DEPARTMENT OF STATE REVENUE

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Letter of Findings: 02-20130134
Corporate Income Tax
For the Tax Years 2007-2010

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ISSUE

I. Corporate Income Tax–Throw-Back Sales.

Authority: IC § 6-3-1-28; IC § 6-3-2-1; IC § 6-3-2-2; IC § 6-3-4-14; IC § 6-8.1-5-1; 45 IAC 3.1-1-38; 45 IAC 3.1-1-50; 45 IAC 3.1-1-64; Public Law 86-272 (codified at 15 U.S.C. § 381); I.R.C. § 63; Treas. Reg. § 1.1502–11; Treas. Reg. § 1.1502–12; Appeal of Finnigan Corporation, Cal. St. Board of Equal., Jan 24, 1990 (88-SBE-022A); Cooper Industries v. Indiana Dep't of State Revenue, 673 N.E.2d 1209 (Ind. Tax Ct. 1996); Tax Policy Directive 6 (June 1992); Multistate Tax Compact Art. IV.3 (1967); Multistate Tax Compact Allocation and Apportionment Regulation, Reg. IV.3 (1973).

Taxpayer protests the inclusion of certain throw-back sales in its Indiana sales numerator that Taxpayer argues were not required to be thrown back.

STATEMENT OF FACTS

Taxpayer is a corporation that is a manufacturer domiciled in Indiana with business operations in Indiana and other states. Taxpayer is a wholly owned subsidiary corporation. Taxpayer's parent corporation does not file a tax return in Indiana. However, Taxpayer's parent corporation has two other subsidiary corporations that also do business in Indiana that have elected to file a consolidated Indiana adjusted gross income tax return with Taxpayer. The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records and tax returns for the 2007 to 2010 tax years.

After reviewing Taxpayer's federal and state income tax returns and supporting information, the Department made adjustments to the calculation of the Indiana consolidated group's adjusted gross income tax. Specifically, the Department increased Taxpayer's sales factor apportionment numerator to include the throwback to Indiana of sales destined to several foreign states, because the Department found that Taxpayer's activities in those states did not exceed the protection of P.L. 86-272. As a result of the audit adjustments, the Department recalculated the consolidated group's Indiana apportioned business income and net operation loss deductions for the 2008 to 2010 tax years and issued an assessment of additional adjusted gross income tax for the 2007 tax year. Taxpayer protested. An administrative hearing was conducted, and this Letter of Findings results. Additional facts will be provided as necessary.

I. Corporate Income Tax–Throw-Back Sales.

DISCUSSION

As a threshold issue, it is Taxpayer's responsibility to establish that the tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made."

The Department determined that, for purposes of calculating Taxpayer's Indiana tax liability, the receipts from certain sales to out-of-state customers should be thrown back to Indiana because the sales were made within jurisdictions where Taxpayer did not have nexus with that state. The audit based its decision on 45 IAC 3.1-1-50 and instructions included on the state return that attribute those sales to Indiana if the taxpayer is not taxable in the state of the purchaser and the property is shipped from Indiana. Such sales are designated as "throw-back" sales. Id.

Indiana imposes a tax on each corporation's adjusted gross income attributable to "sources within Indiana." IC § 6-3-2-1(b). Where a corporation receives income from both Indiana and out-of-state sources, the amount of tax is determined by an apportionment formula established by IC § 6-3-2-2(b). For the years at issue, that formula operated by multiplying Taxpayer's total business income by a fraction composed of a property factor, a payroll factor, and a sales factor. The "sales factor" consists of a fraction, "the numerator of which is the total sales of the taxpayer in [Indiana] during the taxable year, and the denominator of which is the total sales of the taxpayer everywhere during the taxable year." IC § 6-3-2-2(e).

The basic rule for calculating the sales factor is found at IC § 6-3-2-2. IC § 6-3-2-2(e) provides that "[s]ales of tangible personal property are in this state if . . . (2) the property is shipped from an office, a store, a warehouse, a factory, or other place of storage in this state and . . . (B) the taxpayer is not taxable in the state of the purchaser." IC § 6-3-2-2(n) provides that "[f]or purposes of allocation and apportionment of income under this article, 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." Therefore, in order to properly attribute income to a foreign state, a taxpayer must show that one of the taxes listed in IC § 6-3-2-2(n)(1) has been levied against him or that the state has the jurisdiction to impose a net income tax regardless of "whether, in fact, the state does or does not." Id.

Taxpayer asserts that the Department's audit has incorrectly computed its Indiana apportionment sales tax numerator by including throw-back sales from California, Illinois, Michigan, Minnesota, North Carolina, Ohio, Pennsylvania, Utah, Washington, and Wisconsin. Taxpayer maintains that the sales to these states should not be thrown back because at least one of the entities in its consolidated groups has nexus in these states. Moreover, Taxpayer maintains that the sales to certain of the states should not be thrown back because it paid taxes, including "franchise taxes for the privileged of doing business," to those states. Finally, Taxpayer states that, for the 2009 and 2010 tax years, the sales to Wisconsin should not be thrown back because it had a physical presence in Wisconsin as of 2009.

A. Consolidate Group Nexus: "Finnigan" Concept.

The Department determined the amount of Taxpayer's sales factor numerator by including the throw back to Indiana of Taxpayer's sales that were destined to several foreign states, because the Department found that Taxpayer's activities in those states did not exceed the protection of P.L. 86-272. The Department required that Taxpayer throw back those sales made by a member of the affiliated group into states for which that member did not have nexus.

Taxpayer argues that the proper filing method requires Taxpayer and its subsidiary corporations to throwback sales only if none of the entities in the consolidated group have taxable nexus with that state. This is commonly referred to as the "Finnigan" concept.

The Department refers to Tax Policy Directive 6 (June 1992), which explains:

> The basic premise in filing combined/unitary returns is that all activities carried on by separate entities are part of a single unitary business (one taxpayer). Under the "Finnigan" concept a taxpayer is defined to mean all corporations (members) of a unitary group. This directive clarifies, but does not change the Department's position and stresses that in the interest of consistency the Department follows the decision of the California State Board of Equalization in the Appeal of Finnigan Corporation (Finnigan), Cal. St. Board of Equal., Jan 24, 1990 (88-SBE-022A). **This decision only applies to corporations who file unitary/combined tax returns in Indiana and does not apply to corporations not filing combined returns in Indiana.** The application of this California decision requires a change in the computation of the Indiana apportionment factors.
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> Apportionment Computation
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> Under Finnigan, sales made by a member of the unitary group to a destination in another state in which that member was not taxable should not be "thrown back" to Indiana unless no member of the unitary group was taxable in the other state. The Indiana property, payroll and sales of all corporations within a unitary group will be taken into account in apportioning unitary business income to Indiana. This includes property, payroll, and sales attributable to entities that are not subject to Indiana taxation under 15 USC Section 381 (P.L. 86-272). The total business income apportioned to Indiana will then be assigned among the individual corporations taxable in Indiana. Each taxable corporation is assigned a share of the business income according to its relative share (it's percentage share without considering the nontaxable members' share) of the unitary groups' Indiana property, payroll and sales factors.
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> **CONCLUSION**
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> **The adoption of Finnigan only applies to corporations who file unitary/combined returns in Indiana.** This is a change in the method used to compute the Indiana apportionment factors only and not a tax on entities who do not exceed mere solicitation as defined in P.L. 86-272. The development of a relative formula percentage is an integral part of the overall computation and should not be omitted. **Corporations not filing combined/unitary returns in Indiana will continue to apply the throwback sales rule in the normal fashion.**

(Emphasis added).

Accordingly, when the Department requires the taxpayer or when the taxpayer petitions to file a combined return, the Department has decided, as a matter of equity, to allow the "Finnigan" concept for apportionment for those taxpayers filing a combined return. Tax Policy Directive 6 "clarifies, but does not change the Department's position and stresses that in the interest of consistency the Department follows the decision of the California State Board of Equalization in the Appeal of Finnigan Corporation (Finnigan), Cal. St. Board of Equal., Jan 24, 1990 (88-SBE-022A)." This Directive clearly states that Finnegan only applies to corporations that file unitary/combined returns in Indiana.

IC § 6-3-2-2(l), (p), and (q) provide, "[I]f the allocation and apportionment provisions of [article 3] do not fairly represent the taxpayer's income derived from sources within the state of Indiana, the taxpayer may petition for or

the department may require . . . the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income," in IC § 6-3-2-2(l), including the "combined" filing method, in IC § 6-3-2-2(p), (q). A "combined income tax return" is defined as "any income tax return on which one (1) or more taxpayers report income, deductions, and credits on a combined basis with one (1) or more entities." IC § 6-3-1-28.

Next, the Department refers to IC § 6-3-4-14, which provides:

(a) An affiliated group of corporations shall have the **privilege of making a consolidated return with respect to the taxes imposed by IC 6-3**. The making of a consolidated return shall be upon the condition that all corporations which at any time during the taxable year have been members of the affiliated group **consent to all of the provisions of this section including all provisions of the consolidated return regulations prescribed pursuant to Section 1502 of the Internal Revenue Code and incorporated herein by reference and all regulations promulgated by the department implementing this section prior to the last day prescribed by law for the filing of such return**. The making of a consolidated return shall be considered as such consent. In the case of a corporation which is a member of the affiliated group for a fractional part of the year, the consolidated return shall include the income of such corporation for such part of the year as it is a member of the affiliated group.

(b) For the purposes of this section the term "affiliated group" shall mean an "affiliated group" as defined in Section 1504 of the Internal Revenue Code with the exception that the affiliated group shall not include any corporation which does not have adjusted gross income derived from sources within the state of Indiana.

(c) **For purposes of IC 6-3-1-3.5(b), the determination of "taxable income,"** as defined in Section 63 of the Internal Revenue Code, of any affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, **shall be determined pursuant to the regulations prescribed under Section 1502 of the Internal Revenue Code**.

(d) **Any credit against the taxes imposed by IC 6-3 which is available to any corporation which is a member of an affiliated group of corporations making a consolidated return shall be applied against the tax liability of the affiliated group.**

Accordingly, taxpayers are allowed the "privilege" of filing a consolidated return as long as each affiliate with Indiana source income agrees to be included in the consolidated filing and to determine its income "pursuant to the regulations prescribed under Section 1502 of the Internal Revenue Code." IC § 6-3-4-14.

Unlike those taxpayers filing in a combined return in Indiana that are required to be in a unitary business, those taxpayers filing in a consolidated return in Indiana are not required to be involved in a unitary business. The taxpayers are allowed the "privilege" of filing a consolidated return as long as each affiliate with Indiana source income agrees to be included in the consolidated filing and to determine its income "pursuant to the regulations prescribed under Section 1502 of the Internal Revenue Code." IC § 6-3-4-14. Therefore, the concept of an Indiana consolidated return is an entirely different concept than an Indiana combined return. Thus, the rules that apply for combined returns are not the same as the rules that apply for a consolidated return. See generally Cooper Industries v. Indiana Dep't of State Revenue, 673 N.E.2d 1209, 1215 (Ind. Tax Ct. 1996) (finding that since consolidated returns and combined returns "have different purposes and involve different considerations," the provisions that the legislature specifically enacted as exceptions for those filing a consolidated return will not apply for the combined filings unless the provisions were specifically enacted for both.)

Taxpayer supports its argument by stating that since credits for the entities in the consolidated return are taken regardless of which entity in the return earned the credit and how much income that entity earned, the apportionment rules for the consolidated return should also follow this same logic.

However, Taxpayer is mistaken. IC § 6-3-4-14 provides that each entity in the consolidated return shall determine its adjusted gross income pursuant to Section 1502 of the Internal Revenue Code. These regulations state that, in order to determine the taxpayer's "consolidated taxable income" under the regulations, each member of the consolidated group must first calculate its "separate taxable income." Treas. Reg. § 1.1502–11(a). This figure for each member "is computed in accordance with the provisions of the Code covering the determinations of taxable income of separate corporations," subject to sixteen adjustments. Treas. Reg. § 1.1502–12. Thus, each corporation in the group first determines its individual taxable income under chapter 1 (and I.R.C. § 63) and then specially modifies that figure for the purposes of chapter 6. Then, the group's "consolidated taxable income" is determined by aggregating the members' separate taxable incomes, subject to seven additional adjustments. Treas. Reg. § 1.1502–11. Since the regulations prescribed under Section 1502 provide that each member of the consolidated group must first calculate its "separate taxable income" in order to determine the taxpayer's "consolidated taxable income," then for the Indiana consolidated return purposes each taxpayer in the consolidate group is also considered on a separate basis. Therefore, without IC § 6-3-4-14(d) specifically providing the exception–to this separate calculation rule–that the credits will be allowed against the group's consolidated tax liability regardless of the entity's income tax liability that had earned the credit, the statutory return calculation would limit the application of the credits to that specific entity's tax liability.

Accordingly, for taxpayers filing in a consolidated return, the attribution of sales is done prior to the aggregation of those sales into the consolidated factor and only those tax attributes of the member are relevant.

In fact, for each of the tax years, the instructions for Schedule E, "Apportionment of Adjusted Gross Income for Corporations," of the Form IT-20, "Indiana Corporate Adjusted Gross Income Tax Return," followed this separate basis rule and provided that "[e]ach filing entity having income from sources both within and outside Indiana must complete a three-factor apportionment."

In the instant case, Taxpayer has not petitioned to file a combined return, and the Department is not attempting to require such a return. Since Taxpayer files its returns on a consolidated basis and not on a combined unitary basis, the "Finnigan" concept and analysis in making such determination in the context of a combined filing are inapplicable to Taxpayer's return calculation. Taxpayer wishes to take a "best of both worlds" approach and receive one of the equitable benefits that the Department grants to those entities filling on a combined unitary basis without reporting its income to Indiana on the combined unitary basis. Therefore, Taxpayer has failed to provide evidence sufficient to contradict the Department's determination that taxpayer is required to throw back those sales made by a member of the affiliated group into states for which that member did not have nexus, even though another member of its group did have nexus in that state.

B. "Taxable in Another State."

Taxpayer maintains that the audit assessment overlooks the nexus and taxation of Taxpayer in states where Taxpayer was "taxable in another state" including states where Taxpayer was "subject to a franchise tax for the privilege of doing business."

IC § 6-3-2-2(n) provides that "[f]or purposes of allocation and apportionment of income under this article, 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." (Emphasis added). Therefore, in order to properly attribute income to a foreign state, the taxpayer must show that one of the taxes listed in IC § 6-3-2-2(n)(1) has been levied against him or that the state has the jurisdiction to impose a net income tax regardless of "whether, in fact, the state does or does not." Id.

45 IAC 3.1-1-64, in relevant part, further explains:

> "Taxable in Another State" Defined. A corporation is "taxable in another state" under the Act when such state has jurisdiction to subject it to a net income tax. This test applies if the taxpayer's business activities are sufficient to give the state jurisdiction to impose a net income tax under the Constitution and statutes of the United States. Jurisdiction to tax is not present where the state is prohibited from imposing the tax by reason of the provision of Public Law 86-272, 15 U.S.C.A. §381-385.

15 U.S.C. § 381(a) establishes minimum standards for a state to impose a net income tax and states, in relevant part, that:

> **No State**, or political subdivision thereof, **shall have power to impose**, for any taxable year ending after September 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**:
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> (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**
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> (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)**. (**Emphasis added**).

15 U.S.C. § 381(c) further provides:

> Sales or solicitation of orders for sales by independent contractors. For purposes of subsection (a) of this section, **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**. (**Emphasis added**).

Therefore, in every transaction, at least one state has the authority to impose tax on income derived from the sale of tangible personal property. A state may impose a net income tax on a taxpayer only when the taxpayer's activity within the state exceeds "solicitation."

Accordingly, to claim that it is taxable in another state because it is "subject to a net income tax, a franchise tax measured by net income, [or] a franchise tax for the privilege of doing business" in that state, a taxpayer must demonstrate the statutory requirements are satisfied: (1) the taxpayer is actually doing business in that state; (2) the taxpayer is subject to the tax in that state. IC § 6-3-2-2(n).

"For apportionment purposes, a taxpayer is doing business in a state if it operates a business enterprise or activity in such state." 45 IAC 3.1-1-38. 45 IAC 3.1-1-38 provides seven categories illustrating what is considered as "doing business in a state." Specifically, 45 IAC 3.1-1-38 provides, in relevant part, as follows:

[A] taxpayer is "doing business" in a state if it operates a business enterprise or activity in such state including, but not limited to:

(1) Maintenance of an office or other place of business in the state

(2) Maintenance of an inventory of merchandise or material for sale distribution, or manufacture, or consigned goods

(3) Sale or distribution of merchandise to customers in the state directly from company-owned or operated vehicles where title to the goods passes at the time of sale or distribution

(4) Rendering services to customers in the state

(5) Ownership, rental or operation of a business or of property (real or personal) in the state

(6) Acceptance of orders in the state

(7) Any other act in such state which exceeds the mere solicitation of orders so as to give the state nexus under P.L. 86-272 to tax its net income.

. . .

The Multistate Tax Committee (of which Indiana has been an Associate and Project member) utilizes the same language as Indiana for the purposes of determining proper state tax liability of multistate taxpayers. The Multistate Tax Compact Art. IV.3 (1967) provides that:

For purposes of allocation and apportionment of income under this Article, a taxpayer is taxable in another State if (1) in that State he 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 do so.

Multistate Tax Compact Allocation and Apportionment Regulation IV.3.(1) (1973) to the Multistate Tax Compact Article IV.3 explains that:

(1) A taxpayer is "subject to" one of the taxes specified in Article IV.3.(1) if **it carries on business activities in a state** and **the state imposes such a tax thereon**. Any taxpayer which asserts that it is subject to one of the taxes specified in Article IV.3.(1) in another state **shall furnish to the [tax administrator] of this state upon his/her request evidence to support that assertion**. The [tax administrator] of this state may request that such evidence include proof that the taxpayer has filed the requisite tax return in the other state and has paid any taxes imposed under the law of the other state; the taxpayer's failure to produce such proof may be taken into account in determining whether the taxpayer in fact is subject to one of the taxes specified in Article IV.3.(1) in the other state.

Voluntary tax payment. If the taxpayer voluntarily files and pays one or more of such taxes when not required to do so by the laws of that state or pays a minimal fee for qualification, organization or for the privilege of doing business in that state, but

(A) does not actually engage in business activity in that state, or

(B) does actually engage in some business activity not sufficient for nexus and the minimum tax bears no relationship to the taxpayer's business activity within such state, the taxpayer is not "subject to" one of the taxes specified within the meaning of Article IV.3.(1).

Example: State A has a corporation franchise tax measured by net income for the privilege of doing business in that state. Corporation X files a return and pays the $50 minimum tax, although it carries on no business activity in State A. Corporation X is not taxable in State A.

(2) The concept of taxability in another state is based upon the premise that every state in which the taxpayer is engaged in business activity may impose an income tax even though every state does not do so. In states which do not, other types of taxes may be imposed as a substitute for an income tax. Therefore, only those taxes enumerated in Article IV.3.(1) which may be considered as basically revenue raising rather than regulatory measures shall be considered in determining whether the taxpayer is "subject to" one of the taxes specified in Article IV.3.(1) in another state.

(**Emphasis added**).

Thus, the Multistate Tax Committee adopts a similar standard as Indiana. When a taxpayer voluntarily files a return in a state for either a tax based upon net income or for the privilege of doing business, simply filing the return and/or paying such tax are not sufficient to determine whether the taxpayer is subject to the net income tax or state franchise tax for the privilege of doing business in that state and, therefore, taxable in that state. A taxpayer is required to demonstrate that it actually "engage[s] in some business activity" and "the minimum tax bears a relationship to the taxpayer's business activity within such state."

During the hearing, Taxpayer was asked to provide any documentation that establishes that it had business activities in the particular state and that it was subject to tax in that state based upon its business activities in that specific state. In response, during the course of the protest, Taxpayer presented tax returns, for the respective tax years, that were filed with Michigan (2007-2010 tax years), North Carolina (2007-2010 tax years), Ohio (2008-2009 tax years), Pennsylvania (2007-2010 tax years), Washington (2007-2010), Illinois (2007 tax year), California (2007 tax year), Wisconsin (2009 tax year), and Utah (2007 tax year) to demonstrate that Taxpayer was "subject to tax or taxable" in those states. A number of the returns were tax returns filed to report a tax that was either a net income tax or a franchise tax that was based upon net income. However, a number of the tax returns

were filed to report a tax that was not based upon net income but upon the privilege of doing business in those states. The respective states will be discussed based upon the type of return that was filed.

1. "Net Income Taxes" or "Franchise Taxes Based upon Net Income."

The California Corporate Income and Franchise Tax Return, the Illinois Corporate Income or Replacement Tax Return, the Utah Corporation Franchise or Income Tax Return, and the Wisconsin Franchise Income Tax Return presented were tax returns filed to report a tax that was either a "net income tax" or a "franchise tax that was based upon net income."

California

The tax return that Taxpayer presented failed to demonstrate that it operated a business enterprise or conducted business activity in California. Thus, the documentation Taxpayer presented did not show that Taxpayer maintained an office or other place of business in California; maintained an inventory of merchandise or material for sale distribution, or manufacture, or consigned goods in California; conducted the sale or distribution of merchandise to customers in California directly from company-owned or operated vehicles where title to the goods passes at the time of sale or distribution; rendered services to customers in California; owned, rented or operated a business or of property (real or personal) in California; accepted orders in California; and/or had any other act in those states which exceeds the mere solicitation of orders so as to give the state nexus under P.L. 86-272 to tax its net income. Thus, pursuant to 45 IAC 3.1-1-38, Taxpayer did not meet the first statutory requirement–doing business in California.

Specifically, Taxpayer's documentation demonstrated that Taxpayer was included in combined California Corporate Income and Franchise Tax Return filing–apparently "claiming P.L. 86-272 protection" for the 2007 tax year. All three entities, including Taxpayer, that were listed on the combined return had checked the box where the taxpayer makes the declaration that the "entity is not doing business in the state" for the 2007 tax year. Therefore, absent Taxpayer providing additional documentation demonstrating that Taxpayer had business activities in California that "exceed the mere solicitation of orders so as to give the state nexus under P.L. 86-272," the Department cannot agree with Taxpayer's contention that Taxpayer's "California sales" should no longer be thrown back to Indiana.

Illinois

The tax return that Taxpayer presented failed to demonstrate that it operated a business enterprise or conducted business activity in Illinois. Thus, the documentation that Taxpayer presented did not show that Taxpayer maintained an office or other place of business in Illinois; maintained an inventory of merchandise or material for sale distribution, or manufacture, or consigned goods in Illinois; conducted the sale or distribution of merchandise to customers in Illinois directly from company-owned or operated vehicles where title to the goods passes at the time of sale or distribution; rendered services to customers in Illinois; owned, rented or operated a business or of property (real or personal) in Illinois; accepted orders in Illinois; and/or had any other act in those states which exceeds the mere solicitation of orders so as to give the state nexus under P.L. 86-272 to tax its net income. Thus, pursuant to 45 IAC 3.1-1-38, Taxpayer did not meet the first statutory requirement–doing business in Illinois.

Specifically, the Illinois return presented was not Taxpayer's return but was a return filed by Taxpayer's parent corporation for the 2007 tax year. Taxpayer's documentation presented for Illinois demonstrated that Taxpayer's parent corporation filed an Illinois "net income and replacement tax return" imposing an income tax measured or based upon "net income." Since the Illinois return is imposing an income tax that is measured or based upon "net income," P.L. 86-272 applies to the return filed in Illinois. Since Taxpayer is not the entity filing the combined income tax return and merely has its income reported in its parent corporation's combined income to determine the tax due for its parent corporation, the documentation presented only shows that Taxpayer's parent corporation is taxable in Illinois for the 2007 tax year and does not demonstrate that Taxpayer's connections with Illinois exceeded the protections of P.L. 86-272. Thus, without Taxpayer providing additional documentation demonstrating that Taxpayer connection's with Illinois exceed the protections of P.L. 86-272, Taxpayer's documentation presented does not demonstrate that Taxpayer is "subject to tax" in Illinois. Therefore, the Department cannot agree with Taxpayer's contention that Taxpayer's "Illinois sales" should no longer be thrown back to Indiana.

Utah

The tax return that Taxpayer presented failed to demonstrate that it operated a business enterprise or conducted business activity in Utah. Thus, the documentation that Taxpayer presented did not show that Taxpayer maintained an office or other place of business in Utah; maintained an inventory of merchandise or material for sale distribution, or manufacture, or consigned goods in Utah; conducted the sale or distribution of merchandise to customers in Utah directly from company-owned or operated vehicles where title to the goods passes at the time of sale or distribution; rendered services to customers in Utah; owned, rented or operated a business or of property (real or personal) in Utah; accepted orders in Utah; and/or had any other act in those states which exceeds the mere solicitation of orders so as to give the state nexus under P.L. 86-272 to tax its net income. Thus, pursuant to 45 IAC 3.1-1-38, Taxpayer did not meet the first statutory requirement–doing business in Utah.

Specifically, the Utah return that Taxpayer provided was not Taxpayer's return but was a Utah return filed by an affiliated corporation for the 2007 tax year. Since Taxpayer is not the entity filing the income tax return, the documentation presented only shows that Taxpayer's affiliated corporation may be taxable in Utah and does not demonstrate that Taxpayer's connections with Utah exceeded the protections of P.L. 86-272. Thus, without Taxpayer providing additional documentation demonstrating that Taxpayer had business activities in Utah, the Department cannot agree with Taxpayer's contention that Taxpayer's "Utah sales" should no longer be thrown back to Indiana.

Wisconsin

The documentation Taxpayer presented for Wisconsin demonstrates that Taxpayer owned business property in Wisconsin and, therefore, had substantial nexus with Wisconsin for the 2009 tax year. Thus, Taxpayer was "taxable" in the state of Wisconsin for this year. Therefore, Taxpayer's protest to the imposition of tax resulting from the Department's inclusion of Taxpayer sales to Wisconsin as sales thrown back to Indiana for the 2009 tax year is sustained.

Accordingly, Taxpayer's protest to the imposition of tax resulting from the Department's including Taxpayer's sales to California, Illinois, and Utah as sales thrown back to Indiana is denied. However, Taxpayer's protest to the imposition of tax resulting from Taxpayer sales to Wisconsin being thrown back to Indiana for the 2009 tax year is sustained.

2. "Franchise Tax:" "for the Privilege of Doing Business."

The Washington Business and Occupation Actions Returns, the North Carolina Corporation Tax Returns, the Michigan Single Business Tax Returns, the Pennsylvania Corporate Tax Reports, and the Ohio Corporate Franchise Tax Reports presented were tax returns filed to report a tax that was not based upon net income but upon the "privilege of doing business" in those states.

As discussed previously, under IC § 6-3-2-2(n)(1), "a taxpayer is taxable in another state if . . . in that state the taxpayer is subject to . . . a franchise tax for the privilege of doing business." Thus, to claim that it is taxable in another state because it is "subject to a franchise tax for the privilege of doing business" in that state, a taxpayer must demonstrate the statutory requirements are satisfied: (1) the taxpayer is actually doing business in that state; (2) the taxpayer is subject to a franchise tax in that state, which is imposed on the taxpayer for the privilege of doing business in that state; namely, the tax is imposed in connection with the taxpayer's business enterprise or activities in that state. IC § 6-3-2-2(n).

"For apportionment purposes, a taxpayer is doing business in a state if it operates a business enterprise or activity in such state." 45 IAC 3.1-1-38. Specifically, 45 IAC 3.1-1-38 provides seven (7) categories illustrating what is considered as "doing business in a state." However, when a tax is not classified as "net income tax" or is not based upon or measured by "net income," then P.L. 86-272 does not apply.

Taxpayer's documentation demonstrated that Taxpayer operated a business enterprise and/or conducted business activity in such state and that the state tax "franchise tax returns" were filed and the taxes imposed were in connection to Taxpayer's business activities or enterprises in those states. Accordingly, Taxpayer's protest to the imposition of tax resulting from Taxpayer sales to Washington for the 2007 through 2010 tax years, to Michigan for the 2007 through 2010 tax years, to North Carolina for the 2007 through 2010 tax years, to Pennsylvania for the 2007 through 2010 tax years, and to Ohio for the 2008 and 2009 tax years being thrown back to Indiana is sustained.

FINDING

Taxpayer's protest is sustained in part and denied in part. Taxpayer's protest to the imposition of adjusted gross income tax as a result of the Department's determination that Taxpayer is required to throw back those sales made by a member of the affiliated group into states for which that member did not have nexus–even though another member of its group did have nexus in that state–is denied, as discussed in subpart A. Taxpayer's protest to the imposition of tax resulting from the Department's including Taxpayer's sales to California, Illinois, and Utah as sales thrown back to Indiana is denied, as discussed in subpart B(1). Taxpayer's protest to the imposition of tax resulting from Taxpayer sales to Wisconsin being thrown back to Indiana for the 2009 tax year is sustained, as discussed in subpart B(1). Taxpayer's protest to the imposition of tax resulting from Taxpayer sales to Washington for the 2007 through 2010 tax years, to Michigan for the 2007 through 2010 tax years, to North Carolina for the 2007 through 2010 tax years, to Pennsylvania for the 2007 through 2010 tax years, and to Ohio for the 2008 and 2009 tax years being thrown back to Indiana is sustained, as discussed in subpart B(2).

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