New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

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Corporation Tax
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STATE OF NEW YORK
STATE TAX COMMISSION

ADVISORY OPINION PETITION NO. C820628A

On June 28, 1982, a Petition for an Advisory Opinion was received from Hauserman, Inc., 5711 Grant Avenue, Cleveland, Ohio 44105.

At issue is whether Petitioner, a foreign corporation which rents a showroom-sales office in New York to display the products of and act as the sole sales agent for a related alien corporation, is subject to the Franchise Tax on Business Corporations imposed under Article 9-A of the Tax Law. Petitioner also inquires whether the related alien corporation would be subject to such tax.

Hauserman, Inc., an Ohio corporation, operates five showroom-sales offices in the United States, including one in New York, through its division Sunar, U.S.A.. Hauserman, Inc. is the exclusive sales agent in the United States for the furniture products manufactured by the Sunar division of a related Canadian corporation, Hauserman, Ltd.. All contracts or orders solicited by the Sunar, U.S.A. division of Hauserman, Inc. at the New York showroom-sales office are accepted at and filled from the office and plant of Hauserman, Ltd. in Canada.

Hauserman, Inc. leases a showroom-sales office in New York. Leasehold improvements are owned by its division, Sunar, U.S.A.. Hauserman, Ltd. owns the furniture located in the New York showroom-sales office, such furniture being both displayed for sale and used as office furniture. No payment is made by Hauserman, Inc. to Hauserman, Ltd. for such usage. Furniture so used is used solely in connection with the above-described solicitation activities. The display products in the New York showroom-sales office are, on occasion, offered for sale to dealers when the display furniture is changed, as when a new line is introduced. Approximately thirty to forty percent of the display furniture is consigned each year to an unrelated party for sale. Approximately $25,000 is received each year from such sales, which are made in New York. Petitioner's average total annual sales to New York purchasers is approximately $3,000,000.

The relationship between Hauserman, Ltd. and Hauserman, Inc. is governed by an Exclusive Sales Representative Agreement. Section 3 of this agreement grants to Hauserman, Ltd. the right to disapprove the design, location, and appointments of the New York showroom. Section 4 of the agreement provides that Hauserman, Ltd. is to set all prices, terms, and conditions for orders to be solicited at the New York showroom, such orders and bids to be taken on standard forms approved by Hauserman, Ltd.. Section 5 provides that Hauserman, Inc. is to negotiate contracts with individual sales representatives, with the proviso that the negotiation and execution of such contracts is to be made in consultation with Hauserman, Ltd.. Further, Hauserman, Ltd. retains control over the hiring and firing of personnel working at or out of the New York showroom. Finally, the U.S.A. Sales Manager of Hauserman, Inc., who is responsible for the operation of all five showrooms, including the one in New York, reports to the President of the Sunar Division of Hauserman, Ltd.. Hauserman, Ltd. retains ultimate control over the operations conducted at or out of the New York showrooms including the hiring and firing of individuals, as well as the manner in which operations are

to be conducted. Under Section 6 of the agreement, Hauserman, Ltd. will pay Hauserman, Inc. fifteen percent of the final accepted contract price of each order obtained in its territory for the performance of Hauserman, Inc.'s sales service.

Subsequent to the submission of its Petition for Advisory Opinion, Petitioner submitted additional facts with respect to which it also requests a ruling. Effective on and after March 1, 1984 the E. F. Hauserman, Co., subsidiary of Hauserman Inc., changed its corporate name to Sunar Hauserman, Inc.. Sunar Hauserman, Inc. vacated its former branch sales office and moved into and operates out of the Sunar, U.S.A. New York showroom-sales office at 730 Fifth Avenue, New York, New York 10019. Sunar Hauserman, Inc. rents this office space from Sunar, U.S.A. for use in the sale of its Interior Building Partition & Wall Products as well as for the sale of Sunar of Canada's furniture products. Through this reorganization, Sunar Hauserman, Inc. is replacing Hauserman, Ltd. as the ultimate control over operations conducted at or out of the Sunar New York showroom-sales office.

The franchise tax at issue is imposed on every foreign corporation, not otherwise specifically exempted, which is doing business, employing capital, owning or leasing property or maintaining an office in New York (Tax Law, § 209.1; 20 NYCRR 1-3.2). Notwithstanding the imposition of the franchise tax, however, a foreign corporation whose income is derived solely from interstate commerce is not subject to tax if its New York activities do not exceed those prescribed by Public Law 86-272, which is codified at 15 U.S.C. §§381-4. (20 NYCRR §1-3.4(b)(9)). P.L. 86-272 was enacted in order to overcome the U.S. Supreme Court decision in Northwestern States Portland Cement Co. v. Minnesota, 3 L. Ed. 2d 421 (1959). In Northwestern, the U.S. Supreme Court for the first time permitted the application of a state net income tax to the income of a taxpayer engaged exclusively in interstate commerce, holding that such a tax satisfies the Due Process Clause of the U.S. Constitution where a corporation's activities in the taxing state are such that there is created a sufficient nexus between such activities and the tax imposed; that is, that the corporation is "sufficiently included in local events to forge 'some definite link, some minimum connection' sufficient to satisfy due process requirements." (Id. at 431).

The corporations in the two cases consolidated for decision in Northwestern were engaged in the taxing states in the solicitation of orders for tangible personal property, such orders being accepted, filled, and delivered from a location outside of the taxing state. Activities closely related to solicitation were also carried on, such as leasing and operating offices for the use of salesmen and secretarial staff, as well as the furnishing of cars to the salesmen. In one of the two cases salesmen received and transmitted claims against the corporation for loss or damage. The Court held that in each case the derivation of income from "vigorous and continuous sales campaigns run through a central office located in the [taxing] State" satisfied the nexus requirement of the Due Process Clause. Id. It was as a reaction to this extension of the States' taxing powers that Congress enacted, within seven months of the decision, Public Law 86-272. This legislation created a statutory minimum for the nexus required to permit imposition of state net income taxes on businesses

engaged in the taxing state exclusively in interstate commerce, in certain limited situations. The statute thus prohibits state net income taxes (including taxes, like New York's franchise tax, measured by net income) on foreign corporations whose sole contact with the taxing state consists of either, or both, of the following:

> (1) the solicitation of orders by such person [viz., the corporation], or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and
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> (2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1). (15 U.S.C. § 381(a)).

One of the defects of P.L. 86-272 is its failure to define the term "solicitation". The courts of various jurisdictions have grappled with this issue, giving rise to two broad and contrary views of the matter. One such view is that the Congress intended the term "solicitation" to be narrowly construed, in which case ancillary activities such as promoting sales or scanning the inventory of retailers would take the selling corporation's activities outside the ambit of the statutory protection. See, Hervey v. A.M.F. Beaird, 464 S.W.2d 557 (Ark. 1971); See also, Clairol, Inc. v. Kingsley, 262 A.2d 213 (N.J. 1970). A more liberal approach has been taken by other jurisdictions, such as Pennsylvania. See, U.S. Tobacco Co. v. Commonwealth, 386 A.2d 471 (Pa. 1978). The New York State Court of Appeals has apparently opted for a liberal view, bringing within the concept of solicitation those sundry activities which are closely related to the efforts of solicitation taken in the narrow sense. Gillette Co. v. Tax Comm'n., 56 A.D.2d 475 (1977), aff'd, 45 N.Y.2d 846 (1978). The Gillette Company, in addition to "pure" solicitation, had its representatives in New York engage in advising certain retailers, who did not order directly from Gillette, on display techniques. Id. The court held such activities not to transcend the limits of P.L. 86-272, stating that:

> although it is not possible to state a general rule demarcating solicitation from merchandising, certainly where, as here, the complaining taxpayer owns no real or personal property (except salesmen's samples) in the State and makes no repairs on its goods after sale, the purpose of Public Law 86-272 would be frustrated by permitting the tax. Advice to retailers on the art of displaying goods to the public can hardly be more thoroughly solicitation, i.e., in this context, an effort to induce purchase of Gillette products. Making the evanescent distinctions which would be necessary to justify the imposition of the tax upon petitioner herein would, if indulged in by the several States, tend to "balkanize the American economy", a result which it was Congress' purpose to prevent.

Id. at 482. The court also grounded its conclusion on a finding that "some sort of calls upon indirect accounts was expressly anticipated and condoned by the statute .... " For an instance of the Tax Commission's application of this approach, see National Tires, Inc., Decision of the State Tax Commission, October 17, 1980, TSB-H-80(28)C.

In the present case, Hauserman, Ltd's ownership of the furniture held as samples is purely ancillary to its solicitation and, therefore, does not of itself give rise to a basis for taxation. (See 20 NYCRR 1-3.4(b)(9)(iv)(a)).Using samples in connection with solicitation is merely incidental to offering tangible personal property for sale and will not make the corporation taxable. (See also, American Association of Advertising Agencies, State Tax Commission Advisory Opinion, November 7, 1980, TSB-H-80(32)C). However, the maintenance of the New York showroom-sales office by Sunar, U.S.A. on behalf of Hauserman, Ltd. exceeds the statutorily prescribed minimum activities protected by Public Law 86-272, and thereby subjects Hauserman, Ltd. to tax. The embodiment of the Public Law exemption in the Franchise Tax Regulations specifically provides that maintenance of an office in New York exceeds the scope of the federally protected solicitation activities, and renders a corporation subject to tax. (20 NYCRR §l-3.4(b)(9)(vi)). The regulations further define an office as "any area, enclosure, or facility which is used in the regular course of the corporate business." (20 NYCRR 1-3.2(e)). The New York showroom-sales office operated by Sunar, U.S.A. falls within the contemplation of the regulations as an "office", and it is, in effect, maintained by Hauserman, Ltd., via the Exclusive Sales Representative Agreement between Hauserman, Ltd. and Hauserman, Inc. This conclusion flows from the extent of Hauserman, Ltd's control over the operations of the office by Hauserman, Inc.

The regulations, tracking the federal statute, do provide the following exception to taxability based solely on the maintenance of an office:

> [A] corporation will not be considered to have engaged in taxable activities in New York State by reason of maintaining an office in New York State by one or more independent contractors whose activities on behalf of the corporation in New York State consist solely of making sales, or soliciting orders for sales, of tangible personal property. (emphasis added) (20 NYCRR 1-3.4(b) (9) (ii).

The regulations further provide, in accordance with the federal statutory provisions, that:

> [t]he term independent contractor means a commission agent, broker, or other independent contractor who is engaged in selling, or in soliciting orders for the sale of tangible personal property for more than one principal who holds himself out as such in the regular course of his business activities. The term representative does not include an independent contractor. (emphasis added) (20 NYCRR 1-3.4(b) (9) (iii)).

While the maintenance of an office by such an independent contractor is protected by the statute, the same is not true where an office is maintained by an agent or employee of the foreign corporation. (See, Jantzen Inc. v. District of Columbia, 395 A.2d 29 (D.C. 1978)). In Jantzen, the court went on to conclude that the "fact that the statute allows the maintenance of an office by an independent contractor, but makes no such express allowance with respect to a sales representative, supports the inference that the latter is not permitted such an exemption." (Id. at 31).

In the present case, the Exclusive Sales Representative Agreement expressly provides, in section eight, that "[i]t is understood and agreed that the Representative is an independent contractor and is not in any manner an agent or employee of the Company .... " The statutory definition provided in Public Law 86-272, however, requires an independent contractor to be engaged in a representative capacity for more than one principal. (20 NYCRR §1-3.4 (b)(9)(iii)). On the facts presented, Hauserman, Inc. represents only one principal -- that being Hauserman, Ltd.. Therefore, despite the obvious intent of the parties Sunar, U.S.A. is a representative of, not an independent contractor for, Hauserman, Ltd., for purposes of Public Law 86-272. Further, the term independent contractor generally signifies "one who, exercising an independent employment, contracts to do a piece of work according to his own methods, and without being subject to the control of his employer, except as to the result of the work." Ostrander v. Billie Holm's Village Travel, Inc., 87 Misc. 2d 1049, 1051 (1976), citing Hogan v. Comac Sales, 245 A.D. 216, 221 (3d Dept. 1935) (Heffernan, J., dissenting), aff'd, 271 N.Y. 562 (1936). Despite the terminology employed, Sunar, U.S.A. is not in substance an independent contractor, as Hauserman, Ltd. maintains control over essentially all aspects of the services performed by Sunar, U.S.A.

As to Sunar Hauserman, Inc., not only has this corporation replaced Hauserman, Ltd. in its possession of ultimate control over the activities carried on in the New York showroom, under the new arrangement it is Sunar Hauserman, Inc. which itself rents the real property in question and thus clearly falls within the ambit of Article 9-A's jurisdictional standard.

The activities of Hauserman, Inc. performed in new York are two-fold: (1) providing the service of acting as sales representative for Hauserman, Ltd. pursuant to the "Exclusive Sales Representative Agreement," and (2) discharging this agency obligation by, among other things, leasing the New York showroom-sales office and actually soliciting orders for the goods. These activities are properly to be evaluated separately, for purposes of determining taxability under Article 9-A of the Tax Law.

As previously noted, the Franchise Tax is imposed on a corporation for, among other things, doing business in New York State. (Tax Law, §209). In the instant case, those activities performed in the discharge of agency obligations are performed on behalf of Hauserman, Ltd., and accordingly do not constitute doing business for Hauserman, Inc. However, by providing its services as sales representative to Hauserman, Ltd. and creating the agency, Hauserman, Inc. is specifically carrying out a (its) business purpose. Further, Hauserman, Inc. is being remunerated for its services by

Hauserman, Ltd. in accordance with the Exclusive Sales Representative Agreement. Thus, it must be concluded that it is "doing business" for purposes of the Franchise Tax. (20 NYCRR §1-3.2(b)). Accordingly, Hauserman, Inc. is subject to the New York State Franchise Tax on Business Corporations.

DATED: September 9, 1985

s/FRANK J. PUCCIA
Director
Technical Services Bureau

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.