STATE OF ALABAMA DEPARTMENT OF REVENUE,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
v.	§	DOCKET NO. F. 93-183
PRATTVILLE MANUFACTURING, INC. c/o Frank R. DeLuca Price Waterhouse 50 Hurt Plaza, Suite 1700 Atlanta, GA 30303,	§	
Taxpayer.	§	

OPINION AND PRELIMINARY ORDER

The Revenue Department assessed franchise tax against Prattville Manufacturing, Inc. (Taxpayer) for the years 1988 through 1992. The Taxpayer appealed to the Administrative Law Division and a hearing was conducted on April 28, 1993. Frank DeLuca and Doug Brian appeared for the Taxpayer. Assistant counsel Dan Schmaeling represented the Department.

The Taxpayer is a wholly-owned subsidiary of Echlin, Inc. and made intercompany payments to Echlin during the years in issue. The issue in dispute is whether the intercompany payables must be included by the Taxpayer as capital for Alabama franchise tax purposes pursuant to §40-14-41(b)(4). That section requires that bonds, notes or other evidences of indebtedness payable by a subsidiary corporation to a parent owning more than 50% of the stock of the subsidiary must be treated as capital by the subsidiary, but only if the parent is not required to pay franchise tax in Alabama. The issue thus turns on whether Echlin was doing

business in Alabama and thereby required to pay Alabama franchise tax during the years in dispute. If so, then the intercompany payables should not be included as capital by the Taxpayer, and vice versa.

Echlin was incorporated in and has its principle place of business in Connecticut. Echlin manufactures and sells brake parts and related automobile items throughout the United States. Echlin makes sales in Alabama but none of its manufacturing facilities are located in Alabama.

Echlin operated in Alabama through a division, Brake Parts Company, in 1988. Very little information was submitted into evidence concerning when Brake Parts started operating in Alabama, where it was located, and the scope of its activities in Alabama. However, Echlin did report and pay withholding tax on one of Brake Parts' employees in Alabama in 1988. Echlin also leased automobiles in Alabama for use by Brake Parts employees. Brake Parts was incorporated and became an independent subsidiary corporation of Echlin in 1989.

The Taxpayer was incorporated as a wholly-owned subsidiary of Echlin in 1986 for the sole purpose of operating a manufacturing plant in Prattville, Alabama.

The City of Prattville Industrial Development Board subsequently issued bonds which were purchased by Echlin. The bond proceeds were used to finance the manufacturing facility now operated by the Taxpayer. The Taxpayer leases the facility and the

lease proceeds are used to service the bond debt owed to Echlin. Those payments from the Taxpayer to Echlin are the intercompany payables in issue.

The Taxpayer's president was an employee of Echlin during the years in issue. Echlin also self-insured the Taxpayer against claims arising from business conducted by the Taxpayer. Finally, Echlin continued to lease automobiles for use in Alabama by employees of both Brake Parts, Inc. and the Taxpayer during all the years in issue.

Echlin was not qualified to do business in Alabama and also did not file Alabama franchise tax returns for the years in issue until after the Department audited the Taxpayer and included the intercompany payables in issue as capital. The Department entered a preliminary assessment against the Taxpayer on September 9, 1992. Echlin subsequently qualified to do business with the Secretary of State on September 15, 1992, and then filed Alabama franchise tax returns for 1988 through 1991 on September 30, 1992. The returns showed a total liability of $14,841.36.

The Department rejected Echlin's returns based on its position that Echlin was not doing business in Alabama and thus was not subject to Alabama franchise tax during the subject years. The Department thus affirmed its position that the intercompany payables in issue constituted capital to the Taxpayer. The final assessment in issue was entered on February 8, 1993.

This case turns on whether Echlin should have paid Alabama franchise tax during the years in issue. The fact that Echlin was not qualified to do business and failed to file returns until after the Department audited the Taxpayer is not fatal to the Taxpayer's position.

Echlin operated in Alabama during 1988 through an operating division, Brake Parts Company. The extent of Brake Parts' operations in Alabama is not clear. However, Echlin filed a withholding tax return and paid withholding tax on a Brake Parts' employee in Alabama during 1988, and the Department does not dispute that Brake Parts had employees and operated as a division of Echlin in Alabama during 1988. I find that Echlin was doing business in Alabama through Brake Parts in 1988 and should have filed and paid Alabama franchise tax in that year. Consequently, the intercompany payables in issue should not be included as capital by the Taxpayer in 1988.

Brake Parts incorporated at the beginning of 1989 and thereafter operated as an independent corporation in Alabama. Separate corporations, although related, must be treated as separate entities for tax purposes. State v. Capital City Asphalt, Inc., 437 So.2d 1288. Thus, Echlin stopped operating through Brake Parts in Alabama when Brake Parts incorporated in 1989.

Echlin's only contact with Alabama after 1988 was that it made sales into Alabama, one of its employees worked as president of the Taxpayer, it continued to lease vehicles used in Alabama, and it

invested in bonds in Alabama. Those activities do not constitute doing business or employing capital in Alabama sufficient to subject Echlin to Alabama franchise tax. Consequently, the intercompany payables in issue were properly included as capital after 1988.

The Taxpayer's president, although an employee of Echlin, did not conduct business in Alabama in furtherance of Echlin's business as a parts manufacturer and seller. The automobiles leased by Echlin were used in Alabama by employees of Brake Parts and/or the Taxpayer, not by Echlin employees in the line and scope of Echlin's business. Echlin did make sales in Alabama, but the sale and delivery of goods into Alabama by an out-of-state company does not create sufficient nexus so as to subject the out-of-state company to Alabama taxation. National Bellas Hess v. Department of Revenue, 386 U.S. 753; Miller Brothers Company v. Maryland, 347 U.S. 340; Quill Corporation v. North Dakota, 112 S.Ct. 1904. Certainly if a business lacks nexus with Alabama it also cannot be doing business in Alabama for franchise tax purposes. Finally, Echlin's investment in bonds in Alabama does not constitute doing business in Alabama because the ownership of or investment in property or securities in Alabama does not constitute doing business in Alabama unless those activities are directly related to the corporation's primary business activity.[1]

[1] In Docket No. F91-122, the ownership of stocks by a corporation constituted doing business in Alabama because the

corporation's principle business activity was investing in and owning stocks. The Taxpayer's ownership of the Alabama bonds in this case is not related to Echlin's primary business of manufacturing and selling automobile parts, and thus does not constitute doing business in Alabama for franchise purposes.

The Department is directed to remove 1988 from the assessment and thereafter inform the Administrative Law Division of the adjusted amount due. A Final Order will then be entered setting out the Taxpayer's final liability for the subject years. The Final Order when entered can then be appealed to circuit court pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered on October 27, 1993.

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BILL THOMPSON
Chief Administrative Law Judge