

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-97(8)C
Corporation Tax

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C961113C

On November 13, 1996, a Petition for Advisory Opinion was received from KPMG Peat Marwick LLP, 2400 First Indiana Plaza, 135 North Pennsylvania Street, Indianapolis, Indiana 46204.

The issue raised by Petitioner, KPMG Peat Marwick LLP, is whether a corporation's backhauling activity exceeds Public Law 86-272 protection thereby creating nexus for New York State franchise tax purposes under Article 9-A of the Tax Law.

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

The Manufacturing Company is a corporation organized under the laws of the State of Indiana. Manufacturing Company maintains its commercial domicile, headquarters and only production facility in Indiana.

Manufacturing Company's products are sold throughout the country. Manufacturing Company employs a sales staff to solicit orders from customers in various states, including New York. Orders are subject to approval at company headquarters in Indiana. After an order is approved, the Manufacturing Company delivers the products to its New York customers via its own commercial vehicles. These commercial vehicles make routine trips to New York. On occasion, the Manufacturing Company ships its products to its New York customers via common carrier.

Manufacturing Company uses its own commercial vehicles to pick up products in New York that do not meet customer specifications ("backhauling"). These materials are returned to Indiana. The customer either receives a replacement product or gets a credit for the cost of the product. Manufacturing Company also transports the trim and scrap of its New York customers back to Indiana, for which the customers receive a credit against the price of future purchases.

Petitioner states that approximately four percent of Manufacturing Company's total revenues earned in New York State are received from backhauling activities where it picks up goods (other than delivered products) from its customers or goods from other entities and delivers the goods to a location in Indiana (not necessarily to the Manufacturing Company's facility).

Section 209.1 of Article 9-A of the Tax Law imposes an annual franchise tax on domestic or foreign corporations for the privilege of exercising a corporate franchise, doing business, employing capital, owning or leasing property in a corporate or organized capacity, or maintaining an office in New York State for all or any part of each of its fiscal or calendar years.

Section 1-3.4(b)(9) of the Corporation Tax Franchise Tax Regulations ("Article 9-A 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.

...

(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.

(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 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.

In this case, the Manufacturing Company employs a sales staff to solicit orders from customers in New York State. The orders are subject to approval at company headquarters in Indiana. The Manufacturing Company delivers the products from its facility in Indiana to its New York customers via its own commercial vehicles. Pursuant to section 1-3.4(b)(9)(i)(a) of the Article 9-A Regulations, these activities would not make the Manufacturing Company subject to tax under Article 9-A of the Tax Law.

However, in addition to these activities, the Manufacturing Company also does backhauling. That is, the Manufacturing Company uses its vehicles, that delivered its products to customers in New York, to pick up products in New York that do not meet customer specifications and return them to its facility in Indiana. The Manufacturing Company also picks up trim and scrap from its New York customers and transports it back to Indiana and gives the customers credits against the price of their future purchases. These activities are similar to the post delivery examples contained in section 1-3.4(b)(9)(v) of the Article 9-A Regulations, particularly, "replacing the corporation's stale or damaged products". These post delivery backhauling activities in New York by the

Manufacturing Company are activities that go beyond the solicitation of orders as contemplated by Public Law 86-272, and will subject the Manufacturing Company to franchise tax under Article 9-A unless they are deemed to be *de minimis*.

The post delivery backhauling activity, by itself, may be considered to be *de minimis* and might not establish more than a nontrivial additional connection with New York State as contemplated in section 1-3.4(b)(9)(v) of the Article 9-A Regulations. The facts in this case are insufficient to determine whether the Manufacturing Company's post delivery backhauling activity is *de minimis*. However, the Manufacturing Company also engages in backhauling activities unrelated to the delivery of the Manufacturing Company's products. These backhauling activities, which produce four percent of the Manufacturing Company's total revenues earned in New York State, are not protected by Public Law 86-272. Therefore, the Manufacturing Company is doing business, employing capital, or owning or leasing property in a corporate or organized capacity in New York State pursuant to section 209.1 of the Tax Law, and is subject to tax under Article 9-A of the Tax Law.

DATED: March 27, 1997

/s/
John W. Bartlett
Deputy Director
Technical Services Bureau

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.