FLORIDA
DEPARTMENT OF REVENUE
Executive Director
Marshall Stranburg

QUESTION: Whether the sales revenue generated from the Buy and Watch segments constitute Florida gross receipts for purposes of the sales factor.

ANSWER: The income producing activity occurs in Florida, since Florida is where the transactions and activities from Taxpayer's sales occur. The sales revenue generated by the Taxpayer in its Buy and Watch segment activities constitutes a Florida gross receipt and must be sourced to Florida when the location of the data collection service is performed in Florida.

November 21, 2013

XXX
XXX
XXX

Re: Technical Assistance Advisement 13C1-011
Taxpayer: XXX
FEIN:XXX
Corporate Income Tax
Sales Factor
Section ("s.") 220.15, Florida Statutes (F.S.)
Rule 12C-1.0155, Florida Administrative Code (F.A.C.)

Dear XXX:

This is in response to your request dated XXX, for a Technical Assistance Advisement ("TAA") pursuant to s. 213.22, F.S., and Rule Chapter 12-11, F.A.C., regarding the gross receipts calculation for Taxpayer. An examination of your letter has established that you have complied with the statutory and regulatory requirements for issuance of a TAA. Therefore, the Department is hereby granting your request for a TAA.

FACTS SUPPLIED BY TAXPAYER

Your letter states, in part:

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The Taxpayer is a XXX XXX and XXX XXX company that provides its customers with an understanding of XXX and XXX. The Taxpayer enters into contracts with various customers to provide XXX information, XXX regarding XXX, and XXX viewing choices on a XXX. The Taxpayer's revenue is generated through multiple XXX, the principal two of which are (1) XXX and XXX ("Buy"), and (2) XXX ("Watch").

The Buy segment provides XXX data, XXX information, and analytics. This segment collects XXX data via XXX used by unrelated third-party individuals. These individuals are located around the country and use the XXX to record the XXX during their XXX. Through the information obtained by the XXX, the Taxpayer is able to XXX in XXX, which is used by customers to XXX and XXX. Buy segment services are provided primarily to businesses in the XXX.

The Watch segment provides XXX data and analytics primarily to the XXX and XXX across XXX, XXX and XXX. Watch data is used by XXX to understand their XXX, establish the value of XXX, and maximize the value of their content. The Watch segment collects data through the Taxpayer's XXX, which are placed in XXX. These XXX automatically XXX based upon the XXX to which the XXX. Like the Buy segment, the Watch segment collects data and information from XXX throughout the XXX.

The raw data and information the Taxpayer gathers from the XXX and XXX in both segments is transmitted and stored at its data centers across the country, including locations in XXX, XXX, and XXX The Taxpayer formats the data and puts it in a readable report/layout on its servers. Customers located throughout the United States can access this information anytime, from any location, via XXX and XXX provided by the Taxpayer. Each contract in the business segment represents an item of income. Depending on the requirements of a particular contract, the income producing activity may be in any given state.

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ISSUE

The issue is whether the sales revenue generated from the Buy and Watch segments constitute Florida gross receipts for purposes of the sales factor.

LAW

Section 220.15, F.S., states, in part:

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

(a) As used in this subsection, the term "sales" means all gross receipts of the taxpayer except interest, dividends, rents, royalties, and gross receipts from the sale, exchange, maturity, redemption, or other disposition of securities….

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

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

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(h) Sales of services. In the case of a taxpayer engaged in providing services, such as the operation of an advertising agency, the performance of equipment service contracts, or research and development contracts, "sales" includes the gross receipts from the performance of such services including fees, commissions, and similar items.

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(2) Florida sales. The numerator of the sales factor shall include gross receipts attributed to this state which were derived by the taxpayer from transactions and activities in the regular course of its trade or business. All interest income, service charges, carrying charges, or time-price differential charges incident to such gross receipts shall be included regardless of the place where the account records are maintained or the location of the contract or other evidence of indebtedness..

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(h) Computer related sales.

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5. Interactive networks.
a. Where there are charges to Florida customers for direct access to a data base, these charges are considered Florida sales….

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(*l*) Other Sales in Florida. Gross receipts from other sales shall be attributed to this state if the income producing activity which gave rise to the receipts is performed wholly within this state. Also, gross receipts shall be attributed to this state if the income producing activity is performed within and without this state but the greater proportion of the income producing activity is performed in this state, based on costs of performance. The term “income producing activity” applies to each separate item of income and means the transactions and activity directly engaged in by the taxpayer for the ultimate purpose of obtaining gains or profits. Where independent contractors are used to complete a contract, the term “income producing activity” will include amounts paid to the independent contractors.

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ANALYSIS

Section 220.02(1), F.S., provides that it is the intent of the Florida Legislature to impose a corporate income tax on every taxpayer in each taxable year for the privilege of conducting business, deriving income, or being incorporated in this state. Section 220.15(5), F.S., defines the sales factor as "a fraction, the numerator of which is the total sales of the taxpayer in this state during the taxable year or period and the denominator of which is the total sales of the taxpayer everywhere during the taxable year or period." Rule 12C-1.0155, F.A.C., describes how the receipts from several types of sales activities are computed, and then provides information on the computation of the Florida portion of those receipts. Rule 12C-1.0155(2), F.A.C., provides that "the numerator of the sales factor shall include gross receipts attributed to [Florida] which were derived by a taxpayer from transactions and activities in the regular course of its trade or business." In this case, the Taxpayer's activities do not constitute the sale of tangible personal property. Therefore, the discussion below will focus on the sourcing of sales other than tangible personal property, namely the sale of services.

The only Rule which is applicable to the sale of services is Rule 12C-1.0155(2)(*l*), F.A.C. Pursuant to Rule 12C-1.0155(2)(*l*), F.A.C., sales are attributed to Florida "if the income producing activity which gave rise to the receipts is performed wholly within [Florida]. "Income producing activity" is defined in Rule 12C-1.0155(2)(*l*), F.A.C., as "the transactions and activity directly engaged in by the taxpayer for the ultimate purpose of obtaining gains or profits." If the income producing activity is not wholly performed within Florida, it is necessary to conduct a cost of performance analysis. See Rule 12C-1.0155(2)(*l*), F.A.C.

The following two cases illustrate Florida's position on the interpretation of Rule 12C-1.0155(2)(*l*), F.A.C. In Heller Western v. Arizona Department of Revenue[1], Heller Western[2] borrowed money from its Illinois parent in order to lend money to Arizona businesses. Any loan over one million dollars had to be approved by its parent in Illinois and its headquarters in California. The California office also monitored the progress of loans made in Arizona and paid the interest expense on the loans from the parent company to Heller Western in Arizona. Prior to 1978, Heller Western sourced the interest earned from loans to Arizona customers[3] to Arizona. After 1978, Heller Western sourced the interest earned from loans to Arizona customers outside Arizona. Heller Western argued that pursuant to A.C.A.R.R. R15-2-135-8(b)(5)(j)(1978) (an Arizona rule similar to Rule 12C-1.0155(2)(*l*), F.A.C.), borrowing money from its parent was part of its income producing activity in Arizona, and that since more than fifty percent of the costs associated with the borrowing occurred outside of Arizona, the income earned from lending money in Arizona should not be sourced to Arizona. The Arizona Department of Revenue ("Arizona") disagreed and argued that the interest earned from loans to Arizona consumers should be sourced to Arizona because "only the activities of the Arizona branch office immediately resulted in generating income from the Arizona loans. Thus only those activities qualify as 'income producing activity.'"[4]

[1] 161 Ariz. 49 (Ariz. Sup. Ct. 1989)
[2] Heller Western is a branch of a California corporation. The California corporation is a subsidiary of a corporation domiciled in Illinois.
[3] Customer is used interchangeably with consumer.
[4] Id. at 52.

The Arizona Supreme Court ruled in favor of Arizona and stated, "[w]e believe that the term, 'income producing activity,' in our regulation contemplates only direct sales payment activity by the consumer, which in this case occurred in Arizona."[5] This position was further elaborated by the Court:

. . . Further, those activities are uniformly local to the situs of the *consumer*…. For example, payments for interstate transportation of freight are allocated to the state where the freight is delivered, not purchased, because that is where the consumer is. However, payments for interstate transportation of people on a common carrier are allocated to the state where the ticket is purchased, not the traveler's destination, again because that is where the consumer is. Finally, payments resulting from business generated by interstate telephone calls are allocated to the state where the customer placed or received the call; whether the seller called the consumer or the consumer called the seller, it is the consumer's situs that is determinative. . . [6]

The Court states that sourcing sales made to Arizona consumers to Arizona was a "logical conclusion."[7] The Court compares the interest earned from loans to a retailer selling goods and states:

Heller Western can no more argue that its receipts from Arizona loan consumers should not be taxed due to its out-of-state involvement in procuring its 'inventory' than a retailer who is engaged in extensive dealings out of state to buy his merchandise could argue that he should not be taxed on the goods he sells to consumers here.[8]

The Arizona Supreme Court held that based on the "consumer location orientation…'income producing activity' contemplates direct solicitation, negotiation, and sales activities with consumers in this state."[9] As a result, all sales were sourced to Arizona, regardless of where most of the costs of performance occurred.

In Ameritech Publishing, Inc. v. Wisconsin Department of Revenue[10], Ameritech was in the business of selling advertising for placement in telephone directories. The advertising services at issue were sold entirely within Wisconsin. However, the vast majority of the costs of performance of the advertising services occurred outside Wisconsin. The final product, a telephone book containing the advertisements, was delivered to Wisconsin via common carrier. Ameritech initially sourced the sales of these services to Wisconsin. However, it later filed amended returns seeking refunds arguing that the sale of its services should not be sourced to Wisconsin pursuant to WIS. STAT. s. 71.25(9)(d) (1999) similar to Rule 12C-1.0155(2)(*l*), F.A.C. because the majority of the costs of performance

[5] Id.
[6] Id.
[7] Id. at 53.
[8] Id.
[9] Id.
[10] No. 2009AP445 (App. Ct. IV 2009), 788 N.W.2d 383 (Wis. Ct. App. 2010)

occurred outside Wisconsin, and the telephone books were delivered to Wisconsin via common carrier.

The Wisconsin Department of Revenue ("Wisconsin") disagreed and argued that Ameritech's income producing activity occurred within Wisconsin for several reasons. First, Wisconsin argued that Ameritech had significant sales for the four years at issue and if Ameritech's argument was accepted, Ameritech would pay no tax in one of the years and receive a refund of two million dollars for two of the years. Second, Wisconsin argued that Ameritech's position was unreasonable because large amounts of the income producing activity would not be sourced to Wisconsin, where the advertising occurred. Wisconsin also argued that the Tax Appeals Commission's finding that Ameritech's income producing activity was "furnishing its customers access to a Wisconsin audience was reasonable…."[11] Finally, Wisconsin argued that Ameritech's position that solicitation and ad production were the income producing activities was "belied by the fact that these activities were not specified in the contract," and that not all of its customers used these services.[12]

The Wisconsin Court of Appeals ruled in favor of Wisconsin and upheld the Tax Appeals Commission's finding that the:

. . .'[I]ncome-producing activity' associated with [Ameritech]'s service from 1994 to 1997 was, at bottom, the provision of access to a Wisconsin audience. Advertisers paid [Ameritech] to reach Wisconsin consumers through this familiar and well-established advertising medium. It is undisputed that, in the course of providing this service, [Ameritech] employees working in offices outside of Wisconsin executed tasks related to the sale and production of the ads. But [Ameritech]'s customers did not pay primarily for [Ameritech] to service their accounts, design their advertisements, or send their ad copy with the completed directory to the printer. They paid for the broad access [Ameritech] could provide to a Wisconsin audience.[13]

The Wisconsin Court of Appeals also agreed that the income producing activity occurred in Wisconsin, not in the other states in which a majority of the costs of performance occurred and stated:

Moreover, the Commission reasonably concluded that this service of providing access to Wisconsin consumers is income-producing activity performed within the state of Wisconsin under WIS. STAT. § 71.25(9)(d). During the relevant period, API acted as a gatekeeper for its advertisers to the Wisconsin market; API's customers paid a monthly toll to reach that market via a venerable advertising medium. API's income was dependent primarily upon its status as a telephone directory publisher, and its ability to offer advertisers access to a pool of local consumers (Wisconsin consumers in this case) through this medium. Thus, regardless which state API's sales persons and advertising production staff was located, API's primary service of providing access to a Wisconsin audience was performed in the state of Wisconsin.[14]

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[11] Id. at ¶ 30
[12] Id.
[13] Id. at ¶34.
[14] Id. at ¶35.

The Wisconsin Court of Appeal stated that the Tax Appeals Commission reasonably relied on The Hearst Corporation v. DOR[15] in order to determine the income producing activity. In Hearst, WISN-TV was a television broadcaster located in Wisconsin. WISN-TV generated revenue from local and national advertisements. The administration of the local advertisements occurred within Wisconsin, while the administration of the national advertisements occurred outside Wisconsin. WISN-TV argued that the income producing activity in regards to national advertisement was performed outside Wisconsin since all the costs of performance occurred outside Wisconsin. The Tax Appeals Commission in Hearst ruled that the income producing activity was the broadcasting of the national advertisement in Wisconsin, despite the fact that the costs of performance of the advertisement occurred outside Wisconsin. The Tax Appeals Commission reasoned that:"[T]he network and national advertising revenues are based upon the showing or broadcasting thereof. Without broadcasting there is no income." The Tax Appeals Commission further found that "advertisers choose spots based upon the demographic profile of the audience viewing the particular programming during which the spots occur or are available, and that the advertisers are buying the spots due to the programming and its demographic makeup."

In its findings of fact, the Tax Appeals Commission concluded "the income producing activity is the actual broadcasting of the programming desired by the advertiser and the commercial spots during that programming and, thus, is in Wisconsin."[16]

In both Heller Western and Ameritech, the majority of the taxpayer's costs of performance occurred outside the state in which their customers resided and where the income producing activity actually occurred. The taxpayers in both cases argued that sales should be sourced to the state in which the majority of the costs of performance occurred instead of where the customer was located and where the income producing activity occurred. However, the courts in the two cases held that the income producing activities were the actual sale of services to its customers, as opposed to the costs of performing those services. The courts in both cases sourced the taxpayer's gross receipts from the sale of services to the market state, the state in which the customer resided, reasoning that the direct sale to the customer at the customer's domicile is where the income producing activity occurred. In analyzing the income producing activity, the most important factor to determine is where the customer is located.

The background of the adoption of the sales apportionment factor for the Florida corporate income tax is also helpful for this analysis. When the adoption of the corporate income tax was being debated by the Florida legislature in 1971, there were two options available to measure the receipts for the sales apportionment factor: the pure destination test, also known as the market state test, or the combined destination and origin test.[17] The pure destination test sources the goods sold to the market state or the state where the goods are consumed. The combined destination and origin test assign the sales to the state from which the goods were shipped if the taxpayer was not doing business in the state of the purchase or if the purchaser was the federal government.

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[15] Wis. Tax Rptr(CCH) ¶203-149 (WTAC 1990)
[16] Id. at ¶18.
[17] England, Arthur. Corporate Income Taxation in Florida: Background, Scope, and Analysis. 1972. p.14–15. Print.

The Florida legislature adopted the pure destination test and assigned fifty percent of the apportionment factor to the sales factor.[18] Florida deviated from assigning the three apportionment factors equally because Florida is a consumer state, and foreign corporations that do not relocate personnel and property to Florida, would be taxed at a higher rate than local corporations that have significant payroll and property factors assigned to Florida.[19] When analyzing each portion of the receipts, a determination must be made as to the final destination of the product or service being sold.

Numerous sourcing rules in Florida source sales based on the situs of the consumer. For example, Rule 12C-1.0155(2), F.A.C., states that "[a]ll interest income, service charges, carrying charges, or time-price differential charges incident to such gross receipts shall be included regardless of the place where the account records are maintained or the location of the contract or other evidence of indebtedness." Tangible personal property is sourced to Florida if the property is delivered or shipped to Florida.[20] Intangible personal property is sourced to Florida if it is located and used in this state.[21] In Florida, the sourcing of gross receipts depends on the location of the consumer.

The interpretation of Rule 12C-1.0155(2)(*l*), F.A.C., has been difficult in almost all states adopting the rule. Walter Hellerstein, a state corporate income tax expert, has made the following observation in his legal treatise which supports Florida's interpretation of Rule 12C-1.0155(2)(*l*), F.A.C.:

There is, however, a more fundamental objection to UDITPA's costs-of-performance rule for attributing receipts from services—whether applied on an all-or-nothing basis or on a percentage-attribution basis, as some states do —namely, that the rule often fails to serve the purpose of the sales factor to reflect the contribution of the market state to the taxpayer's income. While services may often be performed in the same state in which they are consumed, this is not always the case, especially with regard to services such as advertising, consulting, and other professional services that may be performed in one state but effectively "delivered" in all of the states in which the service provider's customers carry on their activities. Accordingly, as a matter of policy, states adopting a market-oriented approach for service providers have embraced a much sounder solution to the problem of attributing the receipts of service providers than those states that rely either on UDITPA's costs-of-performance methodology or on the traditional rule of assigning services to the state in which they are performed.[22]

Rule 12C-1.0155(2)(*l*), F.A.C., is applicable in this case. The Rule requires that the income producing activity first be identified. If the income producing activity occurs wholly within Florida, the sale is then sourced to Florida. The income producing activity in the present case is fees earned by the Taxpayer from transaction services provided to its customers, including customers located in Florida. The income producing activity is not analyzed holistically as one major activity, but each

[18] Id. at 15.
[19] Id.
[20] Rule 12C-1.0155(2)(a), F.A.C.
[21] Rule 12C-1.0155(2)(f), F.A.C.
[22] Hellerstein & Hellerstein: State Taxation (WG&L), ¶9.18[3][a], (2012).

individual transaction is considered a separate transaction and consequently a separate income producing activity.

The term "income producing activity" is defined as "the transaction *and* activity directly engaged in by the taxpayer for the ultimate purpose of obtaining gains or profits."[23] The word "and" signifies that both transactions and activities must exist simultaneously in order for any activity to be considered the income producing activity. The word "transaction" is used several times in the Florida Statutes and Rules, but is not defined. Black's Law Dictionary[24] defines "transaction as:
1. The act or an instance of conducting business or other dealings.
2. Something performed or carried out; a business agreement or exchange.
3. Any activity involving two or more persons.

The income producing activity in the present case occurs wholly within Florida if the Taxpayer's customer is located in Florida. Such a result is consistent with Ameritech, Heller Western, Florida's legislative history, and Hellerstein's analysis. The collection of data is not the income producing activity because there is no transaction involved, as defined above. The transaction occurs when the Taxpayer sells the final service to its customer and receives compensation for the service in return. When determining what the income producing activity is, Rule 12C-1.0155(2)(*l*), F.A.C., requires that each individual transaction, not the entire business line, be analyzed.

Furthermore, Rule 12C-1.0155(2)(h)5.a., F.A.C., provides that "[w]here there are charges to Florida customers for direct access to a date base, these charges are considered Florida sales." Since the customers access the data through a data base, the sales can be sourced to Florida based on Rule 12C-1.0155(2)(h)5.a., F.A.C.

CONCLUSION

The income producing activity for the Buy and Watch segments occurs in Florida if Taxpayer's customer is located in Florida and Florida is where the transactions and activities occur. Also, charges to Florida customers for direct access to a data base are considered Florida sales. Such sales must be included in the numerator of the sales factor.

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

You are further advised that this response, your request and related documents are public records under Chapter 119, F.S., which are subject to disclosure to the public under the conditions of s.

[23] Rule 12C-1.0155(2)(*l*), F.A.C.
[24] 716 (2nd Pocket Edition 2001)

213.22, F.S. Your name, address, and any other details, which might lead to identification of the taxpayer, must be deleted before disclosure. In an effort to protect the confidentiality of such information, we request you provide the undersigned with an edited copy of your request for Technical Assistance Advisement, backup material and response within fifteen days of the date of this advisement.

Sincerely,

Affan Qureshi, Esq.
Senior Attorney
Technical Assistance and Dispute Resolution
(850)717-7602
ID #146303