New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-05(17)C
Corporation Tax
December 12, 2005

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. C040526A

On May 26, 2004, a Petition for Advisory Opinion was received from Wausau Tile, Inc, P.O. Box 1520, 9001 Business Highway 51, Wausau, Wisconsin 54402-1520.

The issue raised by Petitioner, Wausau Tile, Inc., is whether its activities within New York State exceed mere solicitation under Public Law 86-272, and are thereby sufficient to make Petitioner subject to the franchise tax imposed under Article 9-A of the Tax Law.

Petitioner submits the following facts as the basis for this Advisory Opinion.

Petitioner is located outside of New York State. Petitioner manufactures and sells certain concrete amenities. All of Petitioner's manufacturing is done outside of New York. Petitioner does not have any employees or property located in New York. Petitioner does not lease any property in New York nor does it maintain an office, local mailing address or telephone number in New York. Petitioner does not have any New York bank accounts.

All of Petitioner's product sales in New York originate from out-of-state salesmen or independent contractors whose main offices are located outside of New York. All purchase orders from customers in New York are forwarded to Petitioner's headquarters outside of New York, for acceptance or rejection. All orders of tangible personal property are constructed, fabricated and shipped from outside of New York.

Orders are delivered to customers in New York via common carriers or by Petitioner's wholly owned subsidiary (Subsidiary.) Subsidiary makes 20 or more deliveries of Petitioner's products to New York customers annually.

Petitioner does not provide installation of its products. Petitioner provides instruction on proper installation of its products via the telephone or through sales literature. Petitioner offers minimal assistance with respect to repairs of its products sold in New York. Generally, if a product is damaged, Petitioner sends a new item to the customer instead of repairing the damaged item. Repairs, if needed, are primarily performed by the general contractor or subcontractor (Petitioner's customers) on the job site; any support or assistance provided by Petitioner is via telephone. Only on rare occasions (perhaps once every two or three years) does Petitioner send an employee to New York to repair an item. The return of products to Petitioner for a refund or for repair is rare. If products are returned to Petitioner by its New York customers, such products are returned through common carriers.

Petitioner sells approximately $2 million of products to New York customers annually. New York sales represent an average of 5% of Petitioner's total annual sales.

Petitioner's other contacts with New York include being a defendant in a product liability case and being a party to an agreement with a university in New York (University) for the development of new products in which Petitioner has agreed to pay the University royalties on the sales of these products. According to the agreement, the University is solely responsible for the protocol of the research conducted under the agreement; all persons working on the research are to be employees of the University; and all equipment, materials, and other tangible results of the research vest in the University. The agreement specifically provides that Petitioner is not an agent of the University, and is not in a joint venture or partnership with the University.

Applicable law and regulations

Section 209.1 of Article 9-A of the Tax Law imposes an annual franchise tax as follows:

> For the privilege of exercising its corporate franchise, or of doing business, or of employing capital, or of owning or leasing property in this state in a corporate or organized capacity, or of maintaining an office in this state, for all or any part of each of its fiscal or calendar years, every domestic or foreign corporation, except corporations specified in subdivision four of this section, shall annually pay a franchise tax, upon the basis of its entire net income base, or upon such other basis [capital base, minimum taxable income bases or the fixed dollar minimum] as may be applicable as hereinafter provided, for such fiscal or calendar year or part thereof ....

Section 1-3.2 of the Business Corporation Franchise Tax Regulations ("Regulations") provides, in part:

> (b) *Foreign corporation – doing business.* (1) The term doing business is used in a comprehensive sense and includes all activities which occupy the time or labor of people for profit. Regardless of the nature of its activities, every corporation organized for profit and carrying out any of the purposes of its organization is deemed to be doing business for the purposes of the tax. In determining whether a corporation is doing business, it is immaterial whether its activities actually result in a profit or a loss.
>
> (2) Whether a corporation is doing business in New York State is determined by the facts in each case. Consideration is given to such factors as:
>
> (i) the nature, continuity, frequency, and regularity of the activities of the corporation in New York State;
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> (ii) the purposes for which the corporation was organized;
>
> (iii) the location of its offices and other places of business;
>
> (iv) the employment in New York State of agents, officers and employees; and

(v) the location of the actual seat of management or control of the corporation.

(c) *Foreign corporation – employing capital.* The term employing capital is used in a comprehensive sense. Any of a large variety of uses, which may overlap other activities, may give rise to taxable status. In general, the use of assets in maintaining or aiding the corporate enterprise or activity in New York State will make the corporation subject to tax. Employing capital includes such activities as:

(1) maintaining stockpiles of raw materials or inventories; or

(2) owning materials and equipment assembled for construction.

(d) *Foreign corporation – owning or leasing property.* The owning or leasing of real or personal property within New York State constitutes an activity which subjects a foreign corporation to tax. Property owned by or held for the taxpayer in New York State, whether or not used in the taxpayer's business, is sufficient to make the corporation subject to tax. Property held, stored or warehoused in New York State creates taxable status. Property held as a nominee for the benefit of others creates taxable status. Also, consigning property to New York State may create taxable status if the consignor retains title to the consigned property.

(e) *Foreign corporation – maintaining an office.* A foreign corporation which maintains an office in New York State is engaged in an activity which makes it subject to tax. An office is any area, enclosure or facility which is used in the regular course of the corporate business. A salesperson's home, a hotel room, or a trailer used on a construction job site may constitute an office.

However, section 1-3.4(b)(9) of the Regulations provides for an exemption from taxation under Article 9-A for corporations which are exempt pursuant to the provisions of Public Law 86-272 (15 USCA §§ 381-384) and states as follows:

(i) A foreign corporation whose income is derived from interstate commerce is not subject to tax under article 9-A of the Tax Law if the activities of the corporation in New York State are limited to either, or both of the following:

(*a*) the solicitation of orders by employees or representatives in New York State for sales of tangible personal property and the orders are sent outside New York State for approval or rejection; and if approved, are filled by shipment or delivery from a point outside New York State; and

(*b*) the solicitation of orders for sales of tangible personal property by employees or representatives in New York State in the name of or for the benefit of a prospective customer of such corporation if the customer's orders to the

corporation are sent outside the State for approval or rejection; and, if approved, are filled by shipment or delivery from a point outside New York State.

(ii) For purposes of this exemption, a corporation will not be considered to have engaged in taxable activities in New York State during the taxable year merely by reason of sales in New York State or the solicitation of orders for sales in New York State, of tangible personal property on behalf of the corporation by one or more independent contractors. A corporation will not be considered to have engaged in taxable activities in New York State by reason of maintaining an office in New York State by one or more independent contractors whose activities on behalf of the corporation in New York State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

(iii) The term *independent contractor* means a commission agent, broker, or other independent contractor who is engaged in selling, or in 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. The term *representative* does not include an independent contractor.

(iv) In order to be exempt by virtue of Public Law 86-272, the activities in New York State of employees or representatives must be limited to the solicitation of orders. The solicitation of orders includes offering tangible personal property for sale or pursuing offers for the purchase of tangible personal property and those ancillary activities, other than maintaining an office, that serve no independent business function apart from their connection to the solicitation of orders. Examples of activities performed by such employees or representatives in New York State that are entirely ancillary to the solicitation of orders include:

(*a*) the use of free samples and other promotional materials in connection with the solicitation of orders;

(*b*) passing product inquiries and complaints to the corporation's home office;

(*c*) using autos furnished by the corporation;

(*d*) advising customers on the display of the corporation's products and furnishing and setting up display racks;

(*e*) recruitment, training and evaluation of sales representatives;

(*f*) use of hotels and homes for sales-related meetings;

(*g*) intervention in credit disputes;

(*h*) use of space at the salesperson's home solely for the salesperson's convenience...;

(*i*) participating in a trade show or shows, provided that participation is for not more than 14 days, or part thereof, in the aggregate during the corporation's taxable year for Federal income tax purposes....

(v) Activities in New York State beyond the solicitation of orders will subject a corporation to tax in New York State unless such activities are *de minimis*. Activities will not be considered *de minimis* if such activities establish a nontrivial additional connection with New York State. Solicitation activities do not include those activities that the corporation would have reason to engage in apart from the solicitation of orders but chooses to allocate to its New York State sales force. In determining whether a corporation's activities exceed the solicitation of orders, all of the corporation's activities in New York State will be considered. Examples of activities which go beyond the solicitation of orders include:

(*a*) making repairs to or installing the corporation's products;

(*b*) making credit investigations;

(*c*) collecting delinquent accounts;

(*d*) taking inventory of the corporation's products for customers or prospective customers;

(*e*) replacing the corporation's stale or damaged products;

(*f*) giving technical advice on the use of the corporation's products after the products have been delivered to the customer.

(vi) Maintaining an office ... in New York State will make a corporation taxable....

Opinion

Pursuant to section 1-3.4(b)(9) of the Regulations, a corporation is not subject to franchise tax in New York State if it is exempt pursuant to the provisions of Public Law 86-272. To be exempt pursuant to Public Law 86-272, a corporation's activities in New York State must be either (a) limited to the solicitation of orders by employees or representatives in New York State for sales of tangible personal property, or be entirely ancillary to such solicitation of orders, or (b) if the activities exceed the solicitation of orders, the activities must be considered to be *de minimis*. In addition, the orders must be sent outside New York State for approval or rejection; and if approved, must be filled by shipment or delivery from a point outside New York State.

In *KPMG Peat Marwick LLP*, Adv Op Comm T&F, March 27, 1997, TSB-A-97(8)C, a manufacturing company employed a sales staff that solicited orders from customers in New York State. The orders were approved at the company headquarters in Indiana, and the company delivered the products from its facility in Indiana to its New York customers via its own commercial vehicles. In addition, the company also did *backhauling*. That is, it used the vehicles that delivered its products to customers in New York to pick up products in New York that did not meet customer specifications and returned them to the company's facility in Indiana. The customer either received a replacement product or got a credit for the cost of the product. The company also transported the trim and scrap of its New York customers back to Indiana, for which each customer received a credit against the price of future products. The opinion held that the backhauling activities were post delivery activities in New York that went beyond the solicitation of orders and the company would be subject to tax under Article 9-A of the Tax Law pursuant to section 1-3.4(b)(9)(v) of the Regulations, unless such activities were deemed to be *de minimis*.

In this case, Petitioner has salesmen or independent contractors who solicit orders from customers in New York State. The orders are forwarded to Petitioner's headquarters outside of New York for approval. Petitioner delivers the products from its facilities outside of New York to its New York customers via common carriers or Subsidiary. Petitioner does not install its products and offers only minimal assistance with respect to repairs. Generally, damaged products are replaced rather than repaired. If repairs are needed the work is primarily performed by Petitioner's customer on the job site, with support or assistance provided by Petitioner by telephone from outside of New York. On a rare occasion (perhaps once every two or three years) Petitioner sends an employee to New York to repair an item. Any product that is returned to Petitioner is sent by common carrier to Petitioner's facilities outside of New York. Under section 1-3.4(b)(9)(v)(*a*) of the Regulations, making repairs to the products sold is an activity that exceeds the solicitation of orders. However, in this case, making a repair in New York once every two or three years is *de minimis* activity in New York, and pursuant to section 1-3.4(b)(9), these activities would not make Petitioner subject to tax under Article 9-A of the Tax Law.

In addition to these solicitation activities, Petitioner is a defendant in a product liability case. Also, Petitioner is a party to an agreement with the University for the development of new products in which Petitioner has agreed to pay the University royalties on the sales of the products developed by the University. These activities by Petitioner are activities that go beyond the solicitation of orders as contemplated by Public Law 86-272, and Petitioner would be subject to franchise tax under Article 9-A if these activities meet the standards for taxability under section 209.1 and section 1-3.2(b), (c), (d) and (e) of the Regulations.

With respect to the product liability case, being a defendant in litigation is not an activity for which Petitioner was organized in its pursuit of profit and gain. Such activity does not constitute *doing business* as contemplated under section 209.1 of the Tax Law and section 1-3.2(b) of the Regulations. Such activity also does not constitute employing capital, owning or

leasing property or maintaining an office in New York State as contemplated under section 209.1 of the Tax Law and section 1-3.2(b) of the Regulations.

With respect to the agreement with the University for the development of new products, the University is solely responsible for the research conducted, including the provision of all employees, equipment and materials. The results of the research vest in the University. Petitioner is not an agent, joint venturer or partner of the University. There is no indication that the University is an agent of Petitioner. It appears from the facts presented that under the agreement, Petitioner is merely a licensee allowed to sell the products that may be developed by the University, and will pay a royalty to the University for such right to sell the products. Such activity does not constitute *doing business* as contemplated under section 209.1 of the Tax Law and section 1-3.2(b) of the Regulations.

Accordingly, it appears that the totality of Petitioner's activities in New York State as described in this Advisory Opinion would not meet the standards for taxability under section 209.1 of the Tax Law and sections 1-3.2(b), (c), (d) and (e) and 1-3.4(b)(9) of the Regulations. Therefore, Petitioner would not be subject to tax under Article 9-A of the Tax Law.

Note that while Petitioner may not be subject to tax under Article 9-A of the Tax Law, it is possible that Petitioner could be required to be included in a combined report with Subsidiary and/or other taxpayers under Article 9-A, if both the capital stock and unitary business requirements have been met and the Commissioner of Taxation and Finance determines that inclusion is necessary to properly reflect the tax liability of one or more of the taxpayers because of: (1) substantial intercorporate transactions, or (2) some agreement, understanding, arrangement or transaction whereby the activity, business, income or capital of any taxpayer is improperly or inaccurately reflected. (See section 211.4 of the Tax Law; Subpart 6-2 of the Regulations; *Matter of Sherwin-Williams Company v Tax App Trib Dept T&F*, 12 AD3d 112, (3rd Dept 2004); *Alpharma, Inc.*, Dec Tax App Trib, August 5, 2004, DTA No. 817895).

DATED: December 12, 2005

/s/
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NOTE: The opinions expressed in Advisory Opinions are Limited to the facts set forth therein