**JURISDICTION:** **OKLAHOMA TAX COMMISSION DECISION**
**CITE:** **2005-05-10-22 / PRECEDENTIAL**
**ID:** **P-02-117-H**
**DATE:** **MAY 10, 2005**
**DISPOSITION:** **SUSTAINED**
**TAX TYPE:** **INCOME TAX**
**APPEAL:** **NO APPEAL TAKEN**

The above-named non-resident partnership and partners protest the proposed assessment of Oklahoma income tax on the income derived from the sale and delivery of tangible personal property into the State of Oklahoma. We conclude that the proposed assessments are prohibited by the provisions of Public Law 86-272, and accordingly sustain the protest. We further conclude that, to the extent that one of our promulgated administrative rules is contrary to that law, it is invalid.

## FINDINGS OF FACT

1. PARTNERSHIP is a Texas partnership with its principal place of business located in ANY TOWN, Texas. The partnership has no permanent office or location in Oklahoma. PARTNER ONE and PARTNER TWO are the partners in PARTNERSHIP, each owning a 50% interest therein. Both of the partners are Texas residents.

2. During the tax year 1998, the partnership received orders in person or by telephone at its Texas place of business from Oklahoma customers for sales of propane, motor fuel, oil, oil filters, car batteries and the like. These orders were filled at the Texas location and shipped or delivered from there to the customer's address in Oklahoma. Approximately 84% of these deliveries were made in the partnership's own trucks by either an employee of the partnership or one of the partners.

3. During the year in question, the partnership held an Oklahoma sales tax permit, an Oklahoma motor fuel license (bonded importer, eligible purchaser, exporter), and an Oklahoma gasoline and diesel distributor's license.

4. Gross sales in Oklahoma totaled in excess of $500,000.00, which constituted approximately 31% of the partnership's total gross sales. Oklahoma sales tax was reported and paid on these sales. Neither the partnership nor the partners filed an Oklahoma income tax return.

5. Based on information received concerning the sales in Oklahoma, the Commission's Audit Division proposed an assessment of Oklahoma income tax against the partnership for 1998 on May 31, 2002. On or about November 25, 2003, the Division proposed an assessment against each of the partners individually. As finally revised, the Division proposes to assess Oklahoma income tax against the partnership on the partnership's net income attributable to its earnings within Oklahoma, and individually against the partners on their distributive share thereof. The partnership and partners protest.

## CONCLUSIONS OF LAW

1. PARTNERSHIP generated almost one-third of its income in Oklahoma during the tax year in question. In the absence of federal legislation to the contrary, Oklahoma may constitutionally impose its income tax on that enterprise's net income attributable to its earnings within the State. *See, Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 79 S.Ct. 357 (1959). In the case of a partnership, the partnership is not taxed, but the individual partners are taxed on their distributive share of the partnership income. 68 O.S. §§2362, 2363.[1]

2. Largely in response to the Court's decision in *Northwestern States*, however, in 1959 Congress enacted Public Law 86-272 (15 U.S.C.A. §§ 381 to 384), which prohibits a state from imposing a net income tax on the income of an entity whose only business activities within the state consist of no more than (1) the solicitation of orders for sales of tangible personal property; provided that (2) the orders are sent outside the state for approval; and (3) the goods are delivered from outside the state.[2] According to the evidence presented in the matter before us, all of the orders for sale of goods were taken by the partnership at its place of business in Texas, were approved or rejected there, and, if approved, were filled by shipment or delivery from that point outside the State of Oklahoma. No evidence has been presented that the protestants' activities in Oklahoma exceeded the "safe harbor" provided by the three minimum standards specified by Congress.

3. The Division argues that the regular delivery of products by protestants to Oklahoma customers in company-owned trucks, as opposed to common carrier, is an unprotected activity for purposes of P.L. 86-272, and caused the Oklahoma sales to lose that law's protection from Oklahoma income tax. In support of this argument, the Division points to Oklahoma Tax Commission administrative rule OAC 710:50-17-3, which provides:

> "(a) If a corporation has one or more of the following activities in Oklahoma, it is considered to have **"nexus"** and shall be subject to Oklahoma income taxes:
>
> …
>
> (12) The delivery of merchandise in a company owned or leased vehicle to a destination within the state from a source outside the state, in connection with the solicitation of sales."

While we agree with the Division that delivery of merchandise in company owned or leased vehicles is a valid factor in determining whether a person has a tax "nexus"[3] with the state for constitutional purposes, we do not agree that P.L. 86-272's protection is limited to shipment or delivery *by common carrier*, or that delivery in the seller's vehicles is an unprotected activity for purposes of the federal *statute.*

4. In *National Private Truck Council, Inc. v. Commissioner of Revenue*, 688 N.E.2d 936 (Mass. 1997), *cert. denied*, 523 U.S. 1137, 118 S.Ct. 1840 (1998), the Supreme Judicial Court of Massachusetts rejected the same argument being made by the Division here, and held that that state's regulation, which exempted an out-of-state entity from Massachusetts excise (income) tax

only if its orders were filled by shipment or delivery "by common carrier or contract carrier," was preempted by P.L. 86-272. There, as here, the state contended that the federal statute did not exempt entities that use their own vehicles to deliver their goods into a state. In rejecting this argument, the Court noted that "neither the language of the statute nor its legislative history suggests that Congress intended" the specialized and restrictive meaning of "delivery" that the state urged. *Id.*, 688 N.E.2d at 940.

5. Other states have reached the same conclusion. In *Atlas Foundry & Machine Co. v. State Tax Com'n*, 2 Or. Tax 200, 1965 WL 154 (1965), the Oregon Tax Court held that a Washington company's delivery of its products to Oregon in its own trucks did not deny it the protection of P.L. 86-272 from imposition of the Oregon income tax. In *Commonwealth, Dept. of Tax'n v. National Private Truck Council*, 480 S.E.2d 500 (Va. 1997), the Virginia Supreme Court held that a state regulation that extended the immunity provided by P.L. 86-272 to only those instances in which the shipment or delivery of goods is accomplished by common carrier, violated the "plain meaning" of the federal statute, and consequently held the regulation invalid. *Id.*, 480 S.E.2d at 502. The Court said that, in enacting P.L. 86-272, Congress did not specify any manner of delivery necessary to qualify for the immunity and, in the absence of such a qualification, the state could not add conditions to, or otherwise limit, the statutory protection. *Ibid*.

6. We agree with these decisions. Congress specified that the protection would extend to solicitation of orders within the state, approval of those orders outside the state, and filling of those orders by delivery from a point outside the state' borders. To the extent that OAC 710:50-17-3 may be read to limit the protection of P.L. 86-272 to only those instances where shipment or delivery of the seller's goods is accomplished by common or contract carrier, or to deny the federal statute's protection if the merchandise is delivered in a company owned or leased vehicle, the rule violates the plain meaning of P.L. 86-272 and is invalid.

7. Finally, it is noted that the protestants did possess certain Oklahoma licenses and permits. However, no evidence was presented that protestants actually engaged in any activities in Oklahoma pursuant to those licenses other than delivering products from Texas in filling orders that had been received and accepted there. Lacking such evidence, we are forced to conclude that protestants' purpose in securing those permits and licenses was to enable them to legally solicit orders from Oklahoma customers for protestants' products. *See, Pomco Graphics, Inc. v. Director, Div. of Taxation*, 13 N.J. Tax 578, 1993 WL 520594 (1993).

## ORDER

For the reasons given above, the within and foregoing protest is SUSTAINED.

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[1] The statutory authority for proposing an assessment against the partnership, as opposed to the partners, is not readily apparent.

[2] 15 U.S.C.A. § 381(a) provides:

> "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; …"

[3] Connection or link. For tax purposes, sufficient contacts or presence within a state to allow the state to tax the entity or activity involved.