COMMONWEALTH OF MASSACHUSETTS

APPELLATE TAX BOARD

BAYER CORPORATION **v.** **COMMISSIONER OR REVENUE**
(Successor to Miles Financial Services, Inc. *et. al.*)

Docket Nos. F239697, F239698 & F245722

Promulgated: July 20, 2000

These are consolidated appeals under the formal procedure pursuant to G.L. c. 62C, § 39, from the refusal of the appellee Commissioner of Revenue ("Commissioner") to abate corporate excises assessed against Bayer USA, Inc. and Miles Financial Services, Inc., to whose interests appellant has succeeded, for the tax years 1989, 1990 and 1991.

Commissioner Lomans heard these appeals. Chairman Burns and Commissioners Scharaffa, Gorton and Egan joined in the decision for the appellee.

These findings of fact and report are promulgated at the request of both the appellant and the appellee, pursuant to G.L. c. 58A, §13 and 831 CMR 1.32.

Kathleen King Parker, Esq. and *John R. Baraniak, Jr.* Esq. for the appellant.

Diane M. McCarron, Esq. and *Steven A. Remsberg,* Esq. for the appellee.

FINDINGS OF FACT AND REPORT

Based on an agreed statement of facts and the testimony and exhibits entered into evidence at the hearing of this appeal, the Appellate Tax Board ("Board") made the following findings of fact.

Through a myriad of acquisitions, mergers and name changes, the appellant Bayer Corporation ("Bayer") is the successor in interest to the corporations whose transactions form the basis of these appeals.[1] Bayer was the parent company of Agfa Corporation ("Agfa").[2] Agfa Financial Services, Inc[3] ("Agfa Financial") was Agfa's wholly owned subsidiary.

During the tax years 1989, 1990 and 1991 ("tax years at issue,") Agfa was in the business of manufacturing,

[1]Bayer Corporation's succession of interest is as follows: Rhinechem Corporation was formed on November 21, 1973. On April 3, 1986, Rhinechem changed its name to Bayer USA, Inc.. On December 31, 1991, Bayer USA, Inc. merged with Miles Inc., Mobay Corporation and Agfa Corporation, with Miles Inc. as the survivor. On April 1, 1995, Miles Inc. changed its name to Bayer Corporation.

[2]Agfa Corporation's succession of interest is as follows: Compugraphic Corporation was formed on September 14, 1960. On December 31, 1988, Compugraphic Corporation merged with Agfa-Gevaert, Inc. and Matrix Corporation, with Agfa-Gevaert, Inc. as the survivor. Immediately thereafter, Agfa-Gevaert changed its name to Agfa Corporation. On December 31, 1991, Agfa Corporation merged with Miles Inc., Mobay Corporation and Bayer USA Inc., with Miles, Inc. as the survivor.

[3]Agfa Financial's succession of interest is as follows: on March 8, 1973, Graphic Credit Corporation was formed by Compugraphic Corporation. On February 21, 1984, Graphic Credit Corporation changed its name to Compugraphic Financial Corporation. On January 1, 1989, Compugraphic Financial Corporation changed its name to Agfa Financial Services, Inc.. On January 1, 1992, Agfa changed its name to Miles Financial Services, Inc.. On April 1, 1995, Miles Financial Services, Inc. merged into Miles, Inc.. Miles, Inc. subsequently changed its name to Bayer Corporation.

selling and leasing hardware and software used in computerized typesetting equipment systems. Agfa also manufactured a comprehensive line of associated graphic arts and test management products. It had business in every state, as well as in other countries. Its Massachusetts business was located in Wilmington, Massachusetts.

During the tax years at issue, Agfa employed its own sales force to sell the equipment and software it produced. Agfa typically configured the equipment into customized systems and either sold these systems outright to the customer or entered into short-term or long-term leases. Agfa had no direct involvement in assisting its customers with the financing of their Agfa equipment acquisition.[4]

Agfa Financial was chartered as a Massachusetts corporation in 1973. Its sole business location was in Wilmington, Massachusetts. While registered to do business in various states, Agfa Financial had neither a sales office nor place of business in any state other than Massachusetts. It also did not engage in any business

[4]Prior to 1984, Agfa had arrangements with independent leasing companies such as Chase Manhattan Leasing and CIT Corporation to assist customers with such financing. After 1984, Agfa brought that leasing function in-house, through its subsidiary Agfa Financial.

activity or own property in any other state.[5] Its office was rented from Agfa.

Agfa Financial's primary business operation and purpose, as described in its Articles of Organization and in its business registrations filed in various states, was "lease financing" or "general finance business."[6] In particular, Agfa Financial provided financing for customers who entered into equipment leases with Agfa. It was also involved in collection of payment from customers who had entered into these leases. Once assigned the right to receive interest income related to the lease transactions, Agfa Financial filed Uniform Commercial Code financing statements to perfect its secured status in the account or contract right assigned to it by Agfa in the event that the transaction was deemed a secured transaction rather than a lease.

Agfa Financial had no payroll of its own.[7] All forty-six of Agfa Financial's employees were paid by Agfa. Of these employees, all but two worked out of the Wilmington

[5]The tax returns filed by Agfa Financial in other states indicated that it had no property or payroll in other states.

[6] Jurisdictions in which Agfa Financial filed business registrations include Kansas, New Jersey, Ohio, Pennsylvania, Washington, and the District of Columbia.

[7] Agfa Financial's tax returns indicate that the corporation had no employees. Its Corporate Excise tax return indicated "0" for employees, reported no deductions for salaries, and listed "0" payroll apportionment on the apportionment schedules.

office. One employee, responsible for the Pacific region, worked out of California,[8] and the second, responsible for the Northeast region, including Massachusetts, worked out of Agfa's offices in New Jersey, with some time spent in New York.[9] All of its correspondence was generated from the Wilmington, Massachusetts office, and all customer payments were directed to Massachusetts for processing.

When a customer decided to lease an Agfa product, Agfa and the customer entered into a written lease ("lease"). The leases were typically for three to five year terms, with a "fair market value" purchase option. Because of the nature of the equipment, which was technical and subject to relatively rapid obsolescence, the fair market value of the property at the end of the lease term was nominal. For example, equipment leased by one customer had an initial cost of $67,000, but had a buyout cost at the end of the lease of only $3,500. Similarly, lease expiration purchase prices of $1,300.40 and $874.33 were available for

[8] The California office was owned by Agfa and the employee was paid by Agfa. All credit was investigated and orders approved or rejected in Massachusetts and there was no evidence that the employee's activities exceeded solicitation.

[9] The Appellant sought an abatement of tax from New Jersey, on the grounds that Agfa Financial did not have nexus with that state. On its request for abatement, it stated that it was not registered to do business, had no inventory, did not own or lease real or personal property nor did it perform services in New Jersey. On its New York tax return, Agfa Financial also indicated that it did not own or lease property in that state.

equipment with original costs of $67,393.48 and $25,445, respectively.

After the lease was signed by a customer, an Agfa field salesperson forwarded the document to Agfa at its Wilmington, Massachusetts office. Agfa would then verify the property system configuration and equipment pricing. The lease was also forwarded to Agfa Financial for a determination of the customer's credit worthiness and to verify the lease pricing and lease terms. If the customer passed Agfa Financial's credit check, Agfa signed the lease and then scheduled production of the property within thirty to sixty days. Upon production of the ordered equipment, Agfa shipped the property to the customer.

The lease, signed by Agfa and its customer, expressly reserved title to the leased equipment and the system software to Agfa.[10] The lease required that the customer maintain and insure the equipment and that Agfa be named as the insured. It specified that the customer could assign or transfer the lease only with prior written consent from Agfa. It further specified that Agfa could assign the

[10] Paragraph 6 of the lease, entitled "TITLE," expressly states that the "System and Software shall remain the personal property of Agfa, even if attached to realty or other property. Customer shall not sell, encumber or remove the System or Software without prior written consent of Agfa. Customer shall perform all necessary acts to preserve and protect the right, title and interest of Agfa in the System and Software. Agfa may inspect the System and Software during normal business hours."

lease to Agfa Financial, but upon assignment, Agfa remained responsible for performance of all warranty claims. No warranty claims could be brought against the assignee, Agfa Financial.

Pursuant to the lease, the risk of loss or damage was passed to the customer upon shipment of goods. The customer also paid all transit insurance, transportation and handling costs, in addition to taxes, assessments and charges levied against both the system and software. At the end of the lease term, the lease specified that the customer was required to promptly notify Agfa’s local service office, and that if the equipment were not purchased by the customer, Agfa, at its own expense, would disconnect and remove the system.

It is undisputed that the leases were properly classified for book and financial accounting purposes, pursuant to generally accepted accounting principles

("GAAP"), as "capital leases."[11] Consistent with GAAP, Agfa did not include the leased property on its books and Agfa Financial treated the lease payments as interest.

For federal tax purposes, however, Agfa treated the leases as operating leases[12], treating itself as the owner of the leased property and claiming depreciation on that property. Agfa Financial did not include any leased equipment as an asset on its books or tax returns and did not claim any depreciation for the leased equipment.

During the tax years at issue, Agfa Financial reported on its federal tax returns that it was engaged in the

[11]Statement of Financial Accounting Standards No. 13 ("FAS 13,") "Accounting for leases," is promulgated by the Financial Accounting Standards Board. It establishes general financial accounting and reporting standards for "leases" and other agreements conveying the right to use property, plant or equipment for a stated period of time. It thus establishes, for financial accounting purposes, a uniform and consistent set of rules for both the "lessors" and "lessees" that are parties to such transactions. Under FAS 13, a lease transaction will be classified either as a "capital lease" or as an "operating lease." Pursuant to FAS 13, a "capital lease" or "direct financing lease" is treated as a loan or receivable, an intangible asset that generates interest income. The leased equipment, itself, is not listed as a corporate asset of the Lessor. The *lessee* would reflect that ownership, for *book/financial accounting purposes*, as an asset on its books, and would therefore be entitled to take a depreciation charge for the equipment. In contrast, in an "operating lease," the lessor is treated as the owner of the underlying asset, subject to depreciation, and which generates rental income.

[12]An operating lease would reflect a true lessor-lessee relationship. The lessor is considered the owner of the leased equipment, and would properly be able to take depreciation on that equipment. Payments by the lessee to the lessor would be considered rent for the use of the equipment.

business of lease financing.[13] Consistent with its operations, it reported on Federal Form 1120 the receipts from the lease as "interest income" with other miscellaneous income.[14] The equipment under the lease was never included as an asset on Agfa Financial's books, nor on its various tax returns.[15] Additionally, no depreciation deduction for that equipment was taken. Agfa Financial's books uniformly indicated that it earned interest income from its financing activity.

Bayer USA Inc. and its subsidiaries, including Agfa and Agfa Financial, timely filed combined Massachusetts corporate excise tax returns and paid the tax shown as due for each of the tax years at issue. In its original return, Agfa Financial treated its income from the lease transactions as interest and included the interest in the sales factor of its apportionment formula. During each of the tax years at issue, Agfa Financial apportioned its interest income to various states, including Massachusetts. In 1989, Agfa Financial reported only a portion of its "other income" to Massachusetts. In 1990 and 1991, it apportioned one hundred percent of its "other income" to

[13]Agfa Financial made the same representation on its various state tax returns, including Delaware, New Jersey and Georgia.
[14]Similar reporting was made on its state tax returns, including District of Columbia, Maryland and Michigan.

Massachusetts. In April, 1993, the Commissioner conducted an audit of the tax returns at issue. By Letter of Determination, dated August 18, 1994, the Commissioner notified the Appellant that he would modify Agfa Financial's apportionment formula to exclude, pursuant to G.L. c. 63, § 39(f), the interest receipts from the sales factor formula.[16]

The Commissioner issued two Notices of Intention to Assess ("NIA"), dated August 22, 1994, for the taxable periods at issue. The first NIA, issued to Bayer USA, was for additional tax due with respect to the combined income measure of the corporate excise. The second NIA was issued to Agfa Financial, as successor to Miles Financial Services Inc., for additional excise due with respect to the non-income measure of the corporate excise. Both proposed assessments were based on the increase of the Massachusetts apportionment formula to one-hundred per cent.

On October 17, 1994, the taxpayer requested a conference on the two NIAs. On April 13, 1995, a hearing

[15] The only assets listed on the tax returns of Agfa Financial were accounts receivable.

[16] Since Agfa Financial had apportioned 100% of its other income to Massachusetts in 1991 and 1990, the audit adjustment resulted in 100% of the other income and the interest income earned by Agfa Financial being apportioned to Massachusetts. The Commissioner further determined that Agfa Financial's Massachusetts' apportionment percentage should be 100% for 1989, as its income was from the sale of other than tangible personal property, and the income producing activities for that income were in Massachusetts.

was held with the Commissioner's Appeal and Review Bureau. The appellant presented the hearing officer with amended combined corporate excise returns for the tax years at issue, but these amended returns were not accepted.[17] By notice dated May 1, 1996, the Appeal and Review Bureau issued a determination letter, upholding the NIA's insofar as they concerned Agfa Financial.

By Notice of Assessment ("NOA"), dated May 11, 1996, the appellant was notified of the additional assessment of corporate excise (combined income measure) against Bayer USA Inc., in an amount totaling $2,972,309. By Notice of Assessment, dated May 15, 1996, the appellant was notified of the additional assessment of corporate excise (non-income measure) against Agfa Financial, in an amount totaling $501,139.55.

On May 31, 1996, the appellant paid the additional assessments in full and timely filed applications for

[17]The Appellant claimed, through these amended returns, that its taxes had been overpaid. The Appellant recharacterized Agfa Financial's income as apportionable rental income, resulting in a Massachusetts apportionment percentage of 9.6168% for 1991, 8.6686% for 1990 and 8.2532% for 1989. Additionally, the amended returns transferred Agfa's depreciation deduction to Agfa Financial. Although federal amended returns were prepared and attached to the Massachusetts amended returns, the federal amended returns were not signed. The Appellant never demonstrated that the amended returns were ever submitted to the Internal Revenue Service.

abatement of its corporate excise.[18] By letter to the Commissioner dated December 12, 1996, the appellant withdrew its consent to the Commissioner's failure to act upon the applications for abatement within six months from the date of filing. Pursuant to G.L. c. 58A, § 6, the applications for abatement were deemed denied as of December 12, 1996. On October 22, 1996, the appellant filed a report of federal change with the Commissioner for tax year 1991. That change, when added to the audit adjustments, detailed above, resulted in an additional assessment of $212,341 for tax year 1991. The appellant paid this amount in full.

By Petition dated January 14, 1997, the appellant appealed to this Board the additional assessments as to the non-income measure and income measure of corporate excises for the tax years at issue.

On August 5, 1997, the appellant filed an application for abatement, requesting an abatement of the additional assessment resulting from the federal change and the audit adjustments. By letter dated September 26, 1997, the

[18]The following abatement requests were made as successor to Bayer USA Inc.: for the income measure of corporate excise tax, in the amounts of $476,430 for tax year 1989, $791,831 for tax year 1990 and $399,222 for tax year 1991, totaling $1,677,483. The following abatement requests were made, as successor to Agfa Financial Services: for the non-income measure for corporate excise tax, in the amounts of $93,714 for tax year 1989, $104,823 for tax year 1990 and $115,198 for tax year 1991, totaling $313,735.

Commissioner notified the appellant of his refusal to act on the federal change application for abatement and instructed the appellant to direct any amendments to this Board. On November 24, 1997, the appellant appealed to this Board from the Commissioner’s failure to grant the federal change application.

On the basis of the foregoing, the Board consolidated the appeals, and found them to be in conformity with the requirements of G.L. c. 62C, §§ 37 and 39. The Board, therefore, determined that it had jurisdiction to hear and decide this matter.

On the basis of the evidence presented, and to the extent that it is a finding of fact, the Board found that Agfa Financial earned interest income from the financing of leases entered into between Agfa and its customers. Accordingly, the Board determined that the Commissioner’s assessments were correct and issued a decision for the appellee in these appeals.

OPINION

The issue raised by the present appeal is whether Agfa Financial’s receipts from equipment leasing transactions constitute rental income from assets it owned and leased or interest income from a financing arrangement.[19]

A domestic corporation doing business in Massachusetts is subject to a corporate excise, pursuant to G.L. c. 63, § 32. The corporation's excise tax is determined by combining an "income component" with a "non-income component." If a corporation's income is derived solely from business activities conducted in Massachusetts, all of its income is taxable in Massachusetts. G.L. c. 63, § 38(b). If a corporation has income from business activities conducted both inside and outside of the Commonwealth, it is entitled to apportion that income to Massachusetts and such other states, pursuant to G.L. c. 63, § 38(c).

A corporation is entitled to apportion its income to another state only if the other state has jurisdiction to tax that corporation. A corporation is taxable in another state if

1) in that state such corporation is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege

[19] Because the G.L. c. 63 § 38 apportionment formula is used to calculate the non-income measure of the corporate excise tax, the audit assessments appealed from also increased Agfa Financial's non-income measure. Docket No. 239697 concerns the increase to the non-income measure; Docket No. 239698 concerns the increase to the income measure. The issues in both are the same.

of doing business, or a corporate stock tax, or

2) that state has jurisdiction to subject such corporation to a net income tax regardless of whether, in fact, the state does or does not do so. G.L c. 63, § 38(b) and 830 CMR 63.38.1(5).

The manner in which a corporation may apportion its income is set forth in G.L. c. 63, § 38(c). Income is apportioned by multiplying taxable net income by a fraction, determined pursuant to a formula made up of three factors, a "payroll factor," a "property factor," and a "sales factor." The "payroll factor" compares the employees the corporation has inside and outside the Commonwealth. G.L. c. 63, § 38(e). Similarly, the "property factor," pursuant to G.L. c. 63, § 38(d), and "sales factor," pursuant to G.L. c. 63, § 38(f), compare the corporation's property and sales, respectively, inside and outside of the Commonwealth.[20]

With respect to the "sales factor" under § 38(f), the numerator is the taxpayer's total Massachusetts sales, and the denominator is the total sales from all sources during

[20]For the periods at issue, Agfa Financial originally filed its corporate excise returns with the "property factor" and the "payroll factor" reported as zero. The amount of Agfa Financial's income apportioned to Massachusetts, therefore, was determined solely on the basis of the "sales factor."

the taxable year. The term "sales," as used in § 8(f), means "all gross receipts of the corporation ***except interest***, dividends, and gross receipts from the maturity, redemption, sale, exchange or other disposition of securities." (Emphasis added.) Accordingly, interest income is explicitly excluded from the apportionment factor. All rental income, however, is included in the denominator of the sales factor, and rental income from property located in Massachusetts is included in the numerator. *See* 830 CMR 63.38.1(9)(b)(4) and (6); 830 CMR 63.38.1(9)(c)(1)(f).

The appellant asserts that the property underlying the lease was sold by Agfa to Agfa Financial. The appellant argues that the gross receipts Agfa Financial received under the leases were, therefore, rental income to Agfa Financial which must be included in the sales factor.[21] The appellant further argues that Agfa Financial was entitled to include the leased equipment in its property factor. Finally, the appellant argues that Agfa Financial was entitled to depreciate the equipment under the leases.

The evidence, however, demonstrates otherwise. Agfa Financial was never the owner of the property under

[21] If the receipts generated under the lease are characterized as rental income to Agfa Financial, Agfa Financial would be entitled to include them in the denominator of the sales factor, and to the extent the leased equipment was located in Massachusetts, in the numerator of the sales factor.

the leases. Rather, Agfa Financial was engaged in the business of lease financing, and its transactions with Agfa were financing arrangements generating interest income. This characterization, of both its business and the revenues it generated, is consistent with Agfa Financial's own characterizations, as reported on its corporate filings, its federal tax return and original state tax returns, its business registrations in other states, its Articles of Organization and its books and financial records.

Despite its own characterizations, the appellant asserts that such characterizations were incorrect, and made in error.[22] A taxpayer seeking to challenge the form in which it has cast its own transactions has a heavy burden of proof imposed upon him. ***Redwing Carriers, Inc. v. Tomlinson***, 399 F.2d 652, 659 n.9 (5th Cir. 1968); ***Carlton v. United States***, 385 F.2d 238 (5th Cir. 1967).

> The rule exists because to permit a taxpayer at will to challenge his own form in favor of what

[22]The Appellant asserts that Agfa Financial's representations on its federal tax forms should be disregarded, as they were reported and filed in error, with numerous mistakes. Income included as "interest" should be reclassified as rental income and service fee income. Depreciation, mistakenly taken by Agfa, should be taken on Agfa Financial's return. Lease receipts, service fee income and "other income" should be reflected in the numerator and denominator of the sales factor of the apportionment formula. The lease equipment was also not included, in error, in either the numerator or denominator of the property factor of the apportionment formula.

> he subsequently asserts to be true 'substance' would encourage post-transactional tax planning and unwarranted litigation on the part of many taxpayers and raise a monumental administrative burden and substantial problems of proof on the part of government. ***In Re Steen***, 509 F.2d 1398, 1402-03 n. 4 (9th Cir. 1975).

A taxpayer is, therefore, generally bound by the form in which it represents its transactions on its tax returns:

> The burden is on the taxpayer to see to it that the form of business he has created for tax purposes, and has asserted in his returns to be valid, is in fact not a sham or unreal. If in fact it is unreal, then it is not he but the Commissioner who should have the sole power to sustain or disregard the effect of the fiction since otherwise the opportunities for manipulation of taxes are practically unchecked. ***Maletis v. United States,*** 200 F.2d 97, 98 (9th Cir. 1952), *cert. denied,* 345 U.S. 924 (1953).

Therefore, unless the Appellant meets this burden of proof, he will be unable to undo his characterization of Agfa Financial as a financing business, generating interest income.

How a specific item is treated for book and financial accounting purposes is not necessarily determinative of the particular item's tax treatment. Therefore, how Agfa Financial characterized on its books the income received under the lease may not answer the issue before the Board. Courts do not require conformity between book/financial accounting and tax accounting, where tax accounting objectives differ. *See* ***Thor Power Tool Co. v. Commissioner***, 439 U.S. 522, 540 (1979); ***First Federal Savings and Loan Association of Boston v. State Tax Commission***, 372 Mass. 478, 483 (1977) *aff'd* 437 U.S. 255 (1978).

Financial accounting principles under GAAP have, however, been held to be relevant to the net worth component of the corporate excise. *See* ***Xtra, Inc. v. Commissioner of Revenue,*** 380 Mass. 277 (1980); ***Web Industries, Inc., et al v. Commissioner of Revenue,*** 1999 Mass. A.T.B. Adv. Sh. 122, 128-130; ***Eaton Financial Corp. v. Commissioner of Revenue,*** 2000 Mass. A.T.B. Adv. Sh. 526 (July 20, 2000). Although, unlike the net worth component provisions of G.L. c. 63, §§ 30(7)—(11), there is no explicit reference to GAAP such as "book value" in the net income component and apportionment provisions of the corporate excise at issue in the present appeals, the appellant's treatment of the leases on its books can be considered in connection with whether the leases are operating or capital leases for tax purposes.

In determining whether a true lease exists or a financed sale, the following factors may be considered: 1) whether legal title passes; (2) how the parties treat the transaction; (3) whether an equity interest was acquired in the property; (4) whether the contract creates a present obligation on the seller to execute and deliver a deed and a present obligation on the purchaser to make payments; (5) whether the right of possession is vested in the purchaser; (6) which party pays the property taxes; (7) which party bears the risk of loss or damage to the property; and (8) which party receives the profits from the operation and sale of the property. ***Grodt and McKay Realty, Inc. v. Commissioner***, 77 Tax Court 1221, 1237-38 (1981) *See also* ***Revenue Ruling 55-540*** *and* ***TAM 9237045***.

In addition, the appellant asserts that Agfa sold the leases to Agfa Financial, making Agfa Financial the Lessor of the equipment under lease. In general, a transaction constitutes a sale for federal income tax purposes when the benefits and burdens of ownership have passed to the purported purchaser. ***Frank Lyon Co. v. U.S.***, 435 U.S. 561, 578-81; 678, n. 14 (1978). "The characterization of a transaction for federal income tax purposes is controlled by the substantive provisions of the lease and the parties' conduct, rather than by the particular terminology used in the agreement." ***TAM 9237045***, (5/6/92), *citing* ***Frank Lyon Co. v. United States***, *supra.* (The question of ownership is a question of fact, which must be ascertained by the written agreement, which is read in light of the attending facts and circumstances. ***Tolwinsky v. Commissioner***, 86 T.C. 1009 (1986)). *Also see* ***Revenue Ruling 55-540***, 1955-2 C.B. 39.

In considering the above factors, the evidence demonstrates that Agfa Financial did not own the leased property. In particular, the plain language of the lease required the following: that Agfa retain title to the equipment; that only the lease could be assigned to Agfa Financial; and that Agfa remain responsible for any claims by the customer regarding defects or non-performance of the equipment. Agfa, as the owner of the leased equipment, appropriately deducted depreciation on that equipment.[23] Agfa, as the owner of the leased equipment, appropriately prepared, filed and submitted payment of the sales and property taxes due on that equipment. At the end of the lease period, as well, the leased equipment was returned to Agfa, unless it was sold to the lessee. Agfa Financial reported its business as lease financing and income

[23] Agfa Financial would not be entitled to deduct depreciation on equipment it does not own. *See* ***Erving Paper Mills Corporation v. Commissioner***, 1997 Mass. A.T.B. Adv. Sh. 302 (April 22, 1997), *aff'd* 49 Mass. App. Ct. 14 (2000) ("The person entitled to depreciation under IRC § 167 is the person who possesses the benefits and burdens of ownership with respect to the property.")

received as interest income on its federal and state tax returns, business registrations in other states, Articles of Incorporation, and its books. Accordingly, Agfa remained the owner of the equipment under lease and Agfa Financial held only the right to receive sums due under that lease.

Because Agfa Financial’s income was derived from the service of providing financing, its income was appropriately sourced to the state of the income producing activity, Massachusetts. *See* G.L. c. 63, § 38(f). The Appellant has failed to demonstrate that it had nexus in any state other than Massachusetts.[24] It was incorporated in Massachusetts and its only place of business was in Massachusetts. Its business activities were all performed in Massachusetts. It had no employees of its own. It did not own any property in other jurisdictions. Without nexus to any other state, Agfa Financial was not entitled to apportion its income under G.L. c. 63 § 38(b). Accordingly, the Commissioner properly allocated all of Agfa Financial’s income to Massachusetts for the tax years at issue.

[24] As noted, above, Agfa Financial sought a tax abatement from New Jersey on the grounds that it did not have nexus in that state. It also claimed on its New York tax return to not own or lease property in that state.

The mere registration to do business in a state is insufficient to establish nexus. *See* ***Commissioner of Revenue v. Kelly-Springfield Tire Co.***, 419 Mass. 262 (1994); ***National Tires, Inc. v. Commissioner of Revenue***, ATB Docket Nos. 163334-336, (1996). Similarly, the filing of a tax return in another state will not establish nexus where nexus does not otherwise exist. ***Yankee Companies, Inc. v. Commissioner of Revenue,*** *36 Mass. App. Ct. 1118 (1992) See also* 830 CMR 63.38.1(5)(a)2. (Voluntary filing insufficient.) Appellant failed to establish that Agfa Financial had nexus with any state other than Massachusetts during the relevant time period.

The Appellant maintains that the Massachusetts statutory formula is unconstitutional as applied to the Appellant. The Supreme Court has "long held that the Constitution imposes no single formula on the States." ***Container Corp. v. Franchise Tax Board***, 463 U.S. 159, 164 (1983). Accordingly, the States have:

> wide latitude in the selection of apportionment formulas and . . . a formula-produced assessment will only be disturbed when the taxpayer has proved by clear and cogent evidence that the apportioned income is in fact *out of all proportion* to that business, transacted in that State . . . [or that the formula] has led to a grossly distorted result . . . ." ***Moorman Mfg. Co. v. Blair***, 437 U.S. 267, 274 (1978).

Even a method that "generally will not produce a figure that represents the actual profits earned within the State" will be upheld. ***Id.*** at 273. The Supreme Court has tolerated wide "imprecision," ***Id.*** and recognized that a "substantial margin of error [is] inherent in any method of attributing income among the components of a unitary business." ***Container Corporation,*** *Id.* at 184. The state need strive only for a "rough approximation" of the corporation's income that is "reasonably related to the activities conducted within the taxing state." ***Exxon Corp. v. Wisconsin Department of Revenue***, 447 U.S. 207, 223 (1980) *quoting* **Moorman**, *Id.,* at 273. Under this deferential standard of constitutional review, the Massachusetts Supreme Judicial Court has described the three-factor formula as the "commonly adopted formula." ***W.R. Grace and Co. v. Commissioner of Revenue,*** 378 Mass. 577, 584 (1979) *quoting* ***Dow Chemical Co. v. Commissioner of Revenue***, 378 Mass. 254, 259 (1979). Here, the statutory method of apportioning income does not produce an unconstitutional distortion in light of the presence of Agfa Financial's business location and activities in Massachusetts.

Based on the foregoing, the Board ruled that the Appellant failed to meet its burden of proving that

Agfa Financial was the lessor/owner of the equipment under the lease. The Board determined, therefore, that Agfa Financial received interest income, and that all of its business activities were conducted in Massachusetts without nexus to any other state. Agfa Financial, therefore, was not entitled to apportion its income. ***Staples v. Commissioner of Corporation or Taxation***, 205 Mass. 20, 26 (1940). (Person who claims to be aggrieved by the refusal of the Commissioner to abate a tax in whole or in part has the burden of establishing the right to an abatement.) Accordingly, the Board issued a decision for the appellee in these appeals.

APPELLATE TAX BOARD

By:______________________________
Abigail A. Burns, Chairman

A true copy,

Attest:_______________________
Clerk of the Board