STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition of The Gates Rubber Company	AFFIDAVIT OF MAILING
for Redetermination of a Deficiency or Revision of a Determination or Refund of Corporation Franchise Tax under Article 9A of the Tax Law for the Years 1975 - 1977.	

State of New York }
ss.:
County of Albany }

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 18th day of January, 1984, he served the within notice of Decision by certified mail upon The Gates Rubber Company, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

The Gates Rubber Company
c/o John Mann
999 S. Broadway, P.O. Box 5887
Denver, CO 80217

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
18th day of January, 1984.

David Parchuck

Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

January 18, 1984

The Gates Rubber Company
c/o John Mann
999 S. Broadway, P.O. Box 5887
Denver, CO 80217

Gentlemen:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1090 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition of THE GATES RUBBER COMPANY for Redetermination of a Deficiency or for Refund of Corporation Franchise Taxes under Article 9-A of the Tax Law for the Years 1975, 1976 and 1977.	DECISION

Petitioner, The Gates Rubber Company, 999 S. Broadway, P.O. Box 5887, Denver, Colorado 80217, filed a petition for redetermination of a deficiency or for refund of corporation franchise taxes under Article 9-A of the Tax Law for the years 1975, 1976 and 1977 (File No. 33379).

A formal hearing was held before Frank W. Barrie, Hearing Officer, at the offices of the State Tax Commission, Building 9, State Office Campus, Albany, New York, on February 10, 1983 at 9:15 A.M. with all briefs to be submitted by May 13, 1983. Petitioner appeared by its assistant treasurer and tax specialist, Roger H. Talich and John Mann, respectively. The Audit Division appeared by Paul B. Coburn, Esq. (Harry Kadish, Esq., of counsel).

ISSUE

Whether petitioner, The Gates Rubber Company, is required to file combined corporation franchise tax reports for the years 1975, 1976 and 1977 with its wholly owned subsidiaries, National Tires, Inc. and Gates Export Corporation.

FINDINGS OF FACT

1. On January 9, 1981, the Audit Division issued three Notices of Deficiency against petitioner, The Gates Rubber Company ("Gates Rubber"), alleging corporate tax deficiencies of $15,716.00, $20,897.00 and $26,836.00 for the periods

ended December 31, 1975, December 31, 1976 and December 31, 1977, respectively. On January 9, 1981, the Audit Division also issued three Statements of Audit Adjustment against petitioner explaining that the corporate tax deficiencies were based on a recent field audit.

2. Petitioner filed Forms CT-3, New York State Corporation Franchise Tax Reports, for each of the years at issue and reported entire net income of $12,038,024, $21,157,306 and $34,075,846 for the periods ended December 27, 1975, December 25, 1976 and December 31, 1977, respectively. Petitioner reported New York business allocation percentages of 1.1381%, 1.6239% and 1.6816% for the periods ended December 27, 1975, December 25, 1976 and December 31, 1977, respectively.

3. Petitioner challenged the portion (approximately $45,636.00) of the total corporate tax deficiencies for the periods at issue which resulted from the Audit Division including two subsidiaries of petitioner, National Tires, Inc. ("National Tires") and Gates Export Corporation ("Gates Export") in combined corporate franchise tax reports with petitioner.

4. Gates Rubber, a Colorado corporation which began business in New York on September 1, 1963, is principally engaged in the manufacture and sale of rubber products: automotive hoses and belts, water hoses, and rubber for oil rigs. Petitioner has several manufacturing plants located primarily in the western part of the United States. It also owns or rents warehouses throughout the country where goods are stored pending shipment to customers. Its general executive and accounting offices are located in Denver, Colorado. In New York, petitioner rents sales offices in Syracuse, Williamsville and Burnt Hills.

5. National Tires and Gates Export are wholly owned subsidiaries of Gates Rubber. Both subsidiaries are wholesalers of petitioner's products, purchasing

all of their inventory from petitioner for resale. National Tires wholesales petitioner's auto accessories; Gates Export supplies all inventory to petitioner's wholly owned domestic international sales company, "DISC", Overseas Export Company, for overseas sales. Petitioner and the two subsidiaries have common officers.

6. Gates Export and National Tires have no activities in New York other than soliciting sales orders from cutomers. The orders are sent back to Denver, Colorado for approval and processing. Neither subsidiary maintains an office in New York State.

7. Petitioner is the parent corporation of approximately nineteen wholly owned domestic subsidiaries. It also wholly owns thirteen alien corporations which distribute the rubber products of Gates Rubber within the countries where they are incorporated (with the exception of Fomento de Industrias, S.A., which is a holding company and serves as an intermediate corporation between petitoner and the foreign corporation which distributes petitioner's rubber products). Petitioner calculated that if it included its alien subsidiaries in its New York combined tax reports, its franchise tax for the three years at issue would be reduced in total by $27,745.

8. Petitioner argued that since the State of New York under federal law[1] may not tax National Tires and Gates Export on a separate basis (since the only activity of the subsidiaries within New York is the solicitation of orders), New York should not be able to do so indirectly by requiring petitioner to file a combined return with such subsidiaries. Petitioner further argued at the hearing herein that the Audit Division was arbitrary in including only National Tires and Gates Export in the combined tax reports and none of its wholly owned alien subsidiaries. Finally, petitioner contended at the

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[1] 15 U.S.C. §381.

hearing herein that this Commission's decision in Matter of National Tires, State Tax Commission, October 17, 1980, precludes the Audit Division from requiring petitioner to file a combined tax report with National Tires.

CONCLUSIONS OF LAW

A. That Tax Law §211.4 authorizes the Tax Commission, in its discretion, to require or permit a parent corporation and its wholly owned subsidiaries to file corporation franchise tax reports on a combined basis. This section of law provides further that "(N)o combined report covering any corporation not a taxpayer[2] shall be required unless the tax commission deems such a report necessary, because of inter-company transactions...in order properly to reflect the tax liability under this article."

B. That during 1975, the Tax Commission provided, by regulation, former 20 NYCRR 5.28(b), that in determining whether corporation franchise tax would be computed on a combined basis, it would consider various factors, including the following:

> (1) Whether the corporations were engaged in the same or related lines of business;
>
> (2) Whether any of the corporations were in substance merely departments of a unitary business conducted by the entire group;
>
> (3) Whether the products of any of the corporations were sold to or used by any of the other corporations;
>
> (4) Whether any of the corporations performed services for, or loaned money to or otherwise financed or assisted in the operations of, any of the other corporations;
>
> (5) Whether there were other substantial intercompany transactions among the constituent corporations.

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[2] Tax Law § 208.2 defines "taxpayer" to mean "any corporation subject to tax under this article." Since National Tires and Gates Export merely solicit orders in New York, they are not considered "taxpayers" for purposes of the New York corporation franchise tax.

C. That during 1976 and 1977, the Tax Commission provided by regulation, 20 NYCRR 6-2.3(a), (which carried over the essential elements of the regulation noted in Conclusion of Law "B", supra), that in determing whether to permit or require combined corporation franchise tax reports the following two broad factors must be met:

(1) the corporations are in substance parts of a unitary business conducted by the entire group of corporations, and

(2) there are substantial intercorporate transactions among the corporations.

D. That it is clear from the facts of this case that there were substantial intercorporate transactions between petitioner and National Tires and between petitioner and Gates Export and that the three corporations were parts of the same unitary business. In particular, both National Tires and Gates Export purchased one hundred percent of their inventory from petitioner, their parent corporation, and all three corporations were engaged in the same line of business: the sale of rubber products. In effect, all three corporations were part of the same unitary business with a shared raison d'etre: the selling of the products manufactured by petitioner.

Since "it is not a condition precedent that the income or capital of the taxpayer be improperly or inaccurately reflected" to require a combined report, the Audit Division properly required petitioner to file combined reports with National Tires and Gates Export because of substantial intercorporate transactions and the fact that the three corporations were each part of the same unitary business. Wurlitzer Co. v. State Tax Comm., 35 N.Y.2d 100, 105 and Matter of Campbell Sales Company, State Tax Commission, May 20, 1983. Furthermore, if petitioner, National Tires and Gates Export are allowed to file separately,

the amount of tax properly due to New York may be distorted. See Coleco Industries, Inc. v. State Tax Com'n, 461 N.Y.S.2d 462, 463. There is no certainty that the cost to the subsidiaries for their inventory, which is purchased entirely from petitioner, is based upon arm's length bargaining or market factors. Petitioner may keep its own profits down and its subsidiaries' profits up by selling goods to its subsidiaries at a reduced price. Furthermore, if petitioner is permitted to file separately, any increased income in the form of dividends paid to petitioner by the subsidiaries (resulting from petitioner's bargain sale of inventory to its subsidiaries and the consequential increased profits of the subsidiaries) would not be includible in petitioner's New York income since they would be attributable to subsidiary capital. Tax Law § 208.9(a)(1). Therefore, a combined corporation franchise tax report covering petitioner, National Tires and Gates Rubber is necessary in order to properly reflect petitioner's corporation franchise tax liability.

E. That 15 U.S.C. §381, "Net income tax on interstate income restricted", does not prohibit this Commission from requiring petitioner to file a combined return with its subsidiaries, National Tires and Gates Export. Petitioner, by maintaining offices in New York, does not merely solicit sales in New York. We note further that the United States Supreme Court recently upheld the unitary tax method of California which required a parent corporation doing business in California to include the income of its alien subsidiaries earned outside the United States in its California tax base. Container Corporation of America v. Franchise Tax Board, __U.S.__, 51 U.S.L.W. 4987 (U.S. June 27, 1983) (No. 81-523).

F. That the Audit Division was not arbitrary in including only National Tires and Gates Export in petitioner's combined tax reports. Petitioner may

not include its alien subsidiaries in its New York combined tax reports because there is no authority under New York law to include in a combined report the income of alien subsidiaries which are not created or organized under the laws of the United States or of any state and which have no (i) gross income derived from sources within the United States or (ii) gross income which is effectively connected with the conduct of a trade or business within the United States[3].

G. That the petition of the Gates Rubber Company is denied.

DATED: Albany, New York
JAN 18 1984

STATE TAX COMMISSION

PRESIDENT

COMMISSIONER

COMMISSIONER

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[3] See I.R.C. §§881-884 which details when an alien corporation will be subject to United States taxation. Under Tax Law §208.9, "entire net income" is presumed to be the same as the entire taxable income which a taxpayer is required to report to the United States. Therefore, if an alien corporation is not subject to United States taxation, it will have no "entire net income" for purposes of New York taxation.