

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

TSB-A-98(25)C
Corporation Tax
December 2, 1998

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C980427A

On April 27, 1998, a Petition for Advisory Opinion was received from Crowe, Chizek and Company LLP, 301 S. Main Street, Suite 400, Elkhart, Indiana 46516.

The issue raised by Petitioner, Crowe, Chizek and Company LLP, is whether a foreign corporation that pays fees for storage and handling of goods, held in a New York warehouse, for delivery to a New York customer is 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.

ABC Corporation, a manufacturing company, is legally and commercially domiciled outside New York State. This company has no payroll, office or other business location in New York State. ABC Corporation manufactures component assemblies that become part of its customers' consumer products. All property sold by ABC is custom manufactured to the design specifications of the specific customer. No product manufactured for one customer is ever delivered to a different customer. Delivery of product to customers in New York is provided by common carrier or picked up by the New York customer at one of ABC Corporation's business locations outside New York State. ABC Corporation's primary New York customer operates its manufacturing process utilizing a "just in time" inventory delivery concept. To protect the customer's continued supply, a small quantity (approximately one day's usage for this customer) of ABC Corporation's shipments to this customer are stored in transit at a warehouse operated by a common carrier of freight in New York State. ABC Corporation pays storage and handling charges separate from delivery charges for this service.

Petitioner contends that when the product is shipped, it is in interstate commerce at all times until delivered to the New York customer, including the time it is in temporary storage at a warehouse operated by the common carrier. Petitioner states that (1) the product arrives at the point of temporary storage in New York designated for delivery to a specified customer; (2) no product shipped in this manner is ever returned or diverted to another destination without first being delivered to the designated customer; and (3) all property temporarily stored in this manner is delivered to the designated customer.

ABC Corporation utilizes an account team approach in marketing to its primary customer in New York. The account team includes members from marketing, engineering, finance, manufacturing and quality assurance. Marketing members visit the customer's location on a regular basis, usually at least once a month. All members of the team stay in regular contact with the

assigned customer to assure the customer's satisfaction in utilizing ABC Corporation's products. Petitioner states that this contact is usually by telephone, mail or e-mail with a face-to-face meeting only once or twice a year. This team approaches the design and sale of the company's products as a component of the customer's end product. Under this approach, design changes may be suggested to the customer's products that would better integrate the company products into the customer's manufacturing process, thus improving the customer's manufacturing efficiency. For instance, a customer may want ABC Corporation to manufacture a particular part that will be a component of the customer's manufactured product. ABC's account team may suggest a design change for the component part that would enable ABC Corporation to produce a better and maybe a cheaper part to sell to the customer. Leadership responsibilities for the account teams are placed with the Vice President - Divisional Sales. All technical information presented to the customer has some relation to the components sold by ABC Corporation and no charges are made to the customer for any of this information. ABC Corporation began selling property to customers in New York sometime prior to 1990.

Law and Regulations

Section 209.1 of Article 9-A of the Tax Law imposes the business corporation franchise tax on every foreign corporation, unless specifically exempt, for the privilege of doing business, or of employing capital, or of owning or leasing property in New York State in a corporate or organized capacity, or of maintaining an office in New York State.

However, section 1-3.4(b)(9) of the Business Corporation 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.

(vi) Maintaining an office, shop, warehouse or stock of goods in New York State will make a corporation taxable....

Pursuant to section 1-3.4(b)(9) of the Article 9-A Regulations, a corporation is not subject to 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 limited to 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. Activities that exceed the solicitation of orders will subject a corporation to tax in New York State.

Pursuant to section 1-3.4(b)(9)(vi) of the Article 9-A Regulations, the storage of inventory in New York is an activity that exceeds the solicitation of orders and the activity will make a corporation taxable under Article 9-A.

Further, section 1-3.2(d) of the Article 9-A Regulations provides that:

[t]he 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....

However, section 208.19 of the Tax Law, effective September 1, 1997, provides:

The term "fulfillment services" shall mean any of the following services performed by an entity on its premises on behalf of a purchaser:

(a) the acceptance of orders electronically or by mail, telephone, telefax or internet;

(b) responses to consumer correspondence or inquiries electronically or by mail, telephone, telefax or internet;

(c) billing and collection activities; or

(d) the shipment of orders from an inventory of products offered for sale by the purchaser.

Section 209.2(f) of the Tax Law, effective September 1, 1997, provides that a foreign corporation shall not be deemed to be doing business, employing capital, owning or leasing property, or maintaining an office in New York State, for purposes of Article 9-A of the Tax Law, by reason of "the use of fulfillment services of an entity other than an affiliated entity and the ownership of property stored on the premises of such entity in conjunction with such services".

In Wisconsin Dept of Revenue v Wrigley, 505 US 214, the United States Supreme Court interpreted the term "solicitation" for purposes of PL 86-272. The Court stated that "[a]ctivities that take place after a sale will ordinarily not be entirely ancillary in the sense we have described ... but we are not prepared to say that will invariably be true. Moreover, the pre-sale/post-sale distinction is hopelessly unworkable. Even if one disregards the confusion that may exist concerning when a sale takes place ... manufacturers and distributors ordinarily have ongoing relationships that involve continuous sales, making it often impossible to determine whether a particular incidental activity was related to the sale that preceded it or the sale that followed it."

Conclusion

With respect to the account team approach in marketing to New York customers, Petitioner states that the team approaches the design and sale of ABC Corporation's products as a component of the customer's product, and may suggest design changes to the customer that would better integrate the company's products into the customer's manufacturing process, and that all technical information presented to the customer has some relation to the components sold by ABC Corporation. ABC Corporation does not charge the customer for any of this information.

In accord with Wrigley, supra, ABC Corporation's account team approach in marketing, as described herein, makes it impossible to determine whether a particular incidental activity is related to the sale that precedes it or the sale that follows it. However, it appears that ABC Corporation's account team's activities in New York State do not serve any independent business function apart from their connection to the solicitation of orders. Accordingly, these activities in New York State appear to be ancillary to the solicitation of orders that would constitute the solicitation of orders pursuant to PL 86-272 and section 1-3.4(b)(9) of the Article 9-A Regulations. If this is the case,

these activities would not make ABC Corporation subject to the tax imposed under Article 9-A of the Tax Law.

With respect to the storage of ABC Corporation's product at a warehouse in New York State operated by a common carrier of freight during the shipment of the product to a New York customer, ABC Corporation pays storage and handling charges for this service separate from delivery charges. This storage of goods constitutes a break in the transit of the product from ABC Corporation to the New York customer. Accordingly, pursuant to section 1-3.4(b)(9)(vi) and section 1-3.2(d) of the Article 9-A Regulations, ABC Corporation's storage of inventory in a warehouse in New York State before it is delivered to the customer is an activity that would make ABC Corporation subject to tax under Article 9-A of the Tax Law.

However, pursuant to section 209.2(f) of the Tax Law, effective September 1, 1997, ABC Corporation will not be subject to tax under Article 9-A of the Tax Law due to the storage of inventory in a New York warehouse because it is using the fulfillment services of the common carrier to ship the orders from an inventory of products offered for sale by ABC Corporation pursuant to section 208.19(d) of the Tax Law.

DATED: December 2, 1998

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

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