BEFORE TEE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)) NO. 81R-268-MW
UNITED PARCEL SERVICE, INC.)

Appearances:

For Appellant: Richard D. Birns
Attorney at Law

For Respondent: Kendall E. Kinyon
Assistant Chief Counsel

O P I N I O N

This appeal is made pursuant to section 26075, subdivision (a),1/ of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of United Parcel Service, Inc., for refund of franchise tax in the amounts of $73,520.45, $180,665.68 $41,866.13, and $130,242.66 for the income years 1974, 1975, 1976, and 1977, respectively.

1/ Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the income years in issue.

The question presented by this appeal is whether respondent properly determined the numerators of appellant's property and payroll factors of its apportionment formula.

Appellant, with its parent and affiliated corporations, provides an integrated transportation service for small packages and parcels throughout the United States and in certain foreign countries. Its area of operations in the United States is divided into "operating areas" with a headquarters or "operating center" for each area. At each operating center, vehicles are garaged and dispatched and packages are sorted. Packages are picked up at the shipper's address by a "package delivery car," the familiar UPS brown van. Packages are sorted at the operating center and, if destined for a point within the same operating area, are then delivered by another package delivery car.

Packages destined for an address in another operating center are transferred to the operating center servicing the package destination address. This transfer may be made by a direct trip, but is usually accomplished by passing the package through a centrally located "hub," which is a major dispatching and package-sorting center serving a large number of operating areas. Long-distance service is provided by transporting the package from hub to hub until it reaches the hub nearest its destination. The package then goes to the appropriate operating center and then is delivered to its ultimate destination by a package delivery car. Only 20 percent of appellant's revenues during the appeal years were earned from intrastate commerce, and the majority of packages carried by appellant in California were destined for other states.

Three types of vehicles are used in appellant's operations: package delivery cars, tractors, and trailers. Package delivery cars, the familiar UPS brown vans, range in capacity from 300 to 1,200 cubic feet. They normally operate only within a single operating area and usually do not cross state lines. Tractors and trailers also come in a variety of capacities. They frequently cross state lines on a regular basis, although they may be used within an operating area for package pickup and delivery, such as for pickups from large-volume shippers. As much as 30 to 40 percent of package volume pickups are done by large trucks or tractor-trailers. Ordinarily, trips between operating centers and hubs and between different. hubs are carried out by tractors and trailers, although a package delivery car may be used if that is the most

appropriate-sized vehicle for the particular job. Tractor-trailers and package delivery cars are each driven by separate classes of drivers.

Appellant operates a single unitary business in conjunction with its parent and affiliates and computes its California franchise tax liability *on* the basis of a combined report and formula apportionment. Appellant originally used the standard apportionment formula to apportion its business income to California. Later, upon discovering that the Franchise Tax Board (FTB) had a special "interim" formula guideline for trucking operations, it filed an amended return applying this formula and claimed a refund. The Franchise Tax Board allowed use of the interim formula for computing appellant's property and payroll factors only for vehicles and drivers operating between states, rather than for all of appellant's venicles and drivers. This modification of the numerators of appellant's property and payroll factors resulted in a partial denial of appellant's claim for refund.

Appellant, since it was engaged in a single unitary business, was subject to the apportionment and allocation provisions of the Uniform Division of Income for Tax Purposes Act (UDITPA), found in sections 25120 through 25139, in determining its income attributable to and taxable by California. (Rev. & Tax. Code, § 25101; Cal. Admin. Code, tit. 18, reg. 25101, subd. (f).) Under UDITPA, a taxpayer's income attributable to this state is determined by multiplying its business income by a fraction (commonly called the apportionment formula), the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three. (Rev. & Tax. Code, § 25128.) The prop-, erty, payroll, and sales factors are fractions, the denominators of which are composed of the taxpayer's worldwide property values, payroll, and sales, respectively, and the numerators of which are composed of the taxpayer's California property values, payroll, and sales, respectively. (Rev. & Tax. Code, §§ 25129, 25132, 25134.)

The Franchise Tax Board's interim formula for trucking operations, in existence since approximately 1971, was developed pursuant to section 25137 which allows special allocation and apportionment methods when the normal methods of UDITPA do not fairly represent the extent of the taxpayer's business activity in this state. The parties have agreed that a special formula is necessary

in this case, but disagree about the application of the Franchise Tax Board's special interim formula.

The interim formula developed by the Franchise Tax Board reads, in its entirety, as follows:

Trucks

PROPERTY FACTOR

(a) Real and stationary tangible property - situs.

(i) owned property - original cost

(ii) rented property - 8 times annual rent

(b) Mobile equipment - ton miles or actual miles for each piece of equipment or class of equipment

(i) owned property - original cost times mileage

(ii) rented property - 8 times annual rent

PAYROLL FACTOR

(a) Truck drivers - same mileage formula used for property factor purposes for mobile equipment, both owned and rented

(b) All other employees - see Regulations 25132 and 25133

SALES FACTOR

(a) Intrastate and interstate revenue from trucking operations - revenue miles

(b) Other gross receipts - see Regulations 25134, 25135, and 25136

(Franchise Tax Board, UDITPA Manual, § 1010 (1977).)

The Franchise Tax Board contends that appellant has two classes of trucks and drivers--the package delivery cars and their drivers, which ordinarily operate

within the state, and the tractor-trailer rigs and their drivers, which operate both within and without the state. It argues that the special formula should apply only to the latter class, while the package delivery cars must use the normal apportionment formula.

The special interim formula developed by the Franchise Tax Board makes no distinction between interstate and intrastate use of trucks (or drivers). The formula simply states that, with regard to mobile equipment, "ton miles or miles" are to be used "for each piece of equipment or class of equipment." The Franchise Tax Board argues that the words "class of equipment" justify different treatment for different classes of equipment. We must disagree, since the plain language of the formula provides that "mileage" is the only factor to be used, whether the miles are computed separately for each piece of equipment or collectively for various classes of equipment.

The Franchise Tax Board agreed that appellant, who is engaged in trucking operations, should use a special *formula* to apportion its income and it has developed a special interim formula specifically applicable to taxpayers engaged in trucking operations. Instead of applying that interim formula, however, the Franchise Tax Board is arguing that this taxpayer should use a special formula different from the interim formula. We can see no reason why appellant should be treated any differently from other taxpayers engaged in trucking operations. On its face, the interim formula applies to all of appellant's trucks and drivers, whether in interstate or intrastate commerce. In this situation, we believe that appellant is entitled to use this formula for all its trucks and drivers. The Franchise Tax Board's action in denying part of appellant's claim for refund must, therefore, be reversed.

Appeal of United Parcel Service, Inc.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of United Parcel Service, Inc., for refund of franchise tax in the amounts of **$73,520.45, $180,665.68, $41,866.13,** and **$130,242.66** for the income years 1974, 1975, 1976, and 1977, respectively, be and the same is hereby reversed.

Done at Sacramento, California, this 6th day of **May** , 1986, **by** the State Board of Equalization, with Board Members Mr. Nevins, Mr. Collis, Mr. Bennett, Mr. Dronenburg and Mr. Harvey present.

Richard Nevins** , Chairman

Conway H. Collis , Member

William M. Bennett , **Member**

Ernest **J.** Dronenburg, Jr. , Member

Walter Harvey* , Member

*For Kenneth Cory, per Government Code **section** 7.9

**Abstained