

Selected Current Topics in Indiana Taxation

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I. INTRODUCTION

This Article addresses several current topics in Indiana taxation. First, it will review recent developments in the treatment of partnerships and joint ventures for Indiana income tax purposes. For over 25 years, Indiana has wrestled with the issue of how partnerships and joint ventures should be taxed, changing course several times during those years. Many new and significant commercial operations in the state today are joint ventures or partnerships and it is imperative that Indiana have a clear and, more importantly, a stable position on the taxation of these business forms.

Next, the Article will review recent case law developments in the area of Indiana's personal property tax, particularly those decisions addressing the interstate commerce or warehouse exemptions for finished goods inventory. These exemptions have provided significant property tax relief to Indiana taxpayers over the years, and in three recent decisions the Indiana Tax Court has provided guidance on such issues as *who* is entitled to claim these exemptions,¹ *when* those exemptions are waived by the taxpayer² and *how many* exemptions a taxpayer may claim.³ During the survey period, the tax court also addressed the heretofore controversial issue of whether a taxpayer is entitled to an inventory valuation adjustment for changes in the inventory's market value, and the court's decision on this issue in *Don Meadows Motors, Inc. v. State Board of Tax Commissioners*⁴ will be reviewed.

The Indiana Tax Court's decision in *West Publishing Co. v. Indiana Department of Revenue*,⁵ an important case during the survey period which further develops Indiana law on what constitutes "solicitation" pursuant to Public Law No. 86-272,⁶ will be discussed. Congress provided

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1. *State Line Elevator, Inc. v. State Bd. of Tax Comm'rs*, 528 N.E.2d 501 (Ind. T.C. 1988).

2. *Gulf Stream Coach, Inc. v. State Bd. of Tax Comm'rs*, 519 N.E.2d 238 (Ind. T.C. 1988).

3. *RCA Corp. v. State Bd. of Tax Comm'rs*, 528 N.E.2d 125 (Ind. T.C. 1988).

4. 518 N.E.2d 507 (Ind. T.C. 1988).

5. 524 N.E.2d 1329 (Ind. T.C. 1988).

6. Act approved Sept. 14, 1959, Pub. L. No. 86-272, 73 Stat. 555 (codified as amended at 15 U.S.C. §§ 381-84 (1982)). In this Act, Congress "exercised its power to regulate state taxation of activities related to interstate commerce." 524 N.E.2d at 1335.

in this federal legislation that a state may not subject a nonresident taxpayer to net income tax if that nonresident's activities in the state do not exceed the solicitation of orders for goods.⁷ The *West Publishing* decision not only reaffirms that Indiana interprets the term "solicitation" to include all of those activities inextricably related to solicitation, but also establishes that acts of courtesy and services rendered to a customer to facilitate a sale may be protected activities under the federal law. *West Publishing* clearly aligns Indiana with those states that have refused to adopt an unduly narrow and technical interpretation of the term "solicitation," instead applying that term in its ordinary and reasonable commercial sense.

On the administrative front, the Indiana General Assembly has given taxpayers some degree of assurance that there will be consistency in the administration and application of Indiana's tax laws. This Article will review Indiana Code section 6-8.1-3-3, which prohibits the Indiana Department of Revenue ("Department" or "Revenue" Department) from changing its interpretation of a tax law in such a way that the taxpayer's liability is increased, unless that change in interpretation is prospective in operation and effectuated by the formal *promulgation of a regulation*.⁸ Clearly a legislative reaction to the Revenue Department's repeated "flip-flopping" on significant tax issues, this somewhat novel statute may provide taxpayers with some assurance of consistency in the application of Indiana's tax laws, that in turn will facilitate business and tax planning.

Finally, in light of the recent case of *Blood v. Poindexter*,⁹ this Article will re-examine the issue of the Indiana Tax Court's jurisdiction.¹⁰ During the survey period, the Indiana Tax Court once again faced a challenge to its jurisdiction, specifically, whether that court has exclusive jurisdiction over inheritance tax matters.¹¹ In *Blood*, as in previous cases challenging the jurisdiction of the Indiana Tax Court,¹² Judge Fisher reiterated the tax court's position that in creating the Indiana Tax Court the legislature's intent was to consolidate *all* tax issues in one judicial forum and held that the tax court has exclusive jurisdiction over inheritance tax appeals from final determinations of the Indiana Department of Revenue.¹³

7. 15 U.S.C. § 381 (1982).

8. IND. CODE § 6-8.1-3-3 (1988).

9. 524 N.E.2d 824 (Ind. T.C. 1988).

10. This issue was previously addressed in F. Dlouhy & J. King, *Significant Developments in Indiana Taxation*, 21 IND. L. REV. 383 (1987).

11. *Blood*, 524 N.E.2d at 824.

12. See, e.g., *Herff Jones, Inc. v. State Bd. of Tax Comm'rs*, 512 N.E.2d 485 (Ind. T.C. 1987) (Indiana Tax Court has "exclusive jurisdiction in refund case in which county board of commissioners had no discretion to allow refund claim following State Board's disapproval of claim.").

13. 524 N.E.2d at 825.

II. THE TAXATION OF PARTNERSHIPS IN INDIANA

During the survey period, the number of major operations doing business in Indiana as corporate joint ventures or partnerships has significantly increased. An advantage of doing business as a partnership or a joint venture in Indiana is the exemption from gross income tax granted by Indiana Code section 6-2.1-3-25(b).¹⁴ In 1988, the legislature re-examined this exemption, but only placed a minor limitation on its availability.¹⁵ This exemption should thus be considered in weighing the pros and cons of doing business in Indiana as a partnership vis-a-vis a corporation.

All partnerships today are exempted from Indiana gross income tax,¹⁶ adjusted gross income tax¹⁷ and supplemental net income tax.¹⁸ This includes corporate partnerships, (partnerships with one or more corporate partners) and two-tier partnerships (partnerships where the first-tier partners are themselves partnerships).

This was not always the case, however. Indiana has vacillated numerous times on how partnerships should be taxed. Prior to the enactment of the Adjusted Gross Income Tax Act¹⁹ in 1963, Indiana had only one income tax, the gross income tax,²⁰ that was imposed upon partnerships, joint ventures and pools.²¹ If the gross income tax was paid on the gross income of the partnership, joint venture or pool, the amounts received by the partners or participants as their respective distributive shares of the income of the partnership, joint venture or pool, were exempted from gross income tax.²² In short, prior to the enactment of the Adjusted Gross Income Tax Act, partnerships or joint ventures were treated as separate taxable entities subject to the Indiana gross income tax.

14. IND. CODE § 6-2.1-3-25(b) (1988). This section provides:

Gross income received by a partnership is exempt from gross income tax. However, a gross income is not exempt from the gross income tax if it is received by a publicly traded partnership that is treated as a corporation for federal income tax purposes under section 7704 of the Internal Revenue Code.

15. In the 1988 amendment, the legislature added the second sentence to subsection (b).

16. IND. CODE § 6-2.1-3-25(b) (1988).

17. *Id.* § 6-3-4-11.

18. *Id.* § 6-3-8-5.

19. Adjusted Gross Income Tax Act of 1963, ch. 32 (Spec. Sess.), 1963 Ind. Acts (Spec. Sess.) 82.

20. IND. CODE ANN. §§ 64-2601 to 31 (Burns 1961) (current version at IND. CODE §§ 6-2.1-1-1 to § 6-2.5-10-4 (1988)).

21. IND. CODE ANN. § 64-2601(a) (Burns 1961) (current version at IND. CODE § 6-2.1-1-16 (1988)).

22. IND. CODE ANN. § 64-2607(a) (Burns 1961) (current version at IND. CODE § 6-2.1-3-25 (1988)).

In 1963, the Indiana General Assembly enacted the Adjusted Gross Income Tax Act, drafting the legislation so that it piggy-backed on the federal income tax framework.²³ As a result, the legislature effectively exempted partnerships from the adjusted gross income tax, instead imposing that tax on the partners and the partners' net distributive share of partnership income. Two years later, the legislature exempted partnerships from the gross income tax,²⁴ making such exemption retroactive to June 30, 1963, the effective date of the Adjusted Gross Income Tax Act. Thus, in the early 1960's, for purposes of both of Indiana's income taxes, partnerships were not treated as separate taxable entities, but instead as pass-through entities, with the tax liability being imposed upon the partners or participants.

The enactment of this exemption for partnerships and joint ventures prompted many corporations to join in a partnership with another corporation, individual or partnership. For six years, many Indiana businesses did business as partnerships or joint ventures. Then, in 1969, perhaps prompted by a short fall in revenues, the legislature created the Indiana tax concept of "corporate partnerships" as constituting separate taxable entities.²⁵ The Adjusted Gross Income Tax Act was again amended to add a new subsection that provided as follows:

(b) Every partnership, of which one or more of the partners is a corporation, shall be liable for the tax on gross income imposed by sections 2 and 3 of the Gross Income Tax Act of 1933, as amended. When such a partnership is liable for tax on its gross income, no partner shall be liable for the tax imposed on the partner's distributive share of the partnership income by this Act. Nor shall any partner in such a partnership be liable for the tax imposed on the partner's distributive share of partnership income by the Gross Income Tax Act of 1933, as amended.²⁶

Under this amendment, the Indiana gross income tax was imposed on corporate partnerships as separate taxable entities, and the partners of such corporate partnerships were expressly exempted from liability for both the adjusted gross income tax and gross income tax in respect to their distributive shares. However, since the adjusted gross income tax itself was still piggy-backed on the federal income tax framework, the net effect of exempting the partners of a corporate partnership from

23. Adjusted Gross Income Tax Act of 1963, ch. 32 (Spec. Sess.), 1963 Ind. Acts (Spec. Sess.) 82.

24. Act approved March 10, 1965, ch. 233, § 28, 1965 Ind. Acts 582, 603 (amending the Adjusted Gross Income Tax Act).

25. Act approved March 14, 1969, ch. 326, § 12, 1969 Ind. Acts 1372, 1390.

26. *Id.*

this particular tax liability was to render no one liable for adjusted gross income tax on the net income of a corporate partnership. In short, under the federal tax structure, the corporate partnership was not a taxpayer and, under Indiana's 1969 amendment, the partners of a corporate partnership were not subject to adjusted gross income tax liability. Simply stated, no one was technically subject to adjusted gross income tax attributable to corporate partnership income.

In 1971, additional amendments to the Adjusted Gross Income Tax Act²⁷ provided that corporate partnerships, as separate taxable entities, would be subject to both gross income and adjusted gross income taxes.²⁸ The amendments also reaffirmed that the partners of a corporate partnership would not be liable for gross income or adjusted gross income taxes on the partner's distributive share of income from the corporate partnership.²⁹

To circumvent the amendment's effective elimination of the gross income tax exemptions for corporate partnerships, many corporate partnerships simply reorganized into two-tier partnerships where the first-tier partners were themselves partnerships, composed of corporate partners. As previously noted, the legislature had defined a corporate partnership as a partnership in which one or more of the partners is a corporation.³⁰ The argument put forth by the two-tier partnership was that none of its partners (*i.e.*, the first-tier partners) were corporations and, therefore, the 1969 and 1971 amendments were not applicable to it.³¹ However, in the 1981 case of *Park 100 Development Company v. Indiana Department of State Revenue*,³² the Indiana Supreme Court held that such two-tier partnerships could not be used to circumvent the tax.³³ The court thereupon pierced the partnership's veil, finding that it was only an attempt to cloak two corporations, which the court held were properly liable for gross income tax.³⁴

Two years after the *Park 100* decision, the legislature amended the gross income tax and adjusted gross income tax laws again by eliminating the concept of a corporate partnership, treating all partnerships alike *and* exempting all partnerships from both the adjusted gross income and

27. Act approved [April] 16, 1971, Pub. L. No. 64, 1971 Ind. Acts 311.

28. *Id.* § 7, 1971 Ind. Acts at 327.

29. *Id.*

30. *See supra* text accompanying notes 25-26.

31. *See Park 100 Dev. Co. v. Indiana Dep't of State Revenue*, 388 N.E.2d 293 (Ind. Ct. App. 1979), *rev'd*, 429 N.E.2d 220 (Ind. 1981).

32. 429 N.E.2d 220 (Ind. 1981).

33. *Id.* at 223.

34. *Id.*

gross income taxes.³⁵ Since 1983, the legislature has modified this exemption only once, to deny the exemption to partnerships that are treated as corporations under Internal Revenue Code section 7704.³⁶

With partnerships reclassified as pass-through, nontaxable entities for income tax purposes, the question then became how their partners should be taxed. For adjusted gross income tax purposes, the answer was fairly clear. Because the adjusted gross income tax piggy-backs on the federal Internal Revenue Code,³⁷ the partner is liable on its net distributive share of partnership income as determined under that Code.³⁸

For gross income tax purposes, the issue was more complicated. Many argued that the corporate partner's gross income tax liability should be based upon its pro rata share of the partnership's *receipts*. Others argued that the measure of the tax should be the amount *actually distributed* to the corporate partner. After much debate as to what should be the measure of the corporate partner's gross income tax liability, the Revenue Department adopted the position that a corporate partner shall only be subject to gross income tax on its *net* distributive share of partnership income.³⁹

As the following two hypothetical situations illustrate, the Department's decision on how to tax corporate partners for gross income tax purposes can result in tax savings for a business that operates as a partnership, rather than a corporation. Assume that X Corporation and Y Corporation are partners of Z, an Indiana partnership. Z buys a widget for \$1,000. Z then sells that widget to a third party for \$1,000. As a result, Z recognizes no gain on the sale for federal income tax purposes, and (assuming that Z has no other income or loss for the relevant taxable year) X and Y will each report, for federal income tax purposes, \$0 of taxable income as their distributive shares of Z's taxable income for such year. In a second hypothetical assume the same set of facts, except that Z is an Indiana corporation. Because the Indiana Department of Revenue has concluded that the corporate partner's distributive share of partnership taxable income (per Federal Income Tax Schedule K-1) is subject to gross income tax, in the first hypothetical situation Z, the partnership, would have no gross income tax liability

35. Act approved March 2, 1984, Pub. L. No. 47, 1984 Ind. Acts 617 (currently codified at IND. CODE § 6-2.1-3-25(b) (1988)).

36. Act approved March 5, 1988, Pub. L. No. 63, 1988 Ind. Acts 1144 (currently codified at IND. CODE § 6-2.1-3-25(b) (1988)).

37. See IND. CODE § 6-3-1-3.5 (1988).

38. See *id.* § 6-3-4-11.

39. Letter from Thomas A. Harling, Administrator of Income Tax Division, Indiana Department of Revenue to James L. Turner, Senior State Tax Consultant, Baker & Daniels (August 19, 1988).

pursuant to Indiana Code section 6-2.1-3-25. Since *X*'s and *Y*'s distributive shares of *Z*'s taxable income (for federal income tax purposes) are zero, *X* and *Y* will not have any gross income tax liability. In the second hypothetical situation *Z*, the corporation, will have gross income tax liability on the \$1,000 of gross receipts it received from the sale of the widget.

Contributions of capital to partnerships or joint ventures are exempt from gross income tax, and no gross receipts result to either the recipient of the capital or to the contributor.⁴⁰ Therefore, a partnership or joint venture can be established and assets transferred thereto without gross income tax consequences. It should be noted that the exemption provided by Indiana Code section 6-2.1-3-25(b) is not just available to partnerships engaged in ongoing businesses, but also is available to joint ventures taxpayers involved in one-time transactions or ventures, because technically the term "partnership" under the gross income tax act includes joint ventures.⁴¹ According to the Indiana code:

The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization through or by means of which any business, financial operation or venture is carried on, and which is not, within the meaning of this act, a corporation or a trust or an estate.⁴²

This definition is exactly the same definition of a partnership as is set forth in the Internal Revenue Code.⁴³ As a result, whether an entity is a partnership for purposes of the Indiana exemption will turn in part upon whether the entity is considered to be a partnership under federal income tax standards.⁴⁴

While operating as a partnership may in fact result in considerably less income tax liability, it should be observed that it may not always prove to be beneficial to operate as a partnership, vis-a-vis a corporation, because the Indiana Department of Revenue currently takes the position that partnership income is *always* taxable at the higher gross income tax rate. Thus, in the case of a *corporation* manufacturing and selling widgets, its gross receipts from the sale of widgets would be taxed at the lower gross income tax rate, currently .3%.⁴⁵ A *partnership* in the

40. IND. CODE § 6-2.1-1-2(14) (1988).

41. *Id.* § 6-3-1-25 (partnership defined by reference to *id.* § 6-2.1-3-19).

42. *Id.* § 6-2.1-3-19.

43. I.R.C. §§ 761(a), 7701(a)(2) (1986).

44. *See generally* Commissioner v. Tower, 327 U.S. 280 (1946); Commissioner v. Culbertson, 337 U.S. 733 (1949); 1 W. MCKEE, W. NELSON & R. WHITMIRE, FEDERAL TAXATION OF PARTNERSHIPS AND PARTNERS § 3 (1977); 1 A. WILLIS, J. PENNEL & P. POSTLEWAITE, PARTNERSHIP TAXATION § 2 (3d ed. 1988).

45. IND. CODE § 6-2.1-2-3(a) (1988).

exact same business would be subject to no gross income tax, but according to the revenue department, its corporate partners would be subject to gross income tax on their *net* income at the higher gross income tax rate, currently 1.20%.⁴⁶ Depending on the business' ratio of gross income to net income, the partners of the partnership may or may not pay in the aggregate less tax than the corporation.⁴⁷

One final *caveat* about the taxation of partnerships should be noted. To the extent the Indiana Legislature has vacillated over the years in its approach to the taxation of partnerships, the same could be true in the future. Although partnerships, including corporate partnerships, are now exempted from gross income tax, adjusted gross income tax and supplemental net income tax, the legislature could revert to taxing all partnerships or just corporate partnerships. That, however, would be an unfortunate continuation of the confusion and vacillation about partnerships that have plagued Indiana for over a quarter of a century. We should not subject Indiana business to any further changes in this area. Stable tax policies are essential to business planning and development in Indiana.

III. THE INTERSTATE COMMERCE EXEMPTIONS—RECENT DEVELOPMENTS

In 1961, Indiana enacted the first of what are now *six* interstate commerce exemptions for finished goods inventory present in the state on the date on which personal property tax is assessed.⁴⁸ The interstate commerce (or warehouse exemptions, as they have been called) have been expanded over the years, intended by the legislature to offer personal property tax relief to taxpayers who have a large volume of finished goods inventory in the state destined for shipment in interstate commerce.

The expansion of these exemptions is exemplified by the two most recently enacted. Indiana Code section 6-1.1-10-29 was amended in 1984⁴⁹ to provide that, under certain circumstances, inventory located in an Indiana warehouse on March 1 is not subject to property tax if the personal property is owned by a manufacturer or processor and is destined

46. *Id.* § 6-2.1-2-3(b).

47. There is, of course, a question as to whether the Indiana Department of Revenue's position is even correct. Under Indiana Code sections 6-2.1-2-4 and 6-2.1-2-5, it is the *activity* that produced the income that is determinative of the applicable gross income tax rate. Income from "selling at retail" is taxable at the low gross income tax rate. IND. CODE § 6-2.1-2-4 (1988). In the above example, the *activity* that produced the income to the corporate partners is the selling of widgets at retail and, accordingly, that income should be taxed at the low gross income tax rate.

48. *Id.* §§ 6-1.1-10-29 to -30.

49. Act approved March 6, 1984, Pub. L. No. 41, § 2, 1984 Ind. Acts 548, 549.

for out-of-state shipment.⁵⁰ The main advantage of this and related sections is that the taxpayer may elect to "factor" its inventory destined for out-of-state shipment by using its previous twelve-months actual shipping experience rather than utilizing a specific identification method.⁵¹ Prior to the enactment of Indiana Code section 6-1.1-10-29, Indiana manufacturers and processors could only qualify for the interstate commerce exemptions for inventory produced in the state if they had a firm order for each item of inventory identifying a specific out-of-state destination.

Similarly, Indiana Code section 6-1.1-10-29.3, added in 1987,⁵² further expanded the availability of the interstate commerce exemption. Pursuant to this section, goods originating out-of-state that were shipped to a public or private warehouse in Indiana, repackaged and subsequently shipped to an out-of-state destination are also exempt from personal property tax.⁵³

Notwithstanding the legislature's generosity with respect to the interstate commerce exemptions, taxpayers continue to misunderstand the exemptions, thereby losing the benefits of those exemptions for which they might otherwise qualify. The decision in *Gulf Stream Coach, Inc. v. State Board of Tax Commissioners*⁵⁴ emphasizes the care taxpayers must take in preparing their property tax returns in order not to waive the interstate commerce exemptions. In *Gulf Stream*, the taxpayer (Gulf Stream) manufactured and converted motor homes and travel trailers. Finished units, ready for delivery, were warehoused by Gulf Stream in an area separate from its manufacturing operation. Finished units were stored in a separate warehouse area until either a driver became available to transport the finished unit or Gulf Stream received an order for the finished units.⁵⁵

At issue in this case was \$582,306 worth of finished units Gulf Stream had on hand but treated as sold. These particular units were

50. *Id.* § 6-1.1-10-29.

Personal property owned by a manufacturer or processor is exempt from property taxation if the owner is able to show by adequate records that the property is stored and remains in its original package in an in-state warehouse for the purpose of shipment, without further processing, to an out-of-state destination.

51. *Id.* § 6-1.1-10-29.5(b). Under this section a taxpayer may substantiate his exemption claimed pursuant to Indiana Code section 6-1.1-10-29 by using a ratio of the taxpayer's shipments to out-of-state destinations over the past twelve months to the taxpayer's total shipments over the past twelve months.

52. Act approved March 4, 1986, Pub. L. No. 58, 1986 Ind. Acts 867.

53. *Id.* § 6-1.1-10-29.3. Although the goods may be repackaged in Indiana, they cannot be subject to additional manufacturing or processing at that time. *Id.*

54. 519 N.E.2d 238 (Ind. T.C. 1988).

55. *Id.* at 239.

subject to binding, pre-existing purchase orders and Gulf Stream had removed them from its book inventory. In preparing its business personal property tax return, Gulf Stream omitted these units entirely. Accordingly, for property tax reporting purposes, Gulf Stream did not show these units as being in its inventory and did not claim any of these units as being exempt under the interstate commerce exemptions. However, some of these units were subject to binding orders from out-of-state customers and would have qualified for exemption.⁵⁶

The Indiana Tax Court first addressed the question of whether the subject units, treated as sold and removed from Gulf Stream's book inventory, were properly omitted in computing Gulf Stream's inventory for Indiana business personal property tax purposes. Gulf Stream contended that the units did not have to be reported because their removal from the books was consistent with generally accepted accounting principles. The court, however, concluded that removal of inventory from the taxpayer's books for financial accounting purposes, even though proper and in accordance with generally accepted accounting principles, is not necessarily correct for *state tax accounting* purposes.⁵⁷ Quoting the United States Supreme Court, the court stated, "'A presumptive equivalence between tax and financial accounting . . . create[s] insurmountable difficulties of tax administration. . . . [I]f management election among acceptable options were dispositive for tax purposes, a firm, indeed, could decide unilaterally—within limits dictated only by its accountants—the tax it wished to pay.'"⁵⁸ The court then concluded:

The [State Tax Board's] regulations require full disclosure and 50 IAC 4.1-3-4 must be read to require disclosure of all units still under the control of the taxpayer. . . . The requirement of full disclosure is not a trap for the unwary, it is a clear and necessary procedure to insure fair and accurate administration of the property tax laws.⁵⁹

The court also found that Gulf Stream's failure to comply with the statutes and regulations in reporting the subject units and in claiming the interstate commerce exemption on these units constituted waiver of that exemption to which the taxpayer may have otherwise been entitled.⁶⁰ The court gave short shrift to Gulf Stream's contention that, even though it had not complied with the statutory provisions for claiming an ex-

56. *Id.* at 240.

57. *Id.* at 241 (emphasis added).

58. *Id.* at 241 (quoting *Thor Power Tools Co. v. Commissioner*, 439 U.S. 522 (1979)).

59. 519 N.E.2d at 241.

60. *Id.* at 242.

emption, it should be entitled to that exemption as a constitutional right under the Commerce Clause. The tax court observed that the Commerce Clause affords no personal constitutional right to any individual taxpayer.⁶¹ Instead "the Commerce Clause defines the relationship between the federal government and the governments of the individual states as it relates to the free flow of commerce."⁶² Judge Fisher stated further, "no personal rights, are conferred by provisions which dictate the structure of government."⁶³ Accordingly, Gulf Stream's failure to follow the proper procedures for claiming the interstate commerce exemptions was found to constitute the waiver of these exemptions. Finally, in a further word to the careless, the court found that the twenty percent penalty imposed upon a taxpayer who undervalues property on its tax return by more than five percent of the value that should have been reported is *nonwaivable*.⁶⁴

A petition to transfer the *Gulf Stream* case to the Indiana Supreme Court is currently pending. The tax court's decision in *Gulf Stream* is, of course, consistent with the Indiana Court of Appeals' holding in *Indiana State Board of Tax Commissioners v. Stanadyne, Inc.*⁶⁵ that a taxpayer waives its entitlement to the interstate commerce exemptions by not properly claiming those exemptions on its return, as prescribed by Indiana Code section 6-1.1-10-31.⁶⁶ While admittedly it is a harsh result for a taxpayer to forever lose its entitlement to the interstate commerce exemptions by not making a proper claim on its return or by understating its claim on its return, the *Gulf Stream* decision is solidly based upon statutory law, as well as the law regarding the waiver of constitutional rights. Taxpayers who feel that the result is unfair and results in a windfall to the taxing units in which the inventory is located should recognize that the proper forum to petition for relief is the legislature, not the Indiana courts.⁶⁷

Not only does a taxpayer have to properly claim the interstate commerce exemptions provided by Indiana Code sections 6-1.1-10-29 and 6-1.1-10-30, but that claim can only cover inventory *owned* by the taxpayer. In *State Line Elevator, Inc. v. State Board of Tax Commis-*

61. *Id.*

62. *Id.*

63. *Id.*

64. *Id.* at 243.

65. 435 N.E.2d 278 (Ind. Ct. App. 1982).

66. *Id.* at 283-84.

67. House Bill 1783, introduced in the 1989 General Assembly, would grant the interstate commerce exemptions to a taxpayer that correctly stated total tax liability on its return by excluding the exempt inventory but who was denied the exemption because it failed to file Form 103-W with its return. H.B. 1783 would apply to the years 1985, 1986, 1987 and 1988.

sioners,⁶⁸ the taxpayer, an Indiana grain elevator, stored grain owned by Indiana and Illinois farmers. State Line, however, did not take title to or become the owner of the grain. State Line reported all of the grain that it held (possessed) on its business personal property tax return, and then claimed an exemption under Indiana Code section 6-1.1-10-29 for the grain in its elevators destined for out-of-state locations. The State Tax Board denied State Line the exemption because State Line was not the owner of the property for which the exemption was sought.⁶⁹

In determining whether a taxpayer can claim an interstate commerce exemption for property it does not own, the tax court strictly construed the language of Indiana Code section 6-1.1-10-29, which provides:

Personal property owned by a manufacturer or processor is exempt from property taxation *if the owner is able to show* by adequate records that the property is stored and remains in its original package in an in-state warehouse for the purpose of shipment, without further processing, to an out-of-state destination.⁷⁰

The court concluded that the reference to the term "owner" supports the conclusion that the exemption should only be available to the owner of property. Thus, since State Line admitted that it was not the holder of legal title to the grain for which it sought an exemption, State Line could not properly claim the exemption.⁷¹

The tax court also rejected State Line's argument that, since it was treated as the owner of grain for purposes of assessment, it should be given the right of the owner to claim the exemption.⁷² Under Indiana Code section 6-1.1-2-4(b), "the person holding, possessing, controlling or occupying" the property is *also* liable for property tax thereon, unless he establishes that the property is being assessed and taxed in the name of the owner, or the owner is liable for the taxes under a contract with that person.⁷³ State Line was assessed tax on the grain it held for others under Indiana Code section 6-1.1-2-4(b). The court concluded that State Line's assessment under Indiana Code section 6-1.1-2-4(b) was not based upon *ownership*, but instead was based upon the fact that State Line was a possessor who had not established that the property was assessed and taxed in the name of the owner. In short, the court held that,

68. 528 N.E.2d 501 (Ind. T.C. 1988).

69. *Id.* at 502.

70. *Id.* (quoting IND. CODE § 6-1.1-10-29 (1988)) (emphasis supplied by court).

71. 528 N.E.2d at 502.

72. *Id.* Under Indiana Code section 6-1.1-2-4(a), the owner of property is liable for property taxes due thereon.

73. IND. CODE § 6-1-1.2-4(b) (1988).

while an owner *or* the possessor of inventory may have a personal property tax liability on that inventory, only the owner is entitled to claim the interstate commerce exemptions available for that inventory.⁷⁴

Although the *State Line* decision expressly addressed only the exemption granted to manufacturers and processors under Indiana Code section 6-1.1-10-29, arguably its holding is equally applicable to the interstate commerce exemptions provided by Indiana Code sections 6-1.1-10-29.3, 6-1.1-10-30(a) and 6-1.1-10-30(c).⁷⁵ All of these exemption provisions similarly contain the operative words "if the owner is able to show by adequate records," which the tax court has interpreted to mean two things: (1) that the *owner* has to prove that the goods qualify for the exemption, and (2) that the availability of the exemption is limited to the *owner*, notwithstanding that someone other than the owner, such as the possessor, statutorily bears the property tax liability on the inventory.⁷⁶

74. 528 N.E.2d at 502-03.

75. Respectively, these sections provide in pertinent part:

Personal property shipped into Indiana is exempt from property taxation *if the owner is able to show by adequate records* that the property:

- (1) is stored in an instate warehouse for the purpose of transshipment to an out-of-state destination; and
- (2) is ready for transshipment without additional manufacturing or processing, except repackaging.

IND. CODE § 6-1.1-10-29.3 (1988) (emphasis added).

(a) Subject to the limitation contained in subsection (d) of this section, personal property is exempt from taxation if:

- (1) the property is owned by a nonresident of this state;
- (2) *the owner is able to show by adequate records* that the property has been shipped into this state and placed in its original package in a public or private warehouse for the purpose of transshipment to an out-of-state destination; and
- (3) the property remains in its original package and in the public or private warehouse.

Id. § 6-1.1-10-30(a) (emphasis added).

(c) Subject to the limitation contained in subsection (d) of this section, personal property is exempt from property taxation if:

- (1) the property has been placed in its original package in a public warehouse;
- (2) the property was transported to that public warehouse by a common, contract, or private carrier;
- (3) *the owner is able to show by adequate records* that the property is held in the public warehouse for purposes of transshipment to an out-of-state destination and is labeled to show that purpose; and
- (4) the property remains in its original package and in the public warehouse.

Id. § 6-1.1-10-30(c) (emphasis added).

76. See *State Line Elevator, Inc. v. State Bd. of Tax Comm'rs*, 528 N.E.2d 501 (Ind. T.C. 1988).

Whether the Indiana Legislature really intended this result is unclear. If the interstate commerce exemptions were enacted to provide property tax relief to those who held finished goods inventory in Indiana destined for shipment in interstate commerce, it really makes no sense to distinguish between "owners" and "possessors" in providing that kind of tax relief. Furthermore, the tax court may have construed the operative phrase more narrowly than intended by the legislature, since the "second" meaning noted above is the result of implication, rather than expression. Literally, these words require that the owner *prove* that the goods satisfy the various requirements for exemption.⁷⁷ This phrase does not expressly limit the exemptions to the legal owner of the goods.

In *RCA v. State Board of Tax Commissioners*,⁷⁸ the Indiana Tax Court confirmed, as many taxpayers had believed, that they were entitled to claim *more than one* of the interstate commerce exemptions for inventory pursuant to Indiana Code sections 6-1.1-10-29, 6-1.1-10-29.3 and 6-1.1-10-30.⁷⁹ RCA, a manufacturer of electronic audio and video equipment, owned finished goods inventory "which had been shipped into Indiana and placed into original packages in the warehouse for purposes of transshipment to in-state or out-of-state locations ('imported products'), [as well as] property which was produced in Indiana and placed in original packages in the warehouses for storage pending shipment ('domestic products')." ⁸⁰

Pursuant to Indiana Code section 6-1.1-10-30(a), RCA claimed an exemption for 98% of its *imported* products stored in its Indiana warehouses on March 1, 1986. This exemption was not disputed by the state tax board.⁸¹ A second exemption for a portion of the *domestic* products stored in the warehouses was claimed under Indiana Code section 6-1.1-10-30(b). RCA used the specific identification method⁸² to determine that 36.71% of its domestic products had been ordered and were ready for interstate commerce shipment to specific destinations to which the

77. See, e.g., IND. CODE § 6-1.1-10-29.3 (1988) (property must be stored in an in-state warehouse for out-of-state shipment without requiring additional manufacturing or processing); *id.* § 6-1.1-10-30(a) (property must have been shipped to Indiana and put in its original package for out-of-state shipment).

78. 528 N.E.2d 125 (Ind. T.C. 1988).

79. *Id.*

80. *Id.*

81. *Id.*

82. IND. CODE § 6-1.1-10-29.5(b) (1988) states, in part:

(b) for the purpose of substantiating the amount of his personal property which is exempt from property taxation under section 29, 29.3, 30(a), or 30(c) . . . a taxpayer shall maintain records that reflect the specific type and amount of personal property claimed to be exempt so that the taxpayer's taxable personal property may be distinguished from his exempt personal property.

products were subsequently shipped.⁸³ Finally, RCA also claimed an exemption for *domestic* products stored and remaining in original packages for the purpose of out-of-state shipment. Utilizing the allocation method⁸⁴ and its shipping experience for the preceding twelve months RCA determined that 98% of its domestic inventory was targeted for out-of-state shipment.⁸⁵ Upon an examination of RCA's return, the state tax board disallowed the exemptions claimed by RCA under Indiana Code sections 6-1.1-10-29 and 6-1.1-10-30(b) on the basis that RCA was required to elect one statutory method of exemption.⁸⁶

On RCA's appeal of the state board's decision, the state tax board argued that, "according to the language of Indiana Code section 6-1.1-10-29.5, the taxpayer must elect to use either the allocation method of Indiana Code section 6-1.1-10-29 *or* the specific identification method of Indiana Code section 6-1.1-10-30(b)"⁸⁷ and that RCA had in fact used both methods in arriving at its total exemption. The tax court, however, rejected this argument, noting that Indiana Code section 6-1.1-10-29.5 only provides a method for substantiating the taxpayer's exemption claim under Indiana Code sections 6-1.1-10-29, 30(a) or 30(c). In short, the court concluded that the election which the taxpayer makes under Indiana Code section 6-1.1-10-29.5 relates only to Indiana Code sections 6-1.1-10-29 and 6-1.1-10-30(a) and (c) and does not preclude the taking of the exemption provided by Indiana Code section 6-1.1-10-30(b).⁸⁸

Judge Fisher also rejected the state tax board's argument that RCA had violated Indiana Code section 6-1.1-10-29.5's requirement that the allocation factor be applied to the "total inventory."⁸⁹ The board clearly

83. 528 N.E.2d at 125.

84. As an alternative to the specific identification method, a taxpayer "may elect to establish the value of his exempt personal property by utilizing the allocation method." The statute sets out the formula for a determination under this method. IND. CODE § 6-1.1-10-29.5(b) (1988).

85. 528 N.E.2d at 125. In computing its exemption under Indiana Code section 6-1.1-10-29, RCA took the value of its domestic inventory, multiplied it by the 98% allocation factor, subtracted the value of the exemption it had claimed on its domestic inventory under Indiana Code section 6-1.1-10-30(b) and multiplied the remainder by 60%. The 60% multiplier represents that portion of the exemption that was phased in in 1986 pursuant to P.L. 41-1984, § 5. RCA then added all of its exemption claims together and deducted that sum from its reported inventory. 528 N.E.2d at 126.

86. *Id.*

87. *Id.* at 127 (emphasis in original).

88. *Id.*

89. According to the state board's findings:

[IND. CODE § 6-1.1-10-29.5 (1988)] prohibits *any* deductions from inventory *before* the appropriate percentages are applied under I.C. § 6-1.1-10-29. Therefore, a taxpayer cannot exempt inventory under I.C. § 6-1.1-10-30(b) and then apply

did not understand how RCA calculated its exemption claim because it asserted that RCA applied the allocation factor to its inventory after RCA deducted that portion of the domestic inventory for which an exemption was claimed under Indiana Code section 6-1.1-10-30(b). The court noted correctly that, in fact, RCA *had* complied with the law by applying the allocation factor (98%) to its total inventory and then deducting the value of the inventory it claimed to be exempted under Indiana Code section 6-1.1-10-30(b).⁹⁰

The court also dismissed the state tax board's argument that RCA was simply trying to avoid the phase-in of Indiana Code section 6-1.1-10-29. The court's rejection of this argument was based upon the simple fact that RCA had indeed applied the phase-in percentage to the inventory that it claimed as being exempt under Indiana Code section 6-1.1-10-29, all in accordance with that statute.⁹¹

In conclusion, the court found that nothing in Indiana Code sections 6-1.1-10-29, 6-1.1-10-29.5 or 6-1.1-10-30(b) prohibits contemporaneous exemptions.⁹² Noting that "[o]verlap is common among tax exemption statutes," the court found that taxpayers could qualify for more than one exemption.⁹³ Provided that RCA did not take two exemptions for the same inventory, the court held that nothing in the property tax laws prohibits it from calculating the exemptions in the manner that it did.⁹⁴

The court correctly interpreted the interstate commerce exemptions in the *RCA* case. There is no reason to preclude taxpayers from qualifying for more than one of the interstate commerce exemptions, just as taxpayers can qualify for more than one of the many other tax exemptions granted by the legislature. As long as there is no express prohibition against a single taxpayer claiming two or more exemptions and there is no "double-dipping" by taxpayers claiming the same exemption twice, there is no support for the position that the state tax board took in *RCA*. The state tax board's insistence that RCA was entitled only to the interstate commerce exemption allowed by Indiana Code section 6-1.1-10-30(a) may have been the result of its perception that the legislature intended to curtail the availability of the interstate commerce exemption granted to manufacturers and processors by Indiana Code section 6-1.1-10-29 for the first few years after it was enacted. As noted earlier,⁹⁵

I.C. § 6-1.1-10-29 to the remainder because the allocation factor is not being applied against the total inventory.

528 N.E.2d at 127.

90. *Id.* at 128.

91. *Id.*

92. *Id.* at 129.

93. *Id.*

94. *Id.*

95. *See supra* notes 48-49 and accompanying text.

when the section was added in 1984, it was regarded as a boon to manufacturers and processors, and the exemption it provided was phased in over five years in an effort, *inter alia*, to reduce the revenue impact of this new exemption. RCA took advantage of this new exemption, but then also took advantage of the other existing exemptions. While there may have been valid tax or revenue policy reasons for limiting taxpayers to only one exemption, the fact is that the exemptions were not clearly drafted that way in 1983. The *RCA* decision correctly interprets the law as it was written and enacted.

Notwithstanding the availability of the interstate commerce exemptions, the personal property tax on inventory remains a substantial and, many argue, an unfair burden on Indiana businesses. In recent years, many taxpayers have tried to reduce that burden by claiming an adjustment for abnormal obsolescence in determining the true cash value of their inventory. One such taxpayer was Don Meadows Motors, Inc. (Meadows), an automobile dealer who claimed an abnormal obsolescence adjustment for its vehicle inventory.⁹⁶ The basis for the adjustment Meadows claimed was an unforeseen change in the market value of the vehicle inventory. The state tax board denied Meadows this adjustment and Meadows appealed.⁹⁷

The tax court turned to the regulations of the state tax board⁹⁸ for direction in deciding this issue. The court first observed that the more *general* regulation addressing the issue of abnormal obsolescence provides that “[abnormal obsolescence] includes *unforeseen changes in market values*, exceptional technological obsolescence or destruction by catastrophe that has a direct effect upon the value of the personal property of the taxpayer.”⁹⁹ However, a more *specific* regulation concerning the valuation of inventory confines abnormal obsolescence to situations “where unforeseen changes in values as a result of exceptional technological obsolescence or destruction by catastrophe occur, providing that such events have a direct effect on the value of the inventory of the taxpayer.”¹⁰⁰ Although the more general regulation provides that unforeseen changes in market value may be a basis for an adjustment for abnormal obsolescence, the more specific regulation on valuing inventory does not list unforeseen changes in market value as a basis for such an adjustment.

96. *Don Meadows Motors, Inc. v. State Bd. of Tax Comm'rs*, 518 N.E.2d 507 (Ind. T.C. 1988).

97. *Id.* at 508.

98. The court primarily relied on IND. ADMIN. CODE tit. 50, r. 4.1-3-9 in its decision to remand to the state board. 518 N.E.2d at 508-09.

99. 518 N.E.2d at 508 (quoting IND. ADMIN. CODE tit. 50, r. 4.1-7-1(c) (1988)) (emphasis added).

100. 518 N.E.2d at 508 (quoting IND. ADMIN. CODE tit. 50, r. 4.1-3-9 (1988)).

The tax court applied the rules of statutory construction to these regulations and concluded that the specific regulation controlled over the general provision regarding abnormal obsolescence. Thus, the narrower definition of abnormal obsolescence—*without* changes in market value as an enumerated factor—controls the valuation of inventory.¹⁰¹

Meadows argued that the absence of the “unforeseen changes in market value” factor in Indiana Administrative Code title 50, rule 4.1-3-9 was merely an oversight or typographical error and pointed out that in other provisions of Regulation 16 dealing with abnormal obsolescence (such as Indiana Administrative Code title 50, rule 4.1-2-8 dealing with depreciable personal property), the state tax board had *included* that factor. The tax court, however, determined that this was not a situation requiring the court to exercise its power to read words into a regulation to make the regulation workable or to give it complete sense. The court’s primary reason for this conclusion was that other provisions of Indiana Administrative Code title 50, rule 4.1-3, take account of changes in market conditions in valuing inventory. The court cited the fact that taxpayers are allowed to elect to value inventory on the prior calendar year average to avoid the burden of excess inventory.¹⁰² Taxpayers are also allowed to elect to value inventory at the lower of cost or market value.¹⁰³ Both of these mechanisms give relief from the burden of excess inventory on the assessment date as a result of changes in market conditions.

In its conclusion, the court found that, although the bases of the state tax board’s denial would be relevant to an adjustment for obsolescence pursuant to Indiana Administrative Code title 50, rule 4.1-7-1, application of that section was erroneous. According to the court, the state tax board should determine an adjustment for abnormal obsolescence with respect to inventory pursuant to the requirements of Indiana Administrative Code title 50, rule 4.1-3-9, which *excludes* unforeseen changes in market values and market conditions as a criteria.¹⁰⁴

IV. “SOLICITATION” UNDER PUBLIC LAW NUMBER 86-272 REVISITED

A. *Historical Perspective*

From the late nineteenth century through the first half of the twentieth century, successful constitutional challenges under the Commerce Clause¹⁰⁵ and the Due Process Clause¹⁰⁶ of the United States Constitution

101. 518 N.E.2d at 509.

102. *Id.* (citing IND. ADMIN. CODE tit. 50, r. 4.1-3-5 (1988)).

103. 518 N.E.2d at 509 (citing IND. ADMIN. CODE tit. 50, r. 4.1-3-6 (1988)).

104. 518 N.E.2d at 509.

105. U.S. CONST. art. I, § 8, cl. 3.

106. U.S. CONST. amend. XIV, § 1.

served to prevent states from levying taxes on businesses engaging in interstate commerce where mere solicitation of orders was the sole activity in the taxing state or was dissociated from any intrastate sales.¹⁰⁷ In 1959, Justice Clark used the language that caused "concern and uncertainty"¹⁰⁸ in the commercial world and prompted Congress to act to reinforce the Commerce Clause and the Due Process Clause protections of interstate commerce by legislative fiat, thus, triggering additional protection under the Supremacy Clause.¹⁰⁹

In *Northwestern States Portland Cement Co. v. Minnesota*,¹¹⁰ Justice Clark wrote: "We conclude that net income from the interstate operations of a foreign corporation may be subjected to state taxation provided the levy is not discriminatory and is properly apportioned to local activities within the taxing state forming *sufficient nexus* to support the same."¹¹¹ The Court found a sufficient nexus to support the imposition of a Minnesota tax and a Georgia tax respectively on net income from sales in the taxing states, where the sales were shown to be "promoted by vigorous and continuous sales campaigns run through a central office located in the State."¹¹² This activity was, in Justice Clark's estimation, an affirmative answer to the "controlling question [of] whether the state has given anything for which it can ask return."¹¹³ The Court concluded that "[s]ince by 'the practical operation of [the] tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred . . .,' it 'is free to pursue its own fiscal policies, unembarrassed by the Constitution.'"¹¹⁴

The holding in *Northwestern* was consistent with long-established doctrine under the Commerce Clause and the Due Process Clause in finding that the corporate activity, which included a sales-service office in both cases, was a sufficient nexus to trigger the taxing power of the state.¹¹⁵ From a 1980's perspective and after the four-part test devised

107. See, e.g., *Norton Co. v. Illinois Dep't of Revenue*, 340 U.S. 534 (1951); *Robbins v. Taxing Dist. of Shelby County*, 120 U.S. 489 (1887).

108. S. REP. NO. 658, 86th Cong., 1st Sess., reprinted in 1959 U.S. CONG. & ADMIN. NEWS 2548-49.

109. U.S. CONST. art. VI, cl. 2.

110. 358 U.S. 450 (1959).

111. *Id.* at 452 (emphasis added).

112. *Id.* at 465.

113. *Id.* (quoting *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940)).

114. 358 U.S. at 465 (quoting *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940)).

115. The Iowa corporation that was subject to the Minnesota tax maintained in Minneapolis a three-room leased sales office equipped with its own furniture and fixtures and under the supervision of an employee-salesman known as district manager. The activities

by the court in *Complete Auto Transit, Inc. v. Brady*,¹¹⁶ the activities involved in *Northwestern*, particularly with respect to the local offices, appear to be clearly sufficient, under the Commerce Clause and the Due Process Clause, to trigger the taxing power of a state. Nevertheless, the *Northwestern* court was confronted for the first time with fact situations where the activities sought to be taxed were *exclusively* part of interstate commerce since no property was sold wholly within the state.¹¹⁷

The apprehension of the business community in the wake of *Northwestern* was that a "sufficient nexus" with the taxing state could be found in "sales within a State obtained through the mere solicitation of orders within the state by an out-of-State company having no other activities within the State."¹¹⁸ Within seven months, Congress responded to this concern by taking urgent remedial action¹¹⁹ in the form of Public Law 86-272.

Public Law 86-272 provides, in relevant part, 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

of the foreign corporation subject to the Georgia tax included maintaining a sales-service office in Atlanta which served four states, in addition to Georgia. *Id.* at 453-56.

116. 430 U.S. 274 (1977). In *Complete Auto Transit, Inc. v. Brady*, the Court's test of the constitutionality of state taxes under the Commerce Clause is as follows: (1) the taxpayer must be sufficiently connected to the taxing state to justify the tax; (2) the tax must be fairly related to benefits provided the taxpayer; (3) the tax must be fairly apportioned; and (4) the tax must not discriminate against interstate commerce. *Id.* at 287. This test has been applied to state net income taxes. *See, e.g., Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425 (1980).

117. *See* 358 U.S. at 470 (Frankfurter, J., dissenting).

118. S. REP. NO. 658, 86th Cong., 1st Sess., *reprinted in* 1959 U.S. CODE CONG. & ADMIN. NEWS 2548-49.

119. *Id.*

customer to fill orders resulting from such solicitation are orders described in paragraph (1).¹²⁰

This statute, which was enacted in the interest of national uniformity, spawned a plethora of state court decisions interpreting the word "solicitation."¹²¹

B. *Indiana's Interpretation of "Solicitation"*

The most recent Indiana decision on this issue is found in *West Publishing Co. v. Indiana Department of Revenue*¹²² which built upon a 1981 Indiana Supreme Court decision. In *West*, the Indiana Tax Court interpreted "solicitation" pursuant to the federal restriction on the state's power to tax provided in 15 U.S.C. 381-84.¹²³ The *West* decision arguably broadens the Indiana Supreme Court's interpretation of solicitation rendered in *Indiana Department of Revenue v. Kimberly-Clark Corp.*¹²⁴ and may require a re-evaluation of certain regulations promulgated by the Indiana Department of Revenue.

In *Kimberly-Clark*, the Indiana Supreme Court found that Kimberly-Clark was entitled to the federal exemption provided by Public Law 86-272 because its activities could be characterized as inextricably related to "solicitation."¹²⁵ The court determined Kimberly-Clark's "crucial activities" to be "1) conveying information to customers concerning inventory conditions or delays in shipments, 2) verifying destruction of damaged merchandise and 3) coordinating the delivery of merchandise for special promotions."¹²⁶ Based on the nature of these activities, the Indiana Supreme Court held that Kimberly-Clark's net receipts from these activities were not subject to Indiana's adjusted gross income tax.¹²⁷

The court rejected a definition of "solicitation" that would merely recite a non-exclusive list of exempt activities gleaned from fact situations presented to other state courts. Instead, the court chose to adopt the rationale of the Pennsylvania Supreme Court in *United States Tobacco*

120. Act approved September 14, 1959, Pub. L. No. 86-272, 73 Stat. 555 (codified at 15 U.S.C. § 381(a) (1982)) (emphasis added).

121. See, e.g., *Coors Porcelain Co. v. State*, 183 Colo. 325, 517 P.2d 838 (1973), cert. denied, 419 U.S. 874 (1974); *Jantzen, Inc. v. District of Columbia*, 395 A.2d 29 (D.C. 1978); *United States Tobacco Co. v. Commonwealth*, 478 Pa. 125, 386 A.2d 471, cert. denied, 439 U.S. 880 (1978).

122. 524 N.E.2d 1329 (Ind. T.C. 1988).

123. See *supra* note 120 and accompanying text.

124. 416 N.E.2d 1264 (Ind. 1981).

125. *Id.* at 1268.

126. *Id.* at 1267.

127. *Id.* at 1268.

Co. v. Commonwealth.¹²⁸ Relying on the Pennsylvania court's decision, the Indiana Supreme Court stated the rule as follows:

[E]ach case must be judged upon its own merits, with particular emphasis placed upon the totality of a corporation's activities within a state. No one or two corporate activities performed in a casual or infrequent manner should operate to remove the exemption provided by Public Law 86-272. Such activities are indicative of the extent of a corporation's activities within a state, but it is the entire operation which must be examined.¹²⁹

The Indiana court also joined the Pennsylvania court's belief that "Congress perceived 'solicitation' as 'sundry activities . . . closely related to the eventual sale of a product'"¹³⁰ and that "'acts of courtesy'" in order to accommodate a customer were not "'beyond the realm of solicitation.'"¹³¹ Finding specifically that Kimberly-Clark's activities were "inextricably related to solicitation" or "acts of courtesy," the court vacated the court of appeals' decision and affirmed the judgment of the trial court.¹³² As a result, receipts generated by the activities of Kimberly-Clark's itinerant salesmen were exempt from Indiana's adjusted gross income tax.

In *West Publishing Co. v. Indiana Department of Revenue*,¹³³ the Indiana Tax Court was confronted with a situation where a foreign corporation (West) employed sales representatives who were engaged in activities other than conveying information, verifying distribution, coordinating deliveries and other activities directly related to a sale. West's employees engaged in acceptance and forwarding of deposit checks, as well as certain collection procedures.¹³⁴ Judge Miller¹³⁵ stated the rule in this manner: "Solicitation can include a variety of activities which are related to the eventual sale, and acts of courtesy rendered to a customer to *facilitate* a sale may properly be regarded as solicitation of the sale."¹³⁶ The court found that the "arguably non-solicitous" acceptance of deposit checks was, under this definition, an aspect of solicitation and the

128. 478 Pa. 125, 386 A.2d 471, *cert. denied*, 439 U.S. 880 (1978).

129. 416 N.E.2d at 1268 (citation omitted).

130. *Id.* (quoting *United States Tobacco Co. v. Commonwealth*, 478 Pa. 125, 139, 386 A.2d 471, 478, *cert. denied*, 439 U.S. 880 (1978)).

131. 416 N.E.2d at 1268.

132. *Id.*

133. 524 N.E.2d 1329 (Ind. T.C. 1988).

134. *Id.* at 1336. However, the court also noted the fact that the sales representatives "forwarded checks to West in a *minuscule* 8.15% of the transactions." *Id.* (emphasis added).

135. Presiding Judge, 4th Dist. Court of Appeals, sitting as a Special Judge.

136. 524 N.E.2d at 1336 (emphasis added).

forwarding of the checks to West in a "minuscule" percentage of the total transactions, was a "courtesy . . . in order to facilitate sales."¹³⁷

In two instances, West's representative was arguably involved in collection procedures. Nevertheless, the court observed that "[the salesman] informed the customer that a present sale could not be approved unless the old balances were merged with the amount which would be due under the new sales contract. In these instances, his services amounted to nothing more than removing an obstacle to the sale."¹³⁸

The court also commented that the Department of Revenue was assigning great importance to infrequently performed activities in order to tax West. The court found West's activities in Indiana to be limited to "solicitation of sales" and, therefore, West was entitled to the exemption.¹³⁹

Under the *West* decision, arguably non-solicitous activities, especially if infrequent, may either be considered "facilitating," "accommodating," or "acts of courtesy" in order to bring them under the "solicitation" rubric. This expanded definition of solicitation prompts a scrutiny of the regulations of the Department of Revenue.

For non-resident persons and corporations, Indiana imposes a net income tax¹⁴⁰ upon that portion "of the adjusted gross income derived from sources within Indiana."¹⁴¹ Such income includes that which results from "doing business in a state."¹⁴² According to the Indiana Department of Revenue's regulations, a taxpayer is "doing business" in Indiana if it operates a business activity within Indiana including the following:

- (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 property (real or personal) in the state
- (6) Acceptance of orders in the state

137. *Id.*

138. *Id.*

139. *Id.* at 1337.

140. Adjusted Gross Income Tax Act of 1963, ch. 32 (Spec. Sess.), 1963 Ind. Acts (Spec. Sess.) 82 (current version at IND. CODE §§ 6-3-1-1 to -28 (1988)).

141. IND. CODE § 6-3-2-1(a) (1988).

142. *Id.* § 6-3-2-2(a)(2).

(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.¹⁴³

Although the Department's regulation allows an adjusted gross income tax to be imposed on a taxpayer "[r]endering services to customers in the state,"¹⁴⁴ the *West* decision appears to arguably narrow the scope of that subsection. It is possible, as a result of *West*, that if the services rendered can be characterized as "removing obstacles from a sale," "facilitating" "accommodating," or "acts of courtesy," especially if the services are infrequent, they are protected by Public Law 86-272 and exempt from taxation.¹⁴⁵ Such a conflict has yet to be addressed.

V. RESTRICTIONS ON CHANGES IN THE REVENUE DEPARTMENT'S INTERPRETATIONS OF TAX LAWS

Concerned about taxpayer's allegations that the Indiana Department of Revenue frequently reverses itself on its interpretations of Indiana's tax laws without any parallel change in the statutory law or regulations, the Indiana General Assembly responded with legislation precluding the effectiveness of any change in the Revenue Department's interpretation of any tax administered by the Department.¹⁴⁶ According to the recently enacted legislation, if a change in a revenue department's interpretation will increase the taxpayer's liability for that tax, such change must be adopted in a rule before it is effective. Specifically, the relevant part of the statute states:

(b) No change in the department's interpretation of a listed tax may take effect before the date the change is adopted in a rule under this section, if the change would increase a taxpayer's liability for a listed tax.¹⁴⁷

Simply stated, the Indiana Revenue Department may change its interpretation of a tax law, increasing a taxpayer's liability only if that change is prospective in operation, and the change is effectuated by the formal promulgation of a regulation.

Since 1977, Indiana has had a law similar to Indiana Code section 6-8.1-3-3 that dealt only with interpretations of the gross income tax

143. IND. ADMIN. CODE tit. 45, r. 3.1-1-38 (1988) (emphasis added).

144. *Id.* tit. 45, r. 3.1-1-38(4).

145. See *West Publishing Co. v. Indiana Dep't of Revenue*, 524 N.E.2d 1329 (Ind. T.C. 1988); *Indiana Dep't of Revenue v. Kimberly-Clark Corp.*, 416 N.E.2d 1264 (Ind. 1981).

146. Act approved April 27, 1987, Pub. L. No. 105, 1987 Ind. Acts 1613 (codified at IND. CODE § 6-8.1-3-3(b) (1988)).

147. IND. CODE § 6-8.1-3-3(b) (1988).

act,¹⁴⁸ and it has proven to be very beneficial to taxpayers. The expansion of this statutory restraint on the Department should result in increased fairness and consistency in the administration and collection from year to year of all types of Indiana taxes.

It is important to note that Indiana Code section 6-8.1-3-3 is *not* simply a codification of the concept of legislative acquiescence, such being that "a long adhered to administrative interpretation dating from the legislative enactment, with no subsequent change having been made in the statute involved, raises a presumption of legislative acquiescence which is strongly persuasive upon the courts."¹⁴⁹ Significantly, this statute is instead a legislative prohibition against any retroactive changes in departmental interpretations, no matter how long standing, that will increase a taxpayer's liability. Furthermore, there is no requirement or limitation in this new law that the interpretation the Department seeks to change already be in regulation form. It is, therefore, believed that this prohibition was intended to and does cover informal administrative interpretations, as well. Thus, Indiana taxpayers should be encouraged to preserve and maintain copies of old audit reports, correspondence with the Revenue Department, and other similar documentation because these could provide a basis in the future for establishing what the Revenue Department's administrative interpretation has been. If an interpretation results in an increase in the taxpayer's liability, this type of documentation will support the taxpayer's argument that such interpretation was imposed contrary to the statutorily mandated means.

VI. THE TAX COURT'S JURISDICTION OVER INHERITANCE TAX MATTERS

In *Blood v. Poindexter*,¹⁵⁰ the Indiana Tax Court found that its exclusive jurisdiction over final determinations of the Indiana Department of Revenue includes certain determinations by the Department regarding the inheritance tax liability of the estates of non-resident decedents, previously within the jurisdiction of the county probate courts.¹⁵¹ In this case, the taxpayer argued that no final determination had been made by the Department, therefore, Indiana Code section 6-4.1-7-5 applied and provided for an appeal in the county probate court.¹⁵² The De-

148. Act approved April 29, 1981, Pub. L. No. 77, 1981 Ind. Acts 914 (codified at IND. CODE § 6-2.1-8-3 (1988)).

149. *Baker v. Compton*, 247 Ind. 39, 42, 211 N.E.2d 162, 164 (1965).

150. 524 N.E.2d 824 (Ind. T.C. 1988).

151. *Id.* at 825.

152. *Id.* at 824. That statute provides, in part:

(a) a person who is dissatisfied with an inheritance tax determination or an appraisal . . . may appeal the department's decision to:

(1) the probate court . . .

IND. CODE § 6-4.1-7-5(a) (1988).

partment asserted, and the tax court agreed, that a final determination had occurred, and an appeal was governed by Indiana Code section 33-3-5-2, which vested exclusive jurisdiction in the Indiana Tax Court.¹⁵³ In order to reach this conclusion, the tax court had to find that Indiana Code section 6-4.1-7-5 "was repealed by implication . . . [because] [i]t is not possible to give effect to the jurisdiction provisions of both . . . and still give effect to the intent of the Legislature in creating [the tax court]."¹⁵⁴ The *Blood* decision, which essentially restates the reasoning of the tax court in the 1987 *Herff Jones* decision,¹⁵⁵ evinces once again the tax court's determination that it—not ninety-two different county courts—should be the tribunal of first resort on all Indiana tax matters.

Under the inheritance tax laws, an inheritance tax is imposed upon certain property interests transferred by the decedent at the time of the decedent's death.¹⁵⁶ The statutory procedures and the authority responsible for determining the amount of inheritance tax liability vary depending on the Indiana residence status of the decedent. The personal representative of the resident decedent, with certain exceptions, must file an inheritance tax return with the probate court.¹⁵⁷ The personal representative of the non-resident decedent must file an inheritance tax return with the department.¹⁵⁸

The determination of the net taxable value of the property interests transferred by a resident or non-resident decedent is made according to a statutory procedure.¹⁵⁹ In the case of a resident decedent, the county inheritance tax appraiser submits an appraisal report to the probate court,¹⁶⁰ and, after notice and hearing, the probate court determines the fair market value of the property transferred and the amount of inheritance tax due and enters an order stating the amount of the tax due.¹⁶¹ In the case of a non-resident decedent, the Department determines

153. 524 N.E.2d at 824. The statute cited by the Department states, in relevant part:

(a) The tax court . . . has exclusive jurisdiction over any case that arises under the tax laws of this state and that is an initial appeal of a final determination made by:

(1) the department of state revenue; or
 (2) the state board of tax commissioners.

IND. CODE § 33-3-5-2(a) (1988).

154. 524 N.E.2d at 825.

155. *Herff Jones, Inc. v. State Bd. of Tax Comm'rs*, 512 N.E.2d 485 (Ind. T.C. 1987).

156. IND. CODE §§ 6-4.1-2-1 to -4 (1988).

157. *Id.* § 6-4.1-4-1.

158. *Id.* § 6-4.1-4-7.

159. *Id.* § 6-4.1-5-1.

160. *Id.* § 6-4.1-5-6.

161. *Id.* § 6-4.1-5-10.

the fair market value of the property transferred and the amount of inheritance tax due and enters an order stating the amount of tax due.¹⁶²

A person who is dissatisfied with an inheritance tax determination made by a probate court with respect to a resident decedent's estate may obtain a rehearing, a reappraisal and a redetermination of inheritance tax by petitioning the *probate court*.¹⁶³ A person who is dissatisfied with an inheritance tax determination or an appraisal made by the Department with respect to a property interest transferred by a non-resident decedent may also appeal to the *probate court*. The inheritance tax laws specifically provide that when such an appeal is initiated, with respect to a non-resident decedent, "[t]he [probate] court may decide all questions concerning the fair market value of property interests transferred by the decedent or concerning the inheritance tax due as a result of the decedent's death."¹⁶⁴

Blood's decedent was a non-resident, thus the authority to enter the initial order stating the fair market value of the property and the inheritance tax due was vested in the Department.¹⁶⁵ Blood was dissatisfied with the appraisal and the inheritance tax determination made by the Department, so he appealed the determination to the Gibson Circuit Court, the probate court in that county. The Department promptly filed a motion to dismiss in the Gibson Circuit Court and a pleading in the tax court entitled "Motion for the Court to Exert its Exclusive Jurisdiction in this Cause."¹⁶⁶ The basis of the Department's motion was Indiana Code section 33-3-5-2, which states as follows: "The tax court has exclusive jurisdiction over any case that arises under the tax laws of this state and that is an initial appeal of a final determination made by: (1) the department of state revenue."¹⁶⁷

Blood filed a Motion to Strike the Department's Motion to Dismiss on the grounds that the department's motion was insufficient as a matter of law. Concurrently, Blood filed a Motion to Strike the Department's motion in the tax court on the grounds that the motion was "impertinent and immaterial."¹⁶⁸

In its resolution of this controversy, the tax court first recited a principle that it had previously announced in the *Herff Jones* case, namely, that "one of the reasons for the creation of [the Tax] court was to prevent ninety-two different interpretations of a panoply of tax

162. *Id.* § 6-4.1-5-15.

163. *Id.* §§ 6-4.1-7-1 to -4.

164. *Id.* § 6-4.1-7-5(c).

165. *Id.* § 6-4.1-5-15.

166. 524 N.E.2d 824 (Ind. T.C. 1988).

167. IND. CODE § 33-3-5-2(a) (1988).

168. 524 N.E.2d at 824.

issues.”¹⁶⁹ The court then observed that it was impossible to give effect to Indiana Code sections 6-4.1-7-5 and 33-3-5-2 *and* achieve this legislative objective. Relying upon the basic rule of statutory construction that if two statutes are repugnant, then the later of the two controls, the tax court ruled that Indiana Code section 33-3-5-2 repealed Indiana Code section 6-4.1-7-5.¹⁷⁰

Blood had also argued that the Department’s order was not a “final determination,” and since the statute provided that the tax court shall have exclusive jurisdiction only over appeals from final determinations of the Department, the tax court was without jurisdiction over this matter. In response, the tax court observed that the Department itself had called its appraisal an order and a determination. Furthermore, according to the tax court, the appraisal was “the final step in the administrative process before resort may be had to the judiciary, and is, thus, a final determination.”¹⁷¹

Finally, in response to Blood’s contention that the tax court was without statutory authority to hear its appeal *de novo*, thereby denying Blood the due process right to present evidence and witnesses, the tax court found that in such appeals under Indiana Code section 6-4.1 (Death Taxes), it could hear and consider all admissible evidence in a *de novo* proceeding. Judge Fisher wrote:

Blood also contends that because I.C. 33-3-5-1 refers to this Court as an “appellate court,” the standard of review is limited to a review of the Department’s action for abuse of discretion, etc. This is not the law. This Court, as did the court having probate jurisdiction prior to July 1, 1986, may hear the case *de novo*. It may hear all admissible evidence presented to it for the first time in the judicial proceeding. This type of review affords due process.¹⁷²

Unfortunately, the *Blood* decision creates an asymmetry in the inheritance tax laws, both procedurally and substantively. Under *Blood*, the county probate courts have lost their jurisdiction to determine the value of a non-resident decedent’s estate for inheritance tax purposes, while they retain their jurisdiction to determine the value of a resident decedent’s estate for inheritance tax purposes. Indiana inheritance tax valuation issues will thus be decided by two entirely different judicial forums, the ninety-two county probate courts *and* the Indiana Tax Court,

169. *Id.* (citing *Herff Jones, Inc. v. State Bd. of Tax Comm’rs*, 512 N.E.2d 485, 491 (Ind. T.C. 1987)).

170. 524 N.E.2d at 825.

171. *Id.*

172. *Id.* (citation omitted).

dependent solely upon the residence of the decedent. Needless to say, this asymmetry has created a great deal of confusion among inheritance tax practitioners, many of whom urge that it be resolved by the legislature. There seems to be no policy reason to vest two different courts with the jurisdiction to hear the same matters. The eventual results will only be inconsistencies in determinations and confusion about the proper procedures to follow. Indiana needs a simple, uniform approach to inheritance tax matters, and, while that was the tax court's objective in the *Blood* decision, it is clear that the court cannot achieve that objective alone. The legislature must be urged to examine the inheritance laws and work to achieve that objective as well.

