Florida Department of Revenue
Technical Assistance and Dispute Resolution

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Executive Director

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QUESTION: WHETHER INTERCOMPANY SALES SHOULD BE INCLUDED IN THE SALES FACTOR FOR PURPOSES OF APPORTIONMENT?

ANSWER: GIVEN THE SPECIFIC CIRCUMSTANCES INVOLVED IN THIS CASE, THE GROSS RECEIPTS RECEIVED FROM INTERCOMPANY SALES SHOULD BE INCLUDED IN THE SALES FACTOR.

May 21, 2018

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Re: Technical Assistance Advisement – 18C1-005
Corporate Income Tax – Sales Factor
Sections 220.15, Florida Statutes ("F.S.")
Rule 12C-1.0155, Florida Administrative Code ("F.A.C.")
XXXXX ("Taxpayer")
FEIN: XXXXX

Dear XXXXX:

Your letter dated XXXXX, requests a Technical Assistance Advisement ("TAA") relating to the computation of the sales factor for purposes of apportioning taxable income. This response to your request constitutes a Technical Assistance Advisement under Chapter 12-11, Florida Administrative Code, and is issued to you under the authority of s. 213.22, Florida Statutes.

FACTS SUPPLIED BY TAXPAYER

Taxpayer is a XXXXX. Taxpayer files a consolidated Florida corporate income tax return, which includes affiliated companies XXXXX ("XXXXX") and XXXXX ("XXXXX").

XXXXX, is a Delaware corporation XXXXX. XXXXX consists of two subunits: (1) XXXXX ("XXXXX"); and (2) XXXXX. XXXXX sells Taxpayer's products to Taxpayer's foreign affiliates. XXXXX is a subsidiary XXXXX. Specifically, XXXXX sells to unrelated third parties in foreign markets. All Taxpayer products sold to foreign affiliates or foreign customers are first sold to either XXXXX.

XXXXX uses intercompany accounts to charge foreign affiliates for the products. However, XXXXX directly invoices foreign customers for the products sold.

Taxpayer utilizes a global cash management system. Specifically, intercompany accounts are used to manage receivables and payable positions, which eliminates the need to make multiple cash movements to account for intercompany activity. Taxpayer maintains a receivable and/or payables account with XXXXX, XXXXX and other related entities. The sales transactions to either XXXXX are reflected as sales on the books of Taxpayer or its subsidiaries. Sales transactions between Taxpayer and XXXXX are made pursuant to a contractual agreement between Taxpayer and XXXXX. Taxpayer states that separate invoices are not issued for each intercompany product sale since the payments for product sales are handled through the receivable and/or payable accounts. However, data extracted from Taxpayer's primary sales system shows accounting entries that provide evidence that sales are made. These accounting records reflect the fact that there has been a transfer of ownership of the products from the selling entity to either XXXXX.

The income of both XXXXX is included in the computation of Florida consolidated income. Sales of XXXXX to foreign affiliates and the sales of XXXXX to unrelated foreign customers are the subject of this TAA request.

ISSUE PRESENTED

Whether Taxpayer's gross receipts from intercompany product sales to XXXXX should be included in the sales factor for purposes of apportionment?

LEGAL AUTHORITY

Section 220.15(5), F.S., states in part:

> (5) The sales factor is a fraction the numerator of which is the total sales of the taxpayer in this state during the taxable year or period and the denominator of which is the total sales of the taxpayer everywhere during the taxable year or period…

Section 220.131(4), F.S., states:

> (4) The computation of consolidated taxable income for the members of an affiliated group of corporations subject to tax hereunder shall be made in the same manner and under the same procedures, including all intercompany adjustments and eliminations, as are required for consolidating the incomes of affiliated corporations for the taxable year for federal income tax purposes in

accordance with s. 1502 of the Internal Revenue Code, and the amount shown as consolidated taxable income shall be the amount subject to tax under this code.

Rule 12C-1.0155, F.A.C., states in part:

(1) For the purposes of the sales factor, the term "sales" means all gross receipts received by the taxpayer from transactions and activities in the regular course of its trade or business.

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(j) Intercompany sales. When a consolidated return is filed, intercompany sales may be included in the sales factor. Indications that the amounts may be included as sales include the following factors:

1. Amounts called sales on the books;
2. Amounts invoiced as sold to related party;
3. Actual payment from related party; or
4. Amounts included in consolidated federal income tax return as "gross receipts or sales."

Rule 12C-1.015(7)(a), F.A.C., states:

(7) Consolidated Returns.

(a) Section 220.131(5), F.S., requires members of an affiliated group which file a Florida consolidated income tax return to use the general apportionment method prescribed by Section 220.15, F.S., unless an alternative method is determined to be more appropriate by the Department.

Rule 12C-1.0155(1)(j), F.A.C., states:

(1) For the purposes of the sales factor, the term "sales" means all gross receipts received by the taxpayer from transactions and activities in the regular course of its trade or business…

(j) Intercompany sales. When a consolidated return is filed, intercompany sales may be included in the sales factor. Indications that the amounts may be included as sales include the following factors:

1. Amounts called sales on the books;
2. Amounts invoiced as sold to related party;
3. Actual payment from related party; or
4. Amounts included in consolidated federal income tax return as "gross receipts or sales."

DISCUSSION

Taxpayer asserts that all its products sold outside of the United States are initially sold to a wholly-owned subsidiary, who then sells to the products to foreign customers or foreign affiliates. In addition, Taxpayer argues that the intercompany sales filed on its consolidated returns satisfies each of the requirements set forth in Rule 12C-1.0155(1)(j), F.A.C. and is similar to the methodology set forth in Department of Revenue v. Anheuser-Busch, 527 So.2d 877 (1988).

Section 220.15(5)(a), F.S., defines "sales," as "all gross receipts of the taxpayer except interest, dividends, rents, royalties, and gross receipts from the sale, exchange, maturity, redemption, or other disposition of securities." Rule 12C-1.0155(1), F.A.C., provides the definition of sales, for purposes of the sales factor, as: "all gross receipts received by a taxpayer from transactions and activities in the regular course of its trade or business." In addition, Rule 12C-1.0155(1)(j), F.A.C., regulates intercompany sales. It provides that intercompany sales *may* be included in the sales factor.

Rule 12C-1.0155(1)(j), F.A.C., provides factors that may indicate that those amounts may be included as sales. Those factors are:

1. Amounts called sales on the books;
2. Amounts invoiced or sold to related party;
3. Actual payment from a related party; or
4. Amounts included in consolidated federal income tax as "gross receipts or sales".

In Department of Revenue v. Anheuser-Busch[1], Metal Container Corp. ("MCC") manufactured beer cans for Anheuser-Busch Inc. ("ABI"). The two corporations were affiliates and filed a consolidated corporate income tax for both Federal and Florida purposes. When MCC transferred the beer cans to ABI, the transactions were invoiced to ABI. ABI made payments indirectly to MCC by journal entry, and MCC delivered the cans to ABI. ABI and MCC argued that they were one taxpayer for purposes of apportionment and so the intercompany transactions between them should be eliminated from the sales factor. The Appellate Court disagreed and stated that "[t]his overlooks the well-established law that each of the two or more corporations joining in a consolidated return is none the less a taxpayer."[2] The Appellate Court found the "indicia of a sale" sufficient to constitute a sale, and stated:

[1] 527 So.2d 877 (1988 Fla. 1st DCA)
[2] Id. at 881 (citing Woolford Realty Co. v. Rose, 286 U.S. 319, 328, (1932)).

> Without unduly belaboring the point, we find that unlike the situation in *Coulter,* the indicia of a sale are present in this case. The cans were "invoiced" as "sold to" Anheuser-Busch. Delivery of the cans to Anheuser-Busch by MCC is uncontroverted. Finally, we find that Anheuser-Busch's cash advances to MCC and payment of MCC's third party obligations constitute sufficient evidence of payment. We note, significantly, that the transactions involved meet the sales destination test set forth in section 214.71(3)(a)1.[3]

Anheuser-Busch reviewed all of the indicia previously described in Coulter Electronics v. Department of Revenue[4] and noted that the treatment of the transactions for federal tax purposes in its consolidated returns is "particularly significant" in that it adds confirmation that such delivery of goods for a stated price constitutes true gross receipts and "sales" for federal tax purposes and accordingly for Florida apportionment purposes.[5] Consequently, the transactions are accounted for Florida tax purposes if such transactions are realized and treated as intercompany sales for federal tax purposes.

Anheuser-Busch addressed the failure of the taxpayer to report the so-called intercompany transactions as "gross receipts" on the taxpayer's federal consolidated federal corporate income tax return. Anheuser-Busch stated:

> Although they [intercompany transactions] were called "sales" on their books, this court found that these transactions did not have the indicia of sale; transfer of title, delivery, and payment. More importantly, for purposes of comparison with the can transactions in this case, the intercompany sales in Coulter were "disregarded for the purpose of federal income tax." 365 So.2d at 808. Accordingly, the court held that these transactions did not constitute sales within the meaning of sections 214.71(3) and 220.15(1), and thus were not required to be included in Coulter's sales factor for purposes of the corporate income tax apportionment formula.[6]

Anheuser-Busch continued in its analysis of the federal reporting of "gross receipts" of MCC, the intercompany seller, as used in the computation of separate taxable income as part of the federal consolidated return, and stated the following:

> In determining the best evidence of the gross receipts of these two taxpayers, Anheuser-Busch's treatment of the sale of these beer cans in its corporate income tax return (Form 1120) is particularly significant.

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[3] Id. at 880.
[4] 365 So.2d 806, (Fla. 1st DCA 1978)
[5] Id. at 881.
[6] Id. at 879.

> In the consolidated federal income tax return filed each year on behalf of Anheuser-Busch's affiliated group, on Form 1120, line 1, captioned "1(a) Gross receipts or sales" the gross receipts of all included corporations were aggregated. In an attached taxpayer schedule, which was required to be filed, entitled "Consolidated Profit and Loss Summary," the amount of "gross receipts" was reported separately for each included corporation and the sum of the "gross receipts" indicated for each corporation was reconciled to the total amount on line 1(a) of Form 1120. In each year, the amount of "gross receipts" federally reported as being those of MCC represented the annual aggregation of the "total amounts reported by Anheuser-Busch in its federal income tax returns for the years in question and were not eliminated in any manner from the consolidated "gross receipts or sales" reflected therein.
>
> However, in Anheuser-Busch's consolidated Florida corporate tax returns for each of these tax years, in the computation of the Florida sales factor used for the Florida apportionment purposes, these gross receipts attributable to MCC in the federal income tax returns were omitted from the sales factor. In computing its proposed assessments, DOR restored these gross receipts to the sales factor denominator as representing gross receipts from all sales of beer cans by MCC to Anheuser-Busch.[7]

Accordingly, Anheuser-Busch held that the "best evidence" of the gross receipts of each entity is derived from the federal consolidated corporate income tax return and related schedules to such return. This information is "particularly significant" in determining the intercompany gross receipts and intercompany income included in the intercompany seller's separate taxable income. Where MCC, the intercompany seller in the Anheuser-Busch case included these intercompany receipts in its separate taxable income, it was held by the appellate court such gross receipts should be included in the sales factor.

The reason for including intercompany sales under certain circumstances is to equitably apportion a taxpayer's business activities. The purpose of apportionment is to fairly divide a taxpayer's income amongst the states. Apportionment looks to the business activities of a taxpayer in making this measurement. The states usually measure the business activities of a taxpayer by the use of a three-factor apportionment formula – a combination of a taxpayer's payroll, property, and gross receipts (sales). Apportionment is merely a method to fairly divide a multi-state entity's income among the States in which it conducts business. Apportionment is not an exact science, but it has been widely accepted by both state and federal courts as a reasonable approximation for this purpose.

[7] Id. at 881.

In this case, the Department has found there to exist in substance the transfer of title to goods, the payment of consideration for goods delivered, actual delivery of goods to denote the establishment of "sales destination" of product. In addition, it is also concluded that the "gross profit" which is derived from the intercompany transaction is established in the separate profit and loss accounts for the affiliated entities in Taxpayer's federal consolidated return. For these reasons, the Department concludes that the intercompany transactions are sales for sales factor purposes of the apportionment formula.

CONCLUSION

Given the specific circumstances involved in this case, and based on the representations of the Taxpayer, the gross receipts Taxpayer receives from intercompany product sales to XXXXX should be included in the sales factor. However, Taxpayer is reminded that should the facts provided in its request of XXXXX, be determined to be incorrect or changed, the response will be substantially different from what has been agreed upon in this TAA.

This response constitutes a Technical Assistance Advisement under section 213.22, F.S., which is binding on the Department only under the facts and circumstances described in the request for this advice as specified in section 213.22, F.S. Our response is based on those facts and specific situation summarized above. You are advised that subsequent statutory or administrative rule changes or judicial interpretations of the statutes or rules upon this advice is based may subject future transactions to a different treatment than expressed in this response.

You are further advised that this response, your request and related backup documents are public records under Chapter 119, F.S., and are subject to disclosure to the public under the conditions of section 213.22, F.S. Confidential information must be deleted before public disclosure. In an effort to protect confidentiality, we request you provide the undersigned with an edited copy of your request for Technical Assistance Advisement, the backup material and this response, deleting names, addresses and any other details which might lead to identification of the taxpayer. Your response should be received by the Department within 15 days of the date of this letter.

Sincerely,

Susan R. Coxwell

Susan R. Coxwell
Tax Law Specialist
Technical Assistance and Dispute Resolution
(850) 717-6478

Record ID 7000013772
CC: XXXXX