § 6-3-2-2(p) are not applicable because the return is not a "combined return" within the meaning of IC § 6-3-2-2.

Instead, the Department concluded that Excluded Corporation was part of Taxpayer's affiliated group and that Excluded Corporation was doing business in Indiana. When Taxpayer filed a consolidated return on behalf of Filing Group, Excluded Corporation consented to Taxpayer's election. By consenting to the election to file a consolidated return, Excluded Corporation made itself subject to the provisions of IC § 6-3-4-14, even though Excluded Corporation was not one of the members of Filing Group. The Department's addition of Excluded Corporation to Filing Group was in accordance with Taxpayer's own filing methodology and otherwise accepted by the Department. Thus, by consenting to Taxpayer's election to file a consolidated return, Excluded Corporation agreed to the provisions of IC § 6-3-4-14. The Department's methodology of computing Taxpayer's adjusted gross income with the inclusion of Excluded Corporation was proper and was consistent with Excluded Corporation's own consent.

FINDING

Taxpayer's protest is denied.

CONCLUSION

Taxpayer's protest is sustained in part and denied in part regarding "throwback" sales. Taxpayer's protest is denied with regard to the inclusion of Excluded Corporation.

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