



State of Alabama Department of Revenue

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ALABAMA DEPARTMENT OF REVENUE REVENUE RULING 96-004

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§40-2A-5(a) (1993 Replacement Volume).

TO:

FROM: Commissioner of Revenue
Alabama Department of Revenue

DATE: September 19, 1996

RE: Revenue Ruling 96-004

FACTS

The facts, as you have presented them to the Department, are as follows:

1) The parent corporation ("Parent"), located in London, the indirect parent company of Taxpayer, will purchase raw materials, and store the materials at Taxpayer's Alabama plant site.

2) Parent will retain title to the raw materials at the Alabama site.

3) Taxpayer will be paid an arm's length fee by Parent to toll manufacture an intermediate product, (using the raw materials), to specification at the Alabama plant.

4) The fee received by Taxpayer will be included in Alabama apportionable income, and also, in the numerator and denominator of the receipts factor of the apportionment percentage for Alabama corporate franchise tax and corporate income tax.

5) The toll manufactured intermediate product will be shipped to Parent's manufacturing facility in the United Kingdom for further processing into a finished product.

6) Parent has no employees in Alabama and has no income

from Alabama sources. Its only connection to Alabama is the temporary presence of its raw materials in Alabama for contract processing by the Taxpayer. Parent has no other property located in Alabama, permanently or temporarily.

7) The activities of Parent do not cause it to be engaged in a U.S. trade or business through a U.S. permanent establishment for U.S. federal income tax purposes by virtue of the double taxation treaty between the United States and the United Kingdom and, accordingly, Parent is not subject to U.S. federal income tax on account of these activities.

The following facts were not stated in the ruling request, but were represented subsequently to the Department by Taxpayer:

8) Parent is a United Kingdom corporation engaged in the pharmaceutical business.

9) Parent will bring its raw materials, which are agricultural chemical products, to Taxpayer's Alabama plant for further processing by Taxpayer.

10) "Toll" manufacturing means that Parent will pay a fee to Taxpayer for the processing performed by Taxpayer.

11) Once Taxpayer performs its processing upon the materials of Parent, these materials will be taken to the United Kingdom for further processing.

ISSUE

Whether or not Parent will be subject to Alabama's corporate income tax or Alabama's foreign corporation franchise tax?

ANALYSIS

Section 40-18-31, Code of Alabama 1975, levies and imposes a tax upon the net income of "every foreign corporation doing business in" Alabama. Likewise, §40-14-41(a), Code of Alabama 1975 (1995 Cum. Supp.), provides that "[e]very corporation organized under the laws of any other state, nation, or territory and doing business in this state . . . shall pay . . . an annual franchise tax . . . [based on] the actual amount of its capital employed in" Alabama.

The threshold question is whether or not Parent will be "doing business" in Alabama.

Although the phrase "doing business" has not been defined in

Alabama's tax statutes, that phrase has been interpreted by Alabama's appellate courts on several occasions. In J. R. Watkins Co. v. Hamilton, 26 So.2d 207, 210 (Court of Appeals of Alabama 1946), the court stated the following as to the meaning of the phrase "doing business":

What acts constitute "doing business" in this State by a foreign corporation cannot be judicially defined with precision. The question must be determined by the facts of each particular case. It is clear under our decisions however that before the acts done by the foreign corporation in this State can be said to fall within the purview of our constitutional and statutory provisions, such acts performed in this State must be in the exercise of some of the functions for which the corporation was organized, that is, in the transaction of the real or chief business of the corporation rather than the performance of acts merely within the corporate powers.

. . .

In the Friedlander Bros v. Deal case, supra, our Supreme Court held that where a non qualified foreign mercantile corporation, organized and chartered to do a merchandising business, and authorized to buy, lease or hold real estate suitable to the purposes of the corporation, leased a storehouse in this State for its intended use in its future business in this State, that such act on the part of the corporation did not amount to a transaction of business by the corporation within this State, but was merely an incidental preliminary step to the doing of the real business of the corporation.

Also, the Alabama Supreme Court refused to uphold a franchise tax assessment against a company which owned real estate in Alabama and collected rent therefrom. State v. City Stores Company, 171 So.2d 121 (Ala. 1965). The Court cited the Friedlander case for the proposition that Alabama's foreign corporation franchise tax (which is levied upon foreign corporations "doing business" in Alabama) does not apply to acts which merely are incidental to the exercise of the corporation's ordinary business. City Stores. The Supreme Court in City Stores held that the ownership, management, and collecting of rent was incidental to the company's main business and did not rise to the level of employing capital in Alabama. Id.

Finally, in Omega Minerals, Inc. v. State, 288 So.2d 145 (Ala. Civ. App. 1973), the state attempted to impose franchise tax against Omega Minerals, Inc., as a foreign corporation "doing business in Alabama." Trial testimony showed that Omega's only

activity within Alabama had been the ownership of certain land and mineral rights. Testimony further revealed that the business of Omega was the exploration of minerals. In holding that Omega was not "doing business in Alabama," the Court of Civil Appeals stated that the ownership of the land and mineral rights by Omega was merely incidental to Omega's primary purpose of exploring for minerals.

Based on the representation of facts made to the Department by Taxpayer, Parent will not be "doing business" in Alabama for corporate income or franchise tax purposes. It also is important to note that Parent will derive no income from its property located in this state. See §40-18-2(3).

CONCLUSION

Based on the foregoing, Parent will not be subject to Alabama's corporate income tax or Alabama's foreign corporation franchise tax.

H. E. "Gene" Monroe, Jr.
Commissioner, Alabama Department of Revenue

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