DEPARTMENT OF STATE REVENUE

02-20150384.LOF

(Redacted) Letter of Findings: 02-20150384
Corporate Income Tax
For the Tax Years 2002-2012

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 requires the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Business did not provide sufficient documentation to prove the Department's assessment of additional corporate income tax incorrect.

I. Adjusted Gross Income Tax–Interest Add-back.

Authority: IC § 6-3-2-2; IC § 6-8.1-5-1; IC § 6-3-2-20; IC § 6-3-4-14; Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Dep't of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); Scopelite v. Indiana Dep't of Local Gov't Fin., 939 N.E.2d 1138 (Ind. Tax Ct. 2010); Wendt LLP v. Indiana Dep't of State Revenue, 977 N.E.2d 480 (Ind. Tax Ct. 2012).

Taxpayer protests the Department's assessment of additional income tax based on adding back intercompany interest expense deductions.

II. Adjusted Gross Income Tax –Throw-back Sales.

Authority: IC § 6-8.1-5-1; IC § 6-3-2-2; 45 IAC 3.1-1-53; 45 IAC 3.1-1-38; 45 IAC 3.1-1-64; Indiana Dep't of Revenue v. Kimberly-Clark Corp., 416 N.E.2d 1264 (Ind. 1981); Wisconsin Dep't. of Revenue v. William Wrigley, Jr., Co., 505 U.S. 214 (1992); Tyler Pipe Industries, Inc. v. Washington State Department of Revenue, 483 U.S. 232 (1987).

Taxpayer protests the throw-back of out-of-state sales to its Indiana income.

III. Adjusted Gross Income Tax–Net Operating Losses.

Authority: IC § 6-3-2-2.6; IC § 6-8.1-5-1.

Taxpayer protests the disallowance of net operating losses.

IV. Tax Administration–Penalty.

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the imposition of the negligence penalty.

STATEMENT OF FACTS

Taxpayer manufactures and sells wire and wire products. Taxpayer sells the wire on spools, bobbins, reels, etc. These returnable containers are part of a deposit program; customers pay a deposit for the spools and receives their deposit back once the spool is returned to Taxpayer. Taxpayer has a parent entity with several related entities. There are only two entities of this group that file in Indiana on a consolidated basis.

In 2014, the Indiana Department of Revenue ("Department") conducted an audit for the tax years ending 2002-2012. The Department assessed Taxpayer additional corporate income tax. Taxpayer protested the assessment and the imposition of the negligence penalties. An administrative hearing was held and this Letter of Findings results. Further facts will be supplied as necessary.

I. Adjusted Gross Income Tax–Interest Add-back.

DISCUSSION

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing 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." Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Further, "[W]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to an agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" Dep't of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579, 583 (Ind. 2014). Thus all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

For the years 2002-2012 Taxpayer reported a large interest expense deduction on two loans from its parent company ("Parent"). During the audit, Taxpayer provided the loan agreements. The agreements state that interest is payable at the end of each calendar month at the rate of eight percent for one loan and five percent for the other loan; the agreements also state that the principal payments are due upon demand. Taxpayer makes a book entry each month for the interest expense. The Department determined that Taxpayer was required to add back the interest for the years 2002-2005 pursuant to IC §6-3-2-2(l), for the following four reasons:

1. There was no intent to pay back the loan. A book entry was made at the end of each month to record the interest expense, and the taxpayer has not made any interest payments on the loans.
2. Inter-company interest is eliminated and has no financial effect on the consolidated federal return.
3. The parent company did not report the interest income to any other state.
4. Taxpayer was unable to establish by preponderance of the evidence that the transactions giving rise to the intangible expenses and related interest expenses between the taxpayer and the recipient did not have Indiana tax avoidance as a principal purpose.

In 2006 the legislature enacted IC § 6-3-2-20 requiring taxpayers to add back interest expenses when necessary. The Department determined that Taxpayer was required to add back the interest expense for the years 2006-2012 pursuant to IC § 6-3-2-20.

A. Interest Add-back for years 2002-2005.

For the tax years ending 2002-2005 IC § 6-3-2-2(l) stated:

> If the allocation and apportionment provisions of this article 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, in respect to all or any part of the taxpayer's business activity, if reasonable:
> (1) separate accounting;
> (2) the exclusion of any one (1) or more of the factors;
> (3) the inclusion of one (1) or more additional factors which will fairly represent the taxpayer's income derived from sources within the state of Indiana; or
> (4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

The cited statutory provision provides the Department with authority to apportion or allocate income derived from Indiana sources among commonly owned organizations in order to fairly reflect Indiana income.

During the audit, Taxpayer did offer an alternative accounting method to allow Taxpayer to include Parent on its consolidated return. Taxpayer stated that this would "represent the external interest expense of the company as a whole." The Department determined that this alternative method would not fairly reflect Indiana Income for the following reasons: 1) Parent does not have nexus in Indiana; 2) including Parent on the consolidated return would eliminate the interest expense; 3) Parent's interest expense deductions on the consolidated return increased significantly beginning 2010; and 4) Parent does not provide an open line of credit. Rather, the loans are one time loans for 1995 and 2008. In general, taxpayers file combined Indiana returns when there is Indiana sourced income, and file consolidated Indiana returns when each entity within the return has nexus with Indiana. IC §

6-3-2-2; IC § 6-3-4-14.

B. Interest Add-back for years 2006-2012.

For periods of 2006 through 2012, the audit cited IC § 6-3-2-20, which stated:

(a) The following definitions apply throughout this section:
(1) "Affiliated group" has the meaning provided in Section 1504 of the Internal Revenue Code, except that the ownership percentage in Section 1504(a)(2) of the Internal Revenue Code shall be determined using fifty percent (50[percent]) instead of eighty percent (80[percent]).
(2) "Directly related intangible interest expenses" means interest expenses that are paid to, or accrued or incurred as a liability to, a recipient if:
(A) the amounts represent, in the hands of the recipient, income from making one (1) or more loans; and
(B) the funds loaned were originally received by the recipient from the payment of intangible expenses by any of the following:
(i) The taxpayer.
(ii) A member of the same affiliated group as the taxpayer.
(iii) A foreign corporation.
(3) "Foreign corporation" means a corporation that is organized under the laws of a country other than the United States and would be a member of the same affiliated group as the taxpayer if the corporation were organized under the laws of the United States.
(4) "Intangible expenses" means the following amounts to the extent these amounts are allowed as deductions in determining taxable income under Section 63 of the Internal Revenue Code 3 before the application of any net operating loss deduction and special deductions for the taxable year:
(A) Expenses, losses, and costs directly for, related to, or in connection with the acquisition, use, maintenance, management, ownership, sale, exchange, or any other disposition of intangible property.
(B) Royalty, patent, technical, and copyright fees.
(C) Licensing fees.
(D) Other substantially similar expenses and costs.
(5) "Intangible property" means patents, patent applications, trade names, trademarks, service marks, copyrights, trade secrets, and substantially similar types of intangible assets.
(6) "Interest expenses" means amounts that are allowed as deductions under Section 163 of the Internal Revenue Code 4 in determining taxable income under Section 63 of the Internal Revenue Code before the application of any net operating loss deductions and special deductions for the taxable year.
(7) "Makes a disclosure" means a taxpayer provides the following information regarding a transaction with a member of the same affiliated group or a foreign corporation involving an intangible expense and any directly related intangible interest expense with the taxpayer's tax return on the forms prescribed by the department:
(A) The name of the recipient.
(B) The state or country of domicile of the recipient.
(C) The amount paid to the recipient.
(D) A copy of federal Form 851, Affiliation Schedule, as filed with the taxpayer's federal consolidated tax return.
(E) The information needed to determine the taxpayer's status under the exceptions listed in subsection (c).
(8) "Recipient" means:
(A) a member of the same affiliated group as the taxpayer; or
(B) a foreign corporation; to which is paid an item of income that corresponds to an intangible expense or any directly related intangible interest expense.
(9) "Unrelated party" means a person that, with respect to the taxpayer, is not a member of the same affiliated group or a foreign corporation.
(b) Except as provided in subsection (c), in determining its adjusted gross income under IC 6-3-1-3.5(b), a corporation subject to the tax imposed by IC 6-3-2-1 shall add to its taxable income under Section 63 of the Internal Revenue Code:
(1) intangible expenses; and
(2) any directly related intangible interest expenses; paid, accrued, or incurred with one (1) or more members of the same affiliated group or with one (1) or more foreign corporations.
(c) The addition of intangible expenses or any directly related intangible interest expenses otherwise required in a taxable year under subsection (b) is not required if one (1) or more of the following apply to the taxable year:
(1) The taxpayer and the recipient are both included in the same consolidated tax return filed under IC 6-3-

4-14 or in the same combined return filed under IC 6-3-2-2(q) for the taxable year.
(2) The taxpayer makes a disclosure and, at the request of the department, can establish by a preponderance of the evidence that:
(A) the item of income corresponding to the intangible expenses and any directly related intangible interest expenses was included within the recipient's income that is subject to tax in:
(i) a state or possession of the United States; or
(ii) a country other than the United States; that is the recipient's commercial domicile and that imposes a net income tax, a franchise tax measured, in whole or in part, by net income, or a value added tax;
(B) the transaction giving rise to the intangible expenses and any directly related intangible interest expenses between the taxpayer and the recipient was made at a commercially reasonable rate and at terms comparable to an arm's length transaction; and
(C) the transactions giving rise to the intangible expenses and any directly related intangible interest expenses between the taxpayer and the recipient did not have Indiana tax avoidance as a principal purpose.
(3) The taxpayer makes a disclosure and, at the request of the department, can establish by a preponderance of the evidence that:
(A) the recipient regularly engages in transactions involving intangible property with one (1) or more unrelated parties on terms substantially similar to those of the subject transaction; and
(B) the transaction giving rise to the intangible expenses and any directly related intangible interest expenses between the taxpayer and the recipient did not have Indiana tax avoidance as a principal purpose.
(4) The taxpayer makes a disclosure and, at the request of the department, can establish by a preponderance of the evidence that:
(A) the payment was received from a person or entity that is an unrelated party, and on behalf of that unrelated party, paid that amount to the recipient in an arm's length transaction; and
(B) the transaction giving rise to the intangible expenses and any directly related intangible interest expenses between the taxpayer and the recipient did not have Indiana tax avoidance as a principal purpose.
(5) The taxpayer makes a disclosure and, at the request of the department, can establish by a preponderance of the evidence that:
(A) the recipient paid, accrued, or incurred a liability to an unrelated party during the taxable year for an equal or greater amount that was directly for, related to, or in connection with the same intangible property giving rise to the intangible expenses; and
(B) the transactions giving rise to the intangible expenses and any directly related intangible interest expenses between the taxpayer and the recipient did not have Indiana tax avoidance as a principal purpose.
(6) The taxpayer makes a disclosure and, at the request of the department, can establish by a preponderance of the evidence that:
(A) the recipient is engaged in:
(i) substantial business activities from the acquisition, use, licensing, maintenance, management, ownership, sale, exchange, or any other disposition of intangible property; or
(ii) other substantial business activities separate and apart from the business activities described in item (i); as evidenced by the maintenance of a permanent office space and an adequate number of full-time, experienced employees;
(B) the transactions giving rise to the intangible expenses and any directly related intangible interest expenses between the taxpayer and the recipient did not have Indiana tax avoidance as a principal purpose; and
(C) the transactions were made at a commercially reasonable rate and at terms comparable to an arm's length transaction.
(7) The taxpayer and the department agree, in writing, to the application or use of an alternative method of allocation or apportionment under section 2(l) or 2(m) of this chapter.
(8) Upon request by the taxpayer, the department determines that the adjustment otherwise required by this section is unreasonable.

C. Conclusion for Interest Add-back.

Taxpayer argues that the loan was an external debt used by Parent to acquire Taxpayer and other sibling companies. The loans are guaranteed by Taxpayer's assets and its domestic subsidiaries. Taxpayer argues that because its assets are collateral for the external loan, Taxpayer is directly linked to the external debt and is thus entitled to the interest expense deductions.

Taxpayer provided the original loan document between Taxpayer and the external finance company. The agreement laid out an interest schedule for the type of credit provided to Parent; the highest interest rate presented was 9.75 percent. Furthermore, Taxpayer also provided the two intercompany promissory notes in which the interest rates are 5 and 8 percent. The promissory notes establish that principal payments were due on demand from the parent company. The promissory note did state that interest payments would be made monthly, and there is evidence that Taxpayer is accounting for the expenses in its internal records. However, there is no evidence that Taxpayer made actual payments to Parent. Based on Taxpayer's evidence and the Department's audit findings, the promissory note is separate and distinct from the loan agreement between Parent and its affiliates and the external third-party lender. In addition, by virtue of the complete lack of principal payments, Taxpayer has shown that it has no intention of paying back any principal portion of the loan from Parent.

Taxpayer also mentioned Columbia Sportswear USA Corp. v. Indiana Dep't of Revenue, 45 N.E. 3d 888 (Ind. Tax Ct. 2015). Taxpayer failed however to explain how the case is relevant or reliable in this instance. Poorly developed and non-cogent arguments are subject to waiver. Scopelite v. Indiana Dep't of Local Gov't Fin., 939 N.E.2d 1138, 1145 (Ind. Tax Ct. 2010); Wendt LLP v. Indiana Dep't of State Revenue, 977 N.E.2d 480, 486 n.9 (Ind. Tax Ct. 2012). Therefore, the Department will not assume any argument made by Taxpayer and an analysis of Columbia Sportswear will not be afforded to Taxpayer in this instance.

After review of the documentation, the Department does not agree that Taxpayer was entitled to the interest expense deduction. Taxpayer's loan agreement and promissory note both show that the interest rate was not at an "arm's length transaction" and that there was no intention to pay back the principal amount of the loan. Therefore, in this particular case, Taxpayer has not met its statutory burden under IC § 6-8.1-5-1(c), and Taxpayer's protest is denied.

FINDING

Taxpayer's protest is denied.

II. Adjusted Gross Income Tax–Throw-back Sales.

Taxpayer protests the Department's decision to subject Taxpayer's income from sales to customers in other states to the "Throw-back" rule. Taxpayer states that its activities in those states exceed the protection of P.L. 86-272 and provide sufficient nexus with those states to subject it to net income taxes in those states. Therefore, Taxpayer believes that the income from those sales should not be subject to the throwback rule and that it should not be subject to additional Indiana adjusted gross income tax ("AGIT"). The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The adjusted gross income tax is imposed under IC § 6-3-2-2 for the years at issue, which stated in relevant parts:

> (a) With regard to corporations and nonresident persons, "adjusted gross income derived from sources within Indiana", for the purposes of this article, shall mean and include:
> (1) income from real or tangible personal property located in this state;
> (2) income from doing business in this state;
> (3) income from a trade or profession conducted in this state;
> (4) compensation for labor or services rendered within this state; and
> (5) income from stocks, bonds, notes, bank deposits, patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, and other intangible personal property if the receipt from the intangible is attributable to Indiana under section 2.2 of this chapter.
> Income from a pass through entity shall be characterized in a manner consistent with the income's characterization for federal income tax purposes and shall be considered Indiana source income as if the person, corporation, or pass through entity that received the income had directly engaged in the income producing activity. Income that is derived from one (1) pass through entity and is considered to pass through to another pass through entity does not change these characteristics or attribution provisions. In the case of nonbusiness income described in subsection (g), only so much of such income as is allocated to this state under the provisions of subsections (h) through (k) shall be deemed to be derived from sources within Indiana. In the case of business income, only so much of such income as is apportioned to this state under the provision of subsection (b) shall be deemed to be derived from sources within the state of Indiana. In the case of compensation of a team member (as defined in section 2.7 of this chapter), only the portion of income determined to be Indiana income under section 2.7 of this chapter is considered derived from sources

within Indiana. In the case of a corporation that is a life insurance company (as defined in Section 816(a) of the Internal Revenue Code) or an insurance company that is subject to tax under Section 831 of the Internal Revenue Code, only so much of the income as is apportioned to Indiana under subsection (r) is considered derived from sources within Indiana.

. . .

(e) The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the taxable year, and the denominator of which is the total sales of the taxpayer everywhere during the taxable year. Sales include receipts from intangible property and receipts from the sale or exchange of intangible property. However, with respect to a foreign corporation, the denominator does not include sales made in a place that is outside the United States. Receipts from intangible personal property are derived from sources within Indiana if the receipts from the intangible personal property are attributable to Indiana under section 2.2 of this chapter. Regardless of the f.o.b. point or other conditions of the sale, sales of tangible personal property are in this state if:

(1) the property is delivered or shipped to a purchaser that is within Indiana, other than the United States government; or

(2) the property is shipped from an office, a store, a warehouse, a factory, or other place of storage in this state and:

(A) the purchaser is the United States government; or

(B) the taxpayer is not taxable in the state of the purchaser.

Gross receipts derived from commercial printing as described in IC 6-2.5-1-10 shall be treated as sales of tangible personal property for purposes of this chapter.

. . .

(n) For 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.

. . ..

45 IAC 3.1-1-53 states:

Gross receipts from the sales of tangible personal property (except sales to the United States Government-See Regulation 6-3-2-2(e)(050) [45 IAC 3.1-1-54] are in this state: (a) if the property is delivered or shipped to a purchaser within this state regardless of the F.O.B. point or other conditions of sales; or (b) if the property is shipped from an office, store, factory, or other place of storage in this state, and the taxpayer is not taxable in the state of the purchaser. See Regulation 6-3-2-2(n)(010) [45 IAC 3.1-1-64].

Examples:

. . .

(5) If the taxpayer is not taxable in the state of the purchaser, the sale is attributed to this state if the property is shipped from an office, store, warehouse, factory, or other place of storage in this state. Such sale is termed a "Throwback" sale. Example: The taxpayer has its head office and factory in State A. It maintains a branch office and inventory in Indiana. Taxpayer's only activity in State B is the solicitation of orders by a resident salesman. All orders by the State B salesman are sent to the branch office in Indiana for approval and are filled by shipment from the inventory in Indiana. Since the taxpayer is immune under P.L.86-272 from tax in State B, all sales of merchandise to purchasers in State B are attributed to Indiana, the state from which the merchandise was shipped.

. . ..

(Emphasis added).

45 IAC 3.1-1-38 provides:

For apportionment purposes, 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.

As stated in Regulation 6-3-2-2(b)(010) [45 IAC 3.1-1-37], corporations doing business in Indiana as well as other states are subject to the allocation and apportionment provisions of IC 6-3-2-2(b)-(n). (Emphasis added).

45 IAC 3.1-1-64 states:

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. In the case of any "State," as defined in IC 6-3-1-25, other than a state of the United States or political subdivision of such state, the determination of whether such "state" has jurisdiction to subject the taxpayer to a net income tax shall be made by application of the jurisdictional standards applicable to that state of the United States. If jurisdiction to tax is otherwise present, such "state" is not considered as being without jurisdiction to tax by reason of the provisions of a treaty between that state and the United States.

Example:

Corporation X is actively engaged in manufacturing farm equipment in State A and foreign country B. Both State A and foreign country B impose a net income tax but foreign country B exempts corporations engaged in manufacturing farm equipment. Corporation X is subject to the jurisdiction of State A and foreign country B.

Taxpayers are not subject to throwback on sales into states in which they are taxable under this regulation [45 IAC 3.1-1-64]. See Regulation 6-3-2-2(e)(040) [45 IAC 3.1-1-53]. (Emphasis added).

The Indiana Supreme Court explained in Indiana Dep't of Revenue v. Kimberly-Clark Corp., 416 N.E.2d 1264 (Ind. 1981):

Public Law 86-272 (15 U.S.C.A. § 381), in pertinent part is as follows:

(a) 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:

(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).
Id. at 1265.

The court then explained:

We also believe that Congress perceived "solicitation" as embodying "sundry activities so long as those activities [are] closely related to the eventual sale of a product." Finally, when a corporate representative performs an "act of courtesy" in order to accommodate a customer, he has not ventured beyond the realm of "solicitation."
Id. at 1268.

The United States Supreme Court explained its standard for determining "solicitation of sales" in Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co., 505 U.S. 214 (1992). In Wrigley, the Court explained:

We proceed, therefore, to describe what we think the proper standard to be. Once it is acknowledged, as we have concluded it must be, that "solicitation of orders" covers more than what is strictly essential to making requests for purchases, the next (and perhaps the only other) clear line is the one between those activities that are entirely ancillary to requests for purchases -- those that serve no independent business function

> apart from their connection to the soliciting of orders -- and those activities that the company would have reason to engage in anyway but chooses to allocate to its in-state sales force. National Tires, Inc. v. Lindley, 68 Ohio App. 2d 71, 78-79 426 N.E.2d 793, 798 (1980) (company's activities went beyond solicitation to "functions more commonly related to maintaining an on-going business"). Providing a car and a stock of free samples to salesmen is part of the "solicitation of orders," because the only reason to do it is to facilitate requests for purchases. Contrariwise, employing salesmen to repair or service the company's products is not part of the "solicitation of orders," since there is good reason to get that done whether or not the company has a sales force. Repair and servicing may help to increase purchases; but it is not ancillary to requesting purchases, and cannot be converted into "solicitation" by merely being assigned to salesmen. See, e. g., Herff Jones Co. v. State Tax Comm'n, 247 Ore. 404, 412, 430 P.2d 998, 1001-1002 (1967) (no § 381 immunity for sales representatives' collection activities).
> Id, at 228-30.

The Court further explained:

> By contrast, Wrigley's in-state recruitment, training, and evaluation of sales representatives and its use of hotels and homes for sales-related meetings served no purpose apart from their role in facilitating solicitation. The same must be said of the instances in which Wrigley's regional sales manager contacted the Chicago office about "rather nasty" credit disputes involving important accounts in order to "get the account and [Wrigley's] credit department communicating." App. 71, 72. It hardly appears likely that this mediating function between the customer and the central office would have been performed by some other employee -- some company ombudsman, so to speak -- if the on-location sales staff did not exist. The purpose of the activity, in other words, was to ingratiate the salesman with the customer, thereby facilitating requests for purchases.
>
> Finally, Wrigley argues that the various nonimmune activities, considered singly or together, are de minimis. In particular, Wrigley emphasizes that the gum sales through "agency stock checks" accounted for only 0.00007 [percent] of Wrigley's annual Wisconsin sales, and in absolute terms amounted to only several hundred dollars a year. We need not decide whether any of the nonimmune activities was de minimis in isolation; taken together, they clearly are not. Wrigley's sales representatives exchanged stale gum, as a matter of regular company policy, on a continuing basis, and Wrigley maintained a stock of gum worth several thousand dollars in the State for this purpose, as well as for the less frequently pursued (but equally unprotected) purpose of selling gum through "agency stock checks." Although the relative magnitude of these activities was not large compared to Wrigley's other operations in Wisconsin, we have little difficulty concluding that they constituted a nontrivial additional connection with the State. Because Wrigley's business activities within Wisconsin were not limited to those specified in § 381, the prohibition on net-income taxation contained in that provision was inapplicable.
> Id. at 234-5.

Therefore, the Department may consider a taxpayer's activities as a whole to determine if the activities as a whole exceed the protection of Public Law 86-272.

In determining how the actions of an independent contractor affected nexus for an out-of-state business in Washington, in Tyler Pipe Industries, Inc. v. Washington State Department of Revenue, 483 U.S. 232 (1987), the United States Supreme Court explained:

> Tyler seeks a refund of wholesale taxes it paid on sales to customers in Washington for the period from January 1, 1976, through September 30, 1980. These products were manufactured outside of Washington. Tyler argues that its business does not have a sufficient nexus with the State of Washington to justify the collection of a gross receipts tax on its sales. Tyler sells a large volume of cast iron, pressure and plastic pipe and fittings, and drainage products in Washington, but all of those products are manufactured in other States. Tyler maintains no office, owns no property, and has no employees residing in the State of Washington. Its solicitation of business in Washington is directed by executives who maintain their offices out-of-state and by an independent contractor located in Seattle.
> Id. at 249.

The Court then explained:

> As a matter of law, the Washington Supreme Court concluded that this showing of a sufficient nexus could not be defeated by the argument that the taxpayer's representative was properly characterized as an independent contractor instead of as an agent. We agree with this analysis. In Scripto, Inc. v. Carson, 362 U.S. 207 (1960), Scripto, a Georgia corporation, had no office or regular employees in Florida, but it

> employed wholesalers or jobbers to solicit sales of its products in Florida. We held that Florida may require these solicitors to collect a use tax from Florida customers. Although the "salesmen" were not employees of Scripto, we determined that "such a fine distinction is without constitutional significance." Id., at 211. This conclusion is consistent with our more recent cases.
> Id. at 250.

Finally, the Court explained:

> As the Washington Supreme Court determined, "the crucial factor governing nexus is whether the activities performed in this state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales." 105 Wash. 2d, at 323, 715 P. 2d, at 126.The court found this standard was satisfied because Tyler's "sales representatives perform any local activities necessary for maintenance of Tyler Pipe's market and protection of its interests . . . ." Id., at 321, 715 P. 2d, at 125. We agree that the activities of Tyler's sales representatives adequately support the State's jurisdiction to impose its wholesale tax on Tyler.
> Id. at 250-1.

As explained in the audit report, Taxpayer made sales from Indiana locations to customers in foreign states ("throwback states") in which Taxpayer had not established that it was subject to an income or franchise tax. The terms and conditions of Taxpayer's agreements with its customers, impose a returnable deposit for wire spools and reels; the terms state that Taxpayer maintains ownership of the spools and reels. In the course of the protest process, Taxpayer provided two "Backhaul" invoices, which explain that Taxpayer picked up the spools and/or reels which it owned and transferred them back to Indiana. Taxpayer argues that the terms and conditions in the invoices clearly indicate that Taxpayer is taxable in the state where this order was filled. Taxpayer stated that once the spools are returned from customers they are "refurbished, if needed and then reused." The spools are also returned either by common carrier or by Taxpayer. The invoices show that the spools were returned from a customer in one of the throw-back states. Thus, the spools and reels were not inventory and did not contribute to Taxpayer's income from those states.

Taxpayer, however, did not establish that it had any presence in the throw back states. Taxpayer maintained ownership of the spools, but did not provide evidence that it refilled the spools or maintained a plant or office in the throwback states. Therefore, the presence of the spools and reels in the other states did not contribute to its ability to maintain sales in those states, as described in Tyler Pipe Industries. Taxpayer failed to show that the spool deposit program is not merely ancillary to requesting orders or de minimis, as provided by Wrigley. Thus, Taxpayer did not meet its burden required by IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is denied.

III. Adjusted Gross Income Tax–Net Operating Losses.

The Department adjusted Taxpayer's Net Operating Losses ("NOLs") as a result of the add back of interest expense deductions which adjusted Taxpayer's adjusted gross income for 2002-2009. Taxpayer argues that "the NOLs were generated in 2002-2009 which were carried forward to 2010-2012. As the statute for years the NOLs were generated are closed, the DOR should not be making adjustments for closed periods." In addition, Taxpayer argues that the interest expense deduction was permitted and therefore the NOLs were permitted. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The statute regarding NOLs is IC § 6-3-2-2.6, which states in relevant part:

> (c) An Indiana net operating loss equals the taxpayer's federal net operating loss for a taxable year as calculated under Section 172 of the Internal Revenue Code, derived from sources within Indiana and adjusted for the modifications required by IC 6-3-1-3.5.
> (d) The following provisions apply for purposes of subsection (c):
> (1) The modifications that are to be applied are those modifications required under IC 6-3-1-3.5 for the same taxable year in which each net operating loss was incurred.
> (2) The amount of the taxpayer's net operating loss that is derived from sources within Indiana shall be determined in the same manner that the amount of the taxpayer's adjusted income derived from sources within Indiana is determined under section 2 of this chapter for the same taxable year during which each

loss was incurred.
(3) An Indiana net operating loss includes a net operating loss that arises when the modifications required by IC 6-3-1-3.5 exceed the taxpayer's federal taxable income (as defined in Section 63 of the Internal Revenue Code), if the taxpayer is a corporation, or when the modifications required by IC 6-3-1-3.5 exceed the taxpayer's federal adjusted gross income (as defined by Section 62 of the Internal Revenue Code), if the taxpayer is a nonresident person, for the taxable year in which the Indiana net operating loss is determined.

The audit disallowed NOLs which arose from losses attributable to interest expenses in prior years and carried forward to years under the audit time frame. Based on the audit years use of losses accumulated in prior years allows the Department to adjust the NOLs accumulated in these prior years, as provided by IC § 6-3-2-2.6(c) and (d). In addition, since Taxpayer was denied its protest regarding the interest expense add back, the adjustment to NOLs based on the interest expense add back is proper. Taxpayer has not met its burden under IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is denied.

IV. Tax Administration–Penalty.

Taxpayer requested that the Department abate the negligence penalty.

Pursuant to IC § 6-8.1-10-2.1(a), the Department may assess a negligence penalty if the taxpayer:

(1) fails to file a return for any of the listed taxes;
(2) fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment;
(3) incurs, upon examination by the department, a deficiency that is due to negligence;
(4) fails to timely remit any tax held in trust for the state; or
(5) is required to make a payment by electronic funds transfer (as defined in IC 4-8.1-2-7), overnight courier, or personal delivery and the payment is not received by the department by the due date in funds acceptable to the department.

45 IAC 15-11-2(b) further states:

"Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The Department may waive a negligence penalty when "the taxpayer affirmatively establishes that the failure . . . was due to reasonable cause and not due to negligence." 45 IAC 15-11-2(c). The taxpayer "must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section." Id. The Department is mindful that "[r]easonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case." Id.

In this instance, Taxpayer has not demonstrated that its action was reasonable as described in 45 IAC 15-11-2(c). Thus, Taxpayer's request for penalty abatement is denied.

FINDING

Taxpayer's protest of the negligence penalty is denied.

CONCLUSION

Taxpayer's protest regarding the interest add back deduction, throwback sales, net operating losses, and penalty is denied.

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