

SC REVENUE RULING #97-15

SUBJECT: Public Law 86-272 and South Carolina Income Tax

EFFECTIVE DATE: Applies to all periods open under the statute.

SUPERSEDES: SC Revenue Rulings #93-10, #91-16, and all previous documents and any oral directives in conflict herewith.

REFERENCE: 15 U.S.C. Section 381
S.C. Code Ann. Section 12-6-510 (Supp. 1996)
S.C. Code Ann. Section 12-6-530 (Supp. 1996)

AUTHORITY: S.C. Code Ann. Section 12-4-320 (Supp. 1996)
SC Revenue Procedure #94-1

SCOPE: A Revenue Ruling is the Department of Revenue's official advisory opinion of how laws administered by the Department are to be applied to a specific issue or a specific set of facts, and is provided as guidance for all persons or a particular group. It is valid and remains in effect until superseded or modified by a change in the statute or regulations or a subsequent court decision, Revenue Ruling or Revenue Procedure.

INTRODUCTION

In 1985 the Multistate Tax Commission ("MTC") issued guidelines on the effect of 15 U.S.C. Section 381 ("Public Law 86-272") on the power of a state to impose a tax on income derived from within its borders. The Department of Revenue published guidelines in SC Revenue Ruling #91-16 and SC Revenue Ruling #93-10 to better clarify South Carolina's position on the impact of Public Law 86-272 on income taxation. The MTC adopted revised guidelines in 1994 in response to the U.S. Supreme Court decision in *Wisconsin Department of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214 (1992) ("Wrigley").

This ruling supersedes SC Revenue Ruling #91-16 and SC Revenue Ruling #93-10 and is largely based upon *Wrigley* and the MTC's 1994 guidelines. Its purpose is to provide assistance in determining whether Public Law 86-272 protects certain activities from South Carolina taxation.

South Carolina Code '12-6-510 imposes an income tax on the taxable income of individuals, estates, and trusts. South Carolina Code '12-6-530 imposes an income tax on corporations and reads, in part:

An income tax is imposed annually at the rate of five percent on the South Carolina taxable income of every corporation...transacting, conducting, or doing business within this State or having income within this State, regardless of whether these activities are carried on in intrastate, interstate, or foreign commerce....

Public Law 86-272, as codified at 15 U.S.C. Section 381, places certain limits on the power of a state to impose a tax on the income derived from within its borders. It reads, in pertinent part:

(a) No State, or political subdivision thereof, shall have power to impose... 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).

(b) The provisions of subsection (a) of this section shall not apply to the imposition of a net income tax by any State, or political subdivision thereof, with respect to -

(1) any corporation which is incorporated under the laws of such State; or

(2) any individual who, under the laws of such State, is domiciled in, or a resident of, such State.

(c) For purposes of subsection (a) of this section, a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance, of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

(d) For purposes of this section -

(1) the term “independent contractor” means a commission agent, broker, or other independent contractor who is engaged in selling, or 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; and

(2) the term “representative” does not include an independent contractor. (Emphasis added.)

Public Law 86-272 restricts a state from imposing a net income tax on income derived from within its borders from interstate commerce if the only business activity of the company within the state consists of the solicitation of orders for sales of tangible personal property, which orders are to be sent outside the taxing state for acceptance or rejection, and, if accepted, are filled by shipment or delivery from a point outside the state. The term “net income tax” includes a franchise tax measured by net income.

In *Wrigley*, the Court considered, among other issues, the meaning of the phrase “solicitation of orders” and established a “proper standard” for application of the phrase.

The Court’s opinion states, in part:

...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....(footnote omitted)

Accordingly, “solicitation of orders” extends beyond the sole act of inviting an order and includes the entire process associated with the invitation (*e.g.* a company car or a stock of free samples provided to a salesman). “Solicitation of orders” does not include activities apart from the invitation of orders that the company has reason to do anyway (*e.g.* repair or services activities by sales personnel). Further, the Court determined that the maintenance of an office in a taxing state was not protected by Public Law 86-272 under any circumstances.

The Court also examined whether *de minimis* or insignificant activity apart from solicitation of orders by the company within the taxing state resulted in the loss of immunity from taxation. With respect to this issue, the Court held:

...whether in-state activity other than “solicitation of orders” is sufficiently *de minimis* to avoid loss of the tax immunity conferred by 381 depends upon whether that activity establishes a nontrivial additional connection with the taxing State.

* * * *

...We need not decide whether any of the nonimmune activities was *de minimis* in isolation; taken together, they clearly are not....

Therefore, if a company engages in business activity other than solicitation of orders, the activity serves an independent business function other than the solicitation of orders, and the activity is not trivial, the protection of Public Law 86-272 is lost. Further, any business activities, other than the solicitation of orders, are viewed in the aggregate, rather than separately.

NATURE OF SALES

Only the solicitation to sell tangible personal property is afforded immunity under Public Law 86-272. The leasing, renting, licensing or other disposition of tangible personal property, or transactions involving real property or intangibles, such as franchises, patents, copyrights, trademarks, service marks and the like are not protected activities under Public Law 86-272. The selling or providing of services is also not protected. The sale or delivery and the solicitation for the sale or delivery of any type of service that is not either (1) ancillary to solicitation or (2) otherwise set forth as a protected activity in this Ruling is also not protected under Public Law 86-272.

SOLICITATION OF ORDERS AND ACTIVITIES ANCILLARY TO SOLICITATION

For an in-state activity to be a protected activity under Public Law 86-272, it must be limited solely to solicitation (except for *de minimis* activities described in this section and certain activities conducted by independent contractors described later in this Ruling.) Solicitation means (1) speech or conduct that explicitly or implicitly invites an order; and (2) activities that neither explicitly nor implicitly invite an order, but are entirely ancillary to requests for an order.

Ancillary activities are those activities that serve no independent business function for the seller apart from their connection to the solicitation of orders. Activities that a seller would engage in apart from soliciting orders are not considered as ancillary to the solicitation of orders. The mere assignment of activities to sales personnel does not, merely by such assignment, make such activities ancillary to solicitation of orders. Additionally, activities that seek to promote sales are not necessarily ancillary, because Public Law 86-272 does not protect activities that facilitate sales; it only protects ancillary activities that facilitate the request for an order. The conducting of activities not falling within the foregoing definition of solicitation will cause a company to lose its protection from a net income tax afforded by Public Law 86-272, unless the disqualifying activities, taken together, are *de minimis* or are otherwise permitted under this Ruling.

De minimis activities are those that, when taken together, establish only a trivial connection with the taxing state. An activity conducted within a taxing state on a regular or systematic basis or pursuant to a company policy (whether such policy is in writing or not) will not normally be considered trivial. Whether or not an activity consists of a trivial or non-trivial connection with the state is to be measured on both a qualitative and quantitative basis. If such activity either qualitatively or quantitatively creates a non-trivial connection with the taxing state, then such activity exceeds the protection of Public Law 86-272. Establishing that the disqualifying activities only account for a relatively small part of the business conducted within the taxing state is not determinative of whether a *de minimis* level of activity exists. The relative economic importance of the disqualifying in-state activities, as compared to the protected activities, does not determine whether the conduct of the disqualifying activities within the taxing state is inconsistent with the limited protection afforded by Public Law 86-272.

UNPROTECTED ACTIVITIES

The following activities within South Carolina (assuming they are not of a *de minimis* level) are not considered solicitation of orders or ancillary thereto or otherwise protected under Public Law 86-272 and will cause otherwise protected sales to lose their protection under the Public Law:

1. Making repairs or providing maintenance or service to the property sold or to be sold.
2. Collecting current or delinquent accounts, whether directly or by third parties, through assignment or otherwise.
3. Investigating credit worthiness.
4. Installation or supervision of installation at or after shipment or delivery.
5. Conducting training courses, seminars or lectures for personnel other than personnel involved only in solicitation.
6. Providing any kind of technical assistance or service including, but not limited to, engineering assistance or design service, when one of the purposes thereof is other than the facilitation of the solicitation of orders.
7. Investigating, handling, or otherwise assisting in resolving customer complaints, other than facilitating communication between the company and the customer when the purpose of such mediation is to ingratiate the sales personnel with the customer.
8. Approving or accepting orders.
9. Repossessing property.
10. Securing deposits on sales.
11. Picking up, replacing, giving credit for, or purchasing damaged, outdated or returned property.
12. Hiring, training, or supervising personnel, other than personnel involved only in solicitation.
13. Using agency stock checks or any other process or means by which sales are made within South Carolina by sales personnel.
14. Maintaining a sample or display room in excess of two weeks (14 days) at any one location within South Carolina during the tax year.
15. Carrying samples for sale, exchange or distribution in any manner for consideration or other value.

16. Owning, leasing, using, or maintaining any of the following facilities or property within South Carolina:
- a. Repair shop.
 - b. Parts department.
 - c. Any kind of office other than an in-home office as described as permitted under unregulated activity 17 and regulated activity 2.
 - d. Warehouse.
 - e. Meeting place for directors, officers or employees, except when not done on a regular or systematic basis during the tax year.
 - f. Stock of goods other than samples for sales personnel or that are used entirely ancillary to solicitation.
 - g. Telephone answering service that is publicly attributed to the company or the agent(s) of the company in their representative status.
 - h. Mobile stores, *i.e.* vehicles with drivers who are sales personnel making sales from the vehicles.
 - i. Real property or fixtures to real property of any kind.
17. Maintaining, by any employee or other representative, an office or place of business of any kind (other than an in-home office located within the residence of the employee or representative that (i) is not publicly attributed to the company or to the employee or representative of the company in an employee or representative capacity, and (ii) so long as the use of such office is limited to soliciting and receiving orders from customers; for transmitting such orders outside South Carolina for acceptance or rejection by the company; or for such other activities that are regulated under Public Law 86-272 or under the regulated activities of this Ruling).

A telephone listing or other public listing within South Carolina for the company or for an employee or representative of the company in such capacity or other indications through advertising or business literature that the company or its employee or representative can be contacted at a specific address within South Carolina shall normally be determined as the company maintaining within South Carolina an office or place of business attributable to the company or to its

employee or representative in a representative capacity. However the normal distribution and use of business cards and stationery identifying the employee=s or representative=s name, address, telephone and fax numbers and affiliation with the company shall not, by itself, be considered as advertising or otherwise publicly attributing an office to the company or its employee or representative.

The maintenance of any office or other place of business in this state that does not strictly qualify as an “in home” office as described above shall, by itself, cause the loss of protection under this Ruling.

For the purpose of this subsection, it is not relevant whether the company pays directly, indirectly, or not at all for the cost of maintaining such in-home office.

18. Entering into franchising or licensing agreements; selling or otherwise disposing of franchises and licenses; or selling or otherwise transferring tangible personal property pursuant to such franchise or license by the franchisor or licensor to its franchisee or licensee within the state.
19. Conducting any activity not listed below under “Protected Activities” which is not entirely ancillary to requests for orders, even if such activity helps to increase purchases.

PROTECTED ACTIVITIES

The following activities within South Carolina will not cause the loss of protection for otherwise protected sales:

1. Soliciting orders for sales by any type of advertising.
2. Soliciting of orders by a South Carolina resident employee or representative of the company, so long as such person does not maintain or use any office or other place of business in the state other than an “in-home” office as described above in the unprotected activity 17.
3. Carrying samples and promotional materials only for display or for distribution without charge or other consideration.
4. Furnishing and setting up display racks and advising customers on the display of the company’s products without charge or other consideration.
5. Providing automobiles to sales personnel for their use in conducting protected activities.

6. Passing orders, inquiries and complaints on to the home office.
7. Missionary sales activities; *i.e.* the solicitation of indirect customers for the company's goods. For example, a manufacturer's solicitation of retailers to buy the manufacturer's goods from the manufacturer's wholesale customers would be protected if such solicitation activities are otherwise immune.
8. Coordinating shipment or delivery without payment or other consideration and providing information relating thereto either prior or subsequent to the placement of an order.
9. Checking of customers' inventories without charge therefore (for re-order, but not for other purposes such as quality control).
10. Maintaining a sample or display room for two weeks (14 days) or less at any one location within South Carolina during the tax year.
11. Recruiting, training or evaluating sales personnel, including occasionally using homes, hotels or similar places for meetings with sales personnel.
12. Facilitating communication between the company and the customer when the purpose of such mediation is to ingratiate the sales personnel with the customer.
13. Owning, leasing, using or maintaining personal property for use in the employee or representative's "in-home" office or automobile that is solely limited to the conducting of protected activities. Therefore, the use of personal property such as a cellular telephone, facsimile machine, duplicating equipment, personal computer and computer software that is limited to the carrying on of protected solicitation and activity entirely ancillary to such solicitation or permitted by this Ruling under the protected activities section shall not, by itself, remove the protection under this Ruling.
14. Shipping or delivering goods to a purchaser in this state from a point outside this state by any means of transportation, including private carrier, irrespective of whether a delivery fee is charged.

ACTIVITIES BY INDEPENDENT CONTRACTORS

Public Law 86-272 affords immunity from taxation to certain activities within a state if conducted by an independent contractor that would not be afforded if performed by the company or its employees or other representatives. Independent contractors may engage in the following limited activities within South Carolina without the company's loss of immunity:

1. Soliciting sales.
2. Making sales.
3. Maintaining an office.

Sales representatives who represent a single principal are not considered to be independent contractors. Such representatives are subject to the same limitations as employees of the taxpayer.

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/Burnet R. Maybank III
Burnet R. Maybank III, Director

Columbia, South Carolina
October 22, 1997